Phyto Extractions Inc.
(Formerly Adastra Labs Holdings Ltd.)

MANAGEMENT DISCUSSION AND ANALYSIS

For the three and six months ended June 30, 2021, and 2020

The following management discussion and analysis ("MD&A") of the financial condition and results of operations of Phyto Extractions Inc. (formerly Adastra Labs Holdings Ltd.) constitutes management's review of the factors that affected the Company's financial and operating performance for the three and six months ended June 30, 2021 and 2020. This MD&A has been prepared in compliance with the requirements of National Instrument 51-102 – Continuous Disclosure Obligation. This MD&A should be read in conjunction with Phyto's audited financial statements and related notes for the year ended December 31, 2020 and period ended December 31, 2019, which have been prepared in accordance with International Financial Reporting Standards ("IFRS").

All monetary amounts in the MD&A are expressed in Canadian dollars, except number of shares, or as otherwise indicated.

Additional information regarding the Company is available on SEDAR at www.sedar.com, and the Company's website www.adastralabs.ca. This MD&A has been prepared effective as of August 30, 2021.

FORWARD-LOOKING STATEMENTS

This MD&A includes forward-looking statements that are based upon current expectations, which involve risks and uncertainties associated with our business and the environment in which the business operates. Any statements contained herein that are not statements of historical fact may be deemed to be forward looking statements, including those identified by the expressions "considers", "plans", "expects" or "does not expect", "is expected", "budget", "scheduled", "estimates", "forecasts", "intends", "anticipates" or "does not anticipate", or "believes", or variations of such words and phrases or statements that certain actions, events or results "may", "could", "would", "might" or "will be taken", "occur" or "be achieved", or the negative of these terms or comparable terminology. In this document, certain forward-looking statements are identified by words including "may", "future", "expected", "will", "intends", and "estimates". By their very nature forward-looking statements involve known and unknown risks, uncertainties and other factors, which may cause the actual results, performance or achievements of the Company to be materially different from any future results, performance, or achievements expressed or implied by the forward-looking statements. The Company provides no assurance that forward-looking statements will prove to be accurate, as actual results and future events could differ materially from those anticipated in such statements.

DESCRIPTION OF THE BUSINESS

Phyto Extractions Inc. (formerly Adastra Labs Holdings Ltd.) ("Phyto" or the "Company") was incorporated under the laws of the province of British Columbia on October 14, 1987. The Company changed its name to Adastra Labs Holdings Ltd. (formerly Arrowstar Resources Ltd.), on December 19, 2019. The Company is an extraction and processing solutions company. The Company's mission is to develop and deploy large-scale cannabis and hemp extraction technologies and provide turn-key processing solutions to help licensed standard and micro-cultivators maximize the value of every harvest. The Company is listed on the Canadian Securities Exchange ("CSE") under the symbol "XTRX". The Company's registered and records office is 5451 275th Street, Langley City, British Columbia, V4W 3X8.

On April 9, 2021, the Company consolidated the Company's issued share capital on a ratio of three (3) old common shares for every one (1) new post-consolidated common share. All current and comparative references to the number of common shares, weighted average number of common shares, loss per share, stock options and warrants have been restated to give effect to this Share Consolidation. Additionally, the Company changed its name to Phyto Extractions Inc.

On October 19, 2019, Health Canada issued a Analytical testing license on the Company's facility to Chemia Analytics Inc., ("Chemia"). Chemia is a wholly owned subsidiary of the Company. On March 13, 2020, Health Canada issued a Standard Processing License to Adastra labs Inc. ("Labs"). Labs is a wholly owned subsidiary of the Company.

On December 20, 2019, Arrowstar Resources Ltd. ("Arrowstar") acquired all of the issued and outstanding common shares of Adastra Labs Holdings Ltd. ("Adastra"), a private British Columbia cannabis extraction and processing solutions company incorporated on June 18, 2018. The acquisition was completed by entering into a share exchange agreement whereby the parties completed a business combination by way of a transaction that constituted a reverse takeover ("RTO") of the Company by Adastra (the "Transaction").

The Transaction was accounted for as an RTO of Arrowstar by Adastra for accounting purposes, with Adastra being identified as the accounting acquirer, and accordingly, these financial statements are a continuation of Adastra. The net assets of Arrowstar at the date of the RTO are deemed to have been acquired by Adastra. This MD&A includes the results of operations of Arrowstar since December 20, 2019. At the time of the transaction the Company changed its financial year end from April 30 to December 31.

On March 16, 2021, the Company announced a 51% acquisition of Phyto Extractions™ brands (with a right of first refusal for the remaining 49% interest), with the Company initially agreeing to pay 38,400,000 common shares priced at $1.10 per share, or $42,240,000 to acquire the controlling interest noting that the acquisition was subject to due diligence, the completion of a definitive agreement, and regulatory approvals. On August 24, 2021, the Company announced the acquisition would be revised to a 100% interest on closing date and that the parties were working to finalize definitive terms and anticipate to sign a definitive share purchase agreement on or before September 15, 2021.

