Emerald Health Therapeutics Inc. (CSE : EMH)

Management Discussion & Analysis
For the three and six months ended June 30, 2022 and 2021

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Management's Discussion and Analysis

The following management's discussion and analysis ("MD&A") is prepared as of August 30, 2022 and is intended to assist the understanding of the results of operations and financial condition of the Emerald Health Therapeutics, Inc. and its subsidiaries (together the "Company" or "Emerald").

This MD&A should be read in conjunction with the unaudited condensed interim consolidated financial statements and accompanying notes of the Company for the three and six months ended June 30, 2022, which have been prepared in accordance with IAS 34 – Interim Financial Reporting as issued by the International Accounting Standards Board ("IASB") and the audited consolidated financial statements and accompanying notes of the Company for the years ended December 31, 2021 and 2020 which have been prepared in accordance with International Financial Reporting Standards ("IFRS"). This MD&A contains forward-looking statements that are subject to risk factors set out in a cautionary note contained herein. All figures are in Canadian dollars unless otherwise noted.

Additional information related to the Company is available on its website at www.emeraldhealth.ca. Other information related to the Company, including the Company's financial statements referred to herein are available on the Canadian Securities Administrator's website at www.sedar.com.

Overview

The Company was incorporated pursuant to the *Business Corporations Act* (British Columbia) on July 31, 2007, as Firebird Capital Partners Inc. and changed its name to Firebird Energy Inc. in December 2012. On September 4, 2014, the Company completed the acquisition of all the issued and outstanding common shares of Thunderbird Biomedical Inc. ("Thunderbird") by way of a reverse takeover under the rules of the TSX Venture Exchange (the "TSXV") and concurrently changed its name to T-Bird Pharma, Inc ("T-Bird"). At that time, Thunderbird became a wholly owned subsidiary of T-Bird. In June 2015, the Company changed its name to Emerald Health Therapeutics, Inc. and Thunderbird changed its name to Emerald Health Botanicals Inc. ("Botanicals"). In February 2018, Botanicals changed its name to Emerald Health Therapeutics Canada Inc. ("EHTC").

The Company is a publicly traded company with headquarters in Victoria, British Columbia, Canada. Common shares of the Company (the "Common Shares") are listed on the Canadian Stock Exchange ("CSE") under the trading symbol "EMH".

Since 2015, the Company has been primarily engaged in the production and sale of recreational and medical cannabis in Canada. On November 29, 2021, the company announced that it intended to exit the recreational and medical cannabis business and pivot to a pharmaceutical development focus.

As of June 30, 2022, the Company owns:

a. 100% of the shares of EHTC, a British Columbia-based licence holder under the Cannabis Act (Canada) (the "Cannabis Act");

b. 100% of the shares of Verdélite Sciences, Inc. ("Verdélite"), a Québec-based licence holder under the Cannabis Act; and

c. 100% of the shares of Verdélite Property Holdings, Inc. ("Verdélite Holdings"), a Québec-based holding corporation that owns the Verdélite Facility (as defined below).

d. 100% of the shares of Avalite Sciences Inc. (formerly Northern Vine Canada Inc.) ("Avalite"), a British Columbia-based licenced dealer under the provisions of the Controlled Drugs and Substances Act (Canada) (the "CDSA") and a licence holder under the Cannabis Act. Avalite ceased active operations in January 2021.

Licences

The Company currently indirectly holds a number of licences (the "**Licences**") from Health Canada under the Cannabis Act to produce and sell cannabis products through its wholly owned direct and indirect subsidiaries, EHTC, Verdélite and Avalite. The Licences held by EHTC permit it to cultivate cannabis and produce and sell dried cannabis, cannabis oils, cannabis plants and cannabis seeds. The Licence held by Verdélite permits it to cultivate, extract, manufacture, synthesize, test, and sell cannabis. Verdélite has also obtained a cannabis research license that authorizes sensory and organoleptic testing of cannabis products in accordance with the research protocol and conditions of the licence. The Licence held by Avalite permits it to process cannabis and produce cannabis oil, all in accordance with the terms and conditions specified in the applicable Licence and the Cannabis Act. Avalite also holds a license to possess psilocybin for sale, provision and transport purposes.

Coronavirus

In December 2019, the novel Coronavirus ("COVID-19") began to spread throughout the world. On March 11, 2020, the World Health Organization declared the outbreak of COVID-19 a global pandemic. In response to this, global reactions have led to significant restrictions on travel, quarantines, temporary business closures and a general reduction in consumer activity.

During the three and six months ended June 30, 2022, government restrictions and protocols as a response to COVID-19 have varied in detail and effect in response to fluctuating case levels and hospitalizations. However, as of the date of this MD&A, restrictions have generally been lifted.

All of the Company's operating facilities in Canada were in compliance during the quarter ending June 30, 2022 with the required protocols and guidelines related to COVID-19 within each region where the Company's facilities are located.

The Company's priority during the quarter was to safeguard the health and safety of its personnel, support and enforce government actions to slow the spread of COVID-19, and continually assess and mitigate the risks to its business operations. The Company took several measures to reduce risks and enhance the safety of staff working at all of its facilities. This included working remotely, reorganizing physical layouts, adjusting schedules to improve physical distancing, implementing extra health screening measures for employees, and applying rigorous standards for personal protective equipment.

Development of Business in the three and six months ended June 30, 2022

Discontinuation and Realization of Prior Operations

During the three and six months ended June 30, 2022, the Company continued to focus on winding down its prior operations in a manner intended to reduce operating costs.

On February 28, 2022 and May 31, 2022, the Company ceased all production and packaging operations at the facility located at 4226 Commerce Circle and the facility located at 4223 Commerce Circle, respectively. The lease for the Company's 4226 Commerce Circle facility in Victoria, BC expired on February 28, 2022, and the lease for the 4223 Commerce Circle facility in Victoria, BC expired on May 31, 2022. By June 1, 2022, the Company's Victoria facilities had fully wound down their operations. On April 14, 2022, the Company concluded an agreement under which the lease obligation with the Landlord of the land in Metro Vancouver, British Columbia (a related party) would be concluded effective December 31, 2022 (or such earlier date on which the Landlord informs the Company that it has located a new tenant for the premises), in exchange for the transfer to the landlord of the non-leased equipment owned by the Company at the site. The Company has the option to terminate the lease earlier upon payment to the Landlord of an amount equal to all remaining rent, and all other costs owed the Landlord, to December 31, 2022.

