

Consolidated Financial Statements
(Expressed in Canadian dollars)

GOOD NATURED PRODUCTS INC.

Years ended December 31, 2019 and 2018

MANAGEMENT'S REPORT

MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

The accompanying consolidated financial statements of good natured Products Inc. were prepared by management in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board. The most significant of these accounting principles have been disclosed in the notes to the consolidated financial statements. Management acknowledges responsibility for the preparation and presentation of the consolidated financial statements, including responsibility for significant accounting judgments and estimates and the choice of accounting principles and methods that are appropriate to the Company's circumstances.

Management has established processes, which are in place to provide them sufficient knowledge to support management representations that they have exercised reasonable diligence that (i) the consolidated financial statements do not contain any untrue statement of material fact or omit to state a material fact required to be stated or that is necessary to make a statement not misleading in light of the circumstances under which it is made, as of the date of and for the periods presented by the consolidated financial statements and (ii) the consolidated financial statements fairly present in all material respects the financial condition, results of operations and cash flows of the Company, as of the date of and for the periods presented by the consolidated financial statements.

The Board of Directors is responsible for reviewing and approving the consolidated financial statements together with other financial information of the Company and for ensuring that management fulfills its financial reporting responsibilities. An Audit Committee assists the Board of Directors in fulfilling this responsibility. The Audit Committee meets with management to review the financial reporting process and the consolidated financial statements together with other financial information of the Company. The Audit Committee reports its findings to the Board of Directors for its consideration in approving the consolidated financial statements together with other financial information of the Company for issuance to the shareholders. Management recognizes its responsibility for conducting the Company's affairs in compliance with established financial standards, and applicable laws and regulations, and for maintaining proper standards of conduct for its activities.

Independent Auditor's Report

To the Shareholders and the Board of Directors of
good natured Products Inc.

Opinion

We have audited the consolidated financial statements of good natured Products Inc. (the "Company"), which comprise the consolidated statement of financial position as at December 31, 2019, and the consolidated statement of net loss and comprehensive loss, consolidated statement of changes in shareholders' equity (deficiency) and consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies (collectively referred to as the "financial statements").

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2019, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards ("IFRS").

Basis for Opinion

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

Other Matter

The financial statements as at and for the year ended December 31, 2018 were audited by another auditor who expressed an unmodified opinion on those financial statements on April 29, 2019.

Other Information

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

Our opinion on the financial statements does not cover the other information and we do not and will not express any form of assurance conclusion thereon. In connection with our audit of the financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

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

Responsibilities of Management and Those Charged with Governance for the Financial Statements

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

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

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

Auditor's Responsibilities for the Audit of the Financial Statements

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

As part of an audit in accordance with Canadian GAAS, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

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

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

The engagement partner on the audit resulting in this independent auditor's report is Cameron Walls.

/s/ Deloitte LLP

Chartered Professional Accountants
Vancouver, British Columbia
April 27, 2020

GOOD NATURED PRODUCTS INC.

Consolidated Statements of Financial Position
(Expressed in Canadian dollars)

	December 31 2019	December 31 2018
Assets		
Current assets:		
Cash and cash equivalents	\$ 8,454,882	\$ 2,903,466
Trade and other receivables	682,622	915,800
Inventory (note 4)	1,922,955	404,560
Prepaid expenses	172,141	84,806
	<u>11,232,600</u>	<u>4,308,632</u>
Non-current assets:		
Property and equipment, net (note 5)	373,145	164,940
Other assets, net (note 6)	714,019	597,093
	<u>\$ 12,319,764</u>	<u>\$ 5,070,665</u>

Liabilities and Shareholders' Equity (Deficiency)

Current liabilities:		
Accounts payable and accrued liabilities	\$ 3,039,288	\$ 1,984,542
Credit line (note 7)	649,500	325,000
Current portion of long-term debt (note 8)	196,341	194,100
	<u>3,885,129</u>	<u>2,503,642</u>
Long-term debt (note 8)	13,076,211	5,316,986
Shareholders' Equity (deficiency):		
Common share capital	13,932,452	12,441,108
Shares issuable	-	591,500
Contributed surplus	4,307,870	3,607,221
Foreign currency translation reserve	(18,285)	-
Deficit	(22,863,613)	(19,389,792)
	<u>(4,641,576)</u>	<u>(2,749,963)</u>
	<u>\$ 12,319,764</u>	<u>\$ 5,070,665</u>

Subsequent events (note 18)

See accompanying notes to condensed consolidated interim financial statements.

