

POLLARD **banknote** limited

December 31, 2015

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

FOR THE YEAR ENDED DECEMBER 31, 2015

March 14, 2016

This management's discussion and analysis ("MD&A") of Pollard Banknote Limited ("Pollard") for the year ended December 31, 2015, is prepared as at March 14, 2016, and should be read in conjunction with the accompanying audited financial statements of Pollard and the notes therein as at December 31, 2015. Results are reported in Canadian dollars and have been prepared in accordance with International Financial Reporting Standards ("GAAP" or "IFRS").

Forward-Looking Statements

Certain statements in this report may constitute "forward-looking" statements which involve known and unknown risks, uncertainties and other factors which may cause actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by such forward looking statements. When used in this document, such statements include such words as "may," "will," "expect," "believe," "plan" and other similar terminology. These statements reflect management's current expectations regarding future events and operating performance and speak only as of the date of this document. There should not be an expectation that such information will in all circumstances be updated, supplemented or revised whether as a result of new information, changing circumstances, future events or otherwise.

Use of Non-GAAP Financial Measures

Reference to "Adjusted EBITDA" is to earnings before interest, income taxes, depreciation and amortization, unrealized foreign exchange gains and losses, mark-to-market gains and losses on foreign currency contracts, and certain non-recurring items including start-up costs. Adjusted EBITDA is an important metric used by many investors to compare issuers on the basis of the ability to generate cash from operations and management believes that, in addition to net income, Adjusted EBITDA is a useful supplementary measure.

Adjusted EBITDA is a measure not recognized under GAAP and does not have a standardized meaning prescribed by GAAP. Therefore, this measure may not be comparable to similar measures presented by other entities. Investors are cautioned that Adjusted EBITDA should not be construed as an alternative to net income determined in accordance with GAAP as an indicator of Pollard's performance or to cash flows from operating, investing and financing activities as measures of liquidity and cash flows.

Basis of Presentation

The results of operations in the following discussions encompass the consolidated results of Pollard for the year ended December 31, 2015. All figures are in millions except for per share amounts.

POLLARD BANKNOTE LIMITED

Overview

Pollard Banknote Limited ("Pollard") is one of the leading providers of products and services to the lottery and charitable gaming industries throughout the world. Management believes Pollard is the largest provider of instant-win scratch tickets ("instant tickets") based in Canada and the second largest producer of instant tickets in the world.

Pollard produces and provides a comprehensive line of instant tickets and lottery services including: licensed products, distribution, SureTrack® lottery management system, retail telephone selling ("tel-sell"), marketing, iLottery, interactive gaming, Social Instants™, retail management services and instant ticket vending machines. In addition, Pollard's charitable gaming product line includes pull-tab (or break-open) tickets, bingo paper, pull-tab vending machines and ancillary products such as pull-tab counting machines. Pollard also markets products to the commercial gaming and security sector including such items as promotional scratch and win tickets, transit tickets and parking passes.

Pollard's lottery products are sold extensively throughout Canada, the United States and the rest of the world, wherever applicable laws and regulations authorize their use. Pollard serves over 60 instant ticket lotteries including a number of the largest lotteries throughout the world. Charitable gaming products are mostly sold in the United States and Canada where permitted by gaming regulatory authorities. Pollard serves a highly diversified customer base in the charitable gaming market of over 250 independent distributors with the majority of revenue generated from repeat business.

Product line breakdown of revenue

	Year ended December 31, 2015	Year ended December 31, 2014
Instant Tickets	90%	89%
Charitable Gaming Products	9%	10%
Vending Machines	1%	1%

Geographic breakdown of revenue

	Year ended December 31, 2015	Year ended December 31, 2014
United States	49%	50%
Canada	24%	22%
International	27%	28%

The following financial information should be read in conjunction with the accompanying financial statements of Pollard and the notes therein as at and for the year ended December 31, 2015.

SELECTED FINANCIAL INFORMATION

(millions of dollars, except per share information)

	Year ended December 31, 2015	Year ended December 31, 2014	Year ended December 31, 2013	Year ended December 31, 2012
Sales	\$221.0	\$194.5	\$184.9	\$162.4
Cost of sales	176.7	153.4	149.7	129.7
Gross profit	44.3	41.1	35.2	32.7
<i>Gross profit as a % of sales</i>	20.0%	21.1%	19.0%	20.1%
Administration expenses	19.2	17.0	15.2	13.6
<i>Expenses as a % of sales</i>	8.7%	8.7%	8.2%	8.4%
Selling expenses	7.4	6.9	6.8	6.1
<i>Expenses as a % of sales</i>	3.3%	3.5%	3.7%	3.8%
Net income	7.5	8.7	5.4	6.5
<i>Net income as a % of sales</i>	3.4%	4.5%	2.9%	4.0%
Adjusted EBITDA	26.8	25.6	22.7	19.9
<i>Adjusted EBITDA as a % of sales</i>	12.1%	13.2%	12.3%	12.3%
Earnings per share (basic)	\$0.32	\$0.37	\$0.23	\$0.28
Earnings per share (diluted)	\$0.32	\$0.37	\$0.23	\$0.28
	December 31, 2015	December 31, 2014	December 31, 2013	December 31, 2012
Total Assets	\$164.1	\$149.3	\$133.4	\$127.0
Total Non-Current Liabilities	\$96.3	\$89.2	\$79.2	\$83.4

RECONCILIATION OF NET INCOME TO ADJUSTED EBITDA

(millions of dollars)

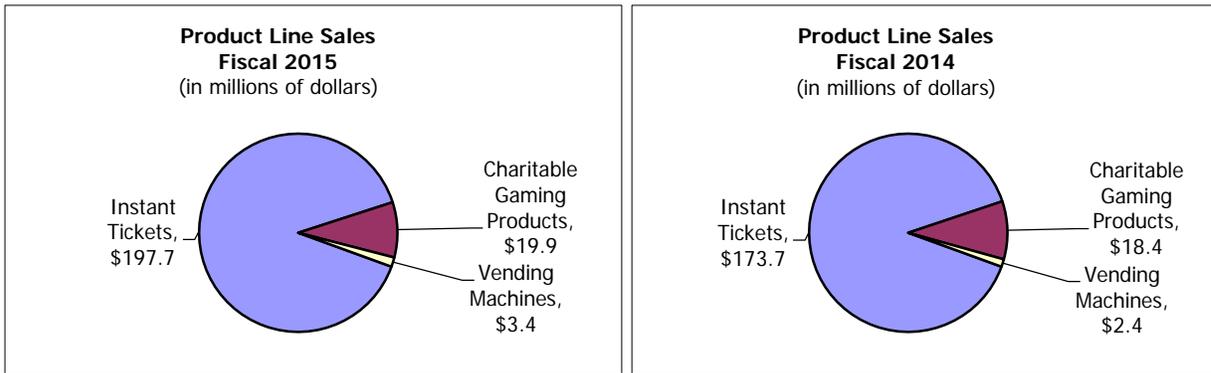
	Year ended December 31, 2015	Year ended December 31, 2014	Year ended December 31, 2013	Year ended December 31, 2012
Net income	\$7.5	\$8.7	\$5.4	\$6.5
Adjustments:				
Amortization and depreciation	8.4	7.9	8.6	7.8
Interest	2.9	2.9	3.4	3.4
Unrealized foreign exchange (gain) loss	3.8	1.7	1.0	(0.1)
Mark-to-market (gain) loss on foreign currency contracts	(0.5)	0.1	0.4	-
Start-up costs – Michigan iLottery	-	0.6	-	-
Income taxes	4.7	3.7	3.9	2.3
Adjusted EBITDA	\$26.8	\$25.6	\$22.7	\$19.9

REVIEW OF OPERATIONS

Financial and operating information has been derived from, and should be read in conjunction with, the consolidated financial statements of Pollard and the selected financial information disclosed in this MD&A.

