# MOLECULE HOLDINGS INC.

## Consolidated Financial Statements

## October 31, 2021 and 2020

***(Expressed in Canadian Dollars)***

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Audit. Tax. Advisory.

**Independent Auditor's Report**

To the Shareholders of Molecule Holdings Inc.

**Opinion**

We have audited the consolidated financial statements of Molecule Holdings Inc. and its subsidiaries (the "Company"), which comprise the consolidated statements of financial position as at October 31, 2021 and 2020, and the consolidated statements of loss and comprehensive loss, consolidated statements of changes in equity and consolidated statements of cash flows for the years then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Company as at October 31, 2021 and 2020 and its consolidated financial performance and its consolidated cash flows for the years then ended in accordance with International Financial Reporting Standards ("IFRS").

**Basis for opinion**

We conducted our audit in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the consolidated financial statements section of our report. We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the consolidated financial statements in Canada. We have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

**Material uncertainty related to going concern**

We draw attention to Note 1 in the consolidated financial statements, which indicates that the Company incurred a net loss during the year ended October 31, 2021 and, as of that date, the Company has a working capital deficiency. As stated in Note 1, these events or conditions, along with other matters as set forth in Note 1, indicate that material uncertainties exist that cast significant doubt on the Company's ability to continue as a going concern. Our opinion is not modified in respect of this matter.

**Other information**

Management is responsible for the other information. The other information comprises Management's Discussion and Analysis.

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially

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inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

We obtained Management's Discussion and Analysis prior to the date of this auditor's report. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

**Responsibilities of management and those charged with governance for the consolidated financial statements**

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

In preparing the consolidated financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Company or cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company's financial reporting process.

**Auditor's responsibilities for the audit of the consolidated financial statements**

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with Canadian generally accepted auditing standards, we exercise professional judgement and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risks of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

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- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

The engagement partner of the audit resulting in this independent auditor's report is Chris Milios.

**McGovern Hurley LLP**

McGovern Hurley LLP

**Chartered Professional Accountants**
**Licensed Public Accountants**

Toronto, Ontario
February 28, 2022

**Molecule Holdings Inc.**
Consolidated Statements of Financial Position
*(Expressed in Canadian dollars)*

| As at | **October 31, 2021** | October 31, 2020 |
|---|---|---|
| | **$** | $ |
| **ASSETS** | | |
| Current assets | | |
| Cash and cash equivalents (Note 3) | **1,203,327** | 902,519 |
| Trade and other receivables (Note 4) | **391,190** | 103,081 |
| Inventory (Note 5) | **640,360** | 145,352 |
| Marketable securities (Note 6) | **-** | 239,904 |
| Prepaid expenses and deposits | **472,529** | 135,722 |
| | **2,707,406** | 1,526,578 |
| Capital assets (Note 8) | **3,248,329** | 3,920,403 |
| Total assets | **5,955,735** | 5,446,981 |
| **LIABILITIES** | | |
| Current liabilities | | |
| Accounts payable and accrued liabilities | **816,964** | 1,094,133 |
| Current portion of lease liability (Note 10) | **50,071** | 43,209 |
| Convertible debt and warrant liabilities at fair value through profit or loss (Note 11) | **3,487,856** | - |
| | **4,354,891** | 1,137,342 |
| Lease liability (Note 10) | **85,369** | 135,440 |
| Convertible debt (Note 11) | **817,087** | 697,625 |
| Other long-term liabilities | **60,000** | 40,000 |
| Total liabilities | **5,317,347** | 2,010,407 |
| **EQUITY** | | |
| Share capital (Note 12) | **8,560,793** | 7,333,619 |
| Warrants (Note 13) | **147,328** | 55,184 |
| Contributed surplus (Notes 14 and 15) | **575,861** | 466,012 |
| Deficit | **(8,645,594)** | (4,418,241) |
| Total equity | **638,388** | 3,436,574 |
| Total liabilities and equity | **5,955,735** | 5,446,981 |

On behalf of the Board

(signed) "Andre Audet"
Andre Audet, Director

(signed) "David Reingold"
David Reingold, Director

*The accompanying notes are an integral part of these consolidated financial statements.*

**Molecule Holdings Inc.**
Consolidated Statements of Loss and Comprehensive Loss
*(Expressed in Canadian dollars)*

| For the year ended October 31, | **2021** | 2020 |
|---|---|---|
| | **$** | $ |
| Net revenue from sale of goods (Note 16) | **455,257** | - |
| Cost of goods sold (Notes 5 and 17) | **881,143** | - |
| Gross profit (loss) before inventory write-down | **(425,886)** | - |
| Write-down of inventory to net realizable value (Note 5) | **(73,857)** | - |
| **Gross profit (loss)** | **(499,743)** | - |
| Operating expenses | | |
| Management and consulting fees (Note 17) | **437,061** | 637,931 |
| Salaries and benefits (Note 17) | **402,904** | 319,527 |
| Office and facilities (Note 17) | **425,493** | 187,229 |
| Professional fees | **171,199** | 285,602 |
| Supplies and testing | **238,031** | 41,765 |
| Travel and promotion | **27,896** | 14,188 |
| Interest on lease liability (Note 10) | **9,372** | 23,270 |
| Depreciation of capital assets (Notes 8 and 17) | **202,517** | 47,976 |
| Stock-based compensation (Notes 12, 14, 15 and 17) | **989,526** | 392,504 |
| Government assistance | **(515)** | (96,932) |
| | **2,903,484** | 1,853,060 |
| **Loss before other items** | **(3,403,227)** | (1,853,060) |
| Other income (loss) | | |
| Interest income | **365** | 7,734 |
| Interest and financing fees on convertible debt (Note 11) | **(651,229)** | (21,324) |
| Change in fair value of financial assets at fair value through profit or loss (Note 6) | **(73,153)** | (65,338) |
| Change in fair value of financial liabilities at fair value through profit or loss | **3,409** | - |
| Listing expense (Note 7) | **-** | (1,395,006) |
| Loss on disposal of capital assets (Note 8) | **(104,877)** | - |
| Foreign exchange gain | **1,359** | - |
| **Net loss and total comprehensive loss** | **(4,227,353)** | (3,326,994) |
| Basic and diluted net loss per common share | **(0.046)** | (0.044) |
| Basic and diluted weighted average number of common shares outstanding | **91,855,662** | 75,710,587 |

*The accompanying notes are an integral part of these consolidated financial statements.*

**Molecule Holdings Inc.**
Consolidated Statements of Changes in Equity
*(in Canadian dollars)*

| | Share Capital | | Warrants | Contributed Surplus | Deficit | Total |
|---|---|---|---|---|---|---|
| | # of shares | $ | $ | $ | $ | $ |
| **Balance, October 31, 2019** | **72,800,100** | **5,251,972** | **-** | **157,475** | **(1,091,247)** | **4,318,200** |
| Shares, warrants and options issued pursuant to RTO (Note 7) | 9,313,447 | 1,490,152 | 1,672 | 40,532 | - | 1,532,356 |
| Shares issued for debt (Note 12) | 1,608,026 | 303,228 | - | - | - | 303,228 |
| Shares issued for services (Note 12) | 900,000 | 90,000 | - | - | - | 90,000 |
| Shares issued on vesting of restricted share units (Note 15) | 614,167 | 98,267 | - | (98,267) | - | - |
| Equity component of convertible debentures (Note 11) | - | - | - | 73,768 | - | 73,768 |
| Broker warrants issued as part of convertible debenture financing (Note 11) | - | - | 53,512 | - | - | 53,512 |
| Stock-based compensation | 1,000,000 | 100,000 | - | 292,504 | - | 392,504 |
| Net loss and total comprehensive loss | - | - | - | - | (3,326,994) | (3,326,994) |
| **Balance, October 31, 2020** | **86,235,740** | **7,333,619** | **55,184** | **466,012** | **(4,418,241)** | **3,436,574** |
| Shares issued for debt (Note 12) | 1,925,300 | 288,795 | - | - | - | 288,795 |
| Shares issued for services (Note 12) | 978,023 | 120,850 | - | - | - | 120,850 |
| Shares issued on vesting of restricted share units (Note 15) | 6,240,263 | 817,529 | - | (817,529) | - | - |
| Broker warrants issued as part of convertible debenture financing (Note 11) | - | - | 85,158 | - | - | 85,158 |
| Stock-based compensation | - | - | 6,986 | 927,378 | - | 934,364 |
| Net loss and total comprehensive loss | - | - | - | - | (4,227,353) | (4,227,353) |
| **Balance, October 31, 2021** | **95,379,326** | **8,560,793** | **147,328** | **575,861** | **(8,645,594)** | **638,388** |

*The accompanying notes are an integral part of these consolidated financial statements.*

**Molecule Holdings Inc.**
Consolidated Statements of Cash Flows
*(Expressed in Canadian dollars)*

| For the year ended October 31, | 2021 | 2020 |
|---|---|---|
| | $ | $ |
| **OPERATING ACTIVITIES** | | |
| Net loss | **(4,227,353)** | (3,326,994) |
| Adjustments for: | | |
| Stock-based compensation (Notes 12, 14, 15 and 17) | **1,055,214** | 392,504 |
| Depreciation of capital assets (Notes 8 and 17) | **567,061** | 47,976 |
| Interest on lease liability (Note 10) | **18,541** | 23,270 |
| Interest on convertible debt (Note 11) | **290,677** | 21,324 |
| Convertible debt financing fees (Note 11) | **360,582** | - |
| Interest income | **(365)** | (7,734) |
| Write-down of inventory to net realizable value (Note 5) | **73,857** | 65,338 |
| Loss on disposal of capital assets (Note 8) | **104,877** | - |
| Change in fair value of financial assets at fair value through profit or loss (Note 6) | **73,153** | - |
| Change in fair value of financial liabilities at fair value through profit or loss (Note 11) | **(3,409)** | - |
| Listing expense (Note 7) | **-** | 1,395,006 |
| Changes in non-cash working capital items | **(1,181,888)** | 462,845 |
| **Net cash flows from operating activities** | **(2,869,053)** | (926,465) |
| **INVESTING ACTIVITIES** | | |
| Interest received | **98** | 7,734 |
| Proceeds from sale of marketable securities (Note 6) | **166,751** | 47,063 |
| Deposit | **-** | 307,079 |
| Investment in capital assets (Note 8) | **(76,864)** | (1,898,280) |
| Proceeds from disposal of capital assets (Note 8) | **77,000** | - |
| Cash acquired in RTO (Note 7) | **-** | 271,340 |
| **Net cash flows from investing activities** | **166,985** | (1,265,064) |
| **FINANCING ACTIVITIES** | | |
| Proceeds from issuance of convertible debt (Note 11) | **3,434,000** | 1,025,000 |
| Convertible debt issuance costs (Note 11) | **(275,428)** | (199,143) |
| Interest paid on convertible debentures (Note 11) | **(113,951)** | - |
| Lease payments (Note 10) | **(61,750)** | (60,000) |
| Proceeds from other long-term obligations | **20,000** | 40,000 |
| **Net cash flows from financing activities** | **3,002,871** | 805,857 |
| Increase (decrease) in cash and cash equivalents | **300,803** | (1,385,672) |
| Cash and cash equivalents, beginning of the year | **902,519** | 2,288,191 |
| **Cash and cash equivalents, end of the year** | **1,203,322** | 902,519 |
| Changes in non-cash working capital items consists of the following: | | |
| Trade and other receivables | **(288,109)** | 236,660 |
| Inventory | **(568,865)** | (145,352) |
| Prepaid expenses and deposits | **(336,540)** | 70,553 |
| Accounts payable and accrued liabilities | **11,626** | 300,984 |
| | **(1,181,888)** | 462,845 |
| Supplemental information: | | |
| Shares issued for debt and services | **409,645** | 393,228 |
| Shares issued for RTO (Note 7) | **-** | 1,490,152 |

*The accompanying notes are an integral part of these consolidated financial statements.*

## 1. NATURE OF OPERATIONS AND GOING CONCERN

Molecule Holdings Inc. (formerly Everton Resources Inc.) ("Molecule Holdings" or the "Company") was incorporated under the Business Corporations Act (Alberta) on November 7, 1996 and currently exists under the *Business Corporations Act* (Canada).