In March 2020, the World Health Organization declared COVID-19 a global pandemic. This contagious disease outbreak, which has continued to spread, and related adverse public health developments, have adversely affected workforces, economies, and financial markets globally, which may lead to economic downturn. The extent of the impact of COVID-19 on the Company's operational and financial performance will depend on various developments, including the duration and magnitude of the outbreak, and the impact on customers, employees and vendors, all of which are uncertain and cannot be predicted at this point.

REVERSE ACQUISITION

On December 20, 2019, Arrowstar and Adastra completed the Transaction which constituted a reverse acquisition.

The Transaction resulted in the shareholders of Adastra obtaining control of the combined entity by obtaining control of the voting rights, governance and management decision making processes, and the resulting power to govern the financial and operating policies of the combined entity.

The transaction constitutes an RTO of Arrowstar by Adastra and has been accounted for as a reverse acquisition transaction in accordance with the guidance provided in IFRS 2, *Share-based payments*. As Arrowstar did not qualify as a business according to the definition in IFRS 3, the RTO does not constitute a business combination; rather it is treated as an issuance of common shares by Adastra for the net assets of Arrowstar and Arrowstar's public listing, with Adastra as the continuing entity. Accordingly, no goodwill was recorded with respect to the transaction as it does not constitute a business combination.

For accounting purposes, Adastra was treated as an accounting parent company (legal subsidiary) and Arrowstar has been treated as the accounting subsidiary (legal parent) in the financial statements and MD&A. As Adastra was deemed to be the acquirer for accounting purposes, its assets, liabilities and operations since incorporation are included in these financial statements at their historical carrying values. Arrowstar's results of operations have been included from December 20, 2019.

	December 20, 2019
Assets and (liabilities) of Arrowstar acquired	$
Cash	111,496
Receivables	10,802
Other assets	7,504
Accounts payable	(356,384)
Net liabilities acquired	**(226,582)**
Consideration paid in RTO of Arrowstar	
Common shares (7,218,678 common shares at $0.15 fair value per share)	1,082,802
Listing expense	**1,309,384**

The Transaction was measured at the fair value of the shares that Adastra would have had to issue to the shareholders of Arrowstar to give the shareholders of Arrowstar the same percentage equity interest in the combined entity that results from the reverse acquisition had it taken the legal form of Adastra acquiring Arrowstar.

OVERALL PERFORMANCE

As at June 30, 2021, the Company had a mortgage payable liability and was in a negative working capital position. The Company's focus for the six months ended June 30, 2021, included the expansion of its centralized processing facility in Langley, BC. The Company received their Analytical Testing License on October 19, 2019 and received their Standard Processing License on March 13, 2020. The Company received an amendment to its Standard Processing license authorizing the sale of cannabis extract, cannabis edibles and cannabis topicals on March 13, 2021 and their Research license for organoleptic testing on April 16, 2021.

Operations and Facility

As of the date of this MD&A, the Company focuses on the generation of revenue through two primary activities, wholesale activities and tolling services related to the production of cannabis extracts and related cannabis products.

As of April 23, 2020 the Company has completed the commissioning and commencement of operations at its 13,000 square feet facility in Langley, British Columbia (the "Langley Facility"). It currently operates a primary supercritical CO_2 extraction line for the production of crude cannabis/hemp extracts, wiped film short path distillation plant for the production of high potency cannabis distillate, a formulation, filling line and packaging line for the manufacture of tincture bottles and vaporizer products as consumer-packaged goods.

During September 2020, the Company installed and commissioned its cryo-ethanol extraction production line that triples the Company's cannabis oil production capacity while reducing overall costs. This production line allows the re-purposing of the CO_2 supercritical extraction line for other cannabis concentrate products such as high terpene full spectrum extracts.

During the quarter ending December 31, 2020, the Company installed and commissioned its hydrocarbon extraction production line using propane and butane or other solvent mixes. This production line allows the company to extract over 400 kilograms per day of cannabis biomass into a variety of high value and rare hydrocarbon cannabis concentrate products.

Wholesale Bulk Extracts Production

During the six months ended June 30, 2021, the Company continued processing their own inventory of dried cannabis through supercritical CO_2 and cryo-ethanol extraction lines and distillation lines for the purpose of selling the resulting bulk cannabis concentrates to licensed clients or using it to fulfill contract manufacturing orders, primarily for vaporizing cartridges. The Company has procured all of its bulk shipments of dried cannabis for its wholesale production lines from various licensed cultivators under the Cannabis Act. During the three and six months ended June 30, 2021, the Company recognized revenue of $1,241,763 and $1,830,901, respectively.

Contract Manufacturing

For the six months ending June 30, 2021, the Company has received and completed purchase orders from CannMart Inc., a majority-owned subsidiary of Namaste Technologies Inc., for vaporizing formulation, filling and packaging for 168,416 units and testing and purchase orders from Radient Technologies (Cannabis) Inc. for 74,083 kg of bulk distillate orders.