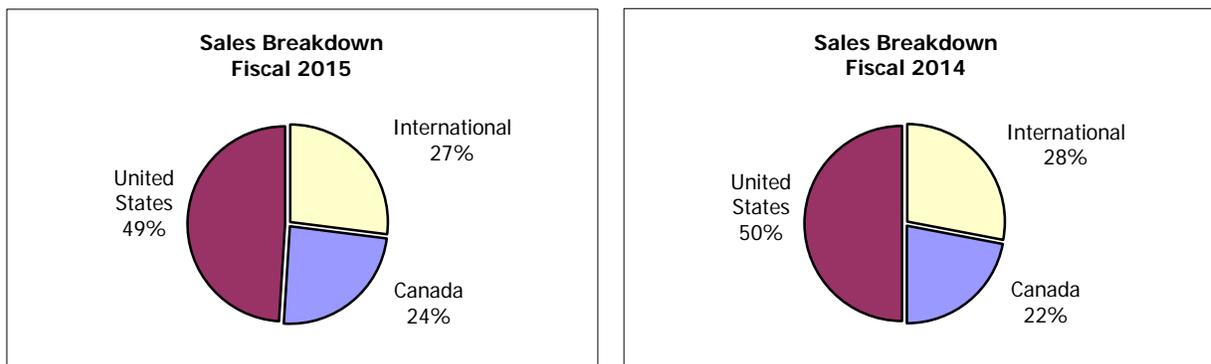
ANALYSIS OF RESULTS FOR THE YEAR ENDED DECEMBER 31, 2015

Sales



During the year ended December 31, 2015 ("Fiscal 2015" or "2015"), Pollard achieved sales of \$221.0 million, compared to \$194.5 million in the year ended December 31, 2014 ("Fiscal 2014" or "2014"). Factors impacting the \$26.5 million sales increase were:

During Fiscal 2015, Pollard generated approximately 65.0% (2014 – 62.3%) of its revenue in U.S. dollars including a portion of international sales which are priced in U.S. dollars. During Fiscal 2015 the actual U.S. dollar value was converted to Canadian dollars at an average rate of \$1.269 compared to an average rate of \$1.097 during Fiscal 2014. This 15.6% increase in the U.S. dollar value resulted in an approximate increase of \$19.4 million in revenue relative to Fiscal 2014. Also during Fiscal 2015, the Canadian dollar strengthened against the Euro resulting in an approximate decrease of \$0.5 million in revenue relative to Fiscal 2014.



Higher instant ticket volumes increased sales in Fiscal 2015 by \$8.8 million compared to Fiscal 2014. Lower sales of our ancillary instant ticket products and services, primarily licensed games, decreased sales by \$1.5 million from Fiscal 2014. Higher instant ticket average selling prices for 2015 increased sales by \$1.0 million compared to 2014. Charitable gaming volumes were lower than Fiscal 2014 decreasing sales by \$1.6 million, which was partially offset by the increase in average selling price which

increased sales by \$0.4 million. An increase in machine volumes in Fiscal 2015 increased sales by \$0.5 million when compared to 2014.

Cost of sales and gross profit

Cost of sales was \$176.7 million in Fiscal 2015 compared to \$153.4 million in Fiscal 2014. Cost of sales was higher in Fiscal 2015 relative to Fiscal 2014 as a result of higher exchange rates on U.S. dollar transactions in 2015, which increased cost of sales approximately \$15.1 million, an increase in instant ticket volumes and higher manufacturing overheads. Partially offsetting these increases were reduced costs due to lower sales of ancillary instant ticket products and services and the elimination of iLottery start-up costs incurred in Fiscal 2014.

Gross profit was \$44.3 million (20.0% of sales) in Fiscal 2015 compared to \$41.1 million (21.1% of sales) in Fiscal 2014. This increase was due mainly to the increase in instant tickets volumes as well as the impact of the weakening of the Canadian dollar relative to the U.S. dollar and the elimination of the non-recurring start-up costs incurred in 2014. The decrease in gross profit percentage was primarily the result of higher manufacturing overheads and lower sales of ancillary instant ticket products. These decreases were partially offset by the impact of the weakening Canadian dollar.

Administration expenses

Administration expenses increased to \$19.2 million in Fiscal 2015 from \$17.0 million in Fiscal 2014 primarily as a result of higher professional fees, the increased Canadian dollar equivalent of U.S. dollar denominated expenses and increased compensation expenses including incentive accruals.

Selling expenses

Selling expenses increased to \$7.4 million in Fiscal 2015 from \$6.9 million in Fiscal 2014 primarily as a result of the increased cost of U.S. dollar denominated expenses as a result of the strengthening against the Canadian dollar.

Interest expense

Interest expense was \$2.9 million in Fiscal 2015 which was similar to \$2.9 million in Fiscal 2014.

Foreign exchange loss

The net foreign exchange loss was \$3.1 million in Fiscal 2015 compared to a net loss of \$1.9 million in Fiscal 2014. The 2015 net foreign exchange loss consisted of a \$3.8 million unrealized loss which was primarily a result of the increased Canadian equivalent value of U.S. denominated debt with the significant weakening of the Canadian dollar relative to the U.S. dollar. This loss was partially offset by the realized foreign exchange gain of \$0.7 million as a result of foreign currency denominated account receivables collected being converted into Canadian dollars at favorable foreign exchange rates.

The 2014 net foreign exchange loss consisted of a \$1.7 million unrealized loss which was primarily as a result of the increased Canadian equivalent value of U.S. denominated debt and accounts payable due to the weakening of the Canadian dollar relative to the U.S. dollar. The realized foreign exchange loss of \$0.2 million was predominately a result of decreased value of foreign currency converted into Canadian dollars during Fiscal 2014.

Amortization and depreciation

Amortization and depreciation, including depreciation of property and equipment and the amortization of deferred financing costs and intangible assets, totaled \$8.4 million during Fiscal 2015 which increased from \$7.9 million during Fiscal 2014 due to increased amortization of deferred financing costs and patents.

Adjusted EBITDA

Adjusted EBITDA was \$26.8 million in Fiscal 2015 compared to \$25.6 million in Fiscal 2014. The primary reasons for the increase in Adjusted EBITDA of \$1.2 million were the increase in gross profit of \$3.1 million (net of amortization and excluding \$0.6 million in non-recurring iLottery start-up costs in 2014) and the increase in the realized foreign exchange gains of \$0.9 million. These increases were partially offset by increased administration expenses of \$2.2 million and an increase in selling expenses of \$0.5 million.

Income taxes

Income tax expense was \$4.7 million in Fiscal 2015, an effective rate of 38.8%, which was higher than our expected effective rate of 26.8% due primarily to differences relating to the foreign exchange impact of Canadian dollar denominated debt in its U.S. subsidiaries. Pollard has capitalized its U.S. operations using intercompany Canadian dollar debt. The weakening of the Canadian dollar versus the U.S. dollar results in a future gain on debt repayment for U.S. tax purposes in the subsidiary, creating a deferred tax expense with no related income (as the gain is eliminated on consolidation). This increased the consolidated provision percentage approximately 30%. Other permanent differences relating to the foreign exchange translation of property, plant and equipment decreased the provision by approximately 15%. Current income tax expense was in a recovery position due to accelerated tax depreciation on capital expenditures.

Income tax expense was \$3.7 million in Fiscal 2014, an effective rate of 30.0%, due primarily to differences relating to the foreign exchange impact of Canadian dollar denominated debt in its U.S. subsidiaries. Pollard has capitalized its U.S. operations using intercompany Canadian dollar debt. The weakening of the Canadian dollar versus the U.S. dollar results in a future gain on debt repayment for U.S. tax purposes in the subsidiary, creating a deferred tax expense with no related income (as the gain is eliminated on consolidation).

