

Q2
2022



CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

**For the three and six months ended
May 31, 2022 and 2021**

Expressed in thousands of Canadian Dollars

TSX: VLNS
Nasdaq: VLNS

The Valens Company Inc.

THE VALENS COMPANY INC.

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THE VALENS COMPANY INC.

Condensed Interim Consolidated Statements of Financial Position

As at May 31, 2022 and November 30, 2021

(Unaudited, Expressed in Thousands of Canadian Dollars)

		May 31, 2022	November 30, 2021
	Notes	\$	\$
ASSETS			
Current			
Cash		24,899	16,053
Marketable securities and derivatives	4	1,244	3,072
Trade and other receivables	5	28,826	28,698
Prepaid expenses and other current assets		6,024	16,261
Income tax receivable	19	4,430	4,430
Indemnity assets	17	11,293	11,368
Inventory	6	31,858	42,039
Assets held for sale	10	3,680	-
Biological assets	7	-	227
		112,254	122,148
Non-Current			
Property, plant and equipment	8	71,973	77,411
Intangible assets	9,17	18,837	91,903
Goodwill	9,17	-	53,222
TOTAL ASSETS		203,064	344,684
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current			
Accounts payable and accrued liabilities		37,102	36,926
Term loan and other debt – current	11	14	9,723
Contractual obligation – current	12	1,642	1,817
Lease liabilities – current	13	1,409	1,406
Contingent consideration – current	17	-	761
Other liability	17	11,293	11,368
		51,460	62,001
Non-Current			
Term loan and other debt	11	38,159	16
Contractual obligation	12	4,632	7,062
Lease liabilities	13	3,490	4,238
Contingent consideration	17	-	1,857
Deferred tax liability	17,19	-	10,072
		97,741	85,246
Shareholders' equity			
Share capital	16	359,189	336,097
Reserves	16	35,510	25,122
Obligation to issue shares	16	1,130	1,463
Accumulated other comprehensive income		1,866	2,573
Deficit		(292,372)	(105,817)
		105,323	259,438
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY		203,064	344,684
Commitments and contingencies (Note 23)			

Approved on behalf of the Board on July 13, 2022:

Signed

"Tyler Robson"

Director

Signed

"Drew Wolff"

Director

The accompanying notes are an integral part of these Condensed Interim Consolidated Financial Statements

THE VALENS COMPANY INC.
Condensed Interim Consolidated Statements of Loss and Comprehensive Loss
For the Three and Six Months Ended May 31,
(Unaudited, Expressed in Thousands of Canadian Dollars Except Share Amounts)

		For the three months ended		For the six months ended	
		2022	2021	2022	2021
	Notes	\$	\$	\$	\$
Revenue		29,275	20,469	59,142	42,243
Excise taxes		(5,276)	(1,705)	(11,963)	(3,465)
Net revenue	14	23,999	18,764	47,179	38,778
Cost of sales	6,8,18	20,639	14,434	40,444	29,327
Inventory valuation allowance	6	13,875	194	15,215	545
Gross profit (loss), excluding fair value items		(10,515)	4,136	(8,480)	8,906
Fair value changes on growth of biological assets	7	86	-	(30)	-
Realized fair value changes on inventory sold or impaired	7	148	-	338	-
Gross profit (loss)		(10,749)	4,136	(8,788)	8,906
Operating expenses					
General and administrative		14,250	9,605	30,050	16,190
Selling and marketing		6,654	1,422	13,150	2,514
Depreciation and amortization	8,9	2,945	2,702	6,131	5,211
Share-based payments	15,16	2,250	1,245	4,003	2,976
Impairment loss on prepaid deposits	6	4,075	-	4,075	-
Restructuring charges	25	3,341	-	4,123	-
		33,515	14,974	61,532	26,891
Loss from operations		(44,264)	(10,838)	(70,320)	(17,985)
Other income (expense)					
Financing costs, net	11,12,13	(1,427)	(150)	(2,779)	(763)
Remeasurement of contingent consideration	17	1,944	-	2,617	-
Foreign exchange gain		14	449	27	658
Gain (loss) on disposal of capital assets		(22)	-	(22)	34
Gain (loss) on marketable securities and derivatives		(1,598)	-	(2,328)	395
Impairment loss	9,10	(123,788)	-	(123,788)	-
Other income		(7)	-	(3)	-
		(124,884)	299	(126,276)	324
Loss before income taxes		(169,148)	(10,539)	(196,596)	(17,661)
Recovery of income taxes	19				
Current		-	(1,603)	-	(2,488)
Deferred		(8,341)	(277)	(10,041)	(361)
		(8,341)	(1,880)	(10,041)	(2,849)
Loss for the period		(160,807)	(8,659)	(186,555)	(14,812)
Basic and diluted loss per common share		(2.13)	(0.16)	(2.60)	(0.30)
Other comprehensive income					
Foreign currency translation loss, net of tax		(741)	-	(707)	-
Comprehensive loss for the period		(161,548)	(8,659)	(187,262)	(14,812)

Weighted average number of common shares outstanding

Basic and diluted	75,341,830	52,557,267	71,629,601	48,930,975
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The accompanying notes are an integral part of these Condensed Interim Consolidated Financial Statements

THE VALENS COMPANY INC.
Condensed Interim Consolidated Statements of Changes in Shareholders' Equity
For the Six Months Ended May 31, 2022 and 2021
(Unaudited, Expressed in Thousands of Canadian Dollars Except Share Amounts)

	<u>Share Capital</u>				Accumulated Other		
	Number	Amount	Reserves	Obligation to	Comprehensive	Deficit	Total
		\$	\$	issue shares	Income	\$	\$
Balance, November 30, 2020	43,057,728	162,585	19,651	1,933	-	(56,783)	127,386
Exercise of RSUs (Note 16(d))	28,078	79	(291)	-	-	-	(212)
Shares issued for exercise of warrants (Note 16(e))	1,167	10	(1)	-	-	-	9
Shares issued for exercise of options (Note 16(f))	72,568	913	(432)	-	-	-	481
Units issued through bought deal financing (Note 16(g))	6,454,666	35,630	4,066	-	-	-	39,696
Share issuance costs (Note 16(g))	-	(2,929)	-	-	-	-	(2,929)
Share-based payments (Note 16(h))	101,667	468	2,597	(222)	-	-	2,843
Shares issued for acquisition of LYF (Note 16(i))	3,106,032	16,214	-	-	-	-	16,214
Loss for the period	-	-	-	-	-	(14,812)	(14,812)
Balance, May 31, 2021	52,821,906	212,970	25,590	1,711	-	(71,595)	168,676
Balance, November 30, 2021	67,832,544	336,097	25,122	1,463	2,573	(105,817)	259,438
Exercise of RSUs (Note 16(a))	86,220	405	(563)	-	-	-	(158)
Share-based payments (Note 16(b))	70,000	471	3,810	(333)	-	-	3,948
Units issued through bought deal financing (Note 16(c))	12,205,186	25,203	7,141	-	-	-	32,344
Share issuance costs (Note 16(c))	-	(2,987)	-	-	-	-	(2,987)
Foreign currency translation loss	-	-	-	-	(707)	-	(707)
Loss for the period	-	-	-	-	-	(186,555)	(186,555)
Balance, May 31, 2022	80,193,950	359,189	35,510	1,130	1,866	(292,372)	105,323

The accompanying notes are an integral part of these Condensed Interim Consolidated Financial Statements

THE VALENS COMPANY INC.

Condensed Interim Consolidated Statements of Cash Flows

For the Six Months Ended May 31, 2022 and 2021

(Unaudited, Expressed in Thousands of Canadian Dollars)

	Notes	2022 \$	2021 \$
OPERATING ACTIVITIES			
Loss for the period		(186,555)	(14,812)
Adjustment for non-cash items:			
Depreciation and amortization		7,587	5,935
Share-based payments		4,003	2,976
Inventory valuation allowance		15,215	545
Fair value changes on growth of biological assets and inventory sold	7	308	-
Impairment loss on trade receivables		2,017	186
Impairment loss on goodwill and intangible assets	9	121,021	-
Impairment loss on assets held for sale	10	2,767	-
Impairment loss on prepaid deposits	6	4,075	-
Recovery of income taxes	19	(10,041)	(2,849)
Interest expense on lease liability	13	107	107
Modification of lease liability	13	(38)	-
Accretion		781	826
Foreign exchange gain		(27)	(658)
Interest income on promissory note receivable		-	(217)
Loss (gain) on disposal of capital assets		22	(34)
Loss (gain) on marketable securities and derivatives		2,328	(395)
Gain on remeasurement of contingent consideration		(2,617)	-
Working capital adjustments:			
Trade and other receivables		(2,160)	(11,407)
Prepaid expenses and other current assets		(188)	1,226
Inventory and biological assets		522	(844)
Contractual obligation		(2,744)	(1,545)
Income taxes recovered		-	798
Accounts payable and accrued liabilities		756	2,911
		(42,861)	(17,251)
INVESTING ACTIVITIES			
Acquisition of property, plant and equipment		(3,919)	(12,562)
Acquisition of intangible assets		(161)	(157)
Purchase of marketable securities and derivatives		(500)	-
Repayment of promissory note receivable		9	1,614
Proceeds from sale of capital assets		87	73
Proceeds from sale of marketable securities and derivatives		-	794
Acquisition of LYF		-	(3,713)
Issuance of promissory note receivable		-	(750)
		(4,484)	(14,701)
FINANCING ACTIVITIES			
Proceeds from term loan	11	40,000	-
Proceeds from bought deal, net of share issue costs	16	29,357	36,767
Proceeds from exercise of warrants		-	9
Proceeds from exercise of stock options		-	481
Payment on exercise of RSUs		(158)	(212)
Payment to settle obligation to issue shares		(54)	(133)
Repayments of term loan and other debt		(9,754)	(1,000)
Financing fees paid		(2,400)	-
Payments on lease liability		(808)	(378)
		56,183	35,534
Effect of exchange rate changes on cash		8	-
CHANGE IN CASH		8,846	3,582
Cash, beginning of period		16,053	20,344
Cash, end of period		24,899	23,926

Supplemental disclosure with respect to cash flows (Note 22)

The accompanying notes are an integral part of these Condensed Interim Consolidated Financial Statements

THE VALENS COMPANY INC.