SELECTED FINANCIAL INFORMATION

Results of Operations

For the three months ended June 30, 2021 compared with the three months ended June 30, 2020

For the three months ended June 30, 2021, the Company had operating expenses of $647,428 and a loss and comprehensive loss of $509,890, compared to operating expenses of $553,151 and a loss and comprehensive loss of $467,584 during the three months ended June 30, 2020.

Revenues increased to $1,241,763 during the three months ended June 30, 2021, compared to $428,355 during the three months ended June 30, 2020, from increased processing of cannabis biomass for third-party licensed producers, in-house distillate production, and hydrocarbon extraction.

Cost of sales increased to $696,122 during the three months ended June 30, 2021, compared to $213,236 during the three months ended June 30, 2020, and consists of biomass, labour, solvents and an allocation of production overheads such as facility costs and amortization of production equipment.

This increase in operating expenses and loss and comprehensive were the result of the Company's expenses with respect to wages and salaries having increased as the Company expanded its production efforts. The most significant changes in operating expenses and other expenses were as follows:

- Advertising and promotion decreased to $105,165 during the three months ended June 30, 2021, compared to $206,704 during the three months ended June 30, 2020, due to the Company developing a more focused investor awareness campaign.

- Accretion decreased to $nil during the three months ended June 30, 2021, compared to $22,549 during the three months ended June 30, 2020, due to the conversion of convertible debentures.

- Office expenses decreased to $60,065 during the three months ended June 30, 2021, compared to $93,696 during the three months ended June 30, 2020, as the Company moved past its startup phase and into regular production.

- Wages and salaries increased to $311,799 during the three months ended June 30, 2021, compared to $86,525 during the three months ended June 30, 2020, due to increased hiring activity and production output for the Company in their initial year of operations.

- Interest expense decreased to $48,141 during the three months ended June 30, 2021, compared to $130,488 during the three months ended June 30, 2020, due to the conversion of the convertible debentures.

- During the three months ended June 30, 2021, the Company incurred impairment of property, plant and equipment of $150,000 related to an ERP software in development that the Company determined would not be completed. No impairment of property, plant and equipment was recorded during the three months ended June 30, 2020.

- During the three months ended June 30, 2021, the Company recognized a write-down of inventory of $210,001 in accordance with IFRS requirements to value inventory at the lower of cost or net realizable value. No write-down of inventory was recorded during the three months ended June 30, 2020.

For the six months ended June 30, 2021 compared with the six months ended June 30, 2020

For the six months ended June 30, 2021, the Company had operating expenses of $1,115,199 and loss and comprehensive loss of $873,402, compared to operating expenses of $3,756,374 and loss and comprehensive loss of $3,810,618 during the six months ended June 30, 2020.

Revenues increased to $1,830,901 during the six months ended June 30, 2021, compared to $428,355 during the six months ended June 30, 2020, from increased processing of cannabis biomass for third party licensed producers and in-house distillate production, and hydrocarbon extraction.

Cost of sales increased to $1,098,338 during the six months ended June 30, 2021, compared to $213,236 during the six months ended June 30, 2020, and consists of biomass, labour, solvents and an allocation of production overheads such as facility costs and amortization of production equipment.

The decrease in operating expenses and loss and comprehensive loss were the result of the Company's expenses with respect to advertising and promotion, accretion, office, professional fees and consulting, and share-based payments having decreased as the Company moved from its startup phase into production and expansion of its business during the six months ended June 30, 2021. The most significant changes in operating expenses and other expenses were as follows:

- Advertising and promotion decreased to $135,352 during the six months ended June 30, 2021, compared to $260,521 during the six months ended June 30, 2020, due to the Company developing a more focused investor awareness campaign.

- Accretion decreased to $nil during the six months ended June 30, 2021, compared to $43,637 during the six months ended June 30, 2020, due to the conversion of convertible debentures.

- Office expenses decreased to $150,109 during the six months ended June 30, 2021, compared to $239,481 during the six months ended June 30, 2020, as the Company moved past its startup phase and into regular production.

- Professional fees and consulting decreased to $207,650 during the six months ended June 30, 2021, compared to $395,901 during the six months ended June 30, 2020, primarily due to the decrease of consultants needed to prepare the extraction process, commissioning of equipment and testing.

- Research expenses increased to $46,664 during the six months ended June 30, 2021, compared to $nil during the six months ended June 30, 2020, due to increased production and testing.

- Share-based payments decreased to $nil during the six months ended June 30, 2021, compared to $2,537,300 during the six months ended June 30, 2020, as it was a non-cash expense representing the fair value of options granted during the six months ended June 30, 2020. No stock option grants occurred during the six months ended June 30, 2021.

- Wages and salaries increased to $493,835 during the six months ended June 30, 2021, compared to $198,987 during the six months ended June 30, 2020, due to increased hiring activity and production output related to the Langley Facility.