On September 16, 2020, the Company completed a reverse takeover transaction pursuant to a statutory plan of arrangement (the "Transaction") whereby the Company acquired all of the issued and outstanding common shares (the "OpCo Shares") of Molecule Inc. ("OpCo"), which became a wholly-owned subsidiary of the Company. Concurrent with the closing of the Transaction, the Company effected a consolidation of its common shares on the basis of one (1) new class "A" common share (each post-consolidation common share, a "Common Share") for every ten (10) pre-consolidation common shares, changed its name to "Molecule Holdings Inc." and assumed the business operations of OpCo, being the production and co-packing of cannabis-infused beverages ("CIBs").

The Transaction was completed pursuant to the terms of an arrangement agreement dated November 27, 2019, as amended (the "Arrangement Agreement"). As a result of the Transaction, the former shareholders of OpCo acquired control of the Company. OpCo is deemed as the acquirer for accounting purposes, and therefore its assets, liabilities and operations are included in the consolidated financial statements at their fair value on September 16, 2020, as described in Note 7.

On February 28, 2020, OpCo was issued a Standard Processing Licence by Health Canada (the "Licence") under the Cannabis Act and Cannabis Regulations. The Licence authorizes OpCo to: (i) possess cannabis; (ii) produce cannabis, other than obtaining it by cultivating, propagating or harvesting it; and (iii) sell cannabis in accordance with subsection 17(5) of the Cannabis Regulations and the conditions of the Licence.

The address of the Company's corporate office is 591 Reynolds Road, Lansdowne, Ontario K0E 1L0. The Common Shares are listed for trading on the Canadian Securities Exchange (the "CSE") under the symbol "MLCL".

### Going Concern

These consolidated financial statements have been prepared on a basis that assumes that the Company will be able to realize its assets and discharge its liabilities in the normal course of operations for the foreseeable future. These consolidated financial statements do not reflect any adjustments that may be necessary should the Company be unable to continue as a going concern.

During the year ended October 31, 2021, the Company commenced generating revenue, has no positive income or cash inflow from operations, has incurred losses since its inception and as at October 31, 2021, has a working capital deficiency. Continued operation of the Company is dependent on achieving profitable commercial operations in the future, which requires continued financial support through equity and/or debt financings until profitable commercial operations are achieved. Management is evaluating alternatives to secure additional financing so that the Company can continue to operate as a going concern. Nevertheless, there is no assurance that these initiatives will be successful or sufficient. These conditions indicate the existence of material uncertainties that cast significant doubt about the Company's ability to continue as a going concern. If the going concern basis is not appropriate, material adjustments may be necessary to the carrying amounts and/or classification of assets and liabilities.

### COVID-19

On January 30, 2020, the World Health Organization ("WHO") declared the ongoing novel coronavirus "COVID-19" outbreak a global health emergency and on March 11, 2020, the WHO expanded its classification of the outbreak to a worldwide pandemic. Federal, state, provincial and municipal governments across North America enacted measures to combat the spread of COVID-19. These measures, which have included travel restrictions, border closures, non-essential business closures, quarantines, self-isolations, and social distancing, have, among other things, resulted in widespread business, employment and economic disruptions. The global pandemic continues to evolve and the ultimate impact of the COVID-19 outbreak is highly uncertain.

The continued global spread of COVID-19 could have an adverse impact on the business, operations and financial results of the Company, including with respect to issues related to labour, processing and supply chain. Since commencing production of CIBSs in the second quarter of fiscal 2021, the Company has implemented precautionary measures, which would not have otherwise been implemented prior to the COVID-19 outbreak, at its production facility (the "Facility") located in Lansdowne, Ontario to ensure the safety of its personnel, suppliers and consumers, which may adversely impact the Company's labour productivity and its supply chains. For example, mandatory or voluntary self-quarantine policies may limit staffing at the Facility. In addition, the COVID-19 pandemic may adversely affect the Company's ability to successfully market and sell its products, as sales volumes of CIBs may be adversely impacted by consumer "social distancing" behaviours. Continued spread of COVID-19 globally could also lead to a deterioration of general economic conditions including a possible national or global recession. Due to the unpredictability and scale of the effects of COVID-19, as at the date hereof the Company is unable to accurately estimate the impact or level of materiality of COVID-19 on its business, operations or financial results. The Company will continue to monitor the situation in order to assess any possible adverse impact on its business, supply chain and customers on an ongoing basis and to determine which measures, if any, will be taken to mitigate such adverse impact.

## 2. SIGNIFICANT ACCOUNTING POLICIES

### (a) Basis of presentation and compliance with IFRS

These consolidated financial statements have been prepared on a historical cost basis and are expressed in Canadian dollars, which is also the functional currency of the Company and its subsidiaries. These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB").

On September 16, 2020, the Company acquired 100% of the issued and outstanding securities of Molecule Inc. ("OpCo") (Note 1), which resulted in the shareholders of OpCo holding the majority of the outstanding shares of the Company. While Molecule Holdings is the legal acquirer, OpCo is the accounting acquirer since shareholders of OpCo held and controlled the majority of the outstanding shares upon completion of the Transaction (the "Reverse Take-Over" or "RTO"). As a result of the RTO, these consolidated financial statements are presented with OpCo as the continuing entity.

These consolidated financial statements were authorized for issue by the Board of Directors on February 28, 2022.

### (b) Basis of consolidation

These consolidated financial statements consolidate those of the parent company and its subsidiaries as at and for the year ended October 31, 2021. The parent controls a subsidiary if it is exposed, or has rights, to variable returns from its involvement with the subsidiary and has the ability to affect those returns through its power over the subsidiary. All subsidiaries have a reporting date of October 31.

All intercompany transactions and balances between the companies are eliminated on consolidation, including unrealized gains and losses on transactions. Amounts reported in the financial statements of subsidiaries have been adjusted where necessary to ensure consistency with the accounting policies adopted by the Company.

Profit or loss and other comprehensive income of subsidiaries acquired or disposed of during the year are recognized from the effective date of acquisition, or up to the effective date of disposal, as applicable.

*(Expressed in Canadian dollars)*

Composition of the Company:

The subsidiaries of the Company and their principal activities as at October 31, 2021 and 2020 were as follows:

| Name of subsidiary | Place of incorporation | Ownership interest as at October 31, 2021 and 2020 | Principal activity |
|---|---|---|---|
| Molecule Inc. | Canada | 100% | Cannabis-Infused Beverages |
| Burrard Bay Capital Corp. | Canada | 100% | Holding Company (Inactive) |
| Everton Minera Dominicana S.A. | Dominican Republic | 100% | Exploration Company (Inactive) |
| Pan Caribbean Metals Inc. | British Virgin Islands | 100% | Holding Company (Inactive) |
| Dominican Metals Inc. | British Virgin Islands | 100% | Holding Company (Inactive) |
| Everton Dominicana (2014) Inc. | Canada | 100% | Exploration Company (Inactive) |
| Linear Gold Caribe S.A. | Dominican Republic | 100% | Exploration Company (Inactive) |
| Hays Lake Gold Inc. | Canada | 100% | Exploration Company (Inactive) |

### (c) Financial instruments

Financial assets and financial liabilities are recognized when the Company becomes a party to the contractual provisions of the financial instrument.

Financial assets are derecognized when the contractual rights to the cash flows from the financial asset expire, or when the financial asset and all substantial risks and rewards are transferred.

A financial liability is derecognized when it is extinguished, discharged, cancelled or when it expires.

Financial assets and financial liabilities are measured initially at fair value plus transactions costs.

Financial assets and financial liabilities are measured subsequently as described below.

*Financial assets at amortized costs*

Financial assets at amortized cost are non-derivative financial assets which are held within a business model whose objective is to hold assets to collect contractual cash flows and its contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding. A financial asset is initially measured at fair value, including transaction costs and subsequently at amortized cost. The Company's cash and other receivables fall into this category of financial instruments.

*Financial assets at fair value through profit or loss ("FVTPL")*

Financial assets are classified as FVTPL when the financial asset is held for trading or it is designated as FVTPL. Financial assets classified as FVTPL are stated at fair value with any resulting gain or loss recognized in profit or loss. Transaction costs are expensed as incurred. The Company's marketable securities and cash equivalents fall into this category of financial instruments.

*Impairment of financial assets*

All financial assets not classified as FVTPL, including an interest in an equity-accounted investee, are subject to review for impairment at least at each reporting date. Financial assets are impaired when there is any objective evidence that a financial asset or a group of financial assets is impaired.

Objective evidence of impairment could include:

- significant financial difficulty of the issuer or counterparty;
- default or delinquency in interest or principal payments;
- it becoming probable that the borrower will enter bankruptcy or financial reorganization;
- the disappearance of an active market for a security; or
- observable data indicating that there is a measurable decrease in the expected cash flows from a group of financial assets.

For an investment in an equity security, objective evidence of impairment includes a significant or prolonged decline in its fair value below its cost. The Company generally considers a decline of 20% to be significant and a period of nine months to be prolonged.

Individually significant receivables are considered for impairment when they are past due or when other objective evidence is received that a specific counterparty will default. Impairment of receivables is presented in profit or loss, if applicable.

Financial liabilities

Financial liabilities are classified as either financial liabilities at FVTPL or at amortized cost. Financial liabilities at FVTPL are stated at fair value, with changes being recognized through profit or loss. Other financial liabilities are initially measured at fair value, net of transaction costs, and are subsequently measured at amortized cost using the effective interest method, with interest expense recognized on an effective yield basis. The Company's financial liabilities include accounts payable and accrued liabilities, convertible debt and warrant liabilities and other long-term liabilities.

Fair value hierarchy

Financial instruments measured at fair value on the statements of financial position are classified using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy has the following levels: Level 1 – valuation based on quoted prices unadjusted in active markets for identical assets or liabilities; Level 2 – valuation techniques based on inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e., as prices) or indirectly (i.e., derived from prices); Level 3 – valuation techniques using inputs for the asset or liability that are not based on observable market data (unobservable inputs). As at October 31, 2021, the Company's cash equivalents and convertible debt and warrant liabilities which are measured at fair value were classified as Level 2 within the fair value hierarchy. As at October 31, 2020, the Company's marketable securities were classified as Level 1 within the fair value hierarchy.

**(d) Trade receivables**

Trade receivables are recognized initially at the amount of consideration that is unconditional, unless they contain significant financing components when they are recognized at fair value. Trade receivables are subsequently measured at amortized cost using the effective interest method, less an allowance for any rights of return on sales, price concessions and discounts.

**(e) Inventory**

Inventory is stated at the lower of cost and net realizable value. Cost is determined using the weighted average method. Cost includes all expenses directly attributable to the production, packaging and quality assurance processes as well as suitable portions of related production overheads, based on normal operating capacity, including materials, overhead, depreciation, amortization, consulting and labour-related costs (including stock-based compensation). The identified capitalized direct and indirect costs related to inventory are subsequently recorded within cost of goods sold on the consolidated statements of loss and comprehensive loss at the time the product is sold, along with impairment losses on the write-down of inventory to net realizable value during the period, which are recorded as a separate line within gross profit (loss). Net realizable value is the estimated selling price in the ordinary course of business less any applicable selling expenses.