Notes to the Condensed Interim Consolidated Financial Statements

For the Six Months Ended May 31, 2022 and 2021

(Unaudited, Expressed in Thousands of Canadian Dollars Except Share Amounts)

1. DESCRIPTION OF BUSINESS

The Valens Company Inc. (the “Company”) was incorporated under the laws of British Columbia on January 14, 1981. On June 18, 2020, the Company completed a continuance under the Canada Business Corporations Act (“CBCA”), making the Company a federal corporation governed by the CBCA. At the same time, the Company changed its name from Valens GroWorks Corp. to The Valens Company Inc. The Company operates in the cannabis industry and is focused on delivering a diverse suite of extraction methodologies, end-to-end development and manufacturing of innovative cannabinoid-based products and analytical testing. The Company’s common shares trade under the trading symbol “VLNS” on the Toronto Stock Exchange (“TSX”) and Nasdaq and under the trading symbol “VLNS”.

On November 16, 2021, the Company effected a three for one consolidation of its common shares in order to meet Nasdaq listing requirements. Comparative period common share and share-based instrument balances have been updated to reflect the share consolidation.

The address of the Company’s registered office is Suite 400, 96 Spadina Avenue, Toronto, ON, M5V 2J6.

2. BASIS OF PREPARATION

Statement of compliance

These condensed interim consolidated financial statements have been prepared in conformity with International Accounting Standard (“IAS”) 34, Interim Financial Reporting, using the same accounting policies as detailed in the Company’s annual audited consolidated financial statements for the year ended November 30, 2021. These condensed interim consolidated financial statements do not include all the information required for full annual financial statements in accordance with International Financial Reporting Standards (“IFRS”), as issued by the International Accounting Standards Board (“IASB”) and interpretations of the International Financial Reporting Interpretations Committee (“IFRIC”). These condensed interim consolidated financial statements should be read in conjunction with the annual audited consolidated financial statements.

These condensed interim consolidated financial statements of the Company were approved and authorized for issue by the Board of Directors on July 13, 2022.

Basis of consolidation

These condensed interim consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. Control exists when the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. The financial statements of the subsidiaries are included in the condensed interim consolidated financial statements from the date that control commences until the date that control ceases. Wholly owned subsidiaries of the Company, included in these condensed interim consolidated financial statements are as follows:

THE VALENS COMPANY INC.

Notes to the Condensed Interim Consolidated Financial Statements

For the Six Months Ended May 31, 2022 and 2021

(Unaudited, Expressed in Thousands of Canadian Dollars Except Share Amounts)

2. BASIS OF PREPARATION – continued

Subsidiary	Geographical Region	Functional Currency	Date of Consolidation
Valens Agritech Ltd. (“VAL”)	Canada	CAD	April 14, 2014
Valens Farms Ltd. (“Farms”)	Canada	CAD	July 19, 2018
Valens Labs Ltd. (“Labs”)	Canada	CAD	October 18, 2018
Southern Cliff Brands Inc. (“Pommies”)	Canada	CAD	November 8, 2019
Valens Australia Pty Ltd. (“VAPL”)	Australia	CAD	June 26, 2020
LYF Food Technologies Inc. (“LYF”)	Canada	CAD	March 5, 2021
Green Roads, Inc. (“Green Roads” or “GR”)	United States	USD	June 17, 2021
Citizen Stash Cannabis Corp. (“Citizen Stash” or “CS”)	Canada	CAD	November 8, 2021

All intra-company transactions, balances, income, and expenses were eliminated in full on consolidation.

Basis of measurement

These condensed interim consolidated financial statements have been prepared on the accrual basis of accounting except for cash flow information, and on a historical cost basis except for certain financial assets and liabilities measured at fair value or fair value less costs to sell. The financial statements are presented in thousands of Canadian Dollars, which is also the Company’s functional currency with exception to Green Roads, which has a functional currency of the U.S. Dollar.

Comparative figures

Certain immaterial comparative figures have been reclassified to conform to the current period’s presentation.

Critical accounting estimates and judgments

IFRS requires management to make judgments, estimates and assumptions that affect the reported amounts of assets, liabilities, and contingent liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Aside from those included within their respective notes to the condensed interim consolidated financial statements, there have been no material revisions or changes to the nature and amount of estimates and judgments from the annual audited consolidated financial statements for the year ended November 30, 2021.

Estimates and assumptions are continuously evaluated and are based on management’s experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. However, actual outcomes can differ from these estimates.

Significant assumptions about the future and other sources of estimation uncertainty that management has made at the end of the reporting period, that could result in a material adjustment to the carrying amounts of assets and liabilities in the event that actual results differ from assumptions made, are disclosed throughout the notes to the condensed interim consolidated financial statements.

3. APPLICATION OF NEW ACCOUNTING STANDARDS**A. New IFRS Standards in issue but not yet effective****(i) Amendments to IAS 37: Onerous Contracts and the Cost of Fulfilling a Contract**

The amendment specifies that ‘cost of fulfilling’ a contract comprises the ‘costs that relate directly to the contract’. Costs that relate directly to a contract can either be incremental costs of fulfilling that contract or an allocation of other costs that relate directly to fulfilling contracts. The amendment is effective for annual periods beginning on or after January 1, 2022 with early application permitted. The Company is currently evaluating the potential impact of these amendments on the Company’s condensed interim consolidated financial statements.

THE VALENS COMPANY INC.

Notes to the Condensed Interim Consolidated Financial Statements

For the Six Months Ended May 31, 2022 and 2021

(Unaudited, Expressed in Thousands of Canadian Dollars Except Share Amounts)

3. APPLICATION OF NEW ACCOUNTING STANDARDS – *continued*

(ii) Amendments to IAS 1: Classification of Liabilities as Current or Non-current

The amendment clarifies the requirements relating to determining if a liability should be presented as current or non-current in the statement of financial position. Under the new requirement, the assessment of whether a liability is presented as current or non-current is based on the contractual arrangements in place as at the reporting date and does not impact the amount or timing of recognition. The amendment applies retrospectively for annual reporting periods beginning on or after January 1, 2023. The Company is currently evaluating the potential impact of these amendments on the Company's condensed interim consolidated financial statements.

(iii) Amendments to IAS 12: Deferred Tax related to Assets and Liabilities arising from a Single Transaction

The amendment narrowed the scope of certain recognition exemptions so that it no longer applies to transactions that, on initial recognition, give rise to equal taxable and deductible temporary differences. An entity applies the amendments to transactions that occur on or after the beginning of the earliest comparative period presented. It also, at the beginning of the earliest comparative period presented, recognizes deferred tax for all temporary differences related to leases and decommissioning obligations and recognizes the cumulative effect of initially applying the amendments as an adjustment to the opening balance of retained earnings (or other component of equity, as appropriate) at that date. The amendment is effective for annual periods beginning on or after January 1, 2023 with early application permitted. The Company is currently evaluating the potential impact of these amendments on the Company's condensed interim consolidated financial statements.

(iv) Amendments to IAS 41: Agriculture

As part of its 2018-2020 annual improvements to IFRS standards process, the IASB issued amendments to IAS 41. The amendment removes the requirement in paragraph 22 of IAS 41 for entities to exclude taxation cash flow when measuring the fair value of a biological asset using a present value technique. This will ensure consistency with the requirements in IFRS 13. The amendment is effective for annual reporting periods beginning on or after January 1, 2022. The Company is currently evaluating the potential impact of these amendments on the Company's condensed interim consolidated financial statements.

(v) Definition of Accounting Estimates (Amendments to IAS 8)

On February 12, 2021, the IASB issued *Definition of Accounting Estimates (Amendments to IAS 8)*.

The amendments introduce a new definition for accounting estimates, clarifying that they are monetary amounts in the financial statements that are subject to measurement uncertainty. The amendments also clarify the relationship between accounting policies and accounting estimates by specifying that a company develops an accounting estimate to achieve the objective set out by an accounting policy.

The amendments are effective for annual periods beginning on or after January 1, 2023. Early adoption is permitted. The Company is currently evaluating the potential impact of these amendments on the Company's condensed interim consolidated financial statements.