- Interest expense decreased to $107,354 during the six months ended June 30, 2021, compared to $272,323 during the six months ended June 30, 2020, due to the conversion of convertible debentures.

- During the six months ended June 30, 2021, the Company incurred impairment of property, plant and equipment of $150,000 related to an ERP software in development that the Company determined would not be completed. No impairment of property, plant and equipment was recorded during the six months ended June 30, 2020.

- During the six months ended June 30, 2021, the Company recognized a write-down of inventory of $291,512 in accordance with IFRS requirements to value inventory at the lower of cost or net realizable value. No write-down of inventory was recorded during the six months ended June 30, 2020.

SUMMARY OF QUARTERLY RESULTS

The following table shows results from the previous eight fiscal quarters:

Period ending	Revenue	Income (loss) and comprehensive income (loss)	Weighted average number of shares	Basic and diluted income (loss) per share
	$	$	#	$
June 30, 2021	1,241,763	(509,890)	43,334,100	(0.01)
March 31, 2020	589,138	(363,512)	43,334,100	(0.01)
December 31, 2020	1,245,097	90,470	39,695,235	-
September 30, 2020	825,903	(3,895,719)	38,511,533	(0.10)
June 30, 2020	428,355	(467,584)	36,685,635	(0.01)
March 31, 2020	-	(3,343,034)	36,571,004	(0.09)
December 31, 2019 *	-	(1,785,818)	27,495,882	(0.06)
October 31, 2019	-	(333,290)	27,046,111	(0.01)

**On December 20, 2019, the Company changed its fiscal year end from April 30 to December 31. Therefore, the period ending December 31, 2019 includes only two months of the Company's operations.*

The Company's loss and comprehensive loss for the three months ended June 30, 2021, was $509,890. The increase of revenues to $1,241,763 are driven by the commencement of operations at the Langley Facility resulting in increased production and sales. The Company recognized impairment of property, plant and equipment of $150,000 related to an ERP software in development that the Company determined would not be completed and a write-down of inventory of $210,001 relating to some older inventory that was deemed to have lower value.

The Company's loss and comprehensive loss for the three months ended March 31, 2021, was $363,512. Revenues of $589,138 represent the Company's fourth quarter of production revenue. The Company recognized a write-down of inventory of $81,511, representing the total fair market adjustments to inventory, and a gain on the settlement of accounts payable of $57,500 representing the value of consulting fees that were forgiven.

The Company's income and comprehensive income for the three months ended December 31, 2020 was $90,470. Revenues of $1,245,097 represent the Company's third quarter of production revenue.

The Company's loss and comprehensive loss for the three months ended September 30, 2020, was $3,895,719. Revenues of $825,903 represent the Company's second quarter of production revenue. The Company also incurred $2,795,200 in non-cash expenses related to stock-based payments to directors, officers, employees and consultants of the Company.

The Company's loss and comprehensive loss for the period ended March 31, 2020, was $3,343,034. The incurred loss and comprehensive loss was due to increased activity and expenditures related to the Company's efforts to expand the business, build its facility, and obtain a public listing.

The Company's loss and comprehensive loss for the period ended December 31, 2019, was $1,785,818. The incurred loss and comprehensive is due to increased activity and expenditures related to the Company's efforts to expand the business, build its facility, and obtain a public listing. The Company paid non-cash consideration of approximately $1,300,000 related to the acquisition of Arrowstar.

LIQUIDITY AND CAPITAL RESOURCES

The Company's objectives when managing its liquidity and capital structure are to support further advancement of the Company's business objectives and existing service offerings, as well as to ensure that the Company is able to meet its financial obligations as they come due.

Cash and working capital

As at June 30, 2021 the Company has working capital deficit of $709,999 (December 31, 2020 – working capital surplus of $105,093).

Cash flow activity

Cash used in operating activities of $239,532 during the six months ended June 30, 2021 was the result of the Company's collection of accounts receivable, offset by purchases of inventory and payments of accounts payable. Cash used in operating activities of $998,851 during the six months ended June 30, 2020 was the result of the Company's accumulation of accounts receivable, purchases of inventory and increased expenditures for advertising and promotion and professional fees and consulting, offset by the accumulation of accounts payable.

Cash used in financing activities of $116,592 during the six months ended June 30, 2021 was the result of interest payments of the mortgage payable by the Company. Cash provided by financing activities of $153,296 during the six months ended June 30, 2020 was the result of subscriptions received by the Company, offset by borrowing costs and interest payments on the mortgage payable.

Cash used in investing activities of $348,596 during the six months ended June 30, 2021 and $590,706 during the six months ended June 30, 2020 was the result of cash payments made for the acquisition of property, plant and equipment.

Capital resource management

The Company defines capital as the components of shareholders' equity. The Company's objectives when managing capital are to support further advancement of the Company's business objectives, as well as to ensure that the Company is able to meet its financial obligations as they come due.