### (f) Capital assets

Capital assets are stated at cost, net of accumulated depreciation and accumulated impairment losses, if any.

Depreciation is calculated using the following methods and terms:

| Asset type | Depreciation method | Depreciation term |
|---|---|---|
| Right-of-use asset | Straight line | 5 years |
| Leasehold improvements | Straight line | 5 years |
| Equipment | Straight line | 5-10 years |

A capital asset is derecognized upon disposal or when no future economic benefits are expected from its use. Any gain or loss arising on derecognition of the asset, calculated as the difference between the net disposal proceeds and the carrying value of the asset, is included in profit or loss in the period the asset is derecognized.

The assets' residual values, useful lives and methods of depreciation are reviewed on an annual basis, and adjusted prospectively, if appropriate.

There have been no impairment losses with respect to capital assets recognized in any of the periods presented in these consolidated financial statements.

### (g) Leases and right-of-use assets

At inception of a contract, the Company assesses whether a contract is, or contains, a lease. Contracts that convey the right to control the use of an identified asset for a period of time in exchange for consideration are accounted for as leases giving rise to right-of-use assets.

At the commencement date, a right-of-use asset is measured at cost, where cost comprises: (a) the amount of the initial measurement of the lease liability; (b) any lease payments made at or before the commencement date, less any lease incentives received; (c) any initial direct costs incurred by the Company; and (d) an estimate of costs to be incurred by the Company in dismantling and removing the underlying asset, restoring the site on which it is located or restoring the underlying asset to the condition required by the terms and conditions of the lease.

A lease liability is initially measured at the present value of the unpaid lease payments discounted using the interest rate implicit in in the lease or if that rate cannot be reliably determined, the Company's incremental borrowing rate. Subsequently, the Company measures a lease liability at amortized cost using the effective interest method. It is then remeasured to reflect revised in-substance fixed lease payments. Except where the costs are included in the carrying amount of another asset, the Company recognizes in profit or loss (a) the interest on a lease liability and (b) variable lease payments not included in the measurement of a lease liability in the period in which the event or condition that triggers those payments occurs. The Company subsequently measures a right-of-use asset at cost less any accumulated depreciation and any accumulated impairment losses; and adjusted for any re-measurement of the lease liability. Right-of-use assets are depreciated over the shorter of the asset's useful life and the lease term.

### (h) Impairment of non-financial assets

The Company assesses non-financial assets for impairment when facts and circumstances suggest that the carrying amount of the assets are impaired. An impairment review is undertaken when indicators of impairment arise.

Where such an indication exists, the recoverable amount of the asset is estimated. For the purpose of assessing impairment, assets are grouped at the lowest level for which there are largely independent cash inflows (cash-generating units or “CGU”). The recoverable amount is the higher of an asset’s fair value less costs to sell and value in use, being the present value of the expected future cash flows of the relevant asset or CGU. An impairment loss is recognized in profit or loss for the amount by which the asset’s carrying amount exceeds its recoverable amount.

Where an impairment subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, subject to the amount not exceeding the carrying amount that would have been determined had impairment not been recognized for the asset in prior periods. Any reversal of impairment is recognized immediately in profit or loss.

### (i) Accounts payable and accrued liabilities

Accounts payable and accrued liabilities represent liabilities for goods and services provided to the Company prior to the end of the financial year which are unpaid. The amounts are unsecured and are usually paid within 30-60 days of recognition. Trade and other payables are presented as current liabilities unless payment is not due within 12 months after the reporting period. Accounts payable and accrued liabilities are recognized initially at their fair value and subsequently measured at amortized cost using the effective interest method.

### (j) Provisions and contingent liabilities

A provision is recognized when the Company has a present legal or constructive obligation as a result of a past event, it is probable that an outflow of economic resources will be required to settle the obligation, and the amount of the obligation can be reliably estimated. Timing or amount of the outflow may still be uncertain. If the effect is material, provisions are measured by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

All provisions are reviewed at each reporting date and adjusted to reflect the current best estimate. The Company had no material provisions as at October 31, 2021 and 2020.

### (k) Compound financial instruments

Compound financial instruments issued by the Company include loans that can be converted into ordinary shares at the decision of the holder, when the number of shares to be issued is fixed and does not vary with changes in fair value.

The liability component of compound financial instruments is initially recognized based on the fair value of a similar liability that does not have an equity conversion option. The equity component is initially recognized at the difference between the fair value of the compound financial instrument as a whole and the fair value of the liability component and is included within contributed surplus.

Subsequent to initial recognition, the liability component of a compound financial instrument is measured at amortized cost using the effective interest method. The equity component of a compound financial instrument is not remeasured.

Transaction costs related to the issue of compound financial instruments are capitalized and applied proportionately against the value of the equity and liability components such that the value assigned to equity and debt is stated net of the transaction costs.

Interest expense accruing to the financial liability is recognized in profit or loss. On conversion, the financial liability is reclassified to equity and no gain or loss is recognized.

**(l) Revenue recognition**

Revenue from the direct sale of CIBs to customers for a fixed price is recognized when the Company transfers the control of the goods to the customer upon delivery and acceptance by the customer. The Company recognizes revenue in an amount that reflects the consideration which the Company expects to receive taking into account the impact which may arise from any rights of return on sales, price concessions or similar obligations. Net revenue is presented net of taxes, estimated returns, allowances and discounts.

Canada Revenue Agency (“CRA”) levies excise taxes on the sale of medical and adult-use cannabis products. The Company becomes liable for these excise duties when cannabis products are delivered to provincial retailers of cannabis products (the “Provincial Retailers”) through other Licensed Producers (“LPs”). Net revenue, as presented on the consolidated statements of loss and comprehensive loss, represents revenue from the sale of goods less applicable excise taxes.

**(m) Cost of goods sold**

Cost of goods sold includes the cost of inventory expensed, packaging costs, shipping costs and related labour.

**(n) Share-based compensation**

The Company operates an equity-settled stock-based remuneration plan (stock option plan) for directors, officers, employees and consultants. The Company's plan does not feature any options for a cash settlement.

All goods and services received in exchange for the grant of any stock-based payments are measured at their fair values, unless that fair value cannot be estimated reliably. If the Company cannot estimate reliably the fair value of the goods or services received, the Company shall measure their value indirectly by reference to the fair value of the equity instruments granted. Where employees, or consultants providing similar services, are rewarded using stock-based payments, the fair values of the services rendered are determined indirectly by reference to the fair value of the equity instruments granted. The fair value is measured at the grant date and if applicable, recognized over the vesting period. The fair value of the options granted is measured using the Black-Scholes option-pricing model, taking into account the terms and conditions upon which the options were granted. Estimates are subsequently revised if there is any indication that the number of stock options expected to vest differs from previous estimates. Any cumulative adjustment prior to vesting is recognized in the current period. No adjustment is made to any expense recognized in prior periods if stock options ultimately exercised are different to that estimated on vesting. Stock-based compensation expense incorporates an expected forfeiture rate.

**(o) Restricted share units (“RSU”)**

Under the Company’s RSU plan, employees and consultants are eligible to be granted RSUs where each RSU has a value equal to one Common Share. RSUs are measured at fair value on the grant date. The fair value of RSUs are recognized as a charge to stock-based compensation over the vesting period with a corresponding increase in equity.

### (p) Basic and diluted earnings (loss) per share

Basic earnings (loss) per share is computed by dividing the net income (loss) for the period by the weighted average number of Common Shares outstanding during the period. The computation of diluted earnings (loss) per share assumes the conversion or exercise of securities only when such conversion or exercise would have a dilutive effect on earnings (loss) per share. The diluted loss per share is equal to the basic loss per share where the effect of convertible securities is antidilutive, as it would decrease the loss per share.

### (q) Income taxes

Tax expense recognized in profit or loss comprises the sum of deferred and current tax not recognized in other comprehensive income or directly in equity.

Current income tax assets and/or liabilities comprise those obligations to, or claims from, fiscal authorities relating to the current or prior reporting periods, that are unpaid at the reporting date. Current tax is payable on taxable profit, which differs from profit or loss in the financial statements. Calculation of current tax is based on tax rates and laws that have been enacted or substantively enacted by the end of the reporting period.

Deferred income taxes are calculated using the liability method on temporary differences between the carrying amounts of assets and liabilities and their tax bases. However, deferred tax is not provided on the initial recognition of an asset or liability unless the related transaction is a business combination or affects tax or accounting profit. Deferred tax on temporary differences associated with shares in subsidiaries and associates is not provided if reversal of these temporary differences can be controlled by the Company and it is probable that the reversal will occur in the foreseeable future.

Deferred tax assets and liabilities are calculated, without discounting, at tax rates that are expected to apply to their respective period of realization, provided they are enacted or substantively enacted by the end of the reporting period. Deferred tax liabilities are always provided for in full. Deferred tax assets are recognized to the extent that it is probable that they will be able to be utilized against future taxable income.

Deferred tax assets and liabilities are offset only when the Company has a right and intention to set off current tax assets and liabilities from the same taxation authority.

Changes in deferred tax assets or liabilities are recognized as deferred income tax expense in profit or loss, except where they relate to items that are recognized in other comprehensive income or directly in equity, in which case the related deferred tax is also recognized in other comprehensive income or equity, respectively.

### (r) Segmented reporting

The Company presents and discloses segmented information based on information that is regularly reviewed by the Company's CEO, who is the chief operating decision maker. The CEO has primary responsibility for allocating resources to the Company's operating segments and assessing their performance. The Company has determined that there is only one operating segment being the production and co-packing of CIBs.

### (s) Significant management judgements

The following are significant management judgments in applying the accounting policies of the Company and have the most significant effect on the financial statements.

*Going concern*

The assessment of the Company's ability to continue as a going concern, to raise sufficient funds to pay for its ongoing operating expenditures, meet its liabilities for the ensuing year, and to fund planned and contractual obligations involves significant judgments based on historical experience and other factors, including expectation of future events that are believed to be reasonable under the circumstances.

*Valuation of Inventory*

In calculating the net realizable value of inventory, management determines the selling prices based on prevalent sales prices, selling costs, and includes an estimate of spoiled or expired inventory based on the most reliable evidence available at the time, to record inventory at the lower of cost or net realizable value.

*Estimated useful lives, impairment considerations and depreciation of capital assets*

Depreciation of capital assets is dependent upon estimates of useful lives based on management's judgment.

Impairment of definite long-lived assets is influenced by judgment in defining a CGU and determining the indicators of impairment, and estimates used to measure impairment losses.

The recoverable value of long-lived assets is determined using discounted future cash flow models, which incorporate assumptions regarding future events, specifically future cash flows, growth rates and discount rates.

*Measurement of right-of-use asset and lease liability on initial recognition*

The right-of-use asset is initially measured at the amount of the lease liability plus any initial direct costs incurred by the lessee. The lease liability is initially measured at the present value of the lease payments payable over the lease term, discounted at the rate implicit in the lease if that can be readily determined. If that rate cannot be readily determined, the lessee shall use their incremental borrowing rate, which is the rate of interest that a lessee would have to pay to borrow over a similar term, and with a similar security, the funds necessary to obtain an asset of a similar value to the right-of-use asset in a similar economic environment. Significant judgment is required to estimate an incremental borrowing rate in the context of a right-of-use asset.

*Convertible debt*

The classification of the Company's convertible debentures required Management to analyze the terms and conditions of the debentures and use judgment to assess whether these debentures are liability, equity, or a combination of the two. IAS 32 – *Financial Instruments – Presentation* ("IAS 32"), provides the criteria for Management to assess these complicated financial instruments to determine their appropriate classification(s). Factors considered are, but not limited to, whether the Company has a future obligation to settle the instrument in cash or exchange other assets or liabilities, the currency of settlement and if the settlement is already known to be equity, the amount will not vary based on the Company's future share price.