Throughout the discontinuation process the Company has retained its cannabis sales agreements with the various provinces and continued to sell newly produced and inventoried cannabis dried flower and oils at a reduced volume through June 30, 2022.

All of the Company's assets were classified as held for sale as at December 31, 2021 and continued to be classified held for sale as at June 30, 2022. Additionally, all of the Company's operations have been deemed to be discontinued operations.

FlowerPod Amending Agreement

On April 28, 2022, the Company entered into an amended agreement with FlowerPod LLC for the sale of certain patents held by the Company, amending the December 28, 2021, binding term sheet payment schedule from a payment on closing of US$1M and a promissory note of US$500 due on the anniversary of the closing bearing an interest rate of 10% per annum to $967 (US$750) on closing and a $967 (US$750) promissory note due on the anniversary of the closing bearing 10% interest per annum. The Company continues to retain the two-year interest-bearing promissory note issued by FlowerPod on May 6, 2021, in the amount of $451 (US$350).

Lease Modification of the Richmond Lease

On April 14, 2022, the Company concluded an agreement under which the lease obligation with the landlord of the land in Richmond, British Columbia (would be concluded effective December 31, 2022 (or such earlier date on which the Landlord informs the Company that it has located a new tenant for the premises), in exchange for the transfer to the landlord of the non-leased equipment owned by the Company at the site. The Company will continue to make quarterly payments of $95 through June 2022 and then $114 quarterly payments from July to December 2022, after which it will have no further obligations or liabilities to the Landlord. The Company has the option to terminate the lease earlier upon payment to the landlord of an amount equal to all remaining rent, and all other costs owed the landlord, to December 31, 2022.

Acquisition by Skye Bioscience, Inc. (Related Party)

On May 12, 2022 Emerald and Skye Bioscience, Inc. ("Skye") announced that the companies have entered into a definitive agreement, as amended on June 14, 2022 and July 15, 2022 with respect to a transaction to be completed by way of a Plan of Arrangement (the "Arrangement") whereby Skye would acquire all of the issued and outstanding shares of Emerald in a share-for-share transaction. The proposed Arrangement is subject to approval by each company's shareholders and by the Supreme Court of British Columbia, Canada. As a result of the Arrangement, current Skye stockholders would own approximately 54% of the common stock of Skye and former shareholders of Emerald would own approximately 46% of Skye's common stock.

Under the Arrangement, Skye will issue Emerald shareholders 1.95 shares of Skye's common stock (the "Exchange Ratio") in exchange for each Common Share. Based on the number of outstanding shares as of May 12, 2022, it is expected that Skye would issue approximately 416M Skye shares to Emerald shareholders. All stock options and warrants of Emerald will be exchanged for replacement options and warrants of Skye on identical terms, as adjusted in accordance with the Exchange Ratio. The completion of the Arrangement is subject to customary terms and conditions, including the following:

a) Approval of the Arrangement by special resolutions and an ordinary resolution of disinterested shareholders of Skye and Emerald;

b) Court approval of the Arrangement; and

c) Receipt of all required regulatory approvals, including acceptance by the Canadian Securities Exchange (the "CSE") of Skye's listing on the CSE.

The Arrangement is anticipated to close in the fourth quarter of 2022.

On June 14, 2022, Skye and EHT entered into an amendment to the Arrangement Agreement to reflect certain changes to the post-closing board of directors of Skye and to waive the closing condition in the Arrangement Agreement requiring Skye to obtain a waiver from Emerald Health Biotechnology Espana S.L. ("EHB SL") for payment of any change of control payments under the Exclusive Sponsored Research Agreement, dated October 11, 2021 between EHB SL and Skye that may arise as a result of the transactions contemplated by the Arrangement Agreement.

Development of Business after the Reporting Period

Common Stock Issued to Emerald Health Sciences Inc. (Related Party)

On July 8, 2022, Emerald Health Sciences Inc. ("Sciences") transferred its 39,401,608 Common Shares to its shareholders as a return of capital but continues to hold its common share purchase warrants. See "Transactions with Related Parties" for more details.

Arrangement Agreement with Skye Bioscience, Inc. (Related Party) - Second Amendment

On July 15, 2022, Skye and EHT entered into the second amendment to the Arrangement Agreement to extend the outside date of the closing of the acquisition to November 15, 2022 in the event that the parties encounter regulatory delays.

On August 19, 2022 the Company obtained the requisite shareholder approval and on August 25, 2022, the Company obtained a final order of the Court approving the Arrangement. Subject to the satisfaction or waiver of the remaining conditions (including Skye shareholder approval).

Disclosure of Outstanding Share Data

The Company's authorized share capital consists of an unlimited number of Common Shares and an unlimited number of preferred shares of which 213,472,095 Common Shares and nil preferred shares were issued and outstanding as of June 30, 2022, and 213,472,095 Common Shares were outstanding as of August 30, 2022.

There were 4,564,720 stock options outstanding as of June 30, 2022. As of August 30, 2022, there were 4,435,125 stock options outstanding.

There were 31,255,085 warrants outstanding as of June 30, 2022 and as of August 30, 2022.