The Company manages its capital structure to maximize its financial flexibility making adjustments to it in response to changes in economic conditions and the risk characteristics of the underlying assets and business opportunities. The Company relies on the expertise of the Company's management to sustain the future development of the business. Management reviews its capital management approach on an ongoing basis and believes that this approach, given the relative size of the Company, is reasonable. There were no changes in the Company's approach to capital management during the period ended June 30, 2021. The Company is not subject to externally imposed capital requirements.

SHARE CAPITAL INFORMATION

The Company's authorized share capital consists of an unlimited number of voting common shares without par value. The Company had the following securities outstanding as at June 30, 2021, and the date of this MD&A:

	June 30,2021	Date of this MD&A
	#	#
Common shares	43,334,100	43,334,100
Stock options	3,400,001	2,800,001
Warrants	8,335,992	8,335,992
Fully diluted	55,070,093	54,470,093

Share issuances

There were no share issuances during the six months ended June 30, 2021.

(i) During the six months ended June 30, 2021, the Company recorded a subscription received for 122,727 units at $1.10 per unit for gross proceeds of $135,000. Each unit will consist of one common share and one transferable common share purchase warrant. These proceeds are included as subscriptions received and will be applied against a future financing.

During the year ended December 31, 2020, the Company had the following share transactions:

(i) On January 17, 2020, the Company issued 189,934 units on conversion of $250,000 of principal and $6,411 of accrued interest of the convertible debenture. Each unit consists of one common share of the Company and one share purchase warrant exercisable at $2.25 for two years from the date of conversion. No value was attributed to the warrant component of the units issued.

(ii) On January 27, 2020, the Company issued 266,760 units on conversion of $350,000 of principal and $10,126 of accrued interest of the convertible debenture. Each unit consists of one common share of the Company and one share purchase warrant exercisable at $2.25 for two years from the date of conversion. No value was attributed to the warrant component of the units issued.

(iii) On July 10, 2020, the Company issued 200,589 units on conversion of $250,000 of principal and $20,795 of accrued interest of the convertible debenture. Each unit consists of one common share of the Company and one share purchase warrant exercisable at $2.25 for two years from the date of conversion. No value was attributed to the warrant component of the units issued.

(iv) On July 13, 2020, the Company completed a non-brokered private placement whereby 3,882,667 units were issued at a price of $0.90 per unit for gross proceeds of $3,494,400. Each unit consists one common share and one common share purchase warrant with each warrant exercisable into one common share at an exercise price of $1.50 until July 13, 2022.

In conjunction with the financing, finders' fees of $21,600 in cash were paid and 24,067 compensation options (each a "Compensation Option") were granted. Each Compensation Option entitles the holder to purchase a unit on the same terms as the offering for a period of two years from the date of issuance. Each underlying common share purchase warrant (a "Compensation Option Warrant") will be subject to the same terms as the warrants attached to the units sold in the financing. If the Compensation Option Warrants are accelerated prior to the exercise of the Compensation Option, each Compensation Option Warrant will expire 30 days after the date of exercise of the Compensation Option. The fair value of the Compensation Option was $38,500 ($1.59 per Compensation Option) and was recognized as a share issuance cost. The fair value of the Compensation Options was estimated using the Black-Scholes option pricing model using the following assumptions: risk-free interest rate of 0.28%, annualized volatility of 100%, expected dividend yield of nil%, and an expected life of 2 years.

Additionally, the Company settled services and outstanding indebtedness of $543,715 through the issuance of 647,385 common shares at a fair value price of $0.84 per common share. The common shares issued in connection with the services and debt settlement are subject to a hold period that expires four months and one day from the date of issuance.

(v) On July 16, 2020, the Company issued 759,605 units on conversion of $945,000 of principal and $80,467 of accrued interest of the convertible debenture. Each unit consists of one common share of the Company and one share purchase warrant exercisable at $2.25 for two years from the date of conversion. No value was attributed to the warrant component of the units issued.

(vi) On July 28, 2020, the Company issued 953,564 units on conversion of $1,182,000 of principal and $105,311 of accrued interest of the convertible debenture. Each unit consists of one common share of the Company and one share purchase warrant exercisable at $2.25 for two years from the date of conversion. No value was attributed to the warrant component of the units issued.

(vii) On August 5, 2020, the Company issued 161,688 units on conversion of $200,000 of principal and $18,279 of accrued interest of the convertible debenture. Each unit consists of one common share of the Company and one share purchase warrant exercisable at $2.25 for two years from the date of conversion. No value was attributed to the warrant component of the units issued.

(viii) During the year ended December 31, 2020, the Company issued 42,967 common shares related to the exercise of 42,967 warrants at an exercise price of $1.80 for proceeds of $77,340.

OFF-BALANCE SHEET ARRANGEMENTS

The Company has no off-balance sheet arrangements as at June 30, 2021 and December 31, 2020, and as at the date hereof.

MORTGAGE PAYABLE

a) On January 7, 2019, the Company entered into a mortgage for $2,446,000 (the "First Mortgage") which bore interest at the rate of 8.25% per annum, calculated monthly. The First Mortgage matured on February 1, 2020 and was renewed as discussed below.