Net income

Net income was \$7.5 million in Fiscal 2015 compared to net income of \$8.7 million in Fiscal 2014. The primary reason for the decrease in net income was the increase in income taxes of \$1.0 million. Additionally, the primary reasons for the decrease in income before income taxes were the increase in administration expenses of \$2.2 million, the increase in selling expenses of \$0.5 million and an increase in foreign exchange loss of \$1.2 million. Partially offsetting these decreases to income before income taxes were the increase in gross profit of \$3.2 million and the increase in the non-cash mark-to-market gain on foreign currency contracts of \$0.6 million.

Earnings per share (basic and diluted) decreased to \$0.32 per share in Fiscal 2015 from \$0.37 per share in Fiscal 2014.

Liquidity and Capital Resources

Cash provided by operating activities

For the year ended December 31, 2015, cash flow provided by operating activities was \$19.7 million compared to \$18.9 million in Fiscal 2014. Higher net income before income taxes after non-cash adjustments in Fiscal 2015 contributed to the increase in cash provided by operating activities compared to Fiscal 2014. Changes in the non-cash component of working capital decreased cash flow from operations by \$2.8 million for Fiscal 2015 (due primarily to increases in accounts receivable, prepaid expenses and income taxes receivable, and a decrease in accounts payable and accrued liabilities, partially offset by a decrease in inventory), compared to a decrease of \$0.7 million for Fiscal 2014 (due primarily to increases in inventory and prepaid expenses, partially offset by a decrease in accounts receivable and an increase in accounts payable and accrued liabilities).

Cash used for interest payments decreased to \$2.8 million in 2015 as compared to \$3.1 million in 2014 due to lower interest rates. As well, cash used for pension plan contributions decreased to \$2.9 million in 2015 as compared to \$3.6 million in 2014 due to the elimination of special payment requirements in 2014. Cash used for income tax payments increased to \$3.1 million in 2015 from \$2.1 million in 2014. Taxable income in Canada increased in 2014 due to improved operating results, however Pollard was not required to make installments during 2014, therefore the income taxes due for 2014 were payable at the end of February 2015.

Cash used for investing activities

In the year ended December 31, 2015, cash used for investing activities was \$16.5 million compared to \$18.8 million in the year ended December 31, 2014. In Fiscal 2015, capital expenditures were \$15.4 million, with \$12.0 million in expenditures relating to the new press project including various auxiliary equipment. Pollard expended \$0.4 million on its investment in its iLottery joint venture and \$0.7 million on additions to intangible assets, net of investment tax credits. These intangible additions primarily related to implementation costs, including capitalized internal costs, for ERP software.

In Fiscal 2014, capital expenditures were \$17.6 million, including \$15.1 million in expenditures relating to the new press project. Pollard expended \$1.2 million on additions to intangible assets, primarily related to implementation costs, including capitalized internal costs, for ERP software.

Cash used for financing activities

Cash used for financing activities was \$2.3 million in the year ended December 31, 2015, compared to cash used for financing activities of \$1.6 million in the year ended December 31, 2014.

During Fiscal 2015 proceeds from long-term debt of \$1.0 million were offset by \$0.4 million of financing costs and dividends paid of \$2.8 million.

During Fiscal 2014 cash was used to reduce long-term debt by \$5.6 million, and incur \$0.2 million in deferred financing costs and pay dividends of \$2.8 million. Partially offsetting was the proceeds from the subordinated debt of \$6.8 million to fund a portion of the new press.

As at December 31, 2015, Pollard had unused committed credit facility of \$17.6 million. This amount is available to be used for future working capital requirements, contractual obligations, capital expenditures and dividends.

**ANALYSIS OF RESULTS FOR THE PERIOD OCTOBER 1, 2015 TO DECEMBER 31, 2015
FOURTH QUARTER OF 2015**

SELECTED FINANCIAL INFORMATION

(millions of dollars)

	Three months ended December 31, 2015	Three months ended December 31, 2014
	(unaudited)	(unaudited)
Sales	\$57.2	\$43.2
Cost of sales	45.6	33.4
Gross profit	11.6	9.8
Administration	5.7	4.6
Selling	2.0	1.7
Other (income) expense	0.1	(0.1)
Income from operations	3.8	3.6
Finance costs	1.8	1.5
Income before income taxes	2.0	2.1
Income taxes:		
Current (recovery)	(4.5)	0.2
Future (reduction)	5.3	(0.2)
	0.8	-
Net income	<u>\$1.2</u>	<u>\$2.1</u>
Adjustments:		
Amortization and depreciation	2.4	2.0
Interest	0.8	0.6
Unrealized foreign exchange loss	1.1	0.9
Income taxes	0.8	-
Adjusted EBITDA	<u>\$6.3</u>	<u>\$5.6</u>

Sales

During the three months ended December 31, 2015, Pollard achieved sales of \$57.2 million, compared to \$43.2 million in the three months ended December 31, 2014. Factors impacting the \$14.0 million sales increase were:

During the three months ended December 31, 2015, Pollard generated approximately 62.0% (2014 – 60.8%) of its revenue in U.S. dollars including a portion of international sales which were priced in U.S. dollars. During the fourth quarter of 2015 the actual U.S. dollar value was converted to Canadian dollars at an average rate of \$1.336, compared to an average rate of \$1.137 during the fourth quarter of 2014. This 17.5% increase in the value of the U.S. dollar resulted in an approximate increase of \$5.3 million in revenue relative to 2014. Also during the fourth quarter of 2015, the Canadian dollar weakened against the Euro resulting in an approximate increase of \$0.2 million in revenue relative to 2014.

Instant ticket sales volumes for the fourth quarter of 2015 were higher than the fourth quarter of 2014 by 9.5%, which combined with an increase in our ancillary instant ticket products and services volumes, primarily sales of our SureTrack® lottery management system, increased sales by \$4.8 million. Instant ticket sales volumes in the fourth quarter of 2014 were lower due to a significant amount of product in transit, which was not recorded in sales until the first quarter of 2015. In addition, an increase in average selling price of instant tickets compared to 2014 further increased sales by \$3.7 million.

Cost of sales and gross profit

Cost of sales was \$45.6 million in the fourth quarter of 2015 compared to \$33.4 million in the fourth quarter of 2014. Cost of sales was higher in the quarter relative to the fourth quarter of 2014 as a result of higher exchange rates on U.S. dollar transactions in 2015 which increased cost of sales approximately \$4.6 million, an increase in instant ticket volumes and higher manufacturing overheads.

Gross profit was \$11.6 million (20.3% of sales) in the fourth quarter of 2015 compared to \$9.8 million (22.7% of sales) in the fourth quarter of 2014. This increase in gross profit dollars was due to the impact of the weakening Canadian dollar, the higher instant ticket sales volumes and higher lottery management sales. The decrease in gross profit percentage was due to the higher manufacturing overheads and the instant ticket sales mix.

Administration expenses

Administration expenses were \$5.7 million in the fourth quarter of 2015 which was higher compared to \$4.6 million in the fourth quarter of 2014 primarily as a result of higher professional fees, the increased Canadian dollar equivalent of U.S. dollar denominated expenses and increased compensation expenses including incentive accruals.

Selling expenses

Selling expenses increased to \$2.0 million in the fourth quarter of 2015 from \$1.7 million in the fourth quarter of 2014 primarily as a result of the increased cost of U.S. dollar denominated expenses due to the strengthening against the Canadian dollar.

Interest expense

Interest expense increased to \$0.8 million in the fourth quarter of 2015 from \$0.6 million in the fourth quarter of 2014 primarily as a result of no longer capitalizing borrowing costs related to the new press project during 2015.