Summary of Quarterly Results

The financial information in the following tables summarizes selected financial information for the Company for the last eight quarters which was derived from annual financial statements prepared in accordance with IFRS or interim financial statements prepared in accordance with IFRS applicable to the preparation of interim financial statements, *IAS 34, Interim Financial Reporting*:

	2022		2021	
000's	**June 30 ($)**	**March 31 ($)**	**December 31 ($)**	**September 30 ($)**
Revenue	1,282	2,487	2,867	2,599
Share-based payments	1	(207)	(721)	204
Interest and other income	936	933	858	354
Gain (loss) on changes in the fair value of the Company's biological assets	Nil	(100)	(446)	521
Net Loss	(1,835)	(3,773)	(13,406)	(9,144)
Net Loss per share	(0.009)	(0.018)	(0.058)	(0.043)

	2021		2020	
000's	**June 30 ($)**	**March 31 ($)**	**December 31 ($)**	**September 30 ($)**
Revenue	3,777	2,653	3,511	4,311
Share-based payments	194	143	432	755
Interest and other income	782	1,084	428	29
Share of loss from Pure Sunfarms Corp.	Nil	Nil	(1,367)	(520)
Gain (loss) on changes in the fair value of the Company's biological assets	540	95	7,229	(2,339)
Net Loss	(13,956)	(2,900)	(8,060)	(11,658)
Net Loss per share	(0.065)	(0.014)	(0.039)	(0.057)

Results of Operations

Quarter ended June 30, 2022 compared to the quarter ended June 30, 2021

The net loss for the quarter ended June 30, 2022, was $1.84 million (loss of $0.009 per share), compared to the net loss of $13.96 million (loss of $0.065 per share) for the quarter ending June 30, 2021. Diluted loss per share is the same as basic loss per share as the outstanding options and warrants have an anti-dilutive effect on the loss per share.

Factors contributing to the net loss for the three-month period ended June 30, 2022, include the following:

Revenue

Revenue for the quarter ended June 30, 2022, was $1.28 million compared to $3.78 million for the same period in the prior year. For the quarter ended June 30, 2022, revenue was comprised of 86% dried product, and 14% concentrates, extracts and edibles, compared to approximately 70% dried product, 30% oils in the quarter ended June 30, 2021. The decrease in revenues from sale of goods is primarily driven by the $2.35 million decrease in recreational sales and $.220 million decrease in bulk sales. These items were offset by a decrease of $0.116 million in sales discounts offered by the Company to its customers.

	For the three months ended June 30, 2022	For the three months ended June 30, 2021
Average selling price of adult-use dried flower per gram & gram equivalents	$2.60	$3.28
Kilograms sold of adult-use dried flower & kilogram equivalents	321	739
Average selling price of medical dried flower per gram & gram equivalents	$0.00	$7.51
Kilograms sold of medical dried flower & kilogram equivalents	0	25
Total Kilograms produced of dried flower	0	667

Cost of Sales

Cost of goods sold currently consists of four main categories: (i) cost of goods sold expensed from inventory, (ii) production costs, (iii) change in the fair value of biological assets and (iv) amortization of the Health Canada licenses.

Cost of goods sold represents the deemed cost of inventory that arose from the fair value measurement of biological assets, subsequent post-harvest costs capitalized to inventory, purchased dried cannabis, and costs to produce cannabis oils capitalized to inventory (including the deemed cost of dried inventory that arose from the fair value measurement of biological assets that were used to produce cannabis oils), and packaging costs. Cost of goods sold expensed from inventory for the quarter ended June 30, 2022, and 2021 was $0.01 million and $2.38 million, respectively. The change is primarily due to a decrease related to the production of recreational products by $2.35 million in comparison to the quarter ending June 30, 2021.

Production costs include all direct and indirect production related costs, including security, compliance, quality control and quality assurance costs, as well as overhead relating to the cultivation activities. All post-harvest inventory production costs in excess of standard cost are not capitalized and recorded as cost of goods sold. Production costs included $0.37 million of costs during the three months ended June 30, 2022 (June 30, 2021 - $1.34 million). The decrease in production costs were primarily driven by a $0.66 million decrease in direct and indirect wages due to reduced headcount in the production department, $0.36 million decrease in depreciation expense due to the classification of substantially all of the Company's assets as held for sale. These decreases were offset by an increased in leased equipment expenses of $5 thousand.

During the three months ended June 30, 2022, the Company recognized $0.45 million June 30, 2021 - $0.73 million) in excise taxes from recreational sales. The decrease in excise taxes is due to the Company's wind down of operations during the three months ended June 30, 2022. Excise taxes are levied based on the quantity of total tetrahydrocannabinol ("THC") contained in the cannabis products sold to customers. Although these taxes are not always billed to customers, the decrease in revenue during the three months ended June 30, 20222 is the primary factor causing the increase in excise taxes. Excise taxes were 35% of revenues during the three months ended June 30, 2022, compared to 19% of revenues during the three months ended June 30, 2021.

The change in biological assets for the quarter ended June 30, 2022, resulted in gain of $Nil compared to a gain of $0.54 million in the same quarter of the prior year. The gain in the prior period was due to a change in estimates used for fair value less costs to sell ("FVLCS") used as an input in the valuation of biological assets during that period.

The Company measures biological assets consisting of cannabis plants at fair value less cost to sell up to the point of harvest, which becomes the basis for the cost of finished goods inventories after harvest. Seeds are measured at fair market value, except for a portion which is restricted with respect to distribution due to the conditions under which they were acquired that are measured at cost. The significant assumptions used in determining the fair value of cannabis plants are as follows: the plant attrition rate for various stages of development; yield per plant; wholesale selling price fewer costs to sell; percentage of total expected costs incurred to date; and costs incurred for each stage of plant growth.

Gains recognized in the fair value of biological assets are recorded in a manner that decreases the cost of sales. Changes in the fair value of biological assets can be significant during periods of large expansion in the cultivation area. In determining the fair value of cannabis plants, assumptions are used regarding the variability in the average age and number of cannabis plants available at each period end.

Inventory write-down – During the quarter ended June 30, 2022, a write-down of $0.15 million (June 30, 2021 - $0.17 million) was recognized for dried cannabis, packaged inventory, and bulk cannabis oils (related to product deterioration, a packaging defect and limited remaining shelf life. The decrease in inventory write-down is due to the inventory written off during the three months ended December 31, 2021. As the Company is in the process of pivoting from the recreational and medicinal cannabis industry to the pharmaceutical development industry, prior period write-downs of inventory have resulted in a lower balance of inventory, and therefore a lower amount of inventory write-downs, in the current period.