Approved on behalf of the Board:

"Jim Zadra" Director

"Salil Munjal" Director

GOOD NATURED PRODUCTS INC.

Consolidated Statements of Net Loss and Comprehensive Loss
(Expressed in Canadian dollars)

	Year ended December 31	
	2019	2018
Product revenue	\$ 10,098,675	\$ 5,103,347
Cost of product revenue	(6,625,010)	(3,374,215)
Gross profit	3,473,665	1,729,132
Other (Expenses) Income:		
Product development (note 15)	(461,974)	(219,045)
Selling, general, and administrative (note 16)	(4,655,198)	(3,383,182)
Share-based compensation (note 9 (b))	(59,904)	(166,486)
Depreciation and amortization	(325,695)	(523,835)
Financing costs	(1,767,921)	(756,364)
Gain on interest free loan (note 8 (a))	46,144	31,981
Net loss before taxes	(3,750,883)	(3,287,799)
Deferred income tax recovery (note 11)	277,062	181,473
Net loss for the year	\$ (3,473,821)	\$ (3,106,326)
Other comprehensive loss, net of tax		
Items that may be reclassified subsequently to profit or loss:		
Unrealized currency loss on translation of foreign operations	(18,285)	-
Other comprehensive loss for the year	\$ (3,492,106)	\$ (3,106,326)
Basic and diluted loss per share	\$ (0.03)	\$ (0.03)
Weighted average shares outstanding – basic and diluted	99,750,181	93,802,449

See accompanying notes to consolidated financial statements.

GOOD NATURED PRODUCTS INC

Consolidated Statements of Changes in Shareholders' Equity (Deficiency)
(Expressed in Canadian dollars)

	Number of common shares	Common share capital	Common shares issuable	Contributed surplus- warrants and conversion features	Contributed surplus- stock options	Foreign currency translation reserve	Deficit	Equity/ (Deficiency)
Balance at December 31, 2017	93,452,354	\$ 12,305,160	\$ 591,500	\$ 2,089,580	\$ 900,894	\$ -	(16,283,466)	\$ (396,332)
Shares issued for debt settlement (note 9 (a))	202,500	21,750	-	-	-	-	-	21,750
Conversion feature and warrants of convertible debenture (note 8 (b))	-	-	-	672,122	-	-	-	672,122
Share issued upon debt conversion (note 9 (a))	133,332	17,560	-	-	-	-	-	17,560
Shares issued upon warrant exercise	562,500	96,638	-	(40,388)	-	-	-	56,250
Share based compensation	-	-	-	-	166,486	-	-	166,486
Deferred tax arising from convertible debenture issuance	-	-	-	(181,473)	-	-	-	(181,473)
Net comprehensive loss	-	-	-	-	-	-	(3,106,326)	(3,106,326)
Balance at December 31, 2018	94,350,686	12,441,108	591,500	2,539,841	1,067,380	-	(19,389,792)	(2,749,963)
Shares issued to Lindar (note 9(a))	5,382,000	591,500	(591,500)	-	-	-	-	-
Shares issued upon warrant exercise	3,231,857	508,173	-	(108,347)	-	-	-	399,826
Warrants issued upon amended terms (note 8 (b))	-	-	-	340,154	-	-	-	340,154
Share issued upon debt conversion (note 9 (a))	2,833,330	425,000	-	(33,329)	-	-	-	391,671
Conversion feature and warrants of convertible debenture (note 8 (b))	-	-	-	686,000	-	-	-	686,000
Share based compensation	-	-	-	-	59,904	-	-	59,904
Deferred tax arising from convertible debenture issuance	-	-	-	(277,062)	-	-	-	(277,062)
Net comprehensive loss	-	-	-	-	-	(18,285)	(3,473,821)	(3,492,106)
Balance at December 31, 2019	105,797,873	\$ 13,965,781	\$ -	\$ 3,147,257	\$ 1,127,284	\$ (18,285)	\$ (22,863,613)	\$ (4,641,576)

See accompanying notes to consolidated financial statements.