Foreign exchange loss

The net foreign exchange loss was \$0.9 million in the fourth quarter of 2015 compared to a net loss of \$0.8 million in the fourth quarter of 2014. The 2015 net foreign exchange loss consisted of a \$1.1 million unrealized loss which was primarily a result of the increased Canadian equivalent value of U.S. denominated debt with the weakening of the Canadian dollar relative to the U.S. dollar. This loss was partially offset by the realized foreign exchange gain of \$0.2 million, as a result of foreign currency denominated account receivables collected being converted into Canadian dollars at favorable foreign exchange rates.

The 2014 net foreign exchange loss consisted of an unrealized foreign exchange loss of \$0.9 million which was primarily as a result of the increased Canadian equivalent value of U.S. denominated payables and long-term debt caused by the weakening of the Canadian dollar relative to the U.S. dollar at the end of the quarter. The additional realized foreign exchange gain of \$0.1 million, was predominately a result of the increased value of U.S. denominated receivables, offset partially by increased cost of U.S. denominated payables.

Amortization and depreciation

Amortization and depreciation, including depreciation of property, plant and equipment and the amortization of deferred financing costs and intangible assets, totaled \$2.4 million during the fourth quarter of 2015 which increased from \$2.0 million during the fourth quarter of 2014 primarily as a result of increased depreciation of property, plant and equipment and amortization of patents in 2015.

Adjusted EBITDA

Adjusted EBITDA was \$6.3 million in the fourth quarter of 2015 compared to \$5.6 million in the fourth quarter of 2014. The primary reasons for the increase in Adjusted EBITDA were the increase in gross profit (net of amortization and depreciation) of \$2.2 million, partially offset by higher administration expenses of \$1.1 million, higher selling expenses of \$0.3 million and an increase in other expenses of \$0.2 million.

Income taxes

Income tax expense was \$0.8 million in the fourth quarter of 2015, an effective rate of 37.8% which was higher than our expected effective rate of 26.8% due primarily to difference relating to the foreign exchange impact of Canadian dollar denominated debt in its U.S. subsidiaries. Pollard has capitalized its U.S. operations using intercompany Canadian dollar debt. The significant weakening of the Canadian dollar versus the U.S. dollar in the fourth quarter results in a future gain on debt repayment for U.S. tax purposes in the subsidiary, creating a deferred tax expense with no related income (as the gain is eliminated on consolidation). This increased the consolidated provision percentage by about 31%. Other permanent differences relating to the foreign exchange translation of property, plant and equipment decreased the provision by approximately 21%. Current income tax expense was in a recovery position due to accelerated tax depreciation on capital expenditures.

Income tax expense was nil in the fourth quarter of 2014, an effective rate of 0.0%. Included in the effective rate are differences relating to the foreign exchange impact of Canadian dollar denominated debt in its U.S. subsidiaries. Pollard has capitalized its U.S. operations using intercompany Canadian dollar debt. The weakening of the Canadian dollar versus the U.S. dollar in the fourth quarter results in a future gain on debt repayment for U.S. tax purposes in the subsidiary, creating a deferred tax expense with no related income (as the gain is eliminated on consolidation). This increased the consolidated provision percentage by about 16%. Other permanent differences relating to the foreign exchange translation of property, plant and equipment decreased the provision by approximately 15%. In addition, adjustments in the annual estimated tax rate to the actual tax rate in the U.S. subsidiaries decreased the provision by approximately 28%.

Net income

Net income was \$1.2 million in the fourth quarter of 2015 compared to \$2.1 million in the fourth quarter of 2014. The primary reason for the decrease in net income was the increase in income tax expense of \$0.8 million. Additionally, the primary reasons for the decrease in income before income taxes were the increase in administration expenses of \$1.1 million, the increase in selling expense of \$0.3 million, the increase in other expense of \$0.2 million and the increase in interest expense of \$0.2 million. Partially offsetting these decreases in income before income taxes was the increase in gross profit of \$1.8 million.

Earnings per share (basic and diluted) decreased to \$0.05 per share in the fourth quarter of 2015 from \$0.09 per share in the fourth quarter of 2014.

Quarterly Information

(unaudited)
(millions of dollars)

	Q4 2015	Q3 2015	Q2 2015	Q1 2015	Q4 2014	Q3 2014	Q2 2014	Q1 2014
Sales	\$57.2	\$57.9	\$51.4	\$54.5	\$43.2	\$53.5	\$47.1	\$50.7
Adjusted EBITDA	6.3	7.5	6.3	6.7	5.6	7.3	6.4	6.3
Net income	1.2	1.9	3.0	1.4	2.1	1.7	3.7	1.2

Q3 and Q4 2015 sales were higher due to the weakening of the Canadian dollar relative to the U.S. dollar.

Q2 2015 net income was higher due to the increased non-cash mark-to-market gain on foreign currency contracts and higher foreign exchange gain.

Q1 2015 sales and adjusted EBITDA were higher due to higher instant ticket volumes and weaker Canadian dollar.

Q4 2014 sales and adjusted EBITDA were lower due to lower instant ticket volumes.

Q3 2014 sales were higher predominately due to higher average selling price of instant tickets. Q3 2014 adjusted EBITDA was higher due to higher gross profit.

Q2 2014 net income was higher due to higher gross profit and increased non-cash mark-to-market gains on foreign currency contracts.

Sales in Q1 2014 were higher due to increased ancillary instant ticket sales, primarily licensed games.

Productive Capacity

Management has defined the current productive capacity, factoring in the new press becoming fully operational, as the level of operations necessary to maintain a minimum Adjusted EBITDA of \$30.0 to \$35.0 million on an annualized basis. Due to varying factors implicit in the nature of the lottery industry and the instant ticket market, productive capacity can best be measured through a financial output such as Adjusted EBITDA and cash flow. A significant impact on our Adjusted EBITDA capacity will be the timing of the ramp up of our new press and how quickly increased volumes will be attained through the relatively long sales cycle of the lottery industry. A number of factors impact the level of Adjusted EBITDA including physical plant capacity, machine capacity, nature of product and service offerings produced and mix of customers. Changes to productive capacity have occurred primarily through expenditures on fixed assets and improved processes and other internal improvement measures. Productive capacity is also impacted by changes in foreign exchange relationships. There have been no increases in productive capacity due to acquisitions since Pollard's initial public offering ("IPO") in August 2005.

Pollard's strategy with respect to productive capacity is to expend the required funds and resources to maintain the assets required to generate the targeted cash flow. In addition, dependent on certain market conditions and limitations on available funds, projects are incurred to increase cash inflow or decrease cash outflow. The nature of the lottery industry does not in itself lead to significant obsolescence risk with the operating assets. To grow productive capacity, ongoing investment in new technology, new fixed assets and new intangible assets is required. Pollard utilizes a number of individual strategies to maintain and grow productive capacity including a capital expenditure budget and a rigorous formal approval process, flexible individual customer management relationships and structured maintenance programs throughout all of the facilities.

An important component to managing and growing productive capacity is the management of certain intangible assets, including customer contracts and relationships, patents, computer software and goodwill. Certain of these assets are reflected in Pollard's financial statements due to the use of continuity of interest method of accounting during the transfer of the business at Pollard's IPO.

Management focuses on maintaining and growing the value of the customer relationship through winning contract renewals, pursuing and obtaining new contracts and assisting existing customers growing their instant ticket product lines. Regular commitment to research and development allows continual development of patents, software and additional technological assets that maintain and increase operating income and cash flow. Detailed cost benefit analysis is performed for any significant investment of funds or resources in order to minimize the associated risks that these assets will not be able to generate the expected level of cash flow. Where new opportunities are identified, such as a new marketing opportunity or a new machine or process able to reduce input costs, consideration is given to revise plans and take advantage of these prospects.

Certain risks are associated with projects aimed at increasing productive capacity, including increases in working capital, acquisition or development of intellectual property, development of additional products

or services and purchases of fixed assets. If these investments fail to increase Adjusted EBITDA and cash flow, then productive capacity will ultimately decrease over time due to the consumption of these investment resources. The impact on productive capacity may also depend upon the completion and start up timing of certain investment projects.