(vi) Disclosure initiative – Accounting Policies (Amendments to IAS 1 and IFRS Practice Statement 2)

On February 12, 2021, the IASB issued *Disclosure Initiative – Accounting Policies (Amendments to IAS 1 and IFRS Practice Statement 2 Making Materiality Judgements)*. The amendments help companies provide useful accounting policy disclosures. The key amendments include:

- requiring companies to disclose their material accounting policies rather than their significant accounting policies;
- clarifying that accounting policies related to immaterial transactions, other events or conditions are themselves immaterial and as such need not be disclosed; and,
- clarifying that not all accounting policies that relate to material transactions, other events or conditions are themselves material to a company's financial statements.

THE VALENS COMPANY INC.

Notes to the Condensed Interim Consolidated Financial Statements

For the Six Months Ended May 31, 2022 and 2021

(Unaudited, Expressed in Thousands of Canadian Dollars Except Share Amounts)

3. APPLICATION OF NEW ACCOUNTING STANDARDS – continued

The amendments are effective for annual periods beginning on or after January 1, 2023. Early adoption is permitted. The Company is currently evaluating the potential impact of these amendments on the Company's condensed interim consolidated financial statements.

4. MARKETABLE SECURITIES AND DERIVATIVES

	May 31, 2022	November 30, 2021
	\$	\$
Common shares of Canadian licensed producer	1,092	3,000
Purchase warrants of Canadian licensed producer	152	72
	1,244	3,072

On September 26, 2021, the Company subscribed for \$3,000 of units in a Canadian licensed producer's private placement. The Company received 375,000 common shares and 375,000 warrants with an exercise price of \$9.20 for a term of two years. During the six months ended May 31, 2022, the Canadian licensed producer completed a qualifying transaction. As part of the listing agreement, the Company's initial investment was revised to include receipt of 473,598 common shares and 473,598 warrants with a revised exercise price of \$7.28 for a term of two years.

On December 23, 2021, the Company subscribed for \$500 of units in a Canadian licensed producer. The Company received 10,000,000 common shares and 10,000,000 warrants with an exercise price of \$0.02 for a term of two years.

For the three and six months ended May 31, 2022, the Company recognized an unrealized loss on the common shares of \$1,073 and \$2,408, respectively, and an unrealized loss on the purchase warrants of \$524 for the three months ended May 31, 2022 and an unrealized gain on the purchase warrants of \$80 for the six months ended May 31, 2022.

5. TRADE AND OTHER RECEIVABLES

	May 31, 2022	November 30, 2021
	\$	\$
Trade accounts receivable	29,470	28,741
Less: trade receivables valuation allowance	(3,686)	(1,679)
Net trade accounts receivable	25,784	27,062
Unbilled revenue on products/services transferred over time	430	387
GST recoverable	23	140
Government assistance receivable (Note 18)	114	114
Other receivables	2,475	995
	28,826	28,698

THE VALENS COMPANY INC.

Notes to the Condensed Interim Consolidated Financial Statements

For the Six Months Ended May 31, 2022 and 2021

(Unaudited, Expressed in Thousands of Canadian Dollars Except Share Amounts)

6. INVENTORY

	May 31, 2022 \$	November 30, 2021 \$
Dried cannabis and hemp biomass	10,345	7,799
Extracted cannabis and hemp oils	27,716	26,533
Finished goods	4,619	5,073
Packaging and supplies	8,878	7,437
	51,558	46,842
Less: inventory valuation allowance	(19,700)	(4,803)
	31,858	42,039

Inventory expensed to cost of sales for the three and six months ended May 31, 2022 was \$19,245 and \$36,979, respectively (May 31, 2021 - \$37,150 and \$49,346). During the three and six months ended May 31, 2022, the Company recorded an inventory valuation allowance of \$13,875 and \$15,215, respectively (May 31, 2021 - \$194 and \$545). The valuation allowance was related to dried cannabis, oils, finished goods, and packaging and supplies, in which the cost exceeds its net realizable value based on the current selling prices of the Company's products.

In fiscal 2020, the Company had made a prepaid deposit for the purchase of certain raw materials at a fixed price. During the period ended May 31, 2022, the Company re-assessed the value of this deposit based on updated market prices for the raw materials and determined it to be onerous. The re-assessment resulted in an impairment loss of \$4,075 for the three and six months ended May 31, 2022, which is included in impairment loss on prepaid deposits in the condensed interim consolidated statements of loss and comprehensive loss.

7. BIOLOGICAL ASSETS

The Company's biological assets related to cannabis cultivation out of the Company's facility in Mission, BC. As at May 31, 2022, the Company is no longer cultivating biological assets, and the facility is currently classified as a disposal group as assets held for sale, as described in Note 10. No further fair value changes are expected, as the Company no longer produces biological assets.

THE VALENS COMPANY INC.

Notes to the Condensed Interim Consolidated Financial Statements

For the Six Months Ended May 31, 2022 and 2021

(Unaudited, Expressed in Thousands of Canadian Dollars Except Share Amounts)

8. PROPERTY, PLANT AND EQUIPMENT

	Land \$	Buildings \$	Leaseholds \$	Computer equipment and software \$	Office furniture and equipment \$	Lab and production equipment \$	Right-of-use asset \$	Total \$
Cost								
Balance, November 30, 2021	6,336	46,801	2,086	1,300	1,889	25,130	6,675	90,217
Additions	-	314	23	68	72	3,682	-	4,159
Amendments to CS acquisition (Note 17)	-	(106)	-	-	-	-	-	(106)
Foreign exchange adjustments	-	-	(1)	-	(2)	(5)	(18)	(26)
Disposals	-	-	(13)	(2)	-	(86)	(47)	(148)
Transfers to assets held for sale (Note 10)	(1,477)	(4,024)	-	(130)	(8)	(297)	-	(5,936)
Balance, May 31, 2022	4,859	42,985	2,095	1,236	1,951	28,424	6,610	88,160
Accumulated depreciation								
Balance, November 30, 2021	-	2,438	51	752	906	7,307	1,352	12,806
Depreciation	-	722	139	148	177	1,647	736	3,569
Foreign exchange adjustments	-	-	-	-	-	(1)	(3)	(4)
Disposals	-	-	(13)	-	-	(26)	-	(39)
Transfers to assets held for sale (Note 10)	-	(73)	-	(37)	(2)	(33)	-	(145)
Balance, May 31, 2022	-	3,087	177	863	1,081	8,894	2,085	16,187
Carrying value								
November 30, 2021	6,336	44,363	2,035	548	983	17,823	5,323	77,411
May 31, 2022	4,859	39,898	1,918	373	870	19,530	4,525	71,973

During the three and six months ended May 31, 2022, the Company recognized \$1,868 and \$3,569 of depreciation, respectively (May 31, 2021 – \$1,276 and \$2,264). Of this amount, \$761 and \$1,456 was allocated to cost of sales during the three and six months ended May 31, 2022, respectively (May 31, 2021 – \$240 and \$407).

THE VALENS COMPANY INC.

Notes to the Condensed Interim Consolidated Financial Statements

For the Six Months Ended May 31, 2022 and 2021

(Unaudited, Expressed in Thousands of Canadian Dollars Except Share Amounts)

9. INTANGIBLE ASSETS AND GOODWILL

	SoRSE Manufacturing and Sales License \$	Health Canada Licenses \$	Customer Relationships \$	Brand \$	Software \$	Goodwill \$	Total \$
Cost							
Balance, November 30, 2021	38,449	13,093	2,602	55,058	1,109	53,222	163,533
Additions	-	-	-	-	161	-	161
Amendments to CS acquisition (Note 17)	-	(125)	-	-	-	(106)	(231)
Amendments to GR acquisition (Note 17)	-	-	-	-	-	109	109
Reclassification adjustments	-	-	-	36	(36)	-	-
Foreign exchange adjustments	-	-	(7)	(338)	(5)	(289)	(639)
Transfers to assets held for sale (Note 10)	-	(668)	-	-	-	-	(668)
Balance, May 31, 2022	38,449	12,300	2,595	54,756	1,229	52,936	162,265
Accumulated amortization and impairment							
Balance, November 30, 2021	17,091	141	436	715	25	-	18,408
Amortization	3,224	258	206	128	200	-	4,016
Impairment	15,437	-	1,579	50,917	152	52,936	121,021
Reclassification adjustments	-	-	192	(390)	198	-	-
Foreign exchange adjustments	-	-	(2)	-	(3)	-	(5)
Transfers to assets held for sale (Note 10)	-	(12)	-	-	-	-	(12)
Balance, May 31, 2022	35,752	387	2,411	51,370	572	52,936	143,428
Carrying value							
November 30, 2021	21,358	12,952	2,166	54,343	1,084	53,222	145,125
May 31, 2022	2,697	11,913	184	3,386	657	-	18,837

THE VALENS COMPANY INC.