GOOD NATURED PRODUCTS INC.

Consolidated Statements of Cash Flows
(Expressed in Canadian dollars)

	Year ended December 31	
	2019	2018
Cash provided by (used in):		
Operations:		
Net loss	\$ (3,473,821)	\$ (3,106,326)
Items not involving cash:		
Depreciation and amortization	325,695	523,835
Unrealized foreign exchange loss	141,561	-
Amortization of right of use assets	46,116	-
Share based compensation (note 9 (b))	59,904	166,486
Gain on interest free loan (note 8 (a))	(46,144)	(31,981)
Gain on disposal of equipment	-	(9,946)
Accretion on loans (note 8)	454,135	280,404
Deferred income tax	(277,062)	(181,473)
Changes in non-cash operating working capital:		
Trade and other receivables	233,178	1,220,480
Inventory	(1,518,395)	(153,818)
Prepaid expenses	(87,335)	20,233
Accounts payable and accrued liabilities	1,054,746	(1,132,832)
Cash used in operating activities	(3,087,422)	(2,404,938)
Financing:		
Exercise of warrants for common shares	399,826	56,250
Credit Line advance (note 7)	324,500	-
Proceeds from convertible debenture, net of of issuance costs (note 8 (b))	2,536,254	4,818,418
Proceeds from long-term debt, net of issuance costs (note 8(c))	6,095,294	-
Repayment of other long-term debt (note 8(a,d))	(228,874)	(144,756)
Advances from other long-term debt (note 8(a,d))	230,276	-
Cash provided by financing activities	9,357,276	4,729,912
Investments:		
Purchase of equipment	(257,587)	(149,266)
Other assets	(301,005)	(93,997)
Proceeds on disposal of equipment	-	23,872
Cash used in investing activities	(558,592)	(219,391)
Effect of foreign exchange rate changes on cash	(159,846)	-
Increase in cash	5,551,416	2,105,583
Cash and cash equivalents, beginning of year	2,903,466	797,883
Cash and cash equivalents, end of year	\$ 8,454,882	\$ 2,903,466

Supplementary disclosure with respect to cash flows (note 17).

See accompanying notes to consolidated financial statements.

GOOD NATURED PRODUCTS INC.

Notes to Consolidated Financial Statements
Year ended December 31, 2019 and 2018
(Expressed in Canadian dollars)

1. Nature of operations:

Good Natured Products Inc. (the “Company”) is a Canadian company incorporated under the British Columbia Business Corporations Act and its common shares are listed on the TSX Venture Exchange (“TSX-V”) as a Tier 2 issuer under the symbol “GDNP”. The Company’s head office is located at 814 - 470 Granville Street, Vancouver, British Columbia, Canada. The Company through its wholly owned subsidiaries Good Natured Products (CAD) Inc. and Good Natured Products (US) Inc., is principally engaged in the design, production and distribution of high-performance bioplastics for use in packaging and durable product applications.

2. Basis of presentation:

(a) Statement of compliance:

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board (“IASB”).

These consolidated financial statements were authorized for issue by the Board of Directors on April 27, 2020.

(b) Basis of measurement:

These consolidated financial statements have been prepared on the historical cost basis.

(c) Use of estimates, assumptions and judgments:

(i) Use of estimates and assumptions:

The preparation of these consolidated financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of assets and liabilities at the date of the consolidated financial statements, and the reported amounts of revenues and expenses during the reporting periods. The underlying assumptions are based on historical experience and other factors that management believes to be reasonable under the circumstances, and are subject to change as new events occur, as more industry experience is acquired, as additional information is obtained and as the Company’s operating environment changes.

GOOD NATURED PRODUCTS INC.

Notes to Consolidated Financial Statements
Year ended December 31, 2019 and 2018
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2. Basis of presentation (continued):

(c) Use of estimates, assumptions and judgments (continued):

(i) Use of estimates and assumptions (continued):

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected. Significant areas having estimation uncertainty include the following:

Financial instruments:

The Company enters financial instrument arrangements which require management to make judgments to determine if such arrangements are derivative instruments in their entirety or contain embedded derivatives, including whether those embedded derivatives meet the criteria to be separated from their host contract, in accordance with IFRS 9, *Financial Instruments*. Key judgments include whether the value of a contract changes in response to a change in an underlying rate, price, index or other variable, and for embedded derivatives, whether the economic risks and characteristics are not closely related to the host contract and a separate instrument with the same terms would meet the definition of a derivative on a standalone basis.