Working Capital

Net non-cash working capital varies throughout the year based on the timing of individual sales transactions and other investments. The nature of the lottery industry is few individual customers who generally order large dollar value transactions. As such, the change in timing of a few individual orders can impact significantly the amount required to be invested in inventory or receivables at a particular period end. The high value, low volume of transactions results in some significant volatility in non-cash working capital, particularly during a period of rising volumes. Similarly, the timing of the completion of the sales cycle through collection can significantly impact non-cash working capital.

Instant tickets are produced specifically for individual clients resulting in a limited investment in finished goods inventory. Customers are predominantly government agencies, which result in regular payments. There are a limited number of individual customers, and therefore net investment in working capital is managed on an individual customer by customer basis, without the need for company wide benchmarks.

The overall impact of seasonality does not have a material impact on the carrying amounts in working capital.

As at December 31, 2015, Pollard's investment in non-cash working capital increased \$2.8 million compared to December 31, 2014, primarily as a result of an increased investment in accounts receivables, prepaid expenses and income taxes receivable, and increased accounts payables, which were partially offset by a decreased investment in inventory.

	December 31, 2015	December 31, 2014
Working Capital	\$39.1	\$30.2
Total Assets	\$164.1	\$149.3
Total Non-Current Liabilities	\$96.3	\$89.2

Credit Facility

Pollard's credit facility was renewed effective June 30, 2015. The credit facility provides loans of up to \$71.8 million for its Canadian operations (denominated in Canadian and U.S. dollars), \$3.9 million for a term facility and up to US\$12.0 million for its U.S. subsidiaries. Borrowings under the credit facility bear interest at fixed and floating rates based on Canadian and U.S. prime bank rates, banker's acceptances or LIBOR. At December 31, 2015, the outstanding letters of guarantee were \$1.3 million. The remaining balance available for drawdown under the credit facility was \$17.6 million.

As at December 31, 2015, \$3.9 million of the term facility remained outstanding. Repayment of the term facility commenced on June 30, 2015, in the form of quarterly principal repayments of \$0.3 million plus interest. Repayments permanently reduce the term facility commitment available.

Under the terms and conditions of the credit facility agreement Pollard is required to maintain certain financial covenants including working capital ratios, debt to income before interest, income taxes, amortization and depreciation (“Adjusted EBITDA”) ratios and certain debt service coverage ratios. As at December 31, 2015, Pollard is in compliance with all covenants.

Pollard’s credit facility, including the term facility, is secured by a first security interest in all of the present and after acquired property of Pollard’s operating subsidiaries. The facility can be prepaid without penalties. Under the terms of the agreement the facility was committed for a period, renewable June 30, 2016 (“Facility Expiry Date”). If the facility is not renewed, the loans are repayable one year after the Facility Expiry Date, except for the scheduled principal repayments on the term facility. As such, the credit facility has effectively a two year term expiring June 30, 2017.

Pollard believes that its credit facility, including the term facility, subordinated loan from Pollard Equities Limited and ongoing cash flow from operations will be sufficient to allow it to meet ongoing requirements for investment in capital expenditures, working capital and dividends at existing business levels.

Subordinated Loan

On April 2, 2014, Pollard’s former subsidiary, Pollard Holdings Limited Partnership, entered into a loan agreement with Pollard Equities Limited (“Equities”) for a subordinated term loan facility with a seven year term in the amount of \$6.8 million. Equities owns approximately 73.5% of Pollard’s outstanding shares. Effective January 1 2015, Pollard Banknote Limited assumed the subordinated debt on completion of the amalgamation of the Canadian entities. Principal payments on the subordinated loan facility will commence the month following the later of: twenty-four months from the date of the first advance, completed on April 4, 2014, or the date of repayment in full of the additional term facility. Based on the current repayment schedule, the term facility will be repaid in full in March 2019, at which time principal payments on the subordinated debt will commence. Interest on the subordinated term loan facility commences with the first draw at a rate of 9%. The loan is fully subordinated to the secured credit facilities.

Outstanding Share Data

As at December 31, 2015 and March 14, 2016, outstanding share data was as follows:

Common shares	23,543,158
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Share Options

Under the Pollard Banknote Limited Stock Option Plan the Board of Directors has the authority to grant options to purchase common shares to eligible persons and to determine the applicable terms. The aggregate maximum number of common shares available for issuance from Pollard’s treasury under the Option Plan is 2,354,315 common shares.

On March 5, 2014, the Board of Directors approved the award of 100,000 options to purchase common shares of Pollard for certain key management personnel. The options were granted on March 10, 2014, and have a seven year term, vesting 25% per year over the first four years. The exercise price of the options was equal to the closing price of the common shares on March 7, 2014.

Contractual Obligations

Pollard rents premises and equipment under long-term operating leases. The following is a schedule by year of commitments and contractual obligations outstanding:

(millions of dollars)	Total	<1 Year	2-3 Years	4-5 Years	Thereafter
Long-term debt	\$73.3	\$1.2	\$72.1	-	-
Subordinated debt	\$6.8	-	-	\$6.0	\$0.8
Other non-current liabilities	\$0.4	-	\$0.4	-	-
Pension liability	\$11.3	-	-	-	\$11.3
Interest on long-term debt	\$3.7	\$2.3	\$1.4	-	-
Interest on subordinated debt	\$2.6	\$0.6	\$1.2	\$0.8	-
Operating leases	\$25.2	\$4.9	\$8.3	\$5.5	\$6.5
Total	\$123.3	\$9.0	\$83.4	\$12.3	\$18.6

Pension Obligations

Pollard sponsors four non-contributory defined benefit pension plans, of which three are final pay plans and one is a flat benefit plan. As of December 31, 2015, the aggregate fair value of the assets of Pollard's defined benefit pension plans was \$40.1 million and the accrued benefit plan obligations were \$51.3 million. Pollard's total annual funding contribution for all pension plans in 2016 is expected to be approximately \$2.6 million, compared to \$2.4 million in 2015.

Off-Balance Sheet Arrangements

Other than the operating leases described previously, Pollard has no other off-balance sheet arrangements.

Related Party Transactions

During the year ended December 31, 2015, Pollard agreed to exercise its renewal clause on one of its Winnipeg properties leased from an affiliate of Equities. The renewal covers the period from April 2021 to September 2023 with an approximate annual lease rate of \$2.4 million, including an annual amortization of a leasehold improvement allowance of approximately \$1.0 million. The total leasehold allowance is \$2.5 million.

During the year ended December 31, 2015, Pollard paid property rent of \$3.1 million (2014 - \$3.0 million) and \$0.3 million (2014 - \$0.2 million) in plane charter costs to affiliates of Equities. In addition, Pollard paid Equities \$0.6 million (2014 - \$0.4 million) of interest on Pollard's subordinated debt.

During the year ended December 31, 2015, Equities paid Pollard \$0.07 million (2014 – \$0.07 million) for accounting and administration fees.

During the year ended December 31, 2015, Pollard reimbursed operating costs of \$0.5 million (2014 - \$.05 million) to its iLottery partner which are recorded in cost of sales.

At December 31, 2015, Pollard owes Equities and its affiliates \$0.8 million (2014 - \$1.2 million) for rent, interest and other expenses. Also included in accounts payable and accrued liabilities is a net amount owing to Pollard's iLottery partner of \$1.1 million (2014 - nil) for reimbursement of operating costs and capital expenditures, and its share of operating profits.

Critical Accounting Policies and Estimates

The preparation of the financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenue and expenses during the reporting period. Management of Pollard regularly reviews its estimates and assumptions based on historical experience and various other assumptions that it believes would result in reasonable estimates given the circumstances. Actual results could differ from those estimates under different assumptions. The following is a discussion of accounting policies which require significant management judgment and estimation.