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9. INTANGIBLE ASSETS AND GOODWILL – *continued*

Impairment of goodwill and intangible assets

During the three months ended May 31, 2022, indicators of impairment were identified as a result of market conditions surrounding the Company and capital markets within the cannabis industry as a whole. This included an excess in the carrying value of the Company's net assets compared to its market capitalization, as well as an increase in market interest rates. These indicators resulted in management re-assessing its future cash flow forecasts, as well as the current valuation of certain intangible assets and goodwill. During the three and six months ended May 31, 2022, a total of \$120,869 in impairment losses have been recognized in the condensed interim consolidated statements of loss and comprehensive loss. Impairment losses recognized within the Canadian cash generating unit ("Canadian CGU") totalled \$63,952, with an additional \$56,917 recognized within the United States and international cash generating unit ("US CGU"). Details of impairment losses recognized, as well as all significant assumptions, estimates, inputs, and recoverable amounts are as follows:

Valuation of CGUs

In accordance with IAS 36 *Impairment of Assets*, management used a value in use ("VIU") to determine each CGU's recoverable amount. In assessing each CGU's VIU, management employed a five-year free cash flow forecast for each CGU tested.

Significant Assumptions, Estimates, and Inputs of Cash Flow Model

Revenue

For the Canadian CGU, management applied a 9% increase in revenue for the remainder of fiscal 2022 from fiscal 2021. The estimated revenue from fiscal 2023 to 2026 is expected to increase by an average of 37%, due to realized synergies from acquisitions, continued capture of Canadian recreational market share, and the continued growth of the overall industry as it matures. For the US CGU, management applied a 5% quarterly increase throughout the remainder of fiscal 2022. The estimated revenue from fiscal 2023 to 2026 is expected to increase by an average of 28%, due to further e-commerce growth, implementation of new direct to consumer media, and realized growth from increased marketing spend since acquisition.

Gross Margin

For the Canadian CGU, management applied a 10% gross margin for the remainder of fiscal 2022, as the Company aims to become more lean and focus on its most profitable products. Management has applied gross margins between 27% and 36% between fiscal 2023 and 2026. For the US CGU, management has applied gross margins ranging between 54% and 60% between the remainder of fiscal 2022 and 2026.

Operating Expenses

For the Canadian CGU, after initial cost saving measures are expected to be realized throughout the remainder of fiscal 2022, annual operating expenses are expected to increase at a steady rate. Management applied annual increases between 3% and 5% from fiscal 2023 to 2026. For the US CGU, increased marketing spend is expected throughout the remainder of fiscal 2022, which thereafter are expected to stabilize. Management has applied a consistent annual increase in operating expenses of 3% from fiscal 2023 to 2026.

Capital Expenditures

For the Canadian CGU, management expects that capacity at all Canadian facilities will be sufficient to support revenue growth from fiscal 2023 to 2026. As such, management has applied significant decreases in capital expense spending for the remainder of fiscal 2022 and 2023, as compared to prior periods. Thereafter, increases ranging between 1% and 2% have been applied between fiscal 2024 and 2026. For the US CGU, operations are expected to be sufficiently managed under current capacity. Management has applied consistent increases of 1% annually from fiscal 2023 to 2026.

Tax Rate

For the Canadian CGU and US CGU, the Company used tax rates applicable to each CGU's jurisdiction.

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9. INTANGIBLE ASSETS AND GOODWILL – *continued*

Discount Rate

For the Canadian CGU and US CGU, respectively, a discount rate of 24.2% and 23% have been applied in the model. Discount rates applied are reflective of each CGU's weighted average cost of capital.

Terminal Growth Rate

For both the Canadian and US CGUs, management applied a 2% terminal growth increase for periods beyond fiscal 2026, based on expected inflationary increases.

Valuation Conclusion

Based on the above assumptions and forecasted free cash flow model, the total VIU of the Company as a whole is calculated to be \$128,553, comprising the Canadian CGU at \$125,393 and the US CGU at \$3,160. An impairment loss during the period was recognized in the amount of \$120,869. Total impairment recognized within the Canadian CGU was \$63,952, with \$56,917 recognized within the US CGU.

Recognition, Measurement, and Allocation of Impairment Losses

In accordance with IAS 36 *Impairment of Assets*, the carrying value of any goodwill allocated to each CGU is to be reduced first, followed by other assets of the CGU on a pro-rata basis, based on the carrying amount of each asset within the CGU. In this case, a reduction to intangible assets was deemed most appropriate, given the nature of the CGUs identified.

The recoverable amount of goodwill within both CGUs after allocation of impairment losses was \$nil. This resulted in impairment losses recognized of \$25,233 and \$27,703 within the Canadian and US CGUs, respectively for the three and six months ended May 31, 2022.

The recoverable amount of these assets was determined to be \$3,488 for the Canadian CGU and \$3,640 for the US CGU. This resulted in impairment losses recognized of \$38,719 and \$29,214 within the Canadian and US CGUs, respectively for the three and six months ended May 31, 2022.

Other Impairment

Unrelated to the above impairment assessment, during the three and six months ended May 31, 2022, an additional \$152 was recognized in impairment for obsolete software which had a carrying value exceeding its fair value, which has been included in impairment loss in the condensed interim consolidated statements of loss and comprehensive loss.

10. ASSETS HELD FOR SALE AND DISCONTINUED OPERATIONS

Accounting Policy

The Company accounts for its assets held for sale in accordance with IFRS 5 *Non-Current Assets Held for Sale and Discontinued Operations*. The Company designates its assets and disposal groups as being held for sale if their carrying amounts will be recovered principally through a sale transaction rather than through their continued use. For assets and disposal groups to be classified as being held for sale, their ultimate sale must be highly probable within one year, they must be available for immediate sale in their current condition, and they must be actively marketed by management. Assets held for sale are carried at the lower of their carrying amount and fair value less costs to sell and are presented separately in the condensed interim consolidated statements of financial position.

THE VALENS COMPANY INC.

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10. ASSETS HELD FOR SALE AND DISCONTINUED OPERATIONS – continued***Accounting Estimates and Judgments***

Judgment is required in determining whether an asset or group of assets meets the criteria for being classified as “assets held for sale” in the condensed interim consolidated statements of financial position. The criteria that must be considered by management includes the existence of an active plan to dispose of the assets or disposal group, the expected selling price of the assets or disposal group, the expected timing of the completion of the sale, and the period of time for which the assets or disposal group have been classified as being held for sale. The Company will review the criteria for assets held for sale each reporting period and will reclassify assets to or from this category, as appropriate. In addition, there is a requirement to evaluate and record assets held for sale at the lower of their carrying value and fair value less costs to sell.

During the period ended May 31, 2022, the Company designated its production facility and Health Canada license in Mission, British Columbia as being held for sale (the “Disposal Group”). The Disposal Group includes all property, plant and equipment associated with the facility (Note 8), as well as the facility’s associated production license (Note 9). The Disposal Group is ready for sale in its current condition as at May 31, 2022. In accordance with IFRS 5 *Non-Current Assets Held for Sale and Discontinued Operations*, the Disposal Group has been presented separately on the condensed interim consolidated statements of financial position. All assets within the disposal group are within the Canada operating segment.

A net balance of property, plant and equipment of \$5,791 and intangible assets of \$656 have been designated as assets held for sale. During the period ended May 31, 2022, the Company recognized an impairment on the Disposal Group, as its carrying value was higher than its fair market value less costs of disposal. The fair market value less costs of disposal of the Disposal Group totals \$3,680, resulting in a loss on impairment of assets held for sale of \$2,767 in the three and six months ended May 31, 2022, which has been included in impairment loss in the condensed interim consolidated statements of loss and comprehensive loss.

11. TERM LOAN AND OTHER DEBT

<i>Term Loan</i>	\$
Balance, November 30, 2021	9,750
Additions	40,000
Repayment	(9,750)
Balance, May 31, 2022	40,000
<i>Deferred financing costs</i>	
Balance, November 30, 2021	38
Accelerated accretion on repayment	(38)
Additions	2,400
Accretion	(550)
Balance, May 31, 2022	1,850
Total term loan, net of deferred financing costs	38,150
Current portion	-
Non-current portion	38,150

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11. TERM LOAN AND OTHER DEBT – continued

On December 16, 2021, the Company entered into a secured non-revolving term loan with a private institutional lender for an aggregate principal amount of \$40 million. The loan accrues interest at a rate of 10% per annum, which is payable quarterly, and matures on December 15, 2023, at which point the full outstanding principal amount becomes payable. The loan carries a minimum liquidity requirement, whereby the Company must maintain a minimum unrestricted cash balance of \$3,000. As at May 31, 2022, the Company is in compliance with all covenant requirements. A portion of the proceeds were used to repay the existing term loans and mortgage assumed in the acquisition of Citizen Stash, in full on December 20, 2021. The Company incurred and deferred \$2,400 of costs to secure the loan. The term loan is recorded at amortized cost, with the deferred financing costs included in the carrying value of the term loan and amortized using the effective interest rate method.

The Company's required repayments on the term loan due in each of the next reporting years are as follows:

2022	\$ -
2023	-
2024	40,000
	<u>40,000</u>

In addition to the credit facility discussed above, there is also debt held in relation to a vehicle used at Green Roads. The vehicle debt contributes \$14 and \$9 to the term loan current and non-current balances, respectively.