Other expenses

General and Administrative – During the quarter ended June 30, 2022, the Company incurred general and administrative expenses of $2.25 million versus $2.26 million for the quarter ended June 30, 2021. In the quarter ended June 30, 2022, general and administrative costs included salaries and benefits of $0.17 million (three months ended June 30, 2021 - $0.98 million). This decrease was driven by the exit of a number of employees from the organization during the three months ended June 30, 2022 due to the wind down of operations. Consulting and professional services fees were $1.27 million during the three months ended June 30, 2022 (three months ended June 30, 2021 - $0.52 million). This increase was caused by increase legal activity related to the winding down of operations and the Arrangement with Skye, increased audit and review fees, increased director fees, and increased subscriptions and membership dues. Increases to consulting and professional services were offset by decreases in recruiting fees which were not incurred during the three months ended June 30, 2022. D&O insurance costs were $0.27 during the three months ended June 30, 2022 (three months ended June 30, 2021 - $0.27). Rent, repairs, and construction expenses of $0.43 million were incurred during the three months ended June 30, 2022 (three months ended June 30, 2021 – $0.32 million). This increase in expenses was primarily due to a increase in rent expenses of $0.036 million, an increase in property taxes of $0.043 million, and an increase in subcontractor fees of $0.027 million. Utilities expenses were $0.07 million during the three months ended June 30, 2022 (three months ended June 30, 2021 - $0.12 million). This decrease is due to lower utility usage as operations wind down.

Sales and marketing – In the quarter ended June 30, 2022, the Company incurred sales and marketing expenses of $0.04 million versus $0.57 million in the comparable 2021 prior period. During the quarter ending June 30, 2022, wages and benefits decreased by $0.324 million due to the exit of employees related to the wind down of business operations. Additionally, sales consultant expenses decreased by $0.148 million and promotional gift related expenses decreased by $44 thousand as overall sales efforts decreased.

Research and development – In the quarter ended June 30, 2022, the Company incurred research and development expenses of $(0.001) million (three months ended June 30, 2021 - $0.64 million). Costs decreased during the current period due to the cessation of new product development. The decrease in research and development expenses is primarily due to a $0.202 million decrease in research consulting fees and a $.263 million decrease in employee wages and benefits. Additionally, there was a $69 thousand decrease in growing supplies related expenses, $44 thousand decrease in production supplies and a $31 thousand decrease in lab testing due to the closure of growing operations in the quarter ending June 30, 2022.

Share-based compensation – In the quarter ended June 30, 2022, the Company incurred share-based compensation expenses of $0.001 million versus $0.194 million in the comparable 2021 prior period. The amounts are compensation expenses related to employee, director, and consultant incentive stock options which are measured at fair value at the date of grant and expensed over the vesting period. During the quarters ended June 30, 2022, and 2021, the Company granted no stock options or restricted share units ("RSU") to employees and consultants.

Gain on modification of lease – During the three months ended June 30, 2022, the Company determined there was a decrease in its lease obligation liability on its Richmond, British Columbia facility due to the lease termination agreement which was modified on April 14, 2022. This resulted in recording a gain on lease modification of $3.2 million.

Loss on disposal of capital assets – During the three months ended June 30, 2022, the Company determined there was a loss on disposal of capital assets which will be surrendered to the landlord of its Metro Vancouver facility as part of the lease termination agreement which was concluded on April 14, 2022. This resulted in recording a loss on disposal of capital assets of $2.85 million.

Period ended June 30, 2022 compared to the period ended June 30, 2021

The net loss for the year to date, was $5.60 million (loss of $0.026 per share), compared to the net loss of $16.86 million (loss of $0.080 per share) for the same period in the prior year. Diluted loss per share is the same as basic loss per share as the outstanding options and warrants have an anti-dilutive effect on the loss per share.

Factors contributing to the net loss for the six-month period ended June 30, 2022, include the following:

	2022	**2021**
000's	**Six months ended June 30 ($)**	**Six months ended June 30 ($)**
Revenue	3,769	6,429
Share-based payments	(206)	337
Interest and other income	1,869	1,869
Gain (loss) on changes in the fair value of the Company's biological assests	100	635
Net Loss	(5,607)	(16,856)
Net Loss per share	(0.026)	(0.080)

Revenue

Revenue for the year to date, was $3.77 million compared to $6.43 million for the same period in the prior year. The revenue for the six months ended June 30, 2022 was impacted by the winding down of the Company's cannabis operations and by a further decline in average selling price per gram of dried cannabis and dried cannabis equivalent in the adult-use channel, which decreased from $3.44 in the same period in 2021 to $3.14 in the current period. The Company shipped 65% less kilograms of dried flower and flower equivalent compared to the same period of the prior year. For the six months ended June 30, 2022, revenue was comprised of approximately 86% dried product and 14% oils, compared to approximately 67% dried product and 33% oils in the six months ended June 30, 2021. During the six months ended June 30, 2022, the Company's revenues were primarily from the adult recreational market.

	For the six months ended June 30, 2022	**For the six months ended June 30, 2021**
Average selling price of adult-use dried flower per gram & gram equivalents	$3.14	$3.44
Kilograms sold of adult-use dried flower & kilogram equivalents	874	1294
Average selling price of medical dried flower per gram & gram equivalents	$6.11	$7.71
Kilograms sold of medical dried flower & kilogram equivalents	19	55
Total Kilograms produced of dried flower	519	1,631

Cost of Sales

Cost of goods sold currently consists of four main categories: (i) cost of goods sold expensed from inventory, (ii) production costs, (iii) change in the fair value of biological assets, and (iv) amortization of the Health Canada licences.

Cost of goods sold represents the deemed cost of inventory that arose from the fair value measurement of biological assets, subsequent post-harvest costs capitalized to inventory, purchased dried cannabis, costs to produce cannabis oils capitalized to inventory (including the deemed cost of dried inventory that arose from the fair value measurement of biological assets that were used to produce cannabis oils), and packaging costs. Cost of goods sold expensed to inventory for the six months ended June 30, 2022 and June 30, 2021 was $0.178 million and $1.08 million, respectively. The decrease in cost of goods sold in the current period was due to smaller volumes of product sold as compared to the prior period.