Inventory provision:

In determining the lower of cost and net realizable value of inventory and in establishing the appropriate provision for inventory obsolescence, management estimates the likelihood that inventory carrying values will be affected by changes in market pricing or demand for the products and by changes in technology or design which could make inventory on hand obsolete or recoverable at less than the recorded value. Management performs regular reviews to assess the impact of changes in technology and design, sales trends and other changes on the carrying value of inventory. Where it is determined that such changes have occurred and will have a negative impact on the value of inventory on hand, an appropriate provision is made.

Share based payments and warrants:

The critical estimates and assumptions underlying the measurement of share-based payments and warrants are set out in notes 9 (b) and 9 (c) respectively.

(ii) Significant judgments:

The Company applied judgment in determining the functional currency of the Company and assessing the impairment of accounts receivable, equipment and intangible assets. Functional currency was determined based on the currency that mainly influences sales prices, labour, materials, other costs of sales and in which financing is raised.

GOOD NATURED PRODUCTS INC.

Notes to Consolidated Financial Statements
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(Expressed in Canadian dollars)

3. Significant accounting policies:

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements, unless otherwise indicated.

(a) Basis of consolidation:

These consolidated financial statements comprise the financial statements of the Company and its subsidiaries as at December 31, 2019.

Subsidiaries are fully consolidated from the date of acquisition, being the date on which the Company obtains control, and continue to be consolidated until the date that such control ceases. The financial statements of the subsidiaries are prepared for the same reporting period as the parent company, using consistent accounting policies. All intra-group balances, income and expenses, unrealized gains and losses and dividends resulting from intra-group transactions have been eliminated on consolidation. A change in the ownership interest of a subsidiary, without a change of control, is accounted for as an equity transaction.

The Company's subsidiaries are as follows:

Good Natured Products (CAD) Inc.	100% owned
Good Natured Products (US) Inc.	100% owned

(b) Foreign currency translation:

The functional currency of each of the Company's entities is determined using the currency of the primary economic environment in which that entity operates. The Company's functional currency and that of Good Natured Products (CAD) Inc. is the Canadian dollar while the functional currency of Good Natured Products (US) Inc. is the US dollar. The presentation currency of these financial statements is the Canadian dollar.

In preparing the financial statements of the individual entities, transactions in currencies other than the entity's functional currency (foreign currencies) are recorded at the rate of exchange prevailing at the dates of the transactions. At each reporting date, monetary items denominated in foreign currencies are retranslated at rates prevailing at the reporting dates and are recognized in profit and loss in the period in which they arise. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

For the purpose of preparing the consolidated financial statements, the assets and liabilities are first expressed in the entity's respective functional currency and translated into the presentation currency using exchange rates prevailing at the reporting date, while the income and expense items are translated at the average exchange rates for the period. Translation differences are recognized in other comprehensive loss and recorded in the "foreign currency translation reserve" included in equity.

(c) Cash and cash equivalents:

Cash and cash equivalents comprise cash at banks and short-term deposits with a maturity of three months or less at the date of purchase. Cash and cash equivalents at December 31, 2019 were \$8,454,882 (December 31, 2018 – \$2,903,466).

GOOD NATURED PRODUCTS INC.

Notes to Consolidated Financial Statements
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3. Significant accounting policies (continued):

(d) Inventory:

Inventory is carried at the lower of cost and net realizable value. Inventory cost is determined on the basis of first-in, first-out (“FIFO”) for finished goods and weighted average for raw material. Cost includes expenditures incurred in acquiring the inventories, production or conversion costs and other costs incurred in bringing them to their existing location and condition.

The amount of any write-down of inventories to net realizable value and all losses of inventories are recognized as an expense in the period the write-down or loss occurs. The amount of any reversal of any write-down of inventories, arising from an increase in net realizable value, is recognized as a reduction in the amount of inventories recognized as an expense in the period in which the reversal occurs.