12. CONTRACTUAL OBLIGATION

The following is a continuity schedule of the contractual obligation related to the SoRSE manufacturing and sales license agreement for the six months ended May 31, 2022:

Balance, November 30, 2021	\$ 8,879
Accretion	193
Payment	(2,744)
Foreign exchange gain	(54)
Balance, May 31, 2022	<u>6,274</u>
Current portion	(1,642)
Non-current portion	<u>4,632</u>

13. LEASE LIABILITIES

The following is a continuity schedule of lease liabilities for the six months ended May 31, 2022:

Balance, November 30, 2021	\$ 5,644
Lease payments	(808)
Foreign exchange adjustments	(6)
Interest expense on lease liabilities	107
Lease modification	(38)
Balance, May 31, 2022	<u>4,899</u>
Current portion	(1,409)
Non-current portion	<u>3,490</u>

When measuring lease liabilities, the Company discounts lease payments using its incremental borrowing rate. For leases recognized in the six months ended May 31, 2022, the weighted average rate applied is 4.82% (May 31, 2021 – 5.02%). During the six months ended May 31, 2022, the Company recorded rent expense of \$589 (May 31, 2021 – \$322) related to short-term and low value agreements.

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14. NET REVENUE

Net revenue is disaggregated by revenue stream and timing of revenue recognition.

	For the three months ended		For the six months ended	
	May 31, 2022	May 31, 2021	May 31, 2022	May 31, 2021
	\$	\$	\$	\$
Toll processing and co-packing	1,289	1,489	2,205	3,234
Product sales	20,973	16,884	42,482	34,737
Analytical testing	664	391	1,041	807
Other revenue	1,073	-	1,451	-
	23,999	18,764	47,179	38,778
Products transferred at a point in time	22,710	17,275	44,974	35,544
Products/services transferred over time	1,289	1,489	2,205	3,234
	23,999	18,764	47,179	38,778

15. RELATED PARTY TRANSACTIONS

Key management personnel are those persons having the authority and responsibility for planning, directing, and controlling the activities of the Company, directly or indirectly. The Company has defined key management personnel to include the CEO, CFO, COO, CCO, President, Executive Vice Presidents, and directors of the Company.

The remuneration and other payments to the Company's directors and other key management personnel are as follows:

	For the three months ended		For the six months ended	
	May 31, 2022	May 31, 2021	May 31, 2022	May 31, 2021
	\$	\$	\$	\$
Wages and salaries	616	554	1,232	1,082
Share-based payments	1,475	985	2,746	2,210
	2,091	1,539	3,978	3,292

16. SHARE CAPITAL AND RESERVES**Authorized share capital**

The Company is authorized to issue an unlimited number of common and preferred shares with no par value.

Issued shares**Six months ended May 31, 2022:**

- (a) The Company issued 86,220 common shares in connection with the vesting and release of 172,419 RSUs resulting in an increase to share capital of \$405 and a decrease in cash and cash equivalents of \$158 in relation to withholding taxes paid.
- (b) The Company issued 70,000 common shares in connection with employment compensation agreements, resulting in a decrease in the obligation to issue shares of \$333 and increase in share capital of \$471.

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Notes to the Condensed Interim Consolidated Financial Statements

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16. SHARE CAPITAL AND RESERVES – continued

- (c) On April 5, 2022, the Company closed a bought deal financing pursuant to which the Company issued 12,205,186 units at a price of \$2.65 per unit, valued at \$32,344 which were comprised of one common share of the Company and one-half share purchase warrant. The total consideration of the units issued was allocated \$25,203 to common shares and \$7,141 to share purchase warrants. Each full share purchase warrant is exercisable at a price of \$3.20 per share for a period of forty-eight months from the date of closing. In connection with the financing, the Company incurred share issuance costs of \$2,987 that were recorded to equity.

Six months ended May 31, 2021:

- (d) The Company issued 28,078 common shares in connection with the vesting and release of 56,152 RSUs resulting in an increase to share capital of \$79 and a decrease in cash and cash equivalents of \$212 in relation to withholding taxes paid.
- (e) The Company issued 1,167 common shares at a price of \$7.65 per common share in connection with the exercise of warrants for gross proceeds of \$9. As a result of the exercise of the warrants, the fair value of the warrants amounting to \$1 was reclassified from reserves to share capital.
- (f) The Company issued 72,568 common shares in connection with the exercise of options for gross proceeds of \$481. As a result of the exercise of options, the fair value of the options amounting to \$432 was reclassified from reserves to share capital.
- (g) On January 29, 2021, the Company closed a bought deal financing pursuant to which the Company issued 6,454,666 units valued at \$39,696 which were comprised of one common share of the Company and one-half share purchase warrant. The total consideration of the units issued was allocated \$32,701 to common shares and \$4,066 to share purchase warrants. Each full share purchase warrant is exercisable at a price of \$7.65 per share for a period of thirty-six from the date of closing. In connection with the financing, the Company incurred share issuance costs of \$2,929 that were recorded to equity.
- (h) The Company issued 101,667 common shares in connection with employment compensation agreements resulting in a decrease in the obligation to issue shares of \$222 and increase in share capital of \$468.
- (i) The company issued 3,106,032 common shares valued at \$16,214 in connection with the acquisition of LYF (Note 17)

Warrants

The following table summarizes warrant activity during the six months ended May 31, 2022 and the year ended November 30, 2021:

	Number of Warrants	Weighted Average Exercise Price \$
Balance, outstanding November 30, 2021	17,646,150	9.75
Issued	6,102,593	3.20
Balance, outstanding May 31, 2022	23,748,743	8.06

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16. SHARE CAPITAL AND RESERVES – continued

The following table summarizes the warrants outstanding as at May 31, 2022:

Warrants Outstanding	Warrants Exercisable	Exercise price \$	Expiry date
400,000	400,000	10.50	October 26, 2023
300,000	300,000	11.25	October 26, 2023
300,000	300,000	12.00	October 26, 2023
9,678,500	9,678,500	7.65	January 29, 2024
6,967,650	6,967,650	12.45	June 4, 2024
6,102,593	6,102,593	3.20	April 5, 2026
23,748,743	23,748,743		

Obligation to issue shares

The Company has entered into agreements with officers, to issue the following shares:

	Number of shares to be issued		
	2022	2023	Total
Officers	100,000	150,000	250,000

Of the amount recognized for the obligation to issue shares, \$87 and \$192 was recorded as share-based payments expense related to the issue of 35,000 and 70,000 shares for the three and six months ended May 31, 2022, respectively (May 31, 2021 – \$176 and \$379 related to the issue of 100,000 and 200,000 shares).

Escrow shares

In connection with the acquisition of Pommies, 201,351 common shares were placed in escrow, which included 86,293 indemnity shares and 115,057 milestone shares. These shares' release was subject to certain indemnity provisions and the achievement of specific milestones and provisions outlined in the share purchase agreement. As of May 31, 2022, all indemnity shares had been released from escrow, while 28,764 of the milestone shares had been released from escrow, with a total of 86,293 milestone shares remaining in escrow.

In connection with the acquisition of LYF (Note 17), 755,555 common shares were placed in escrow subject to indemnity provisions and the achievement of specific milestones outlined in the share purchase agreement. As of May 31, 2022, these shares remain in escrow as the milestones have not yet been achieved.

In connection with the acquisition of GR (Note 17), there were 1,434,767 common shares placed in escrow subject to the resolution and settlement of certain tax matters, in which the sellers are required to indemnify the Company. As of May 31, 2022, these shares remain in escrow as the resolution and settlement has not yet occurred.

Omnibus long-term incentive plan

The Company has in place an omnibus LTIP, which allows for a variety of equity-based awards that provide different types of incentives to be granted to certain officers, employees, and consultants (in the case of options ("Options"), performance share units ("PSU") and restricted share units ("RSU")) and directors (in the case of deferred share units ("DSU")). Any existing options that were granted prior to the effective date of the LTIP pursuant to the Company's existing stock option plan ("Legacy Option Plan").

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16. SHARE CAPITAL AND RESERVES – continued**LTIP option plan**

The following table summarizes LTIP stock option activity during the six months ended May 31, 2022:

	Number of Options	Weighted Average Exercise Price \$
Balance outstanding, November 30, 2021	499,244	5.71
Issued	2,568,462	3.93
Cancelled and forfeited	(163,731)	4.21
Balance outstanding, May 31, 2022	2,903,975	4.22
Options exercisable, May 31, 2022	781,014	4.63

The following table summarizes the LTIP stock options outstanding and exercisable as at May 31, 2022:

Options outstanding	Options exercisable	Exercise price \$	Expiry date
413,086	347,863	5.19	October 18, 2025
50,000	16,672	10.41	May 16, 2026
2,440,889	416,479	3.93	January 17, 2026
2,903,975	781,014		

The Company used the Black-Scholes option pricing model to establish the fair value of LTIP options granted by applying the following weighted average assumptions at issuance:

	2022	2021
Average dividend per share	-	-
Average forecasted volatility	90%	97%
Average risk-free interest rate	1.68%	0.95%
Average expected life	5 years	5 years
Forfeiture rate	8.57%	4.68%
Fair value – weighted average of options issued	\$2.75	\$2.52

LTIP RSU's and DSU's

The omnibus LTIP plan permits the Board of Directors of the Company to grant RSU's to certain officers, employees, and consultants and DSU's to non-management directors. The RSU's vest quarterly over a period of three years from grant date.