Production costs include all direct and indirect production related costs, including security, compliance, quality control and quality assurance costs, as well as overhead relating to the cultivation activities. All post-harvest inventory production costs in excess of standard cost are not capitalized and recorded as a write-down of production costs. This included $1.03 million of costs during the six months ended June 30, 2022 (June 30, 2021 - $2.78 million).

During the six months ended June 30, 2022, the Company also recognized $1 million (June 30, 2021 - $1.1 million) in excise taxes from recreational sales.

The change in biological assets for the six months ended June 30, 2022 was a gain of $0.1 million compared to a gain of $0.64 million in the same period of the prior year. The decrease is substantially due to a smaller number of plants grown during the current period.

The Company measures biological assets consisting of cannabis plants at fair value less cost to sell up to the point of harvest, which becomes the basis for the cost of finished goods inventories after harvest. Seeds are measured at fair market value, except for a portion which are restricted with respect to distribution due to the conditions under which they were acquired that are measured at cost. The significant assumptions used in determining the fair value of cannabis plants are as follows: plant attrition rate for various stages of development; yield per plant; selling price less costs to sell; percentage of total expected costs incurred to date; and costs incurred for each stage of plant growth.

Gains recognized in the fair value of biological assets are recorded in a manner that decreases the cost of sales. Changes in the fair value of biological assets can be significant during periods of large expansion in the cultivation area. In determining the fair value of cannabis plants, assumptions are used regarding the variability in the average age and number of cannabis plants available at each period end.

Inventory write-down – During the six months ended June 30, 2022, a write-down of $0.60 million was recognized for packaged inventory and extracted cannabis oils (June 30, 2021 - $.40 million) related to product deterioration, limited remaining shelf life and fair market value.

Other Expenses

General and Administrative – During the six months ended June 30, 2022, the Company incurred general and administrative expenses of $4.98 million versus $4.48 million for the six months ended June 30, 2021. The current period saw decreased expenses in wages and benefits, corporate communications and media, travel and accommodations expense and office expense. In the six months ended June 30, 2021, general and administrative costs included; salaries and benefits of $1.18 million (six months ended June 30, 2021 - $1.77million), consulting and professional services fees of $2.18 million (six months ended June 30, 2021 - $1.21 million), and office and insurance of $1.6 million (six months ended June 30, 2020 - $1.43 million).

Sales and marketing – In the six months ended June 30, 2022, the Company incurred sales and marketing expenses of $0.48 million versus $0.99 million in the comparable 2021 prior period. These costs are related to general sales and marketing, patient acquisition, and education expenses. The current period decrease reflects the reduction in Sales and Marketing activity due to the wind down of the Company’s cannabis operation.

Research and development – In the six months ended June 30, 2022, the Company incurred research and development expenses of $0.25 million (six months ended June 30, 2021 - $0.91 million). These costs related to consulting fees and wages associated with the development of new cannabis products. The decrease in research and development costs relate to the wind down of the Company’s cannabis operations.

Share-based compensation – In the six months ended June 30, 2022, the Company incurred share-based compensation expenses of $(0.21) million versus expenses of $0.34 million in the comparable 2021 prior period. The amounts are compensation expenses related to employee, director and consultant incentive stock options and restricted share units which are measured at fair value at the date of grant and expensed over the vesting period. During the six months ended June 30, 2022, the Company granted nil stock options and nil restricted share units to employees and consultants, compared to 300,000 stock options and nil restricted share units during the same period in 2021.

Gain on modification of lease – During the six months ended June 30, 2022, the Company determined there was a decrease in its lease obligation liability on its Richmond, British Columbia facility due to the lease termination agreement which was modified on April 14, 2022. This resulted in recording a gain on lease modification of $3.2 million.

Loss on disposal of capital assets – During the six months ended June 30, 2022, the Company determined there was a loss on disposal of capital assets which will be surrendered to the landlord of it's Metro Vancouver facility as part of the lease termination agreement which was concluded on April 14, 2022. This resulted in recording a loss on disposal of capital assets of $2.85 million.

Liquidity and Capital Resources

The Company continually monitors and manages its cash flow to assess the liquidity necessary to fund operations and capital projects. The Company manages its capital resources and adjusts them to consider changes in economic conditions and the risk characteristics of the underlying assets. To maintain or adjust its capital resources, the Company may, where necessary, control the amount of working capital, pursue financing, or manage the timing of its capital expenditures. As at June 30, 2022, the Company had working capital of $12.04 million (current assets of $18.10 million less current liabilities of $6.07 million).

The unaudited consolidated interim financial statements have been prepared on a going concern basis which assumes that the Company will be able to realize its assets and discharge its liabilities in the normal course of business for the foreseeable future. It is unlikely that the Company will be able to generate sufficient gross margins to reach profitability as the Company is winding down its cannabis operations which represented its only source of active income.

As at June 30, 2022, the Company had $15.52 million in cash and cash equivalents.

Management will continue to closely monitor its cash flows as it purposely shifts away from the cannabis sector, reduces its burn rate and seeks to divest its remaining cannabis assets and complete the Arrangement.

The composition of the Company's accounts payable and accrued liabilities was as follows:

(000's)	June 30, 2022 ($)	June 30,2021 ($)
Trade Payables	1,820	2,960
Accrued Liabilities	1,457	811
Excise Tax Payable	1,048	1,309
Payroll Liabilities	31	222
Sales tax liabilities	943	734
Other Payables	7	80

The Company also has the following undiscounted gross contractual obligations as of June 30, 2022, which are expected to be payable in the following respective periods:

000's	Total $	≤ 1 year $	Over 1 year $
Accounts payable and accrued liabilities	5,306	5,306	—
Insurance payable	485	485	—
Lease liability	260	260	—

Included in the leases above, is the $156 thousand lease liability related to the Metro Vancouver greenhouse facility.

Operating, Investing and Financing Activities

The chart below highlights the Company's cash flows:

(000's)	For the six months ended June 30,2022 ($)	For the six months ended June 30,2021 ($)
Net Cash provided by (used in):		
Operating activities	($2,632)	($10,055)
Investing Activities	$131	$10,145
Financing activities	($493)	$798
Increase (decrease) in cash	($2,994)	$888

Year to Date June 30, 2022, compared to June 30, 2021

Cash used in operating activities for the period ended June 30, 2022, was $2.63 million, compared to cash used of $10.05 million through Q2 of the prior year. The current year amount reflects the decrease in general and administrative, sales and marketing and research and development expenditures, and decreases in cash outflows for payments of current liabilities from the period ended June 30, 2022.