*Revenue – Principal versus Agent*

The Company evaluates whether it is the principal (reports on gross basis) or agent (reports on a net basis) for revenues generated by the direct sale of CIBs. The LP partners of the Company control the CIBs prior to the sale to its customers as regulated and mandated under the Cannabis Act and Health Canada legislation. The Company's LP partners possessing the sole ability to monetize the sale of CIBs through the held sales agreements and purchase orders with Provincial Retailer customers. The Company presents the revenues from the sale of CIBs on a net basis, net of associated fees from the LPs, as it presently sells only to LPs, who then sell to Provincial Retailers.

*Income, value added, withholding and other taxes*

The Company is subject to income, value added, withholding and other taxes. Significant judgment is required in determining the Company's provisions for taxes. There are many transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business. The Company recognizes liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. The determination of the Company's income, value added, withholding and other tax liabilities requires interpretation of complex laws and regulations. The Company's interpretation of taxation law as applied to transactions and activities may not coincide with the interpretation of the tax authorities. All tax related filings are subject to government audit and potential reassessment subsequent to the financial statement reporting period. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the tax related accruals and deferred income tax provisions in the period in which such determination is made.

*Share-based compensation*

The fair value of share-based compensation expenses is estimated using the Black-Scholes option pricing model and relies on a number of estimates, such as the expected life of the option, the volatility of the underlying share price, the risk free rate of return, and the estimated rate of forfeiture of options granted.

**(t) Standards, amendments and interpretations not yet effective**

Certain pronouncements were issued by the IASB or the IFRS Interpretations Committee ("IFRIC") that are mandatory for accounting periods commencing on or after January 1, 2020. Many are not applicable or do not have a significant impact to the Company and have been excluded. Adoption of these pronouncements is mandatory for entities with year ends beginning on or after January 1, 2020.

*IAS 1, Presentation of Financial Statements and IAS 8, Accounting Policies, Changes in Accounting Estimates and Errors*

In October 2018, IAS 1 – *Presentation of Financial Statements* ("IAS 1") and IAS 8 – *Accounting Policies, Changes in Accounting Estimates and Errors* ("IAS 8") were amended to refine the definition of materiality and clarify its characteristics. The revised definition focuses on the idea 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. The amendments are effective for annual reporting periods beginning on or after January 1, 2020. The extent of the impact on the Company of adopting these amendments has not yet been determined.

*IFRS 3, Business Combinations*

In October 2018, IFRS 3 – *Business Combinations* ("IFRS 3") was amended to clarify the definition of a business. This amended definition states that a business must include inputs and a process and clarified that the process must be substantive and the inputs and process must together significantly contribute to operating outputs. In addition, it narrows the definitions of a business by focusing the definition of outputs on goods and services provided to customers and other income from ordinary activities, rather than on providing dividends or other economic benefits directly to investors or lowering costs and added a test that makes it easier to conclude that a company has acquired a group of assets, rather than a business, if the value of the assets acquired is substantially concentrated in a single asset or group of similar assets. The amendments are effective for annual reporting periods beginning on or after January 1, 2020. The extent of the impact on the Company of adopting these amendments has not yet been determined.

Certain pronouncements were issued by the IASB or the IFRIC that are mandatory for accounting periods commencing on or after January 1, 2021. Many are not applicable or do not have a significant impact to the Company and have been excluded.

*IFRS 10, Consolidated Financial Statements and IAS 28, Investments in Associates and Joint Ventures*

*(Expressed in Canadian dollars)*

IFRS 10 – *Consolidated Financial Statements* ("IFRS 10") and IAS 28 – *Investments in Associates and Joint Ventures* ("IAS 28") were amended in September 2014 to address a conflict between the requirements of IAS 28 and IFRS 10 and clarify that in a transaction involving an associate or joint venture, the extent of gain or loss recognition depends on whether the assets sold or contributed constitute a business. The effective date of these amendments is yet to be determined, however early adoption is permitted.

*IAS 1, Presentation of Financial Statements*

IAS 1 – *Presentation of Financial Statements* ("IAS 1") was amended in January 2020 to provide a more general approach to the classification of liabilities under IAS 1 based on the contractual arrangements in place at the reporting date. The amendments clarify that the classification of liabilities as current or noncurrent is based solely on a company's right to defer settlement at the reporting date. The right needs to be unconditional and must have substance. The amendments also clarify that the transfer of a company's own equity instruments is regarded as settlement of a liability, unless it results from the exercise of a conversion option meeting the definition of an equity instrument. The amendments are effective for annual periods beginning on January 1, 2023.

*IAS 37, Provisions, Contingent Liabilities, and Contingent Assets*

IAS 37 – *Provisions, Contingent Liabilities, and Contingent Assets* ("IAS 37") was amended. The amendments clarify that when assessing if a contract is onerous, the cost of fulfilling the contract includes all costs that relate directly to the contract – i.e. a full-cost approach. Such costs include both the incremental costs of the contract (i.e. costs a company would avoid if it did not have the contract) and an allocation of other direct costs incurred on activities required to fulfill the contract – e.g. contract management and supervision, or depreciation of equipment used in fulfilling the contract. The amendments are effective for annual periods beginning on January 1, 2022.

*IAS 16, Property, Plant and Equipment*

IAS 16 – *Property, Plant and Equipment* ("IAS 16") was amended. The amendments introduce new guidance, such that the proceeds from selling items before the related property, plant and equipment is available for its intended use can no longer be deducted from the cost. Instead, such proceeds are to be recognized in profit or loss, together with the costs of producing those items. The amendments are effective for annual periods beginning on January 1, 2022.

The Company is currently assessing the impact of adopting these pronouncements.

### (u) Comparative figures

Certain figures for 2020 have been reclassified to conform to the presentation adopted in 2021.

## 3. CASH AND CASH EQUIVALENTS

Cash and cash equivalents consist of the following:

| | **October 31, 2021** | October 31, 2020 |
|---|---|---|
| | **$** | $ |
| Cash at banks | **178,327** | 902,519 |
| Short-term deposits | **1,025,000** | - |
| Total cash and cash equivalents | **1,203,327** | 902,519 |

*(Expressed in Canadian dollars)*

Short-term deposits consist of cashable Guaranteed Investment Certificates ("GICs") with one-year terms that are redeemable prior to maturity, and earn interest at rates between 0.35% to 0.65% per annum.

## 4. TRADE AND OTHER RECEIVABLES

Trade and other receivables consist of the following:

| | **October 31, 2021** | October 31, 2020 |
|---|---|---|
| | **$** | $ |
| Trade accounts and other receivables | **289,903** | - |
| Sales taxes receivable | **101,287** | 103,081 |
| Total trade and other receivables | **391,190** | 103,081 |

## 5. INVENTORY

Inventory consists of the following:

| | **October 31, 2021** | October 31, 2020 |
|---|---|---|
| | **$** | $ |
| Raw materials | **416,160** | 145,352 |
| Finished goods | **224,200** | - |
| Total inventory | **640,360** | 145,352 |

The Company recognizes the costs of inventory expensed in two separate lines on the consolidated statements of loss and comprehensive loss. Capitalized costs expensed and included in cost of goods sold was $881,143 for the year ended October 31, 2021 (2020 – $nil). The write-down of inventories to net realizable value on the consolidated statements of loss and comprehensive loss for the year ended October 31, 2021 was $73,857 (2020 – $nil). As at October 31, 2021 and 2020, raw materials are carried at cost. As at October 31, 2021, finished goods are carried at net realizable value.

Total share-based compensation capitalized to inventory in the year ended October 31, 2021 was $65,689 (October 31, 2020 – $nil). Total depreciation capitalized to inventory in the year ended October 31, 2021 was $364,544 (October 31, 2020 – $nil). Total interest on lease liability capitalized to inventory in the year ended October 31, 2021 was $9,169 (October 31, 2020 – $nil).

## 6. MARKETABLE SECURITIES

Marketable securities are classified as FVTPL and are comprised of:

| | **October 31, 2021** | October 31, 2020 |
|---|---|---|
| | **$** | $ |
| Precipitate Gold Corp. (1) | **-** | 239,904 |
| | **-** | 239,904 |

*(Expressed in Canadian dollars)*

(1) As at October 31, 2021 and October 31, 2020, nil and 999,600 common shares, respectively, of Precipitate Gold Corp. ("Precipitate") are included in marketable securities, within current assets. During the year ended October 31, 2021, the Company recorded a decrease in fair value of financial assets at FVTPL of $73,153 (2020 – $nil) in connection with the sale of the remainder of these marketable securities. During the year ended October 31, 2021, the Company sold 999,600 common shares of Precipitate in aggregate for gross proceeds of $166,751 (2020 – $nil).

## 7. REVERSE TAKE-OVER

On September 16, 2020, the Company completed the Transaction, pursuant to which it acquired all of the issued and outstanding OpCo Shares of OpCo (Note 1).

While Molecule Holdings was the legal acquirer, OpCo was the accounting acquirer since shareholders of OpCo held and controlled the majority of the outstanding Common Shares upon completion of the Transaction (the "Reverse Take-Over" or "RTO"). As a result of the RTO, the consolidated financial statements are presented with OpCo as the continuing entity.

The acquisition of Molecule Holdings (formerly Everton Resources Inc.) was accounted for as an asset acquisition, as the assets acquired and liabilities assumed did not constitute a business, as defined in IFRS 3, Business Combinations. The total consideration was allocated to the fair value of the net assets acquired and liabilities assumed, as follows:

| **CONSIDERATION PAID** | **Estimated fair value** |
|---|---|
| | $ |
| 9,313,447 common shares | 1,490,152 |
| 1,103,250 warrants | 1,672 |
| 1,060,000 stock options | 40,532 |
| | 1,532,356 |

| **ALLOCATION** | |
|---|---|
| | $ |
| *ASSETS* | |
| Cash | 271,340 |
| Marketable securities | 352,305 |
| Sales taxes receivable | 31,257 |
| Deferred transaction costs | 22,276 |
| Prepaid expenses | 129,600 |
| **Total identifiable assets acquired** | 806,778 |
| *LIABILITIES* | |
| Accounts payable and accrued liabilities | (554,128) |
| Loan payable | (92,700) |
| Amount due to related party | (22,600) |
| **Total liabilities assumed** | (669,428) |
| **Net assets acquired** | 137,350 |

*(Expressed in Canadian dollars)*

In connection with the RTO, the Company recognized a listing expense in the amount of $1,395,006 in the year ended October 31, 2020, such amount being equal to the consideration paid less the net assets acquired under the Transaction.

## 8. CAPITAL ASSETS

| | Right-of-use asset (1) | Leasehold improvements (2) | Equipment (3,4) | Total |
|---|---|---|---|---|
| | $ | $ | $ | $ |
| **Cost** | | | | |
| Balance, October 31, 2020 | 239,865 | 1,412,551 | 2,343,949 | 3,996,365 |
| Additions | - | 32,172 | 44,692 | 76,864 |
| Disposals | - | - | (198,415) | (198,415) |
| **Cost, October 31, 2021** | **239,865** | **1,444,723** | **2,190,226** | **3,874,814** |
| **Accumulated depreciation** | | | | |
| Balance, October 31, 2020 | 75,962 | - | - | 75,962 |
| Depreciation | 47,976 | 240,610 | 278,475 | 567,061 |
| Disposals | - | - | (16,538) | (16,538) |
| **Accumulated depreciation, October 31, 2021** | **123,938** | **240,610** | **261,937** | **626,485** |
| **Net book value, October 31, 2021** | **115,927** | **1,204,113** | **1,928,289** | **3,248,329** |

(1) Effective April 1, 2019, OpCo entered into a lease for a parcel of land and building for an initial term of five years, for which a right-of-use asset was recognized in the amount of $239,865 (Note 10).