The First Mortgage payable was recorded at amortized cost and bore an effective interest rate of 10.44%.

The carrying value of the First Mortgage at December 31, 2019 was $2,437,175. Included in mortgage payable on initial recognition were the related mortgage transaction costs of $50,755 which were amortized over the term of the First Mortgage using the effective interest rate method.

The Company maintained minimum interest-only payments of $16,816 per month in connection with the First Mortgage. Total interest expense of the First Mortgage during the six months ended June 30, 2021 was $nil (2020 - $33,632).

b) On February 1, 2020, the Company renewed the First Mortgage of $2,446,000 (the "Second Mortgage") which bears interest at the rate of 8.00% per annum, calculated monthly. The Second Mortgage matured on February 1, 2021 and was renewed as discussed below.

The Second Mortgage payable was recorded at amortized cost and bore an effective interest rate of 8.79%.

The carrying value of the Second Mortgage payable as at December 31, 2020 was $2,442,830. Included in mortgage payable on initial recognition were the related mortgage transaction costs of $18,345 which were being amortized over the term of the Second Mortgage using the effective interest rate method.

The Company maintained minimum interest-only payments of $16,307 per month in connection with the Second Mortgage. Total interest expense of the Second Mortgage during the three and six months ended June 30, 2021 was $nil and $35,783, respectively (2020 - $32,613 and $48,920, respectively).

c) On February 1, 2021, the Company renewed the Second Mortgage of $2,446,000 (the "Third Mortgage") which bears interest at the rate of 8.00% per annum, calculated monthly. The Third Mortgage matures on February 1, 2022 and can be repaid before maturity without penalty and is secured by the mortgage property and building improvements.

The Third Mortgage payable was recorded at amortized cost and bares an effective interest rate of 8.79%.

The carrying value of the Third Mortgage payable at June 30, 2021 was $2,433,592. Included in mortgage payable are the related mortgage transaction costs of $18,345 which are being amortized over the term of the Third Mortgage using the effective interest rate method. Subsequent to period end, this mortgage was refinanced.

The Company maintains minimum interest-only payments of $16,307 per month. As at June 30, 2021 the total non-discounted remaining scheduled payments related to the mortgage including interest payments totaled $2,576,453. Total interest expense during the three and six months ended June 30, 2021 was $53,389 and $71,164, respectively (three and six months ended June 30, 2020 - $nil and $nil, respectively).

CONVERTIBLE DEBENTURE

On October 31, 2019, the Company closed a 2,353,333 convertible debenture unit offering at a price of $1.35 per debenture unit for gross proceeds $3,177,000. Each debenture consisted of a 12% secured convertible debenture with a maturity of two years from the date of issuance. If the holder converted their debenture unit, they were entitled to one common share and one share purchase warrant exercisable at $2.25 per share two years from the date of the convertible debenture closing October 31, 2021 at the holder's discretion.

If the closing price of the Common Shares of the Company was higher than $3.00 for any 10 consecutive trading days, the expiry date of the Warrants may be accelerated to the 30th day after the date of a news release announcing such acceleration. The debentures were secured to the facility subordinate to the mortgage currently on the facility.

As the debentures were convertible into units, the liability and equity components were presented separately on the consolidated statement of financial position. The initial carrying amount of the financial liability was determined by discounting the stream of future payments of interest and principal at a market interest rate of 16% totaling $2,878,539. Using the residual method, the carrying amount of the conversion feature is the difference between the principal amount and the initial carrying value of the financial liability. The equity component was recorded in debenture reserves on the consolidated statement of financial position totaling $298,461. The debentures, net of the equity components were accreted using the effective interest method over the term of the debentures, such that the carrying amount of the financial liability was equal to the principal balance at maturity.

During the year ended December 31, 2020, the Company settled principal plus accrued interest of $3,418,390 relating to the debentures through the issuance of 2,532,140 units. The Company reversed $298,461 from debenture reserves in connection with the settlement.

During the three and six months ended June 30, 2021, the Company recorded interest expense of $nil and $nil, respectively (2020 - $77,098 and $158,700, respectively) and accretion expense of $nil and $nil, respectively (2020 - $22,549 and $43,637, respectively).

RELATED PARTY TRANSACTIONS

A number of key management personnel and Directors hold positions in other entities that result in them having control or significant influence over the financial or operating policies of these entities. There were no loans to key management personnel or Directors, or entities over which they have control or significant influence during the periods ended June 30, 2021 or June 30, 2020.

During the period ended June 30, 2021, no options were granted (2020 – 1,133,333) to Officers and Directors having a fair value on grant of $nil (2020 – $1,139,612).