Cash provided by investing activities for the period ended June 30, 2022, was $131 thousand, compared to cash provided by investing activities of $10.15 million during the same period in the prior year. The decrease is due to the sale of joint venture interests, payment of deferred payment, and purchase of plant and equipment which occurred during the period ended June 30, 2021, but not during the period ended June 30, 2022.

Cash used in financing activities for the period ended June 30, 2022 was $493 thousand, compared to cash provided of $798 thousand in the prior period. The decrease is primarily due to warrant exercises which occurred during the period ended June 30, 2021, but not during the period ended June 30, 2022.

Financial Risk Management

The Company's board of directors has overall responsibility for the establishment and oversight of the Company's risk management policies on an annual basis. Management identifies and evaluates the Company's financial risks and is charged with the responsibility of establishing controls and procedures to ensure financial risks are mitigated in accordance with the approved policies.

Measurement Uncertainty and Impairment Assessments

During the year ended December 31, 2021, the Company initiated a plan to close operations of its facility located in Metro Vancouver, British Columbia, as announced subsequent to the year-end, which is an indicator of impairment. The fair value of this facility was determined based on a third-party appraisal using an FVLCD approach including the market and cost approaches. Consideration was given to information from manufacturers, historical data and industry standards which constitute both observable and unobservable inputs (level 2 and level 3).

Biological assets of $76 were impaired due to the lack of sales through the date that the unaudited condensed interim consolidated financial statements were issued.

Management continues to review each of its assets for indicators of impairment.

Transactions with Related Parties

The Company has entered into transactions with an entity that could have been considered to be a control person of the Company, a wholly-owned subsidiary of such entity, a company controlled by the Company's former Executive Chairman, a company whose CEO is also a director of the Company. In addition, on April 29, 2022, the Company entered into an arrangement agreement with Skye Bioscience Inc. ("Skye"), which could be considered a related party of the Company due to the fact that Sciences is also a control person of Skye, as further described below under "Proposed Transactions".

Emerald Health Sciences Inc.

As at June 30, 2022, Sciences held an aggregate of 39,401,608 Common Shares, representing 19% (June 30, 2021 – 39,401,608 shares, representing 18%) of the issued and outstanding Common Shares and it also held 9,099,706 (June 30, 2021 – 9,099,706) common share purchase warrants of the Company. On July 4, 2022, Sciences transferred 39,401,522 of its Common Shares to the shareholders of Sciences by way of a return of capital. Sciences continues to hold 86 Common Shares and could no longer be considered a control person of the Company.

On July 4, 2022, Sciences and the Company terminated the amended and restated independent contractor agreement with Sciences originally dated October 5, 2017, as subsequently amended and restated on January 1, 2018 and as further amended on October 1, 2019.

Subsidiaries of Emerald Health Sciences Inc.

On October 3, 2018, the Company announced that it entered into a research agreement with VivaCell Biotechnologies Spain S.L.U. ("VivaCell"), a corporation located in Córdoba, Spain and focused on cannabinoid pharmaceutical research, which will provide its cannabinoid-industry-leading contract research organization (“CRO”) services to the Company to elucidate the mechanism of action of proprietary formulations and dosage forms that the Company is developing. EH Spain is a wholly owned subsidiary of Sciences, which could be considered a control person of the Company at the time and was therefore a related party of the Company. To date, the Company has used the CRO services of EH Spain with total costs incurred of €20,000. The Company has no obligation to use further services from EH Spain.

A Company Controlled by the Company's Former Executive Chairman

During the year ended December 31, 2017, the Company entered into a 30-year lease with a company (the “Landlord”) that is 50% owned by Avtar Dhillon, MD, the former Executive Chairman and CEO of the Company with respect to land in Metro Vancouver, British Columbia on which the Company constructed its greenhouse production facilities. The lease amount was determined by an independent valuation and was approved by the nonconflicted directors of the Company. During the three and six months ended June 30, 2022, the Company paid to the Landlord $95 and $190 respectively (June 30, 2021 - $95 and $190) in rent. As at June 30, 2022, the Company recognized lease liabilities held for sale of $156 (June 30, 2021 - $3,506) relating to the land in Metro Vancouver. On April 14 2022, the Company entered into an agreement to amend and terminate the lease (see Development of Business after the Reporting Period for additional information). As of August 6, 2021, the Landlord ceased to be a related party upon the resignation of Avtar Dhillon as Executive Chairman of the Company.

Proposed Transactions

There are no material decisions by the Company's board of directors with respect to any other imminent or proposed transactions that have not been disclosed herein.

Critical Accounting Policies and Estimates

The critical accounting policies and estimates are included in each of the notes of the Company's audited consolidated financial statements for the year ended December 31, 2021 and 2020. These are the accounting policies and estimates that are critical to the understanding of the business operations and results of operations.

Changes in Accounting Standards not yet Effective

Refer to Note 2 of the Company's audited consolidated financial statements for the years ended December 31, 2021, and 2020 for additional information on new standards, amendments to standards and interpretations, which are not effective yet, and have not been applied in preparing these consolidated financial statements but may affect the Company when applied in the future.

Off-Balance Sheet Arrangements

The Company has not entered into any material off-balance sheet arrangements such as guarantee contracts, contingent interests in assets transferred to unconsolidated entities, derivative financial obligations, or with respect to any obligations under a variable interest equity arrangement.

Risks and Uncertainties

The Company's actual results may differ materially from those expected or implied by the forward-looking statements and forward-looking information contained in this management discussion and analysis due to the proposed nature of the Company's business and its present stage of development. A non-exhaustive list of risk factors associated with the Company follows below.

The following is a non-exhaustive list of certain additional risk factors associated with the Company.

Additionally, during the year ended December 31, 2021, management identified a material weakness in our internal control over financial reporting whereas we did not design or maintain effective controls to ensure that there is an independent review and approval of schedules and reconciliations related to inventory, biological assets and cost of sales to ensure completeness and accuracy, which continued to exist as of June 30, 2022. We are currently in the process of implementing a detailed plan for remediation of the material weakness.