(2) During the year ended October 31, 2021, the Company incurred capital expenditures of $32,172 in leasehold improvements on the Facility. The Company commenced recording depreciation on the leasehold improvements when the Facility became ready for use in December 2020.

(3) During the year ended October 31, 2021, the Company purchased equipment in the amount of $44,692, to be used in the production of CIBs. The Company commenced recording depreciation on the equipment used at the Facility in January 2021 while the completion of its first production-scale CIB run.

(4) During the year ended October 31, 2021, the Company capitalized $364,544 (October 31, 2020 – $nil) of depreciation to inventory. During the year ended October 31, 2021, depreciation expensed to the consolidated statements of loss and comprehensive loss was $202,517 (2020 – $47,976).

During the year ended October 31, 2021, the company sold equipment with book value of $181,877 for net proceeds of $77,000, resulting in a loss of $104,877.

*(Expressed in Canadian dollars)*

| | Right of use asset | Leasehold improvements (5) | Equipment | Total |
|---|---|---|---|---|
| | $ | $ | $ | $ |
| **Cost** | | | | |
| Balance, October 31, 2019 | 239,865 | 1,082,628 | 775,592 | 2,098,085 |
| Additions | - | 329,923 | 1,568,357 | 1,898,280 |
| **Cost, October 31, 2020** | **239,865** | **1,412,551** | **2,343,949** | **3,996,365** |
| **Accumulated depreciation** | | | | |
| Balance, October 31, 2019 | 27,986 | - | - | 27,986 |
| Depreciation | 47,976 | - | - | 47,976 |
| **Accumulated depreciation, October 31, 2020** | **75,962** | **-** | **-** | **75,962** |
| **Net book value, October 31, 2020** | **163,903** | **1,412,551** | **2,343,949** | **3,920,403** |

(5) During the year ended October 31, 2020, the Company incurred capital expenditures of $329,923 in leasehold improvements on the Facility. The Company did not record any depreciation on the leasehold improvements during the year ended October 31, 2020 as the Facility was not then ready for use.

(6) During the year ended October 31, 2020, the Company purchased equipment in the amount of $1,568,357, to be used in the production of CIBs. The Company did not record any depreciation on the equipment during the year ended October 31, 2020 as it was not then ready for use.

## 9. FINANCIAL INSTRUMENTS, RISK MANAGEMENT AND CAPITAL MANAGEMENT

*Financial instruments*

The Company's financial instruments consist of cash and cash equivalents, trade accounts and other receivables, marketable securities, accounts payable and accrued liabilities, convertible debt and warrant liabilities and other long-term liabilities. The fair value of the Company’s financial instruments approximates their carrying value due to their short-term nature.

*(Expressed in Canadian dollars)*

The classification of financial instruments is as follows:

| | **October 31, 2021** | October 31, 2020 |
|---|---|---|
| | **$** | $ |
| **Financial assets** | | |
| Amortized cost | | |
| Cash | **178,327** | 902,519 |
| Trade accounts and other receivables | **289,903** | - |
| Fair value through profit or loss | | |
| Cash equivalents | **1,025,000** | - |
| Marketable securities | **-** | 239,904 |
| Total financial assets | **1,493,230** | 1,142,423 |
| **Financial liabilities** | | |
| Amortized cost | | |
| Accounts payable and accrued liabilities | **(816,964)** | (1,094,133) |
| Convertible debt | **(817,087)** | (697,625) |
| Other long-term liabilities | **(60,000)** | (40,000) |
| Fair value through profit or loss | | |
| Convertible debt | **(3,001,008)** | - |
| Warrant liability | **(486,848)** | - |
| Total financial liabilities | **(5,181,907)** | (1,831,758) |

*Risk management*

The Company thoroughly examines the various financial risks to which it is exposed and assesses the impact and likelihood of those risks. These risks include credit risk, liquidity risk and market risk. Where material, these risks are reviewed and monitored by the Board of Directors.

*(i) Credit risk*

Credit risk is the risk of an unexpected loss if a customer or counterparty to its financial instruments fails to meet its contractual obligations. The Company's financial assets exposed to credit risk are primarily composed of trade accounts receivable and cash and cash equivalents. The Company provides credit to its customer in the normal course of business and has established credit evaluation and monitoring processes to mitigate credit risk. Since that customer sells end products to Provincial Retailers, the Company has limited credit risk. The Company's cash and cash equivalents are held at reputable financial institutions with high external credit ratings. It is Management's opinion that the Company is not exposed to significant credit risk.

None of the Company's financial assets are secured by collateral or other credit enhancements.

Management considers that all the above financial assets that are not impaired or past due for each of the reporting dates are of good credit quality. There are no financial assets that are past due but not impaired for the periods presented.

*(ii) Liquidity risk*

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they come due. The Company's liquidity and operating results may be adversely affected if its access to the capital markets is hindered, whether as a result of a downturn in stock market conditions generally or matters specific to the Company. The Company regularly evaluates its cash position to ensure preservation and security of capital as well as liquidity. The Company's accounts payable and other liabilities generally have contractual maturities of less than 30 days and are subject to normal trade terms.

*(iii) Market risk*

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises three types of risk: interest rate risk, currency risk and other price risk, such as equity price risk and commodity risk. Financial instruments affected by market risk include marketable securities and derivative financial instruments, like the convertible debt and warrant liabilities measured at FVTPL.

The Company previously held shares in a publicly listed company in the mineral exploration industry. The Company was thus previously exposed to market risk regarding these shares as unfavourable market conditions could result in their disposal at less than their carrying value. As at October 31, 2021, the Company held no more of these shares after selling the remainder in fiscal 2021, resulting in a loss of $73,153 for the year ended October 31, 2021 (2020 – $nil).

There are anti-dilution provisions in the convertible debt and warrant liabilities measured at FVTPL that expose the company to interest rate risk and equity price risk, including the exercise price and conversion feature terms for the convertible debentures and the exercise price for the associated warrants, in the event of a future financing at more favourable terms.

*Capital management*

The Company's objectives when managing capital are to safeguard the Company's ability to continue as a going concern, to meet its capital expenditures for its continued operations, and to maintain a flexible capital structure which optimizes the cost of capital within a framework of acceptable risk. The Company manages its capital structure and adjusts it in light of changes in economic conditions and the risk characteristics of the underlying assets. To maintain or adjust its capital structure, the Company may issue new shares through equity offerings or return capital to shareholders. The Company is not subject to externally imposed capital requirements.

Management reviews its capital management approach on an ongoing basis. There have been no changes to the Company's capital management approach during the years ended October 31, 2021 and 2020.

*(Expressed in Canadian dollars)*

## 10. LEASE LIABILITY

| | $ |
|---|---|
| **Balance, October 31, 2019** | **215,379** |
| Interest expense | 23,270 |
| Lease payments | (60,000) |
| **Balance, October 31, 2020** | **178,649** |
| Interest expense | 18,541 |
| Lease payments | (61,750) |
| **Balance, October 31, 2021** | **135,440** |
| Current | 50,071 |
| Long-term | 85,369 |
| | **135,440** |

Effective April 1, 2019, OpCo entered into a lease with Thousand Island Farms Inc., a company owned by a Director of Molecule Holdings, for a parcel of land and a building included in the Facility. The lease has an initial five-year term which expires in April 2024, unless extended by the Company. For and during the first and second year of the lease, the base rent was $60,000 per annum, payable in equal monthly instalments of $5,000. For and during the third and fourth year of the lease, the base rent is $63,000 per annum, payable in equal monthly instalments of $5,250. For and during the fifth year of the lease, the base rent is $66,150 per annum, payable in equal monthly instalments of $5,513. Provided that the Company is not in default in the performance of any term of the lease, Molecule Holdings has an irrevocable option to purchase, during the lease term, the premises and land for a purchase price which was $875,000 if exercised in the first year of the lease, which purchase price increases each year of the lease based on the annual Consumer Price Index percentage. The Company was charged an amount of $5,000 during the year ended October 31, 2019, in consideration for the grant of the purchase option, which is non-refundable.

During the year ended October 31, 2021, the Company capitalized $9,169 (October 31, 2020 – $nil) of interest on lease liability to inventory. During the year ended October 31, 2021, interest on lease liability expensed to the consolidated statements of loss and comprehensive loss was $9,372 (October 31, 2020 – $23,270).

*(Expressed in Canadian dollars)*

## 11. CONVERTIBLE DEBT

Convertible debt consists of the following:

| | **October 31, 2021** | October 31, 2020 |
|---|---|---|
| | **$** | $ |
| Convertible debentures and warrants measured at FVTPL | | |
| Convertible debentures and warrants issued March 18, 2021 | **1,050,866** | - |
| Convertible debentures and warrants issued July 30, 2021 | **1,418,402** | - |
| Convertible debentures and warrants issued August 13, 2021 | **1,018,588** | - |
| Total convertible debt and warrant liabilities measured at FVTPL | **3,487,856** | - |
| Convertible debentures measured at amortized cost | | |
| Convertible debentures issued September 16, 2020 | **817,087** | 697,625 |
| Total long-term portion of convertible debt | **817,087** | 697,625 |
| Total convertible debt | **4,304,943** | **697,625** |

Convertible Debenture issued September 16, 2020

On September 16, 2020, and in connection with the completion of the Transaction (Note 7), the Company satisfied the escrow release conditions of the brokered private placement offering of subscription receipts led by Gravitas Securities Inc. (the “Agent”), pursuant to the terms of an agency agreement dated July 29, 2020 (the “Agency Agreement”) and the concurrent non-brokered private placement offering of subscription receipts (collectively, the “September 2020 Offerings”), which closed on July 29, 2020. Upon the satisfaction of all related release conditions as agreed by the Company and the Agent, each of the 1,025 subscription receipts issued pursuant to the September 2020 Offerings, which were issued at a price of $1,000 per subscription receipt, were deemed to be automatically exchanged without any additional consideration or further action on the part of the holders thereof into one convertible debenture of the Company. The September 2020 Offerings included a related party transaction as certain Directors of the Company participated in the private placement for a total amount of $85,000.

Each convertible debenture is an unsecured debt obligation of the Company and consists of a principal amount of $1,000 bearing interest at the simple rate of 8% per annum and maturing on September 16, 2023. Prior to the maturity date, and subject to exercise by the Company of an acceleration provision, all the outstanding principal and accrued interest of the convertible debentures may be converted into units of the Company at a price of $0.20 per unit, at the sole option of the respective holder of the convertible debenture. Unless the option is exercised prior to the maturity date, the Company will subsequently make a cash payment to the holders of the convertible debentures to settle the outstanding principal and accrued interest of each respective convertible debenture.

Upon exercise of the option, each unit will be comprised of one Common Share and one-half of one Common Share purchase warrant. Each warrant will be exercisable to purchase one Common Share at an exercise price of $0.30 per Common Share until September 16, 2023.

In connection with the non-brokered offering, the Agent also provided fiscal advisory services pursuant to the terms of a fiscal advisory agreement (the “Fiscal Advisory Agreement”). Pursuant to the Agency Agreement and the Fiscal Advisory Agreement, the Company issued an aggregate of 410,000 broker warrants and 40 convertible debentures (the “Compensation Debentures”). Each broker warrant is exercisable into one unit at a price of $0.20 per unit until September 16, 2023. Each Compensation Debenture has the same terms as the convertible debentures.