(e) Impairment:

(i) Financial assets:

The Company applies the simplified approach in determining expected credit losses, which requires a probability-weighted estimate of expected lifetime credit losses to be recognized upon initial recognition of financial assets measured at amortized cost. Credit losses are measured as the present value of cash shortfalls from all possible default events, discounted at the effective interest rate of the financial asset. Loss allowances for financial assets at amortized cost are deducted from the gross carrying amount of the assets.

(ii) Non-financial assets:

Non-financial assets are reviewed for impairment at each reporting date to determine whether events or changes in circumstances indicate that an asset’s carrying amount may be less than its recoverable amount. When there is any indication of impairment, the asset’s recoverable amount is estimated.

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For impairment testing, non-financial assets that do not generate independent cash flows are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (the “cash-generating unit” or “CGU”).

An impairment loss is recognized if the carrying value of an asset, CGU or group of CGU’s exceeds its estimated recoverable amount. Impairment losses recognized in respect of CGUs are allocated to reduce the carrying amounts of the other assets in the unit (group of units) on a pro rata basis.

GOOD NATURED PRODUCTS INC.

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3. Significant accounting policies (continued):

(e) Impairment:

(ii) Non-financial assets (continued):

Impairment losses recognized in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortization, if no impairment loss had been recognized.

(f) Property and equipment:

Property and equipment are recorded at cost when acquired. Depreciation is recognized in profit or loss over the estimated useful lives of each part of an item of property and equipment. Depreciation is charged using the following methods and rates:

Asset	Basis	Rate
Manufacturing equipment	Straight line	5-20 years
Furniture and office equipment	Straight line	3-5 years

(g) Other assets:

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is recorded at its estimated fair value at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortization and any accumulated impairment losses. Internally generated intangible assets, excluding capitalized development costs, are not capitalized and expenditures are reflected in the income statement in the period in which the expenditure is incurred.

Other assets consist of customer relationships acquired, capitalized development costs, right-of-use assets and other intangibles. Amortization is recognized in profit or loss over the estimated useful lives of 3 to 5 years on a straight-line basis.

GOOD NATURED PRODUCTS INC.

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3. Significant accounting policies (continued):

(h) Product development:

Research costs are expensed as they are incurred. Product development costs are expensed as incurred except when they meet specific criteria for capitalization. Development activities involve a plan or design for the production of new or substantially improved products and processes. Development costs are capitalized only if costs can be measured reliably, the product or process is technically and commercially feasible, future economic benefits are probable, and the Company intends to and has sufficient resources to complete development to use or sell the asset. Capitalized development costs are measured at cost less accumulated amortization and accumulated impairment losses. Capitalized development costs are amortized when commercial production begins. During the year ended December 31, 2019, \$175,644 of development costs have been capitalized (Year ended December 31, 2018 - \$93,997).

(i) Share-based payment transactions:

Share-based compensation arrangements are measured at fair value using the Black-Scholes option pricing model and the fair value is expensed on a straight-line basis over the vesting period, with a corresponding increase in equity. The amount recognized as an expense is adjusted to reflect the number of awards for which the related service and non-market vesting conditions are expected to be met, such that the amount ultimately recognized as an expense is based on the number of awards that do meet the related service and non-market performance conditions at the vesting date.

For options granted to non-employees, the share-based compensation cost is measured at the fair value of the goods or services received, unless that fair value cannot be estimated reliably. For non-employees if the fair value cannot be estimated reliably, then the Company will measure the fair value by reference to the fair value of the equity instruments granted using the Black-Scholes option pricing model. The share-based compensation is measured at fair value at each vesting date and is recorded when goods or services from non-employees are received.

Management uses judgment to determine the inputs to the Black-Scholes option pricing model including the expected lives and underlying share price volatility. Volatility is estimated by comparing to companies with similar operations over similar periods to the expected life of the awards under consideration. Changes in these assumptions will impact the calculation of fair value and the amount of compensation expense recognized in profit or loss.

Share-based payment arrangements in which the Company receives goods or services as consideration for its own equity instruments are accounted for as equity-settled share-based payment transactions, regardless of how the equity instruments are obtained by the Company.

GOOD NATURED PRODUCTS INC.