Completion of the Arrangement

Consummation of the Arrangement is subject to the satisfaction of several conditions, certain of which are outside the Company's control, including, without limitation, obtaining the requisite approvals of the shareholders of Skye. The Company obtained Emerald shareholder approval at its annual general and special meeting held on August 19, 2022 and obtained the final order approving the Arrangement from the British Columbia Supreme Court on August 25, 2022. There can be no certainty, nor can the Company provide any assurance, that the remaining conditions will be satisfied or, if satisfied, when they will be satisfied. Certain conditions may be waived at the Company's discretion, however certain other conditions are not subject to waiver. Both the Company and Skye have the right to terminate the Arrangement Agreement in certain circumstances. Accordingly, there is no certainty, nor can either party provide any assurance, that the Arrangement Agreement will not be terminated by the other party before completion of the Arrangement.

If the Arrangement Agreement is terminated as a result of either party entering into a superior proposal and in certain other limited circumstances, the other party may be entitled to receive a termination fee in the amount of $0.500 million. However, the termination fee is not payable in all circumstances and therefore the situation may arise that the Arrangement Agreement is terminated by Skye and the Company does not receive the termination fee or other consideration. In addition, notwithstanding that such fee may be payable in the event of such a termination by Skye, Skye may be unable to pay such fee or may dispute whether it is required to do so.

If the Arrangement is not completed for any reason, the market price of the Company's shares may decline to the extent that the current market price reflects a market assumption that the Arrangement will be completed, and the Company's business may suffer. In addition, the Company will remain liable for significant consulting, accounting and legal costs relating to the Arrangement and will not realize anticipated synergies, growth opportunities and other benefits of the Arrangement if the Arrangement is not completed. If the Arrangement is delayed, the achievement of synergies and the realization of growth opportunities could be delayed and may not be available to the same extent.

Public Health Crises

The Company's business, operations and financial condition could be materially adversely affected by the outbreak of epidemics, pandemics, or other health crises, such as the current COVID-19 pandemic.

The risks to the Company of such public health crises also include risks to employee health and safety and a slowdown or temporary suspension of operations in geographic locations impacted by an outbreak. The Company has taken what it believes to be appropriate safety precautions at its facilities to safeguard the health of its employees including remote work plans and additional protective measures on-site, and there have been no outbreaks to date at any of the Company's facilities. Widespread uncertainty, government restrictions on personal mobility and the other impacts of the COVID-19 crisis on the Company's employees, together with the potential to contract COVID-19 and/or be subject to quarantine may have an impact on the ability or willingness of the Company's employees to attend their workplace.

Such public health crises can also result in disruptions and volatility in financial markets and global supply chains as well as declining trade and market sentiment and reduced mobility of people, all of which could impact public markets, interest rates, credit ratings, credit risk and inflation. In addition, the Company's business may be impacted by supply chain disruptions caused by the COVID-19 crisis. While these effects are expected to be temporary, the duration of the disruptions to business and the related financial impact cannot be estimated with any degree of certainty at this time.

Although restrictions on businesses in most Canadian jurisdictions have been largely repealed, the continued spread of COVID-19 and the emergence of new variants of the virus have led to the implementation of new restrictions. There can be no guarantee that these restrictions will be successful or that additional future outbreaks will not lead to increased restrictions. In addition, while vaccination programs for COVID-19 have experienced wide take-up in Canada, such programs may not be as efficacious as expected due to a variety of factors including the unwillingness of significant numbers of people to become vaccinated, or the emergence of new strains which are resistant to vaccines. At this point, the extent to which COVID-19 may impact the Company is uncertain; however, it is possible that COVID-19 could have a material adverse effect on the Company's business, results of operations and financial condition.

Disposition of Assets

As part of the Company's strategy to pivot its business focus, it is seeking opportunities to dispose of certain of its assets. In pursuit of such opportunities, the Company may fail to negotiate acceptable arrangements related to such dispositions. Such dispositions may also lead to substantial losses recognized by the Company, particularly as values in the cannabis sector have fallen in recent years with many distressed assets currently on the market. In addition, any such transaction will require the dedication of substantial management effort, time and resources which may divert management's focus and resources from other strategic opportunities and from operational matters during this process. Dispositions of certain assets may also lead to the loss of key employees and the disruption of ongoing business and employee relationships that may adversely affect the Company.

Operations in the USA

The Company does not currently have any direct operations, business or sales in the United States. However, the Company has entered into a license agreement with FlowerPod, pursuant to which it agreed to exclusively license certain patented technology to FlowerPod for the development and sale of cannabis-related products for use in all US states and other key geographical areas where adult use and/or medical cannabis is locally legal. The Company has entered into a binding term sheet to dispose of its interest in FlowerPod and sell such technology however closing has not yet occurred. See "Development of Business After the Reporting Period". In addition, the Company has also entered into a letter of intent with The Uplifters' Prima, PBC ("Prima"), based in Santa Monica, California, contemplating joint initiatives to co-develop new cannabinoid-based wellness products for sale in the United States, Canada, and internationally. On May 25, 2021, the Company completed a $50,000 investment in Prima's Seed-1 Preferred Stock financing round. The Company is not aware of any material non-compliance with applicable laws related to initiatives undertaken by FlowerPod or Prima. At this time, the Company does not have any significant balance sheet or operating statement exposure with respect to such ancillary operations. The Company does not expect there to be any impact on its ability to access capital as a result of such ancillary operations in the United States. No additional legal opinions have been obtained by the Company regarding compliance with regulatory frameworks in the United States or potential exposure to and implications arising from federal laws in the United States.

Cannabis is a restricted drug under federal law in the United States and its sale and possession is generally prohibited. Enforcement of relevant laws in an adverse manner would be a significant risk to the Company and could have a material adverse effect on the Company. Future operations in the United States or transactions or relationships with cannabis-related businesses in the United States, depending on the nature and extent of such operations, transactions, or relationships, may also impact the Company's ability to raise funds in the public and private markets. Regulatory authorities may also impose certain restrictions on the Company's ability to operate in the United States. The Company will consult with appropriate legal counsel to ensure it considers all relevant factors prior to engaging in any operations in the United States or any transactions with entities in the United States.