*(Expressed in Canadian dollars)*

In accordance with IAS 32, the Company allocated the proceeds from the convertible debentures ($1,025,000), net of transaction costs ($314,931), between a liability component ($640,235) and an equity component ($69,834), representing the conversion feature. Similarly, the Company allocated the value of the Compensation Debentures between a liability component ($36,066) and an equity component ($3,934).

The fair value of the liability components at the time of issue was calculated as the discounted cash flows of the convertible debentures and the Compensation Debentures, assuming a market interest rate of 12% which was their estimated rate for the without the equity component (i.e. conversion feature). Their combined effective interest rate after reflecting issuance costs was 25%. The value of the conversion feature of the debentures was recognized as the difference between the principal amount of the debentures and the fair value of the liability component.

In connection with the September 2020 Offerings, the Company paid cash commissions of $82,000. The fair value of the 410,000 broker warrants was estimated at $53,512, using the Black-Scholes option pricing model using the following assumptions: stock price of $0.16, weighted-average exercise price of $0.23, risk-free interest rate of 0.28%, expected life of warrants of 3 years, expected volatility of 100% and expected dividend rate of 0%, and is included in ‘Warrants’ within shareholders’ equity in the consolidated statement of financial position. The Company incurred other issuance costs in the amount of $139,419. The issuance costs, which include the cash commissions, broker warrants, Compensation Debentures and other issuance costs, have been allocated to the liability and equity components in proportion to their initial carrying amounts.

| | **Debentures** | **Conversion feature** | **Total** |
|---|---|---|---|
| | $ | $ | $ |
| **Balance, October 31, 2019** | **-** | **-** | **-** |
| Proceeds from issuance of Convertible Debentures | 924,195 | 100,805 | 1,025,000 |
| less: | | | |
| Cash commissions | (73,936) | (8,064) | (82,000) |
| Broker warrants | (48,249) | (5,263) | (53,512) |
| Compensation debentures | (36,066) | (3,934) | (40,000) |
| Other issuance costs | (125,709) | (13,710) | (139,419) |
| Net proceeds from issuance of Convertible Debentures | 640,235 | 69,834 | 710,069 |
| Issuance of Compensation Debentures | 36,066 | 3,934 | 40,000 |
| Interest accretion on Debentures | 21,324 | - | 21,324 |
| **Balance, October 31, 2020** | **697,625** | **73,768** | **771,393** |
| Interest accretion on Debentures | 187,385 | - | 187,385 |
| Interest paid on Debentures | (67,923) | - | (67,923) |
| **Balance, October 31, 2021** | **817,087** | **73,768** | **890,855** |

Convertible Debenture issued March 18, 2021

On March 18, 2021, the Company completed a non-brokered private placement offering (the “March 2021 Offering”) of 1,000 senior secured convertible debenture units for gross proceeds of $1,000,000. Each unit is comprised of $1,000 in principal amount of senior secured convertible debenture and one share purchase warrant for each $0.30 of principal amount, each warrant entitling the holder thereof to acquire one Common

Share at an exercise price of $0.23 per Common Share (subject to adjustment) for a period of thirty-six months from the date of closing of the March 2021 Offering, expiring on March 18, 2024.

The debentures bear interest at a simple rate of 8.00% per annum, payable quarterly in cash beginning on June 30, 2021, and maturing eighteen months from the date of issuance, being September 18, 2022. The holders of the debenture are entitled to convert the principal amount of the debentures at any time prior to the maturity date into Common Shares at a conversion price of $0.15, subject to adjustment. As of the date that is four months and one day following the closing date, the Company will have a right to prepay or redeem the principal amount in cash, in whole or in part, at par plus accrued and unpaid interest at any time by providing a minimum of 30 days' and a maximum of 60 days' notice.

The obligations under the debentures are secured by the assets of the Company and OpCo, which has also acted as guarantor, including a pledge of the shares of the guarantor.

The debentures and the warrants provide for change of control as well as anti-dilution adjustments, including corporate actions of the Company as well as future equity issuances below the conversion price or exercise price, as applicable

As a result of the anti-dilution provisions associated with the debenture, the entire convertible debenture and warrants are accounted for as derivative financial liabilities at FVTPL, as the financial liabilities cannot be settled for a fixed number of the Company's own equity instruments.

The fair value of the convertible debenture at the time of issue of $856,435 was calculated as the higher of the discounted expected future cash outflows required to settle the liability and the fair value of the Common Shares required to settle it upon conversion.

The fair value of the warrants at the time of issue was estimated at $182,888, using the Black-Scholes pricing model using the following assumptions: stock price of $0.115, weighted-average exercise price of $0.23, risk-free interest rate of 0.52%, expected life of warrants of 3 years, expected volatility of 100% and expected dividend rate of 0%.

The excess of the fair value of the convertible debenture and warrant liabilities over the proceeds from the convertible debenture of $39,323 was recorded as a loss in fair value of financial liabilities at FVTPL.

In connection with the March 2021 Offering, the Company paid cash commissions of $57,500 and issued 533,333 compensation warrants exercisable at $0.15 for 36 months. The fair value of the compensation warrants was estimated at $34,605, using the Black-Scholes option pricing model using the following assumptions: stock price of $0.115, weighted-average exercise price of $0.15, risk-free interest rate of 0.52%, expected life of warrants of 3 years, expected volatility of 100% and expected dividend rate of 0%, and is included in 'Warrants' within shareholders' equity in the consolidated statement of financial position.

The Company incurred total transaction costs in the amount of $158,495. The issuance costs, which include the cash commissions, broker warrants, and other issuance costs, have been immediately expensed in financing fees in the consolidated statements of loss and comprehensive loss.

*(Expressed in Canadian dollars)*

On July 30, 2021, as a result of the anti-dilution provisions of the March 2021 Offering and the more favourable July 2021 Offering terms described below, the following modifications to the March 2021 Offering resulted:

- The warrant exercise price of the March 2021 Offering was reduced from $0.23 to $0.15 per Common Share;
- The number of warrants issued to the participants of the March 2021 Offering was increased to six thousand per $1,000 in principal amount (or 6,000,000 warrants in aggregate) from 3,333,333 warrants originally issued on March 18, 2021; and
- The conversion price of the March 2021 Offering was reduced from $0.15 to $0.10 on July 30, 2021.

All other terms of the March 2021 Offering remain unmodified by the July 2021 Offering or August 2021 Offering, which did not differ from the terms of the July 2021 Offering, including the maturity date of September 18, 2022 and the warrant exercise expiry date of March 18, 2024.

On October 31, 2021, the fair value of the convertible debenture liability component was adjusted to $910,856, plus accrued interest of $10,247 ($921,103 in aggregate), calculated as the higher of the discounted expected future cash outflows required to settle the liability and the fair value of the Common Shares required to settle it upon conversion, resulting in a loss in fair value of financial liabilities at FVTPL of $54,421 for the year ended October 31, 2021.

Also on October 31, 2021, the fair value of the warrants was adjusted to $129,763, using the Black-Scholes pricing model using the following assumptions: stock price of $0.06, weighted-average exercise price of $0.15, risk-free interest rate of 1.00%, expected life of warrants of 2.38 years, expected volatility of 100% and expected dividend rate of 0%, resulting in a gain in fair value of financial liabilities at FVTPL of $53,125 for the year ended October 31, 2021.

| | **Debentures** | **Warrants** | **Other income (loss)** | **Total** |
|---|---|---|---|---|
| | $ | $ | $ | $ |
| **Balance, October 31, 2020 and October 31, 2019** | **-** | **-** | **-** | **-** |
| Proceeds from issuance of Convertible Debentures | 856,435 | 182,888 | (39,323) | 1,000,000 |
| less: | | | | |
| Cash commissions | - | - | (57,500) | (57,500) |
| Broker warrants | - | - | (34,605) | (34,605) |
| Other issuance costs | - | - | (66,390) | (66,390) |
| Net proceeds from issuance of Convertible Debentures | 856,435 | 182,888 | (197,818) | 841,505 |
| Interest accrued on Debentures | 56,275 | - | (56,275) | - |
| Interest paid on Debentures | (46,028) | - | - | (46,028) |
| Change in financial liabilities at FVTPL | 54,421 | (53,125) | (1,296) | - |
| **Balance, October 31, 2021** | **921,103** | **129,763** | **(255,389)** | **795,477** |

Convertible Debenture issued July 30, 2021

On July 30, 2021, the Company completed the first closing of a non-brokered private placement offering (the “July 2021 Offering”) of 1,414 unsecured convertible debenture units for gross proceeds of $1,414,000. Each unit is comprised of $1,000 in principal amount of unsecured convertible debenture and six thousand share purchase warrants for each $1,000 of principal amount, each warrant entitling the holder thereof to acquire one Common Share at an exercise price of $0.15 per Common Share (subject to adjustment) for a period of thirty-six months from the date of closing of the July 2021 Offering, expiring on July 30, 2024.

The debentures bear interest at a simple rate of 8.00% per annum, payable semi-annually in cash beginning on January 30, 2022, and maturing twenty-four months from the date of issuance, being July 30, 2023. The holders of the debenture are entitled to convert the principal amount of the debentures at any time prior to the maturity date into Common Shares at a conversion price of $0.10, subject to adjustment. As of the date that is four months and one day following the closing date, the Company will have a right to prepay or redeem the principal amount in cash, in whole or in part, at par plus accrued and unpaid interest at any time by providing a minimum of 30 days' and a maximum of 60 days' notice.

The debentures and the warrants provide for change of control as well as anti-dilution adjustments, including corporate actions of the Company as well as future equity issuances below the conversion price or exercise price, as applicable.

As a result of the anti-dilution provisions associated with the debenture, the entire convertible debenture and warrants are accounted for as derivative financial liabilities at FVTPL, as the financial liabilities cannot be settled for a fixed number of the Company's own equity instruments.

The fair value of the convertible debenture at the time of issue of $1,154,767 was calculated as the higher of the discounted expected future cash outflows required to settle the liability and the fair value of the Common Shares required to settle it upon conversion.

The fair value of the warrants at the time of issue was estimated at $333,192, using the Black-Scholes pricing model using the following assumptions: stock price of $0.08, weighted-average exercise price of $0.15, risk-free interest rate of 0.61%, expected life of warrants of 3 years, expected volatility of 100% and expected dividend rate of 0%.

The excess of the fair value of the convertible debenture and warrant liabilities over the proceeds from the convertible debenture of $73,959 was recorded as a loss in fair value of financial liabilities at FVTPL.

In connection with the July 2021 Offering, the Company paid cash commissions of $96,720 and issued 951,200 compensation warrants exercisable at $0.15 per Common Share for thirty-six months. The fair value of the compensation warrants was estimated at $37,357, using the Black-Scholes option pricing model using the following assumptions: stock price of $0.080, weighted-average exercise price of $0.15, risk-free interest rate of 0.61%, expected life of warrants of 3 years, expected volatility of 100% and expected dividend rate of 0%, and is included in 'Warrants' within shareholders' equity in the consolidated statement of financial position.

The Company incurred total transaction costs in the amount of $153,291. The issuance costs, which include the cash commissions, Broker Warrants, and other issuance costs, have been immediately expensed in financing fees in the consolidated statements of loss and comprehensive loss.

On October 31, 2021, the fair value of the convertible debenture liability component was adjusted to $1,182,782, plus accrued interest of $29,132 ($1,211,914 in aggregate), calculated as the higher of the discounted expected future cash outflows required to settle the liability and the fair value of the Common Shares required to settle it upon conversion, resulting in a loss in fair value of financial liabilities at FVTPL of $28,015 for the year ended October 31, 2021.