Notes to Consolidated Financial Statements
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(Expressed in Canadian dollars)

3. Significant accounting policies (continued):

(j) Income taxes:

Income tax expense comprises current tax expense and deferred tax expense. Current and deferred taxes are recognized as an expense and included in income or loss for the period, except to the extent that the tax arises from a transaction which is recognized in other comprehensive income or directly in equity.

Current tax expense is the amount of income taxes payable (recoverable) in respect of the taxable income (tax loss) for a period. Current liabilities (assets) for the current and prior periods are measured at the amount expected to be paid to (recovered from) the taxation authorities, using the tax rates that have been enacted or substantively enacted by the end of the reporting period.

Deferred tax assets and liabilities are recognized for temporary differences which are differences between the carrying amount of an asset or liability in the statement of financial position and its tax base, the carry-forward of unused tax losses and unused tax credits. Deferred tax assets and liabilities are measured at the tax rate that are expected to apply when the asset is realized or the liability is settled, based on tax rates that have been enacted or substantively enacted by the end of the reporting period.

The carrying amount of a deferred tax asset is reviewed at the end of each reporting period. The Company reduces the carrying amount of a deferred tax asset to the extent that it is no longer probable that sufficient taxable income will be available to allow the benefit of part or all of these deferred tax assets to be utilized. Such reduction is reversed to the extent that it becomes probable that sufficient taxable income will be available.

(k) Revenue recognition:

The Company recognizes the amount of revenue to which it expects to be entitled, for the transfer of promised goods or services to customers under a five-step model: (i) identify contract(s) with a customer; (ii) identify the performance obligations in the contract; (iii) determine the transaction price; (iv) allocate the transaction price to the performance obligations in the contract; and (v) recognize revenue when or as a performance obligation is satisfied.

The Company generates revenue primarily through sale of products to various customers.

GOOD NATURED PRODUCTS INC.

Notes to Consolidated Financial Statements
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(Expressed in Canadian dollars)

3. Significant accounting policies (continued):

(l) Financial instruments:

(i) Financial assets:

The Company initially recognizes receivables and deposits on the date that they are originated and all other financial assets on the trade date at which the Company becomes a party to the contractual provisions of the instrument. The Company derecognizes a financial asset when the contractual rights to the cash flows from the asset expire, or when it transfers substantially all the risks and rewards of ownership of the financial asset.

Financial assets which include cash, trade and other receivables have fixed or determinable payments and are not quoted in an active market. Such assets are recognized initially at fair value and subsequently at amortized cost using the effective interest method, less any impairment losses.

(ii) Financial liabilities:

Financial liabilities comprise the Company's accounts payable and accrued liabilities, credit facility and loans. The financial liabilities are initially recognized on the date they are originated and are derecognized when the contractual obligations are discharged or cancelled or expire. These financial liabilities are recognized initially at fair value and subsequently are measured at amortized cost using the effective interest method, when materially different from the initial amount. Fair value is determined based on the present value of future cash flows, discounted at the market rate of interest.

(iii) Share capital and contributed surplus:

Share capital and contributed surplus are classified as equity. Incremental costs directly attributable to increases in share capital and paid-in capital are recognized as a deduction from equity. When share capital and paid-in capital are reduced, the amount of the consideration paid, including directly attributable costs, is recognized as a deduction from equity.

(m) New standards and interpretations applied:

On January 1, 2019, the Company adopted IFRS 16 - Leases ("IFRS 16") which superseded IAS 17 - Leases. IFRS 16 applies a control model to the identification of leases, distinguishing between a lease and a service contract on the basis of whether the lessee controls the asset. Control is considered to exist if the customer has the right to obtain substantially all of the economic benefits from the use of an identified asset and the right to direct the use of that asset. For those assets determined to meet the definition of a lease, IFRS 16 introduces significant changes to the accounting by lessees, introducing a single, on balance sheet accounting model, with limited exceptions for short-term leases or leases of low value assets

GOOD NATURED PRODUCTS INC.

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3. Significant accounting policies (continued):

(m) New standards and interpretations applied (continued):

The Company adopted IFRS 16 on its effective date, using the modified retrospective application method, with the cumulative effect of initially applying the standard recorded as an adjustment to retained earnings and no restatement of comparative information. The Company has elected to measure its right-of-use assets at amounts equal to the associated lease liabilities as at the adoption date, which resulted in a \$138,350 increase in right-of-use assets (note 6) and lease liabilities (note 8(d)), with no adjustment necessary to retained earnings.