The following table summarizes LTIP RSU and DSU activity during the six months ended May 31, 2022:

	Number of RSUs and DSUs	Weighted Average Issue Price of RSUs/DSUs
Balance outstanding, November 30, 2021	199,771	\$5.63
Granted	983,494	\$2.01
Released and issued	(172,419)	\$3.27
Cancelled and forfeited	(53,672)	\$2.75
Balance outstanding, May 31, 2022	957,174	\$2.50

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16. SHARE CAPITAL AND RESERVES – continued

The following table summarizes the LTIP RSUs and DSUs outstanding as at May 31, 2022:

RSUs and DSUs outstanding	Grant date
72,720	October 19, 2020
16,851	February 26, 2021
9,375	May 27, 2021
16,125	August 27, 2021
33,035	November 26, 2021
603,088	January 18, 2022
57,470	March 1, 2022
148,510	May 27, 2022
957,174	

Legacy option plan

The following table summarizes legacy stock option activity during the six months ended May 31, 2022:

	Number of Options	Weighted Average Exercise Price
		\$
Balance outstanding, November 30, 2021	1,538,020	9.56
Cancelled and forfeited	(83,044)	11.42
Balance outstanding, May 31, 2022	1,454,976	9.46
Options exercisable, May 31, 2022	1,413,057	9.37

The following table summarizes the legacy stock options outstanding and exercisable as at May 31, 2022:

Options outstanding	Options exercisable	Exercise price	Expiry date
		\$	
100,000	100,000	3.21	July 9, 2023
553,051	553,051	5.85	October 13, 2023
250,000	250,000	12.63	May 26, 2024
528,592	490,562	12.96	July 14, 2024
23,333	19,444	8.37	October 14, 2024
1,454,976	1,413,057		

Share-based payments

For the three and six months ended May 31, 2022 and 2021, the Company recorded the following share-based payments:

	For the three months ended		For the six months ended	
	May 31, 2022	May 31, 2021	May 31, 2022	May 31, 2021
	\$	\$	\$	\$
LTIP and legacy stock options	1,585	739	2,708	1,799
LTIP RSUs and DSUs	578	330	1,103	798
Obligation to issue shares	87	176	192	379
	2,250	1,245	4,003	2,976

THE VALENS COMPANY INC.**Notes to the Condensed Interim Consolidated Financial Statements****For the Six Months Ended May 31, 2022 and 2021****(Unaudited, Expressed in Thousands of Canadian Dollars Except Share Amounts)**

17. BUSINESS ACQUISITIONS**Acquisition of LYF**

On March 5, 2021, the Company entered into an agreement to acquire all of the shares of LYF ("LYF Agreement"). The transaction constituted a business combination under IFRS 3, Business Combinations.

The consideration paid at closing was \$18,410, which is comprised of \$3,909 cash and 2,777,827 common shares valued at \$14,501. In addition, there were 328,205 common shares, valued at \$1,713 placed in escrow subject to release based on the indemnity provisions of the LYF Agreement. Further, there was a \$750 promissory note funded from the Company to LYF pre-acquisition, which gained \$12 of accrued interest and was assumed at \$762. In addition to the promissory note, there was also \$310 of deferred revenue and \$1,100 of accounts payable that was settled as a pre-existing relationship on acquisition.

The contingent consideration of \$2,198 represents four earn-out EBITDA milestone payments of which two milestones ended February 28, 2022 (with a total potential payout of \$7,500 and currently valued at \$nil) and two milestones end February 28, 2023 (with a potential payout of \$10,000 and currently valued at \$nil). The contingent consideration can be settled using cash or common shares at the Company's discretion. 427,350 of the Company's shares were placed into escrow subject to release upon the achievement of the first earn-out EBITDA milestone ending February 28, 2022. As of May 31, 2022, these shares were still held in escrow, as milestone requirements were not yet met. Initial valuation of the contingent consideration was calculated using a Monte Carlo simulation and is subsequently reviewed and remeasured on a quarterly basis (Note 21).

During the six months ended May 31, 2022, remeasurement of the contingent consideration under the Monte Carlo simulation resulted in a liability of \$nil (November 30, 2021 – \$2,250) with a gain on remeasurement of \$1,940 and \$2,250 during the three and six months ended May 31, 2022, respectively.

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17. BUSINESS ACQUISITIONS – continued

Consideration	Number of Shares	Amount \$
Cash paid on closing		3,909
Shares issued on closing	2,777,827	14,501
Contingent consideration	Note (i)	2,198
Indemnity shares	328,205	1,713
Working capital adjustment		1,110
Settlement of pre-existing relationships		2,172
Total fair value of consideration		25,603
Net assets acquired		
Current assets		
Cash		196
Accounts receivable		150
Prepaid expenses and other current assets		243
Inventory		1,612
Non-current assets		
Prepaid deposits		82
Intangible assets		12,982
Property, plant and equipment		7,070
Total assets		22,335
Current liabilities		
Accounts payable and accrued liabilities		1,215
Canadian Emergency Business Account (“CEBA”) Loan		40
Non-current liabilities		
Deferred taxes		2,090
Total liabilities		3,345
Total net assets acquired		18,990
Purchase price allocation		
Net identifiable assets acquired		18,990
Goodwill		6,613
		25,603
Net cash outflows		
Cash consideration paid		(3,909)
Cash acquired		196
		(3,713)

Goodwill arising from the business combination represents expected synergies, future income and growth that are not separately recognized. As at May 31, 2022, Goodwill related to LYF was \$nil following the recognition of impairment losses (Note 9).

The Company finalized the determination of the fair value of the net identifiable assets acquired and liabilities assumed related to the acquisition of LYF as at February 28, 2022. There were no changes as compared to the preliminary values reported as at November 30, 2021.

Acquisition of Green Roads

On June 17, 2021, the Company entered into an agreement to acquire all of the shares of Green Roads (“GR Agreement”). The transaction constituted a business combination under IFRS 3, Business Combinations.

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17. BUSINESS ACQUISITIONS – continued

The consideration paid at closing was \$40,815, which is comprised of \$14,400 cash and 2,659,959 common shares valued at \$26,415. In addition, there were 1,434,767 common shares, valued at \$14,248 placed in escrow subject to the resolution and settlement of certain tax matters, in which the sellers are required to indemnify the Company (indemnity asset and other liability of \$10,957 was recognized in the purchase price allocation on the acquisition date). Furthermore, there was \$1,902 in cash that was placed in escrow subject to adjustments related to net working capital.

The contingent consideration of \$940 represents an earn-out EBITDA milestone payment in which the milestone ends November 30, 2022 (with a total potential payout of \$24,556 and valued at \$940 on acquisition date). The contingent consideration can be settled using cash or common shares at the Company's discretion. Preliminary valuation of the contingent consideration was calculated using a Monte Carlo simulation and is subsequently reviewed and remeasured on a quarterly basis (Note 21).

During the six months ended May 31, 2022, amendments were made to the provisional fair value of assets acquired and liabilities assumed. The result was an increase in goodwill of \$109 and a corresponding decrease in inventory of \$109.

During the six months ended May 31, 2022, remeasurement of the contingent consideration under the Monte Carlo simulation resulted in a liability of \$nil (November 30, 2021 – \$367) with a gain on remeasurement of \$4 and \$367 for the three and six months ended May 31, 2022, respectively.

	Number of Shares	Amount \$
Consideration		
Cash paid on closing		14,400
Cash held in escrow		1,902
Shares issued on closing	2,659,959	26,415
Tax escrow shares	1,434,767	14,248
Contingent consideration		940
Working capital adjustment		(1,462)
Total fair value of consideration		56,443
Net assets acquired		
Current assets		
Cash		669
Accounts receivable		508
Promissory note receivable		100
Prepaid expenses and other current assets		385
Indemnity assets		10,957
Inventory		2,799
Non-current assets		
Property, plant and equipment		3,083
Intangible assets		33,145
Other assets		293
Total assets		51,939

THE VALENS COMPANY INC.

Notes to the Condensed Interim Consolidated Financial Statements

For the Six Months Ended May 31, 2022 and 2021

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17. BUSINESS ACQUISITIONS – continued

Current liabilities	
Accounts payable and accrued liabilities	2,380
Lease liability – current	682
Deferred revenue	875
Other liability	10,957
Non-current liabilities	
Lease liability – non-current	1,234
Deferred taxes	6,543
Miscellaneous liabilities	33
Total liabilities	22,704
Total net assets acquired	29,235
Purchase price allocation	
Net identifiable assets acquired	29,235
Goodwill	27,208
	56,443
Net cash outflows	
Cash consideration paid	(16,420)
Cash acquired	669
	(15,751)

Goodwill arising from the business combination represents expected synergies, future income and growth that are not separately recognized. As at May 31, 2022, Goodwill related to Green Roads was \$nil following the recognition of impairment losses (Note 9).

During the period ended May 31, 2022, the Company finalized the determination of the fair value of the net identifiable assets acquired and liabilities assumed related to the acquisition of Green Roads. Aside from the changes mentioned above, there were no changes as compared to the preliminary values reported as at November 30, 2021.

Acquisition of Citizen Stash

On November 8, 2021, the Company finalized the plan of arrangement (“CS Arrangement”) to acquire all of the shares of Citizen Stash. The transaction constituted a business combination under IFRS 3, Business Combinations.