The following related parties transacted with the Company or Company controlled entities during the periods:

(a) Andrew Hale was a Director and the Company's President and CEO. He resigned on March 1, 2021.
(b) Blaine Bailey was a Director and Chairman of the Company's Audit Committee. He resigned on March 26, 2021.
(c) Stephen Brohman is the Company's CFO. He is a principal of Donaldson Brohman Martin CPA Inc. ("DBM CPA") a firm in which he has significant influence. DBM CPA provides the Company with accounting and tax services. Stephen Brohman resigned on July 14, 2021.
(d) George Routhier is a Company Director. He is the owner of Pipedreemz Inc. ("Pipedreemz"), which provides advisory services to the Company.
(e) Michael Forbes is a Director and the Company's President and CEO. He was appointed on April 29, 2021 and is the owner of MDC Forbes, which provides CEO services to the Company.
(f) Donald Dinsmore is a Director and the Company's COO. He was appointed on April 29, 2021.

The aggregate value of transactions key management personnel and Directors and entities over which they have control or significant influence were as follows:

	Three months ended June 30,		Six months ended June 30,	
	2021	2020	**2021**	2020
	$	$	**$**	$
DBM CPA	**31,091**	36,000	**61,091**	72,000
Andrew Hale	**-**	45,021	**47,479**	90,049
Donald Dinsmore	**20,833**	-	**20,833**	-
MDC Forbes	**10,000**	-	**10,000**	-
Pipedreemz	**-**	-	-	2,500
	61,924	81,021	**139,403**	164,549

As at June 30, 2021, the Company had an outstanding accounts payable balance with related parties of $25,500 (December 31, 2020 - $12,915).

All related party balances are unsecured and are due within thirty days without interest and incurred in the normal course of business.

The transactions with the key management personnel and Directors are included in operating expenses as follows:

(a) Consulting fees

Includes advisory services of George Routhier, charged to the Company via Pipedreemz, and CEO services by Michael Forbes, charged to the Company via MDC Forbes.

(b) Professional fees

Includes accounting and tax services of the Company's prior CFO, Stephen Brohman, charged to the Company via DBM CPA.

(c) Wages and salaries

Includes services by Andrew Hale as the prior CEO, and Donald Dinsmore as COO.

NEW ACCOUNTING STANDARDS

Accounting standards issued but not yet effective

Certain pronouncements have been issued by the IASB or IFRIC that are effective for accounting periods beginning on or after January 1, 2021. The Company has reviewed these updates and determined that many of these updates are not applicable or consequential to the Company and have been excluded from discussion within these significant accounting policies.

RISKS AND UNCERTAINTIES

The Company operates in a rapidly changing environment that involves risks and uncertainties and as a result, management's expectation may not be realized for a number of reasons. An investment in the Company's common shares is speculative and involves a high degree of risk and uncertainty. The current regulatory uncertainty poses additional risks and uncertainties which may materially affect management's expectations.

Regulatory Risks

The operations of the Company will be subject to various laws governing the production and distribution of cannabis oil, taxes, labour standards and occupational health, toxic substances, land use, water use, and other matters.

The Cannabis Act is a new regime and as such, revisions to the regime could be implemented which could have an impact on operations.

Furthermore, although the operations of the Company are currently carried out in accordance with all applicable rules and regulations, no assurance can be given that new rules and regulations will not be enacted or that existing rules and regulations will not be applied in a manner which could limit or curtail the ability to produce cannabis oil and related products. Amendments to current laws and regulations governing the distribution, transportation and/or production of cannabis oil or related products, or a more stringent implementation thereof, could have a substantial adverse impact.

Ongoing Need for Financing

The Company's ability to continue operations will be largely reliant on its continued attractiveness to equity investors. The Company is expected to incur operating losses as it continues to expend funds to develop its business operations. Even if its financial resources are sufficient to fund its current operations, there is no guarantee that the Company will be able to achieve its business objectives. The continued development of the Company will require substantial additional financing. The failure to raise such capital could result in the delay or indefinite postponement of current business objectives or the going out of business. The primary source of funding available to the Company will consist of equity financing. There can be no assurance that additional capital or other types of financing will be available if needed or that, if available, the terms of such financing will be favorable. In addition, from time to time, the Company may enter into transactions to acquire assets or the shares of other corporations. These transactions may be financed wholly or partially with debt, which may temporarily increase the Company's debt levels above industry standards.

Competition

The marijuana production industry is competitive in all of its phases. The Company will face strong competition from other companies in connection with such matters. Many of these companies have greater financial resources, operational experience and technical capabilities than Phyto. As a result of this competition, the Company may be unable to maintain its operations or develop them as currently proposed, on terms it considers acceptable or at all. Consequently, the revenues, operations and financial condition of the Company could be materially adversely affected.

Because of the early stage of the industry in which the Company operates, the Company may face additional competition from new entrants. If the number of users of marijuana in Canada increases, the demand for products will increase and management expects that competition will become more intense as current and future competitors begin to offer an increasing number of diversified products. To remain competitive, the Company will require a continued high level of investment in research and development, marketing, sales and client support. The Company may not have sufficient resources to maintain research and development, marketing, sales and client support efforts on a competitive basis which could materially and adversely affect the business, financial condition and results of operations.