Current and Future Litigation

On June 16, 2020, a plaintiff filed a Statement of Claim on behalf of a proposed class in the Court of Queen's Bench of Alberta in Alberta, Canada, against several Canadian cannabis manufacturers and/or distributors (the "Defendants"). The Company is named as a Defendant in the proceedings. In the action it is alleged that the Defendants, including the Company, marketed medicinal and recreational cannabis products with advertised THC or CBD content levels different than those products actually contained. The action only specifically mentions one particular product manufactured and sold by the Company – Sync 25, a CBD oil which is alleged to have had at the time of testing an advertised THC level of 1 mg/mL, but an alleged actual THC potency of 0.46 mg/mL. The plaintiff claims damages against the Defendants as a group of $500 million, plus punitive damages of $5 million, an accounting of revenues, and interest and costs. The plaintiff has not yet demanded that the Company defend the action. The plaintiff has not made a certification application for the class.

The Company believes that the allegations made against it in the action are flawed. The plaintiff''s testing methodologies have not yet been disclosed. The difference in THC content between the alleged labelled amount and the alleged tested amount in this particular product is not material. No loss or damages have been proven. No consumer was likely to have been harmed because of the labelling difference as the minimal amount of THC in a CBD product is immaterial..

The Company disputes the allegations and has been and will continue to vigorously defend against the claims. The proceedings are still at an early stage. Estimating an amount or range of possible losses resulting from litigation proceedings is inherently difficult, particularly where key factual and legal issues have not been resolved. For these reasons, the ultimate timing or outcome cannot be predicted, or possible losses or a range of possible losses cannot be reasonably estimated.

The Company may become party to litigation (including arbitration or mediation) from time to time, which could adversely affect its business. In addition, the directors or officers of the Company may become involved in litigation unrelated to the Company which may have an impact on the Company due to the time and attention required to attend to such litigation or may affect the reputation of the Company. Should any litigation in which the Company becomes involved be determined against the Company or should the Company enter into a settlement, the amount of the award or settlement could adversely affect the Company's resources and its ability to continue operating and the market price for the Common Shares. Monitoring and defending litigation, whether meritorious, can be time-consuming and may result in significant expenses, including legal fees and other costs. Even if the Company is involved in litigation and is successful, litigation can redirect significant Company resources and attention away from the business of the Company and may have a material adverse effect on the Company's business, reputation, financial condition, financial performance and financial prospects.

Securities class action litigation often has been brought against cannabis companies following periods of volatility in the market price of their securities. The Company may in the future be the target of similar litigation. Securities litigation could result in substantial costs and damages and divert management's attention and resources.

Non-GAAP Measures

The Company has included "Working capital" (current assets less current liabilities), which is a non-GAAP measure, in this MD&A to supplement its consolidated financial statements, which are presented in accordance with IFRS. The terms IFRS and generally accepted accounting principles ("GAAP") are used interchangeably throughout this MD&A.

The Company believes that these measures, together with measures determined in accordance with IFRS, provide investors with an improved ability to evaluate the underlying performance of the Company. Non-GAAP measures do not have any standardized meaning prescribed under IFRS, and therefore they may not be comparable to similar measures employed by other companies. The data is intended to provide additional information and should not be considered in isolation or as a substitute for measures of performance prepared in accordance with IFRS.

Forward-Looking Statements

Certain statements contained in this MD&A constitute forward-looking information or forward-looking statements under applicable securities laws (collectively, "forward-looking statements"). These statements relate to future events or future performance, business prospects or opportunities of the Company. All statements other than statements of historical fact may be forward-looking statements. Any statements that express or involve discussions with respect to predictions, expectations, beliefs, plans, projections, objectives, assumptions or future events or performance (often, but not always, using words or phrases such as "seek", "anticipate", "plan", "continue", "estimate", "expect", "may", "will", "project", "predict", "forecast", "potential", "targeting", "intend", "could", "might", "should", "believe" and similar expressions) are not statements of historical fact and may be "forward-looking statements".

Examples of forward-looking statements in this MD&A include, but are not limited to, statements in respect of: the Company’s business objectives; the Company's intention to dispose of its cannabis assets; expectations regarding whether the Arrangement will be consummated, including whether conditions to the consummation of the Arrangement will be satisfied, or the anticipated timing for the closing of the Arrangement; the Company's ability to control its working capital, obtain financing or manage capital expenditures; operations of the Company's subsidiaries; potential transactions and development strategies, including those of its subsidiaries; the impact of the ongoing COVID-19 crisis; strategic alternatives related to the Company's assets; the focus of the Company's efforts; strategic partnerships entered into by the Company; and the effect that each risk factor will have on the Company

Forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause actual results or events to differ materially from those anticipated in such forward-looking statements. The reader of these statements is cautioned that any such statements are not guarantees of future performance and actual results or developments may differ materially from those projected in the forward-looking statements. These forward-looking statements involve risks and uncertainties relating to, among others: the impact of the ongoing COVID-19 crisis; the ability of the Company to complete the Arrangement; the ability of the Company to dispose of its assets; the continued availability of capital financing and general economic, market or business conditions; the Company's ability to execute its business plans; changes in laws, regulations and guidelines; changes in government; changes in government policy; the Company's reliance on key persons; failure of counterparties to perform contractual obligations; difficulties in securing additional financing; results of litigation; reputational risks; risks related to key persons; changes in the Company's over-all business strategy; and the Company's assumptions stated herein being correct. See "Risks and Uncertainties" in this MD&A.

The Company believes that the expectations reflected in any forward-looking statements are reasonable, but no assurance can be given that these expectations will prove to be correct and such forward-looking statements included in, or incorporated by reference into, this MD&A should not be unduly relied upon. These statements speak only as of the date of this MD&A. The Company does not intend, and does not assume any obligation, to update these forward-looking statements, except as required by applicable laws. Actual results may differ materially from those expressed or implied by such forward-looking statements.