Impairment of goodwill

Goodwill represents the excess of the purchase price over the fair value of the net assets acquired of Pollard's U.S. subsidiaries and the excess purchase price over the underlying carrying amount of the portion of the net assets sold as at August 5, 2005, as part of the 26.7% of Pollard sold in conjunction with the IPO, and is not amortized. Goodwill is subject to an annual impairment test. This requires an estimation of the "value in use" or "fair value less costs to sell" of the cash-generating units ("CGUs") to which goodwill is allocated. Estimating a value in use requires Pollard to make an estimate of the expected future cash flows from the CGUs and also to choose a suitable discount rate in order to calculate the present value of those cash flows.

Employee future benefits

Accounting for defined benefit plans requires Pollard to use actuarial assumptions. These assumptions include the discount rate and the rate of compensation increases. These assumptions depend on underlying factors such as economic conditions, government regulations, investment performance, employee demographics and mortality rates.

Income taxes

Pollard is required to evaluate the recoverability of deferred income tax assets. This requires an estimate of Pollard's ability to utilize the underlying future income tax deductions against future taxable income before they expire. In order to evaluate the recoverability of these deferred income tax assets, Pollard must estimate future taxable income.

Future Changes in Accounting Policies

In July 2014, the International Accounting Standards Board ("IASB") issued International Financial Reporting Standards ("IFRS") 9 *Financial Instruments* ("IFRS 9"), which replaces the existing guidance in IAS 39 *Financial Instruments: Recognition and Measurement*. IFRS 9 includes revised guidance on the classification and measurement of financial instruments, a new expected credit loss model for calculating impairment on financial assets, and new general hedge accounting requirements. It also carries forward the guidance on recognition and derecognition of financial instruments from IAS 39. IFRS 9 is required for fiscal years beginning on or after January 1, 2018. Pollard is currently assessing the impact of the new standard on its consolidated financial statements.

In May 2014, the IASB issued IFRS 15 *Revenue from Contracts with Customers*. The new standard specifies the steps and timing for recognizing revenue, as well as requiring more informative, relevant disclosures. IFRS 15 supersedes IAS 11 *Construction Contracts* and IAS 18 *Revenue*. IFRS 15 is required for fiscal years beginning on or after January 1, 2018 with early adoption available. Pollard is currently assessing the impact of the new standard on its consolidated financial statements.

In May 2014, the IASB issued amendments to IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets*. The amendments prohibit the use of revenue based depreciation for property, plant and equipment and significantly limit the use of revenue based amortization for intangibles. These amendments are effective for fiscal years beginning on or after January 1, 2016. Pollard does not expect these amendments to have a material impact on its consolidated financial statements.

In May 2014, the IASB issued amendments to IAS 11 *Interests in Joint Operations*. The amendments require business combination accounting to be applied to acquisition of interest in a joint operation that constitute a business. These amendments are effective for fiscal years beginning on or after January 1, 2016, with early adoption available. Pollard does not expect these amendments to have a material impact on its consolidated financial statements.

In September 2014, the IASB issued amendments to IFRS 10 Consolidated Financial Statements and IAS 28 *Investments in Associates and Joint Ventures* (2011). The amendments address an acknowledged inconsistency between the requirements in IFRS 10 and those in IAS 28 (2011), in dealing with the sale or contribution of assets between an investor and its associate or joint venture. The main consequence of the amendments is that a full gain or loss is recognized when a transaction involves a business (whether it is housed in a subsidiary or not). A partial gain or loss is recognized when a transaction involves assets that do not constitute a business, even if these assets are housed in a subsidiary. These amendments were to be effective for fiscal years beginning on or after January 1, 2016, with early adoption available; however, in December 2015 the IASB decided to defer the effective date for these amendments indefinitely. Pollard is currently assessing the impact of the amendments on its consolidated financial statements.

In December 2014, the IASB issued amendments to IAS 1 *Presentation of Financial Statements*. The amendments will not require any significant change to current practice, but should facilitate improved financial statement disclosures. These amendments are effective for fiscal years beginning on or after January 1, 2016, with early adoption available. Pollard does not expect these amendments to have a material impact on its consolidated financial statements.

In January 2016, the IASB issued IFRS 16 *Leases* which replaces IAS 17 *Leases*. This standard introduces a single lessee accounting model and requires a lessee to recognize assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value. A lessee is required to

recognize a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments. This standard substantially carries forward the lessor accounting requirements of IAS 17, while requiring enhanced disclosures to be provided by lessors. Other areas of the lease accounting model have been impacted, including the definition of a lease. Transitional provisions have been provided. The new standard is effective for annual periods beginning on or after January 1, 2019. Earlier application is permitted for entities that apply IFRS 15 *Revenue from Contracts with Customers* at or before the date of initial adoption of IFRS 16. Pollard is currently assessing the impact of the new standard on its consolidated financial statements.

Industry Risks and Uncertainties

Pollard is exposed to a variety of business and industry risks. A summary of the major risks faced by Pollard is noted below.

Dependence on Key Products

Instant lottery tickets and related services accounted for approximately 90% of Pollard's Fiscal 2015 revenues. Pollard's financial results and condition are substantially dependent on the continued success and growth in sales of this product and the profitability of such sales. Competitive efforts by other manufacturers of similar or substitute products, shifts in consumer preferences or the introduction and acceptance of alternative product offerings could have a material adverse effect on Pollard's business, financial condition, liquidity and results of operations.

Economic Uncertainty

Considerable economic uncertainty and concern over possible recessions and economic downturns have dominated the news in the past few years. Instant lottery tickets account for approximately 90% of revenue and Pollard's financial results and condition are substantially dependent on the continued success and growth in sales of this product and the profitability of such sales. Historically the lottery industry, and particularly the instant ticket product lines, has not shown any significant negative impact during downturns in the economic cycles. However, lotteries, similar to many government agencies, are increasingly under pressure to reduce costs and expenditures. As such, Pollard has witnessed downward pressure on its selling prices. Continued pressure on lotteries to reduce their costs may further negatively impact Pollard's selling prices. Significant shifts in consumer preferences or the introduction and acceptance of alternative product offerings could have a material adverse effect on Pollard's business, financial condition, liquidity and results of operations.

Inability to Sustain Sales or EBITDA Margins

Pollard's income depends upon its ability to generate sales to customers and to sustain its EBITDA margins. These margins are dependent upon Pollard's ability to continue to profitably sell lottery tickets and gaming products and to continue to provide products and services that make it the supplier of choice to its customers. If Pollard's costs of sales or operating costs increase, or other manufacturers of gaming products could compete more favourably with it, Pollard may not be able to sustain its level of sales or EBITDA margins.

Dependence on Major Customers

Pollard's 10 largest customers accounted for approximately 52% of its revenue during Fiscal 2015. Pollard's largest customer accounted for approximately 9% of Pollard's revenues during Fiscal 2015.

The nature of the worldwide lottery industry limits the absolute number of lottery operations. As is customary in the industry, Pollard does have long-term contracts with most of its customers. However, most allow the customer to cancel the contract at will and none guarantee volumes or order levels. A significant reduction of purchases by any of Pollard's largest customers could have a material adverse effect on Pollard's business, financial condition, liquidity and results of operations including the amount of cash available for dividends to shareholders.

Exchange Rate Fluctuation

A significant portion of Pollard's revenues are denominated in foreign currencies, primarily U.S. dollars and Euros, as well as expenses, principally related to its U.S. operations and to the purchase of raw materials, which are denominated in U.S. dollars. Furthermore, although certain raw materials may be purchased in Canadian dollars, they may have inputs that are denominated in foreign currencies. Any changes in the exchange rate between the Canadian dollar and these foreign currencies could have a material effect on the results of Pollard.