COVID-19 Pandemic

The COVID-19 outbreak continues to rapidly evolve and is causing business disruptions across the entire global economy and society. The Company has taken various measures to prioritize the health and safety of its employees, customers and partners, including restricted work travel and site access, improved safety & hygiene, and the requirement of nonessential staff members to work remotely. As a manufacturer of consumable and medicinal products, the Company's practice is to always operate consistently with global pharma-quality standards to the best of its abilities, with strict hygiene practices and mandated personal protective equipment. The extent of the impact of COVID-19 on the Company's operational and financial performance will depend on various developments, including the duration and magnitude of the outbreak and the impact on customers, employees and vendors, all of which are uncertain and cannot be predicted at this point.

FINANCIAL RISK MANAGEMENT

Capital management

The Company defines capital as the components of shareholders' equity. The Company's objectives when managing capital are to support further advancement of the Company's business objectives, as well as to ensure that the Company is able to meet its financial obligations as they come due.

The Company manages its capital structure to maximize its financial flexibility making adjustments to it in response to changes in economic conditions and the risk characteristics of the underlying assets and business opportunities. The Company relies on the expertise of the Company's management to sustain the future development of the business. Management reviews its capital management approach on an ongoing basis and believes that this approach, given the relative size of the Company, is reasonable. There were no changes in the Company's approach to capital management during the six months ended June 30, 2021. The Company is not subject to externally imposed capital requirements.

Financial instruments - fair value

The Company's financial instruments consist of cash, trade receivables, deposits, accounts payable and accrued liabilities, mortgage payable and loan payable.

The carrying value of accounts payable and accrued liabilities, and loan payable approximated their fair value because of the short-term nature of these instruments. Mortgage payable approximate fair value due to its market rates of interest charged.

Financial instruments measured at fair value on the consolidated statements of financial position are summarized into the following fair value hierarchy levels:

Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2: inputs other than quoted prices included within 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: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

Financial instruments - risk

The Company's financial instruments are exposed to certain financial risks, including credit risk, liquidity risk and currency risk.

Credit risk

The Company is exposed to credit risk by holding cash. This risk is minimized by holding the funds in Canadian banks and credit unions or with Canadian governments. The Company has minimal receivable exposure, and its various refundable credits are due from Canadian governments.

Liquidity risk

Liquidity risk is the risk that the Company is unable to meet its financial obligations as they come due. The Company manages this risk by careful management of its working capital to ensure its expenditures will not exceed available resources.

Economic dependence

Economic dependence risk is the risk of reliance upon a select number of customers which significantly impact the financial performance of the Company. During the three and six months ended June 30, 2021, the Company's sales were generated by two customers representing approximately 74% and 26% (December 31, 2020 – one customer representing 100% of sales).

CRITICAL ACCOUNTING ESTIMATES AND FINANCIAL INSTRUMENTS

Refer to the Company's annual audited financial statements for the year ended December 31, 2020 and period ended December 31, 2019.

SUBSEQUENT EVENTS

(a) During the period subsequent to June 30, 2021, the Company cancelled 600,000 stock options.

(b) On July 3, 2021, 1,300,000 shares were released from escrow.

(c) On July 14, 2021, the Company appointed Oliver Foeste as CFO in conjunction with the resignation of Stephen Brohman. On the same day, the Company also appointed Paul Morgan as a Director of the Company.

(d) On August 1, 2021, the Company refinanced the Third Mortgage and increased the facility to $3,500,000 which bears interest at the rate of 6.50% per annum, calculated monthly for one year. The mortgage matures on July 1, 2022 and is secured by the mortgage property and building improvements.

(e) On August 24, 2021, the Company announced that the Phyto Extractions™ brands acquisition, previously announced on March 16, 2021, would be revised to a 100% interest on closing date and that the parties were working to finalize definitive terms and anticipate to sign a definitive share purchase agreement on or before September 15, 2021. The original agreement was for a 51% acquisition of Phyto Extractions™ brands (with a right of first refusal for the remaining 49% interest) for 38,400,000 common shares. Closing of the acquisition is subject to satisfactory due diligence and regulatory approval, as applicable.

(f) On August 27, 2021, the Company announced that it entered into a share purchase agreement dated August 10, 2021 (the "Share Purchase Agreement") pursuant to which the Company agreed to acquire, indirectly through its wholly-owned subsidiary Adastra Labs Inc., all the issued and outstanding shares of 1225140 B.C. Ltd., doing business as PerceiveMD ("PerceiveMD"), from the shareholders of PerceiveMD (the "Acquisition"), for a total purchase price of $2,300,000 comprising a $10,000 non-refundable deposit paid on execution of the Share Purchase Agreement; and $2,290,000 by way of the issuance of unrestricted common shares of the Company. Closing of the acquisition is subject to satisfactory due diligence and regulatory approval, as applicable.

(g) On August 27, 2021, the Company announced that it will change its name to Adastra Holdings Ltd. effective September 1, 2021

"Michael Forbes"

Director

"George Routhier"

Director