The consideration paid at closing was \$35,760, which was comprised of 5,786,360 common shares.

During the six months ended May 31, 2022, amendments were made to the provisional fair value of assets acquired and liabilities assumed. The result was a decrease in property, plant and equipment of \$108, a decrease in accounts payable and accrued liabilities of \$339, and a corresponding decrease in goodwill of \$231.

During the period ended May 31, 2022, the Company finalized the determination of the fair value of the net identifiable assets acquired and liabilities assumed related to the acquisition of Citizen Stash. Aside from the changes mentioned above, there were no changes as compared to the preliminary values reported as at November 30, 2021.

THE VALENS COMPANY INC.

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17. BUSINESS ACQUISITIONS – continued

Consideration	Number of Shares	Amount \$
Shares issued on closing	5,786,360	35,760
Settlement of pre-existing relationships		1,052
Total fair value of consideration		36,812
Net assets acquired		
Current assets		
Cash		1,417
Marketable securities and derivatives		72
Accounts receivable		1,282
Prepaid expenses and other current assets		449
Inventory and biological assets (provisional)		2,110
Non-current assets		
Property, plant and equipment (provisional)		5,970
Intangible assets (provisional)		20,717
Other assets		53
Total assets		32,070
Current liabilities		
Accounts payable and accrued liabilities		4,045
Term loan – non-current		2,500
Non-current liabilities		
Deferred taxes		3,028
Lease liability – non-current (provisional)		53
Total liabilities		9,626
Total net assets acquired		22,444
Purchase price allocation		
Net identifiable assets acquired		22,444
Goodwill (provisional)		14,368
		36,812
Net cash inflows		
Cash consideration paid		-
Transaction costs paid		(62)
Cash acquired		1,417
		1,355

Goodwill arising from the business combination represents expected synergies, future income and growth that are not separately recognized. As at May 31, 2022, Goodwill related to Citizen Stash was \$nil following the recognition of impairment losses (Note 9).

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18. GOVERNMENT ASSISTANCE

The Company applied for COVID-19 financial relief in Canada under the Canada Emergency Wage Subsidy (“CEWS”) program. The CEWS program was a wage subsidy program launched by the Canadian federal government to qualifying employers to subsidize payroll costs during the COVID-19 pandemic. The qualified subsidy amounts received under the CEWS program are non-repayable.

The CEWS program had ended prior to November 30, 2021; as such, the Company did not apply for any amounts in the three and six months ended May 31, 2022 (May 31, 2021 – \$874 and \$2,741), with \$114 (May 31, 2021 – \$1,357) accrued for under trade and other receivables (Note 5). For the amounts applied for in the three and six months ended May 31, 2022 and 2021, the Company has applied the CEWS as a reduction against the following:

	For the three months ended		For the six months ended	
	May 31, 2022	May 31, 2021	May 31, 2022	May 31, 2021
	\$	\$	\$	\$
Inventory	-	114	-	261
Cost of sales	-	322	-	510
Wages and salaries	-	1,795	-	3,327
	-	2,231	-	4,098

19. INCOME TAXES

A reconciliation of income taxes at statutory rates with the reported taxes for the three and six months ended May 31, 2022 and 2021 is as follows:

	For the three months ended		For the six months ended	
	May 31, 2022	May 31, 2021	May 31, 2022	May 31, 2021
	\$	\$	\$	\$
Loss before income taxes	(169,148)	(10,539)	(196,596)	(17,661)
Statutory rate	27%	27%	27%	27%
Expected income tax (recovery) at statutory rates	(45,670)	(2,846)	(53,081)	(4,768)
Change in statutory rates and other	1,039	8	1,116	8
Permanent differences	14,313	384	14,541	856
Share issue costs	-	791	-	-
Change in unrecognized deductible temporary differences	21,977	(217)	27,383	1,055
Income taxes	(8,341)	(1,880)	(10,041)	(2,849)

20. CAPITAL MANAGEMENT

The Company manages its capital structure and makes adjustments to it, based on the funds available to the Company, in order to maintain operations. The Board of Directors does not establish quantitative return on capital criteria for management, but rather relies on the expertise of the Company’s management to sustain future development of the business. The Company defines capital that it manages as shareholders equity and debt.

The Company has historically relied on the equity markets and debt markets to fund its activities. Management reviews its capital management approach on an on-going basis and believes that this approach, given the relative size of the Company, is reasonable to ensure optimal capital structure to reduce the cost of capital.

The Company currently is not subject to externally imposed capital requirements.

THE VALENS COMPANY INC.

Notes to the Condensed Interim Consolidated Financial Statements

For the Six Months Ended May 31, 2022 and 2021

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21. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

The carrying values of the financial instruments as at May 31, 2022 are summarized in the following table:

	Amortized cost \$	Financial assets and liabilities designated as FVTPL \$	Total \$
Assets			
Cash	24,899	-	24,899
Restricted short-term investments	-	401	401
Marketable securities and derivatives	-	1,244	1,244
Receivables (excluding unbilled revenue)	28,396	-	28,396
Indemnity asset	11,293	-	11,293
Liabilities			
Accounts payable and accrued liabilities	37,102	-	37,102
Contingent consideration	-	-	-
Other liability	11,293	-	11,293
Contractual obligation	6,274	-	6,274
Lease liabilities	4,899	-	4,899
Term loan and other debt	38,173	-	38,173

Fair value of financial instruments is the price that would be received to sell an asset or paid to transfer a liability in an orderly fashion between market participants. The Company records certain financial instruments at fair value.

Fair value measurements are categorized into Level 1, 2 or 3 based on the degree to which the inputs to the fair value measurements are observable and the significance of the inputs to the fair value measurement in its entirety, which are described as follows:

- Level 1 inputs are quoted prices in active markets for identical assets or liabilities that the entity can access at the measurement date;
- Level 2 inputs, other than quoted prices included within Level 1, that are observable for the asset or liability, either directly or indirectly; and,
- Level 3 inputs are unobservable inputs for the asset or liability.

The carrying amounts of cash, receivables and accounts payable and accrued liabilities approximate their fair values due to their short-term nature. Unbilled revenue on products/services transferred over time is not a financial instrument and is excluded from the table above.

The fair values of restricted short-term investments and marketable securities were measured based on Level 1 inputs for publicly traded companies and at Level 3 for private companies. The fair values of derivatives were measured based on Level 2 inputs.

The fair value of LYF contingent consideration payable was measured at fair value based on unobservable inputs and is considered a level 3 financial instrument. A Monte Carlo simulation was run to determine the fair value of contingent consideration based on the level 3 inputs. Any changes to primary inputs would not have a significant impact on the fair value of the contingent consideration payable. As at May 31, 2022, the fair value of the contingent consideration payable was \$nil.

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21. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT – *continued*

The fair value of GR contingent consideration payable was measured at fair value based on unobservable inputs and is considered a level 3 financial instrument. A Monte Carlo simulation was run to determine the fair value of contingent consideration based on the level 3 inputs. Any changes to primary inputs would not have a significant impact on the fair value of the contingent consideration payable. As at May 31, 2022, the fair value of the contingent consideration payable was \$nil.

The Company is exposed to varying degrees to a variety of financial instrument related risks. The Board approves and monitors the risk management processes, inclusive of counterparty limits, controlling and reporting structures. The type of risk exposure and the way in which such exposure is managed is provided as follows:

Interest risk

The Company's exposure to interest risk relates to its investment of surplus cash, and restricted short-term investments. The Company may invest surplus cash in highly liquid investments with short terms to maturity and would accumulate interest at prevailing rates for such investments. At May 31, 2022, the Company had cash and restricted short-term investments of \$25,300 and a balance of \$nil on term loans and other debt subject to fluctuations in interest rates (November 30, 2021 – \$16,354 and \$9,739). At May 31, 2022, a 1% decrease in interest rates would result in a reduction in interest income by \$253 (November 30, 2021 – \$164) and a reduction of interest expense of \$nil (November 30, 2021 – \$97), compared to a 1% increase in interest rates which would have an equal and opposite effect.

Credit risk

Credit risk is the risk of an unexpected loss if a customer or third party to a financial instrument fails to meet its contractual obligations. Financial instruments that potentially subject the Company to significant concentrations of credit risk consist primarily of cash, marketable securities and derivatives, restricted short-term investments, and receivables. The Company's cash, and restricted short-term investments are held through large Canadian financial institutions and no losses have been incurred in relation to these items.

The Company's receivables are comprised of trade accounts receivable, GST input tax credits, unbilled revenues, and government assistance receivable. In addition, the Company has \$9,885 in trade accounts receivable outstanding over 60 days at May 31, 2022 (November 30, 2021 – \$6,820). The expected credit loss for overdue balances is estimated to be \$3,405 (November 30, 2021 – \$821) based on historical collection experience, discussions with associated customers and analysis of the credit worthiness of the customer. Of the total invoiced trade receivables at May 31, 2022, the Company has subsequently collected, has trade payables outstanding with the same customers, or has recorded a trade receivables valuation allowance loss provision representing 56% of the total balance. Of the Company's trade receivables outstanding at May 31, 2022, 38% are held with two Health Canada licensed customers of the Company and 25% are held with two provincial boards (November 30, 2021 – 43% held with four Health Canada licensed customers and 24% held with three provincial boards).