Also on October 31, 2021, the fair value of the warrants was adjusted to $206,488, using the Black-Scholes pricing model using the following assumptions: stock price of $0.06, weighted-average exercise price of $0.15, risk-free interest rate of 1.00%, expected life of warrants of 2.75 years, expected volatility of 100% and expected dividend rate of 0%, resulting in a gain in fair value of financial liabilities at FVTPL of $126,704 for the year ended October 31, 2021.

*(Expressed in Canadian dollars)*

| | Debentures | Warrants | Other income (loss) | Total |
|---|---|---|---|---|
| | $ | $ | $ | $ |
| **Balance, October 31, 2020 and October 31, 2019** | **-** | **-** | **-** | **-** |
| Proceeds from issuance of Convertible Debentures | 1,154,767 | 333,192 | (73,959) | 1,414,000 |
| less: | | | | |
| Cash commissions | - | - | (96,720) | (96,720) |
| Broker warrants | - | - | (37,357) | (37,357) |
| Other issuance costs | - | - | (19,214) | (19,214) |
| Net proceeds from issuance of Convertible Debentures | 1,154,767 | 333,192 | (227,250) | 1,260,709 |
| Interest accrued on Debentures | 29,132 | - | (29,132) | - |
| Interest paid on Debentures | - | - | - | - |
| Change in financial liabilities at FVTPL | 28,015 | (126,704) | 98,689 | - |
| **Balance, October 31, 2021** | **1,211,914** | **206,488** | **(157,693)** | **1,260,709** |

Convertible Debentures Issued August 13, 2021

On August 13, 2021, the Company completed the second closing of a non-brokered private placement offering that had a first closing on July 30, 2021 (the "August 2021 Offering") of 1,020 unsecured convertible debenture units for gross proceeds of $1,020,000. Each unit is comprised of $1,000 in principal amount of unsecured convertible debenture and six thousand share purchase warrants for each $1,000 of principal amount, each warrant entitling the holder thereof to acquire one Common Share at an exercise price of $0.15 per Common Share (subject to adjustment) for a period of thirty-six months from the date of closing of the August 2021 Offering, expiring on August 13, 2024.

The debentures bear interest at a simple rate of 8.00% per annum, payable semi-annually in cash beginning on January 30, 2022, and maturing twenty-four months from the date of issuance, being August 13, 2023. The holders of the debenture are entitled to convert the principal amount of the debentures at any time prior to the maturity date into Common Shares at a conversion price of $0.10, subject to adjustment. As of the date that is four months and one day following the closing date, the Company will have a right to prepay or redeem the principal amount in cash, in whole or in part, at par plus accrued and unpaid interest at any time by providing a minimum of 30 days' and a maximum of 60 days' notice.

The debentures and the warrants provide for change of control as well as anti-dilution adjustments, including corporate actions of the Company as well as future equity issuances below the conversion price or exercise price, as applicable.

As a result of the anti-dilution provisions associated with the debenture, the entire convertible debenture and warrants are accounted for as derivative financial liabilities at FVTPL, as the financial liabilities cannot be settled for a fixed number of the Company's own equity instruments.

The fair value of the convertible debenture at the time of issue of $867,000 was calculated as the higher of the discounted expected future cash outflows required to settle the liability and the fair value of the Common Shares required to settle it upon conversion.

The fair value of the warrants at the time of issue was estimated at $333,192, using the Black-Scholes pricing model using the following assumptions: stock price of $0.085, weighted-average exercise price of $0.15, risk-free interest rate of 0.65%, expected life of warrants of 3 years, expected volatility of 100% and expected dividend rate of 0%.

*(Expressed in Canadian dollars)*

The excess of the fair value of the convertible debenture and warrant liabilities over the proceeds from the convertible debenture of $108,964 was recorded as a loss in fair value of financial liabilities at FVTPL.

In connection with the August 2021 Offering, the Company paid cash commissions of $35,600 and issued 336,000 compensation warrants exercisable at $0.15 for 36 months. The fair value of the compensation warrants is estimated at $14,382, using the Black-Scholes option pricing model using the following assumptions: stock price of $0.085, weighted-average exercise price of $0.15, risk-free interest rate of 0.65%, expected life of warrants of 3 years, expected volatility of 100% and expected dividend rate of 0%, and will be included in 'Warrants' in shareholders' equity in the consolidated statement of financial position.

The Company incurred total transaction costs in the amount of $49,982. The issuance costs, which include the cash commissions and broker warrants, have been immediately expensed in financing fees in the consolidated statements of loss and comprehensive loss.

On October 31, 2021, the fair value of the convertible debenture liability component was adjusted to $850,106, plus accrued interest of $17,885 ($867,991 in aggregate), calculated as the higher of the discounted expected cash outflows required to settle the liability and the fair value of the Common Shares required to settle it upon conversion, resulting in a gain in fair value of financial liabilities at FVTPL of $16,894 for the year ended October 31, 2021.

Also on October 31, 2021, the fair value of the warrants was adjusted to $150,597, using the Black-Scholes pricing model using the following assumptions: stock price of $0.06, weighted-average exercise price of $0.15, risk-free interest rate of 1.00%, expected life of warrants of 2.79 years, expected volatility of 100% and expected dividend rate of 0%, resulting in a gain in fair value of financial liabilities at FVTPL of $111,367 for the year ended October 31, 2021.

| | **Debentures** | **Warrants** | **Other income (loss)** | **Total** |
|---|---|---|---|---|
| | $ | $ | $ | $ |
| **Balance, October 31, 2020 and October 31, 2019** | **-** | **-** | **-** | **-** |
| Proceeds from issuance of Convertible Debentures | 867,000 | 261,964 | (108,964) | 1,020,000 |
| less: | | | | |
| Cash commissions | - | - | (35,600) | (35,600) |
| Broker warrants | - | - | (14,382) | (14,382) |
| Other issuance costs | - | - | - | - |
| Net proceeds from issuance of Convertible Debentures | 867,000 | 261,964 | (158,946) | 970,018 |
| Interest accrued on Debentures | 17,885 | - | (17,885) | - |
| Interest paid on Debentures | - | - | - | - |
| Change in financial liabilities at FVTPL | (16,894) | (111,367) | 128,261 | - |
| **Balance, October 31, 2021** | **867,991** | **150,597** | **(48,570)** | **970,018** |

*(Expressed in Canadian dollars)*

## 12. SHARE CAPITAL

**Authorized**
An unlimited number of the following shares:

Common Shares – voting, no par value
Preferred Shares – issued in connection with the Transaction (Note 19)

**Issued**
9,313,447 Preferred Shares as at October 31, 2021 and 2020

Common Shares issued are as follows:

| | Number of shares # | $ |
|---|---|---|
| **Balance, October 31, 2019** | **72,800,100** | **5,251,972** |
| Shares issued pursuant to RTO (Note 7) | 9,313,447 | 1,490,152 |
| Shares issued for debt (3) | 1,608,026 | 303,228 |
| Shares issued for services (1) | 900,000 | 90,000 |
| Shares issued on vesting of restricted share units (Note 15) | 614,167 | 98,267 |
| Stock-based compensation (2) | 1,000,000 | 100,000 |
| **Balance, October 31, 2020** | **86,235,740** | **7,333,619** |
| Shares issued for debt (4) | 1,925,300 | 288,795 |
| Shares issued for services (5) | 978,023 | 120,850 |
| Shares issued on vesting of restricted share units (Note 15) | 6,240,263 | 817,529 |
| **Balance, October 31, 2021** | **95,379,326** | **8,560,793** |

(1) On December 15, 2019, March 15, 2020 and June 15, 2020, the Company issued 300,000 Common Shares, respectively, to a consultant at a price per share of $0.10, for advisory services rendered to the Company.

(2) On December 1, 2019, the Company issued 1,000,000 Common Shares to the Company's Chief Regulatory Officer, in accordance with his terms of employment. An amount of $100,000 was included within stock-based compensation expense in the consolidated statements of loss and comprehensive loss for the year ended October 31, 2020.

(3) On September 16, 2020, the Company issued 1,340,500 Common Shares in settlement of $263,100 in debt. On October 14, 2020, the Company issued 267,526 Common Shares in settlement of $40,128 in debt. In total, the Company issued 1,608,026 Common Shares in settlement of $303,228 in debt during the year ended October 31, 2020, including a Director that received a total of 1,215,500 Common Shares in settlement of $243,100 in debt.

(4) On January 29, 2021, the Company issued 1,925,300 Common Shares in settlement of $288,795 in debt, including Directors of the Company that received a total of 933,333 Common Shares in settlement of $140,000 in consulting fees.

*(Expressed in Canadian dollars)*

(5) During the year ended October 31, 2021, the Company issued 978,023 Common Shares valued at $120,850 to consultants for services rendered.

## 13. WARRANTS

Upon exercise, all Warrants that have been issued by the Company entitle the holders thereof to receive an equivalent number of Common Shares as the Warrants that were exercised.

The following table reflects the continuity of warrants:

| | Number of warrants | Weighted average exercise price |
|---|---|---|
| | # | $ |
| **Balance, October 31, 2019** | **-** | **-** |
| Issued pursuant to RTO (Note 7) | 1,103,250 | 0.70 |
| Issued as part of September 2020 convertible debenture financing (Note 11) | 615,000 | 0.23 |
| **Balance, October 31, 2020** | **1,718,250** | **0.53** |
| Issued as part of March 2021 convertible debenture financing (Note 11) | 533,333 | 0.15 |
| Issued as part of July 2021 convertible debenture financing (Note 11) | 951,200 | 0.15 |
| Issued as part of August 2021 convertible debenture financing (Note 11) | 336,000 | 0.15 |
| **Balance October 31, 2021** | **3,538,783** | **0.34** |

As at October 31, 2021, the following warrants were issued and outstanding:

| Number of warrants | Issue date fair value | Exercise price | Expiry date |
|---|---|---|---|
| # | $ | $ | |
| 499,750 | 3,739 | 0.70 | February 6, 2022 (1) |
| 603,500 | 4,919 | 0.70 | February 21, 2022 (1) |
| 410,000 | 37,477 | 0.20 | September 16, 2023 |
| 205,000 | 16,035 | 0.30 | September 16, 2023 |
| 533,333 | 34,605 | 0.15 | March 18, 2024 |
| 951,200 | 37,357 | 0.15 | July 30, 2024 |
| 336,000 | 14,382 | 0.15 | August 13, 2024 |
| **3,538,783** | **148,514** | | |

(1) On January 20, 2021, the Company extended the expiry date of an aggregate of 1,103,250 previously issued warrants for one additional year. In total, an additional $6,986 in stock-based compensation expense relating to Warrants was included in profit or loss for the year ended October 31, 2021 related to this extension (2020 – $nil) and credited to 'Warrants' in shareholders' equity in the consolidated statement of financial position.

*(Expressed in Canadian dollars)*

As at October 31, 2020, the following Warrants were issued and outstanding:

| Number of warrants | Issue date fair value | Exercise price | Expiry date |
|---|---|---|---|
| # | $ | $ | |
| 499,750 | 757 | 0.70 | February 6, 2021 |
| 603,500 | 915 | 0.70 | February 21, 2021 |
| 410,000 | 37,477 | 0.20 | September 16, 2023 |
| 205,000 | 16,035 | 0.30 | September 16, 2023 |
| **1,718,250** | **55,184** | | |

Refer to Note 11 for details on warrants measured at FVTPL.

## 14. STOCK OPTIONS

The Company's incentive stock option plan was adopted to provide the Company with a share-related mechanism to attract, retain and motivate qualified directors, officers, employees and consultants and to reward them for their contributions toward creating shareholder value through the achievement of the short and long-term goals of the Company.