For the purposes of financial reporting, any change in the value of the Canadian dollar against the U.S. dollar and Euro during a given financial reporting period would result in a foreign exchange loss or gain on their translation into Canadian dollar equivalent. Further, Pollard's reported earnings could fluctuate materially as a result of revenues and expenses denominated in foreign currencies under GAAP. There can be no assurance that changes in the currency exchange rate will not have a material adverse effect on Pollard or on its ability to maintain a consistent level of dividends in Canadian dollars.

Additional Capital Requirements

Pollard believes that its future operating income will be sufficient to fund operations and planned capital expenditures. However, Pollard may be required to raise additional capital in the future if it decides to make additional acquisitions or significant additional capital expenditures.

The availability of future borrowings and access to capital markets for longer-term future financing depends on prevailing conditions and the acceptability of financing terms offered. There can be no assurances that future borrowings or equity financing will be available or available on acceptable terms.

Competition

The instant ticket and charitable gaming business is highly competitive, and Pollard faces competition from a number of domestic and foreign instant ticket manufacturers and other competitors. Pollard currently has two instant ticket competitors in North America: Scientific Games Corporation and IGT. Charitable gaming competitors include a number of manufacturers such as Arrow International, Inc. and International Gamco, Inc. Internationally, there are a number of lottery instant ticket vendors which compete with Pollard including Scientific Games, IGT, and the Eagle Press Group of Companies.

Some of Pollard's competitors have longer operating histories, greater name recognition, larger customer bases and greater financial, technical and marketing resources than Pollard. These resources may allow them to respond more quickly than Pollard can to new or emerging technologies and to changes in customer requirements. It may also allow them to devote greater resources than Pollard can to the development, promotion and sale of their products. Pollard's competitors may also engage in more extensive research and development, undertake more far-reaching marketing campaigns and adopt more aggressive pricing policies. The market for Pollard's products is highly competitive at both the lottery and charitable gaming levels. Pollard expects competition to continue to be intense. Pollard also faces

competition from emerging and existing lottery and charitable gaming products, such as internet gaming products and video lottery terminals. Competition from these and other gaming products may weaken demand for Pollard's products.

Licensing and Regulatory Requirements

Pollard is subject to regulation in most jurisdictions in which its products are sold or used by persons or entities licensed to conduct gaming activities. The gaming regulatory requirements vary from jurisdiction to jurisdiction and licensing, other approval or finding of suitability processes with respect to Pollard, its personnel and its products, can be lengthy and expensive. Many jurisdictions have comprehensive licensing, reporting and operating requirements with respect to the sale and manufacture of bingo and bingo related products, including bingo paper and pull-tab tickets. These licensing requirements have a direct impact on the conduct of the day-to-day operations of Pollard. Generally, gaming regulatory authorities may deny applications for licenses, other approvals or findings of suitability for any cause they may deem reasonable. There can be no assurance that Pollard, its products or its personnel will receive or be able to maintain any necessary gaming licenses, other approvals or findings of suitability. The loss of a license in a particular jurisdiction will prohibit Pollard from selling products in that jurisdiction and may prohibit Pollard from selling its products in other jurisdictions. The loss of one or more licenses held by Pollard could have an adverse effect on the business.

Certain jurisdictions require extensive personal and financial disclosure and background checks from persons and entities beneficially owning a specific percentage (typically five percent or more) of a vendor's securities. The failure of beneficial owners of Pollard's securities to submit to background checks and provide such disclosure could result in the imposition of penalties upon these beneficial owners and could jeopardize the award of a lottery contract to Pollard or provide grounds for termination of an existing lottery contract.

Income and Other Taxes

Pollard and its incorporated subsidiaries are subject to Canadian federal and provincial, and U.S. federal, state and withholding taxes. As taxing regimes change their tax basis and rates or initiate reviews of prior tax returns, Pollard could be exposed to increased costs of taxation, which would reduce the amount of funds available for operations.

Intellectual Property

Pollard's commercial success depends, in part, on its ability to secure and protect intellectual property rights that are important to its business, including patent, trademark, copyright and trade secret rights, to operate without infringing third party intellectual property rights and to avoid having third parties circumvent the intellectual property rights that Pollard owns or licenses. In particular, the patents and trademarks Pollard owns or licenses may not be valid or enforceable. In addition, Pollard cannot be certain that its proprietary technology affords a competitive advantage, does not infringe third party rights, or will not need to be altered in response to competing technologies. Pollard also cannot be certain that technologies developed in the future will be the subject of valid and enforceable intellectual property rights.

In addition, litigation may be necessary to determine the scope, enforceability and validity of third party intellectual property rights or to establish Pollard's intellectual property rights. Regardless of merit, any such litigation could be time consuming and expensive, divert management's time and attention, subject

Pollard to significant liabilities, require Pollard to enter into costly royalty or licensing agreements, or require Pollard to modify or stop using intellectual property that it owns or licenses.

Interest Rates

Pollard has certain floating rate loans and may be negatively impacted by increases in interest rates, the effects of which would be to reduce net income and the amount of cash available for operations and on its ability to maintain a consistent level of dividends in Canadian dollars.

Future Acquisition and Integration Risks

To grow by acquisition, Pollard must identify and acquire suitable acquisition candidates at attractive prices and successfully integrate any acquired businesses with its existing operations. If the expected synergies from acquisitions do not materialize or Pollard fails to successfully integrate any new businesses into its existing business, Pollard's financial performance could be significantly impacted. To the extent that businesses acquired by Pollard or their prior owners failed to comply with or otherwise violated applicable laws, Pollard, as a successor owner, may be financially responsible for these violations.

In connection with future acquisitions by Pollard, there may be liabilities that Pollard failed or was unable to discover in its due diligence prior to the consummation of the acquisition. The discovery of any material liabilities could have a material adverse effect on Pollard's business, financial condition, liquidity and results of operations or future prospects.

Financial Instruments

Pollard is exposed to financial risks that arise from fluctuations in interest rates and foreign exchange rates and the degree of volatility of these rates, liquidity risk and credit risk. Pollard uses financial instruments, from time to time, to manage these risks.

Pollard's risk management policies are established to identify and analyze the risks, to set appropriate risk limits and controls to monitor risks and adherence to limits. The Audit Committee oversees how management monitors compliance with Pollard's risk management policies and procedures. The Audit Committee is assisted in its oversight role by Internal Audit, who undertakes regular reviews of risk management controls and utilizes the annual risk assessment process as the basis for the annual audit plan.

Risk Exposure

Currency risk

Pollard sells a significant portion of its products and services to customers in the United States and to international customers where sales are denominated in U.S. dollars. In addition, a significant portion of its cost inputs are denominated in U.S. dollars. Pollard also generates revenue in currencies other than Canadian and U.S. dollars, primarily in Euros.

In addition, translation differences arise when foreign currency monetary assets and liabilities are translated at foreign exchange rates that change over time.

Interest rate risk

Pollard is exposed to interest rate risk relating to its fixed and floating rate instruments. Fluctuation in interest rates will have an effect on the valuation and repayment of these instruments.

Credit risk

Credit risk is the risk of financial loss if a customer or counterpart to a financial instrument fails to meet its financial obligations.

Liquidity risk

Liquidity risk is the risk that Pollard will not be able to meet its financial obligations as they fall due.

Risk Management

Currency risk

Pollard utilizes a number of tools to manage its foreign currency risk including sourcing its manufacturing facilities in the U.S. and sourcing other cost of sales in U.S. dollars.

A 50 basis point strengthening/weakening in the foreign exchange rate between the Canadian and U.S. dollar would decrease/increase the income before income taxes due to changes in operating cashflow by approximately \$0.05 million for year ended December 31, 2015 (2014 - \$0.09 million). A 50 basis point strengthening/weakening in the foreign exchange rate between the Canadian dollar and Euro would decrease/increase the income before income taxes due to changes in operating cashflow by approximately \$0.05 million for year ended December 31, 2015 (2014 - \$0.02 million).