The carrying amount of cash, marketable securities and derivatives, restricted short-term investments, and trade and other receivables represent the maximum exposure to credit risk, and as at May 31, 2022, this amounted to \$55,370 (November 30, 2021 – \$48,124).

THE VALENS COMPANY INC.

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21. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT – continued**Economic dependence risk**

Economic dependence risk is the risk of reliance upon a select number of customers which significantly impact the financial performance of the Company. The Company recorded sales from one Health Canada licensed customer of the Company representing 27% and 24% of total revenue in the three and six months ended May 31, 2022, respectively (2021 – four Health Canada licensed customers representing 44% and 44% of total revenue). The Company recorded sales from three provincial boards representing 69% and 69% of total revenue in the three and six months ended May 31, 2022, respectively (2021 – three provincial boards representing 32% and 36% of total revenue).

Liquidity risk

Liquidity risk is the risk that the Company will not be able to pay financial liabilities as they come due. The Company manages its liquidity risk by reviewing on an ongoing basis its capital requirements, as well as by forecasting cash flows from operations for future periods. As at May 31, 2022, the Company has \$25,300 of cash, and restricted short-term investments (November 30, 2021 – \$16,354). The Company is obligated to pay accounts payable and accrued liabilities, current portions of the lease liability, contractual obligation, contingent consideration, and term loan and other debt with a carrying amount of \$40,167 (November 30, 2021 – \$50,633).

Foreign currency risk

The Company is exposed to foreign currency risk on fluctuations related to cash, trade and other receivables, accounts payable and accrued liabilities, other liability, and contractual obligations (including contingent consideration) that are denominated in US dollars and Australian dollars. As at May 31, 2022, a 10% appreciation of the Canadian dollar relative to the US dollar would have decreased loss for the period by approximately \$902 (November 30, 2021 – \$1,048). A 10% depreciation of the Canadian dollar relative to the US dollar would have had the equal but opposite effect. A 10% appreciation of the Canadian dollar relative to the Australian dollar would have decreased loss for the period by approximately \$75 (November 30, 2021 – \$15). A 10% depreciation of the Canadian dollar relative to the Australian dollar would have had the equal but opposite effect.

In addition, the Company is exposed to foreign currency risk on fluctuations related to a commitment that is denominated in Australian dollars. As at May 31, 2022, a 10% appreciation of the Canadian dollar relative to the Australian dollar would have decreased the commitment by approximately \$541 (November 30, 2021 – \$631). A 10% depreciation of the Canadian dollar relative to the Australian dollar would have had the equal but opposite effect.

22. SUPPLEMENTAL DISCLOSURE WITH RESPECT TO CASH FLOWS

Non-cash transactions relate to the following:

	May 31, 2022	May 31, 2021
	\$	\$
Equipment accrued through accounts payable	573	329
Share units released – non-cash portion	563	291
Settlement of obligation to issue shares	525	601
Exercise of warrants – non-cash portion	-	1
Exercise of options – non-cash portion	-	432
Reclassification of capital assets to assets held for sale	6,447	-
Warrants issued pursuant to bought deal financing	7,141	4,066

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23. COMMITMENTS AND CONTINGENCIES

Effective May 14, 2020, the Company entered into a five-year non-exclusive distribution agreement with Cannvalate Pty Ltd. ("Cannvalate"). The agreement is based on a pay for performance model, providing Cannvalate achieves milestones based on certain financial targets and facility construction and licensing timelines outlined in the agreement. The Company will pay \$9,247 in consulting fees over the term of the agreement, subject to Cannvalate meeting the milestones as defined in the agreement. As at May 31, 2022, there remains \$5,406 (November 30, 2021 – \$6,312) payable under the terms of this agreement.

Based on the above, the future commitments, which include other purchase commitments due in each of the next five reporting years are as follows:

	\$
2022	901
2023	1,802
2024	1,802
2025	901
Thereafter	-
	5,406

24. SEGMENTED INFORMATION

The Company has two reportable segments: Canada and United States and International, which is the way the Company reports information to its chief decision makers and Board of Directors.

The Canada operating segment includes all business-to-business and business-to-consumer activity within Canada. This includes toll processing and co-packing, product sales, and analytical testing. Segment assets include those arising from the Company's main operations in Kelowna, BC, the Pommies beverage facility in Bolton, Ontario, the LYF manufacturing facility in Kelowna, BC, and the Citizen Stash cultivation facility in Mission, BC.

The United States and International operating segment includes all activity related to the Green Roads CBD health and wellness manufacturing facility in Florida, United States. Segment assets include those arising from Green Roads' operations. Also included are operations in Australia related to the distribution agreement with Cannvalate (Note 23).

The operating segments for the three months ended May 31, 2022 and 2021:

	May 31, 2022		
	Canada	United States and	Total
	\$	International	\$
Net revenue	17,252	6,747	23,999
Cost of sales, inventory allowance, and fair value changes	31,248	3,500	34,748
	(13,996)	3,247	(10,749)
Operating expenses	26,075	7,440	33,515
	(40,071)	(4,193)	(44,264)
Impairment loss	66,719	57,069	123,788
Other non-operating (income) expense	(6,141)	(1,104)	(7,245)
Net loss	(100,649)	(60,158)	(160,807)
Total assets	186,794	16,270	203,064
Total liabilities	86,642	11,099	97,741

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24. SEGMENTED INFORMATION – continued

	May 31, 2021		
	Canada	United States and International	Total
	\$	\$	\$
Net revenue	18,716	48	18,764
Cost of sales, inventory allowance, and fair value changes	14,628	-	14,628
	4,088	48	4,136
Operating expenses	14,974	-	14,974
	(10,886)	48	(10,838)
Non-operating income	(2,179)	-	(2,179)
Net income (loss)	(8,707)	48	(8,659)
Total assets	209,984	-	209,984
Total liabilities	41,308	-	41,308

The geographical breakdown for the three months ended May 31, 2022 and 2021:

	May 31, 2022			May 31, 2021		
	Domestic	Foreign	Total	Domestic	Foreign	Total
	\$	\$	\$	\$	\$	\$
Net revenue	17,252	6,747	23,999	18,716	48	18,764

Included in net revenue arising from the Canada operating segment is \$5,452 from Customer A, \$5,100 from Customer B, \$4,908 from Customer C, and \$2,719 from Customer D. Customers A through D each contributed 10 per cent or more to the Company's net revenue for the three months ended May 31, 2022 (2021 – Customer A \$2,869, Customer B \$2,423, Customer C \$2,290, Customer D \$2,100, and Customer E \$2,068).

The operating segments for the six months ended May 31, 2022 and 2021:

	May 31, 2022		
	Canada	United States and International	Total
	\$	\$	\$
Net revenue	35,001	12,178	47,179
Cost of sales, inventory allowance, and fair value changes	49,793	6,174	55,967
	(14,792)	6,004	(8,788)
Operating expenses	46,859	14,673	61,532
	(61,651)	(8,669)	(70,320)
Impairment loss	66,719	57,069	123,788
Other non-operating (income) expense	(6,466)	(1,087)	(7,553)
Net loss	(121,904)	(64,651)	(186,555)
Total assets	186,794	16,270	203,064
Total liabilities	86,642	11,099	97,741

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24. SEGMENTED INFORMATION – continued

	May 31, 2021		
	Canada	United States and International	Total
	\$	\$	\$
Net revenue	38,672	106	38,778
Cost of sales, inventory allowance, and fair value changes	29,872	-	29,872
	8,800	106	8,906
Operating expenses	26,891	-	26,891
	(18,091)	106	(17,985)
Non-operating income	(3,173)	-	(3,173)
Net income (loss)	(14,918)	106	(14,812)
Total assets	209,984	-	209,984
Total liabilities	41,308	-	41,308

The geographical breakdown for the six months ended May 31, 2022 and 2021:

	May 31, 2022			May 31, 2021		
	Domestic	Foreign	Total	Domestic	Foreign	Total
	\$	\$	\$	\$	\$	\$
Net revenue	35,001	12,178	47,179	38,672	106	38,778

Included in net revenue arising from the Canada operating segment is \$12,704 from Customer A, \$9,923 from Customer B, \$9,457 from Customer C, and \$4,295 from Customer D. Customers A through D each contributed 10 per cent or more to the Company's net revenue for the six months ended May 31, 2022 (2021 – Customer A \$5,728, Customer B \$4,752, Customer C \$4,581, Customer D \$4,552, and Customer E \$3,927).

25. RESTRUCTURING CHARGES

In the fourth quarter of fiscal 2021, the Company implemented a cost saving strategic restructuring plan, whereby headcount reductions were initiated to focus on short-term and long-term profitability.

The restructuring resulted in expenses recognized on the condensed interim consolidated statements of loss and comprehensive loss, which continued through the first two quarters of fiscal 2022. The following table summarizes the Company's restructuring accrual for the six months ended May 31, 2022:

	Employee Termination Benefits
	\$
Restructuring charge accrual, November 30, 2021	1,358
Year-to-date expense	4,123
Payments	(1,988)
Restructuring charge accrual, May 31, 2022	3,493



**AT VALENS,
IT'S PERSONAL.**

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