The following table reflects the continuity of stock options issued by the Company (the "Options"):

| | Number of options | Weighted average exercise price |
|---|---|---|
| | # | $ |
| **Balance, October 31, 2019** | **2,500,000** | **0.10** |
| Issued pursuant to RTO (Note 7) | 1,060,000 | 0.46 |
| **Balance, October 31, 2020** | **3,560,000** | **0.21** |
| Granted (1 and 2) | 3,100,000 | 0.16 |
| Expired (3) | (1,060,000) | 0.46 |
| **Balance, October 31, 2021** | **5,600,000** | **0.13** |

(1) On January 7, 2021, 500,000 Options were granted to a consultant of the Company at an exercise price of $0.20 per Common Share, with 34% vesting on the grant date, and 34% and 33% vesting three and six months following the grant date respectively, which expire one year following the grant date.

(2) On February 8, 2021, 2,600,000 Options were granted to certain directors, officers, employees and consultants of the Company at an exercise price of $0.15 per share. The Options all vest on the four months following the grant date and expire on February 8, 2026.

(3) On April 14, 2021, 80,000 Options with an exercise price of $0.50 per Common Share expired. On August 15, 2021, 230,000 Options with an exercise price of $1.30 per Common Share expired. On September 15, 2021, 750,000 Options with an exercise price of $0.20 per Common Share expired.

*(Expressed in Canadian dollars)*

As at October 31, 2021, the following Options were outstanding and exercisable:

| | Outstanding | | | Exercisable | |
|---|---|---|---|---|---|
| **Exercise prices** | **Number outstanding** | **Weighted average remaining contractual life** | **Weighted average outstanding exercise price** | **Number vested** | **Weighted average vested exercise price** |
| $ | # | (in years) | $ | # | $ |
| $0.10 | 2,500,000 | 3.17 | 0.10 | 2,500,000 | 0.10 |
| $0.15 | 2,600,000 | 4.28 | 0.15 | 2,600,000 | 0.15 |
| $0.20 | 500,000 | 0.19 | 0.20 | 500,000 | 0.20 |
| | **5,600,000** | **3.42** | **0.13** | **5,600,000** | **0.13** |

The following table reflects the weighted-average fair value of Options for the periods presented and the related Black-Scholes option pricing model inputs that were used in the calculations:

| | **Year ended October 31, 2021** | Year ended October 31, 2020 |
|---|---|---|
| Stock options granted | 3,100,000 | 1,060,000 |
| Weighted average fair value | 0.09 | 0.04 |
| Weighted-average exercise price | 0.16 | 0.46 |
| Weighted-average market price at date of grant | 0.14 | 0.16 |
| Expected life of stock options (years) | 4.35 | 1.06 |
| Expected stock price volatility | 100% | 100% |
| Risk-free interest rate | 1.40% | 0.27% |
| Expected dividend yield | 0% | 0% |

The underlying expected stock price volatility is based on historical data of similar companies, as the Company has limited historical data itself on which it could be based.

The risk-free interest rate is based on the yield of a Government of Canada benchmark bond in effect at the time of grant with an expiry commensurate with the expected life of the Options.

In total, $275,078 of stock-based compensation expense relating to Options was included in the consolidated statements of loss and comprehensive loss or capitalized in inventory for the year ended October 31, 2021 (2020 – $29,008) and credited to contributed surplus.

## 15. RESTRICTED SHARE UNITS

On June 1, 2020, the Company adopted a Restricted Share Unit ("RSU") plan (the "RSU Plan"), pursuant to which the Company may issue RSUs to various participants. The purpose of the RSU Plan is to provide the Company with a share-related mechanism to attract, retain and motivate qualified directors, officers, employees and consultants and to reward them for their contributions toward creating shareholder value through the achievement of the short and long-term goals of the Company.

*(Expressed in Canadian dollars)*

Upon vesting, the RSU holder is entitled to receive payment from the Company in settlement of such vested RSUs, in a number of Common Shares, issued from treasury, equal to the number of RSUs being settled.

The following table reflects the continuity of RSUs:

| | **Number of RSUs** | **Weighted-average market price at date of grant** |
|---|---|---|
| | # | $ |
| **Balance, October 31, 2019** | **-** | **-** |
| Granted (1)(2) | 2,456,667 | 0.16 |
| Vested | (739,167) | 0.16 |
| **Balance, October 31, 2020** | **1,717,500** | **0.16** |
| Granted (3) | 4,522,763 | 0.12 |
| Vested | (6,240,263) | 0.13 |
| **Balance, October 31, 2021** | **-** | **n/a** |

(1) On June 1, 2020, 1,706,667 RSUs were granted to officers, employees and certain consultants of the Company, of which 1,540,000 vest quarterly over a twelve-month period and 166,667 vested on September 18, 2020.

(2) On September 9, 2020, 750,000 RSUs were granted to certain consultants of the Company, which vest quarterly over a twelve-month period.

(3) On January 29, 2021, 4,522,763 RSUs were granted to officers, employees and certain consultants of the Company, with 1,422,138 vesting on the grant date and the remainder vesting quarterly over two quarters from the grant date.

In total $652,300 of stock-based compensation expense relating to RSUs was included in the consolidated statements of loss and comprehensive loss or capitalized in inventory for the year ended October 31, 2021 (2020 – $nil) and credited to contributed surplus.

## 16. REVENUES FROM THE SALES OF GOODS

On January 26, 2021, the Company announced that it had signed a binding term sheet with Vortex Cannabis Inc. ("Vortex"), setting out the terms of a service agreement (the "Service Agreement") whereby Vortex will sell products produced by Molecule to the provincial retailers of cannabis products (the "Provincial Retailers"). The Service Agreement allows Molecule to begin selling its line of CIBs throughout Canada, starting initially with Ontario and Quebec. Under the terms of the Service Agreement, Molecule will pay a percentage of revenues to Vortex for its services. The initial term of the Service Agreement was six months. The term was subsequently extended for an additional six months and then indefinitely, while allowing the Company to end the Service Agreement with sixty days' notice.

The Company's Licence allows the Company to produce CIBs and sell them to other LPs. A Standard Processing Licence, such as the License, requires an amendment to allow the holder thereof to sell cannabis products directly to Provincial Retailers (a "Sales Amendment"). Rather than waiting until a Sales Amendment is issued to the Company, the Service Agreement allows the Company to bring CIBs to market through Vortex, while completing its own sales amendment application.

*(Expressed in Canadian dollars)*

Total revenue from the sale of goods consists entirely of sales to Vortex for the year ended October 31, 2021, and is presented net of provisions for sales returns and price concessions. During the year ended October 31, 2021, the Company reserved or realized $15,511 (2020 – $nil) for sales provisions and price concessions. The Company has not yet incurred excise taxes in its net revenues as those taxes are incurred by the LP that sells to the Provincial Retailers.

## 17. SELECTED OPERATING EXPENSES BY NATURE

The following table disaggregates the following operating expenses as presented on the consolidated statements of loss and comprehensive loss into specified classifications based upon their nature:

| | Management and consulting fees | Salaries and benefits | Office and facilities | Depreciation and amortization | Stock-based compensation | Total |
|---|---|---|---|---|---|---|
| | $ | $ | $ | $ | $ | $ |
| Operating expenses | 437,061 | 402,904 | 425,493 | 202,517 | 989,526 | 2,457,501 |
| Capitalized to inventory | 759 | 217,532 | 98,243 | 364,544 | 65,689 | 746,767 |
| **Total for the year ended October 31, 2021** | **437,820** | **620,436** | **523,736** | **567,061** | **1,055,215** | **3,204,268** |

## 18. RELATED PARTY TRANSACTIONS

*Transactions with key management personnel*

Related parties include the Board of Directors and key management personnel, as well as close family members and enterprises that are controlled by these individuals as well as certain persons performing similar functions. Unless otherwise stated, none of these transactions incorporated special terms and conditions and no guarantees were given or received.

Remuneration of directors and key management personnel of the Company and office and facilities lease amounts paid or payable to a company related to a Director of the Company (Note 10) was as follows:

| For the year ended October 31, | 2021 | 2020 |
|---|---|---|
| $ | **$** | $ |
| Salaries | **86,799** | 95,000 |
| Consulting fees (1) | **256,071** | 80,000 |
| Stock-based compensation | **381,449** | 268,228 |
| Total remuneration | **724,319** | 443,228 |
| Office and facilities | **88,750** | 60,000 |

(1) As at October 31, 2021, unpaid consulting fees and office and facilities lease payments in the aggregate amount of $74,950 are owed to management and a company related to a Director and have been included in accounts payable and accrued liabilities (2020 – $139,000). The amounts owing are unsecured, non-interest bearing and due on demand.

See Notes 10, 11 and 12 additional related party disclosure.

*(Expressed in Canadian dollars)*

## 19. CONTINGENCIES

Preferred Share Issuance

Pursuant to the terms of the Arrangement Agreement (Note 1) the Company created and issued 9,313,447 preferred shares (the "Preferred Shares"). The purpose of the Preferred Shares is to provide the shareholders of the Company other than original OpCo shareholders with a right to receive, on a pro rata basis, an economic benefit, subject to an aggregate maximum of up to $500,000, in the event that any of the Company's remaining mining royalties are triggered and generate revenue within a maximum period of five (5) years from the date of the issuance of the Preferred Shares. The Preferred Shares provide that, if triggered, the Preferred Shares will be redeemable, on a pro rata basis, for cash up to an aggregate maximum of $500,000. The Preferred Shares do not otherwise have any rights or recourses. As these royalties relate to properties with no verified resources and as no other triggering event has occurred, the Preferred Shares are valued at $nil in the consolidated financial statements.

## 20. INCOME TAXES

*Provision for income taxes*

The Company's expected tax rate is different from the combined federal and provincial income tax rate in Canada. The differences result from the following elements:

| For the year ended October 31 | **2021** | 2020 |
|---|---|---|
| | **$** | $ |
| Earnings before income taxes | **(4,227,353)** | (3,326,994) |
| Statutory tax rate | **26.50%** | 26.50% |
| Expected tax benefit resulting from the loss | **(1,120,000)** | (882,000) |
| Adjustments for the following items: | | |
| Non-deductible items | **254,000** | 104,000 |
| Changes in estimates and other | **(32,000)** | 15,000 |
| Change in deferred tax assets not recognized | **898,000** | 763,000 |
| Income tax provision (recovery) | **-** | - |

*Deferred income tax*

Deferred income tax assets in excess of deferred income tax liabilities have not been recognized in respect of the following attributes because it is not probable that future taxable profit will be available against which the Company can use the benefits:

| As at | **October 31, 2021** | October 31, 2020 |
|---|---|---|
| | **$** | $ |
| Non-capital loss carry-forwards | **5,470,000** | 15,135,000 |
| Share issuance costs | **847,000** | 372,000 |
| Capital assets | **159,000** | - |
| Mineral properties | **5,912,000** | 5,912,000 |
| | **12,388,000** | 21,419,000 |

*(Expressed in Canadian dollars)*

*Tax loss carry-forwards*

The Company has approximate non-capital losses available to reduce future years' federal and provincial taxable income which expires as follows:

| Year of Expiry | Amount |
|---|---|
| | $ |
| 2038 | - |
| 2039 | 857,000 |
| 2040 | 1,431,000 |
| 2041 | 3,109,000 |
| | **5,397,000** |

## 21. SUBSEQUENT EVENTS

Subsequent to October 31, 2021, the Company issued 1,692,000 Common Shares valued at $240,690 for services rendered, issued 335,577 Common Shares to settle $33,990 of debt and issued 575,000 Options exercisable at $0.15 per Common Share with a two-year term to consultants of the Company.

Also subsequent to October 31, 2021, 500,000 Options with an exercise price of $0.20 per Common Share expired and 1,103,250 warrants with an exercise price of $0.70 per Common Share expired.