Two manufacturing facilities are located in the U.S. and a significant amount of cost inputs for all production facilities are denominated in U.S. dollars, offsetting a large portion of the U.S. dollar revenue in a natural hedge.

As at December 31, 2015, the amount of financial liabilities denominated in U.S. dollars exceeded the amount of financial assets denominated in U.S. dollars by approximately \$4.1 million (\$2014 - \$7.9 million). A 50 basis point weakening/strengthening in the value of the Canadian dollar relative to the U.S. dollar would result in a decrease/increase in income before income taxes of approximately \$0.02 million (2014 - \$0.04 million).

Pollard also uses financial hedges, including foreign currency contracts, to help manage foreign currency risk. At December 31, 2015, Pollard had no outstanding foreign currency contracts.

Interest rate risk

A 50 basis point decrease/increase in interest rates would result in an increase/decrease in income before income taxes of \$0.4 million for the year ended December 31, 2015 (2014 - \$0.3 million).

Credit risk

Credit risk on Pollard's accounts receivable is minimized since they are mainly from governments and their agencies and are collected in a relatively short period of time. Credit risk on foreign currency

contracts is minimized since the counterparties are restricted to Schedule 1 Canadian financial institutions.

The carrying amount of accounts receivable is reduced through the use of an allowance account and any adjustment to the allowance account is recognized in the statement of income within selling and administration expenses. When a receivable balance is considered uncollectible, it is written off against the allowance account.

Liquidity risk

Pollard's approach is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due. Pollard maintains a committed credit facility including up to \$71.8 million for its Canadian operations, as well as the additional term facility of \$3.9 million and up to US\$12.0 million for its U.S. subsidiaries. At December 31, 2015, the unused balance available for drawdown was \$17.6 million (2014 - \$17.8 million).

The 2016 requirements for capital expenditures, working capital and dividends are expected to be financed from cash flow provided by operating activities and unused credit facility. Pollard enters into contractual obligations in the normal course of business operations.

Outlook

The lottery industry, and specifically the instant ticket product line, continues a trend seen for the last number of years: robust growth. Even though total overall revenue growth of lotteries was tepid during 2015, the revenue growth of the instant ticket category has been strong, with most jurisdictions reporting in the high single digit growth rates and often record levels of instant ticket sales. We continue to believe this long term solid growth trend will continue, as lotteries focus on increasing their returns for good causes and expand their products and services to do so. Even during times of large jackpot sales for draw based games as recently witnessed in the United States, additional foot traffic is drawn into retail locations which in turn feeds incremental sales of instant tickets. Recent studies show a positive correlation between increased lottery sales and lower gasoline prices at the pumps, highlighting lower oil prices as a positive factor supporting the growth in sales. Overall consumer demand remains strong for instant lottery tickets and we believe all of the reasons supporting this demand will continue.

Our current contract portfolio remains strong. There has been no significant changes in our contracts during 2015 and we do not anticipate any significant changes during 2016. Our portfolio includes a number of jurisdictions that have achieved instant ticket growth higher than the industry average and these trends, combined with prospects to strategically bid for work on contracts that are shared amongst multiple suppliers, will support our current level of business and provide opportunities to grow.

One of the strengths in our recent results has been the ability to innovate and develop value added products which enable us to maintain our average selling prices in the face of continued competitive pressure on prices. We have made significant commitments of resources to innovation to generate these value added propositions so that our customers can have leading edge products in the retail environment to grow their business and generate greater returns for their good causes.

Operationally our focus for 2016 will be the continuing ramp up and increasing the utilization of our new press which began live production in the fall of 2015. We will begin to see more of the positive impacts as the press becomes fully integrated into our production environment during 2016. We do anticipate higher volumes in 2016 relative to 2015 due to the increased capacity now available, however the long

term sales cycle and timing of contract renewals does impact how quickly we can generate higher volumes. Increasing instant ticket sales of our existing customers does provide some built in organic growth opportunities, and we will be strategic in bidding for new opportunities to expand our volumes.

The Michigan Lottery iLottery operation continues to set the North American standard for successful iLottery operations and with the recent introduction of draw based games, we are now offering the complete suite of lottery products over the internet. In 2016 we, in conjunction with our partner, will initiate the operation of our second North American iLottery contract with the Virginia Lottery eSubscription platform. We are actively telling the story of the importance of iLottery to the industry and although there are currently no immediate formal bid opportunities available, we believe we are well positioned to capitalize as this distribution method develops.

We are seeing an increased interest in some of our ancillary product lines, in particular our SureTrack[®] lottery management system. As lotteries focus on improving their operations, opportunities to provide them the additional assistance of our inventory, distribution and lottery management system have increased and we have made a number of sales in this area. It is a growing area and provides additional value added services to both our existing customers and provides an important tool in developing new relationships.

The continued weakness in the Canadian dollar relative to both the U.S. dollar and the Euro is positive to our business, both in terms of higher net Canadian cash flow and giving us a stronger competitive position. Over the last number of years we have taken a number of steps to lessen our net exposure to foreign exchange variability through increasing our natural hedges by procuring inputs denominated in U.S. currency. This has reduced the volatility and overall impact of changes in the Canadian/U.S. relationship on our financial results, however an ongoing weak Canadian dollar is still positive for our business.

Our charitable games business had a very good year in 2015 and we anticipate this success to continue. While the overall market for pull-tabs and bingo paper remains flat or slightly declining, we have made a number of improvements in our cost structure and have seen new sales in specific product types that has generated some top line growth as well. The sale of our pull tab vending machines have increased and should continue due to new opportunities opening up in certain jurisdictions.

Our 2016 budgeted capital expenditures are expected to be significantly lower than those that occurred over the past two years due to the completion of the new press installation. We are anticipating our capital expenditure focus to be in maintenance areas and smaller growth projects and be at a dollar level more consistent with that experienced in 2012 and 2013.

As a result of lower capital expenditures we anticipate our free cash flow to be higher than experienced in the last few years. Our priority with this cash flow is to continue to invest in a number of opportunities we see in our business including future iLottery opportunities, financing our expanding strategic alliances and various partnerships, pursuing more aggressively acquisition opportunities and reducing our bank debt.

Disclosure Controls and Procedures

Under National Instrument 52-109, "Certification of Disclosure in Issuers' Annual and Interim Filings," issuers are required to document the conclusions of the Chief Executive Officer and Chief Financial Officer (the "Certifying Officers") regarding the design and effectiveness of the disclosure controls and procedures. Pollard's management, with the participation of the Certifying Officers of Pollard, has

concluded that the disclosure controls and procedures as defined in National Instrument 52-109 are designed appropriately and are effective at providing reasonable assurance of achieving the disclosure objectives.

Internal Controls over Financial Reporting

Under National Instrument 52-109, "Certification of Disclosure in Issuers' Annual and Interim Filings," issuers are required to document the conclusions of the Certifying Officers regarding the design and effectiveness of the internal controls over financial reporting. Management used the Internal Control – Integrated Framework published by the Committee of Sponsoring Organizations of the Treadway Commission (COSO 2013) as the control framework in designing its internal controls over financial reporting. Pollard's management, with the participation of the Certifying Officers of Pollard, has concluded that the internal controls over financial reporting as defined in National Instrument 52-109 are designed appropriately and are effective at providing reasonable assurance of achieving the financial reporting objectives.

No changes were made in Pollard's internal control over financial reporting during the year ended December 31, 2015, that have materially affected, or are reasonably likely to materially affect, Pollard's internal control over financial reporting.

Additional Information

Shares of Pollard Banknote Limited are traded on the Toronto Stock Exchange under the symbol PBL.

Additional information relating to Pollard, including the Audited Consolidated Financial Statements and the Annual Information Form for the year ended December 31, 2015, is available on SEDAR at www.sedar.com.

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