In transitioning to IFRS 16, the Company analyzed its contracts to identify whether they are or contain a lease arrangement. This analysis identified contracts containing leases that have an equivalent increase to both the Company's right-of-use assets and lease liabilities. The Company has also elected to apply the available exemptions as permitted by IFRS 16 to recognize a lease expense on a straight line basis for short term leases (lease term of 12 months or less) and low value leases. Upon the adoption of IFRS 16, the Company recognized additional right-of-use asset and lease liability related to the Company's office rental contract. The incremental borrowing rates for lease liabilities initially recognized on adoption of IFRS 16 was 6.5%. Due to the recognition of additional right-of-use assets and lease liabilities, during the year ended December 31, 2019, depreciation expense increased by \$46,116 and financing costs increased by \$7,702, respectively, under IFRS 16 compared to the previous standard. Additionally, operating cash flows increased by \$41,825 with a corresponding \$41,825 increase in financing cash outflows, with no net impact on overall cash flows.

4. Inventory:

	December 31, 2019	December 31, 2018
Raw materials and consumables	\$ 1,204,010	\$ 134,934
Finished goods	718,945	269,626
	<u>\$ 1,922,955</u>	<u>\$ 404,560</u>

On December 1, 2019, the Company assumed responsibility for supply chain management previously covered by an outsourcing agreement resulting in the increased inventory on hand. The Company made the change in order to better manage the Company's supply chain and back office efficiency.

During the year ended December 31, 2019, inventory, valued at \$6,258,909 was expensed as cost of goods sold and reflected within cost of product revenues (December 31, 2018 - \$3,215,224).

GOOD NATURED PRODUCTS INC.

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5. Property and equipment, net:

	Manufacturing Equipment	Other equipment	Accumulated Depreciation	Net Book Value
December 31, 2017	\$ 55,424	\$ 31,990	\$ (35,654)	\$ 51,760
Additions	141,950	7,316	(22,160)	127,106
Disposals	(23,872)	-	9,946	(13,926)
December 31, 2018	\$ 173,502	\$ 39,306	\$ (47,868)	\$ 164,940
Additions	232,665	24,922	(49,382)	208,205
December 31, 2019	\$ 406,167	\$ 64,228	\$ (97,250)	\$ 373,145

6. Other assets:

	Customer Lists	Other assets ¹	Accumulated Depreciation	Net Book Value
December 31, 2017	\$ 1,740,750	\$ -	\$ (735,979)	\$ 1,004,771
Additions	-	93,997	(501,675)	(407,678)
December 31, 2018	\$ 1,740,750	\$ 93,997	\$ (1,237,654)	\$ 597,093
Additions	-	439,355	(322,429)	116,926
December 31, 2019	\$ 1,740,750	\$ 533,352	\$ (1,560,083)	\$ 714,019

¹ Included in additions for the year ended December 31, 2019 is \$138,350 of right of use assets recognized as at January 1, 2019 upon the adoption of IFRS 16 (note 3(m)).

Other assets consist of customer relationships acquired, capitalized development costs, right-of-use assets and other intangibles.

7. Credit Line

On June 5, 2019, Comerica Bank agreed to provide the Company with a 1 year, \$1,000,000 USD revolving operating line of credit with a variable interest rate of prime + 1% secured by all assets of the Company. The Company is required to maintain \$1,000,000 CAD of cash in its accounts for the term of the revolving loan. As at December 31, 2019, the Company was in compliance with all covenants. The Company incurred interest expense related to the credit line of \$31,523 for the year ended December 31, 2019 (year ended December 31, 2018 - \$19,809). On June 27, 2019, an outstanding loan balance of CAD\$325,000 related to a 2016 term loan with Comerica was fully repaid.

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8. Long-term debt:

	WINN loan (a)	Convertible debenture (b)	BDC Capital (c)	Other debt (d) ¹	Total
Dec. 31, 2017	\$ 1,278,683	\$ -	\$ -	\$ -	\$ 1,278,683
Proceeds	85,851	4,028,464	-	-	4,114,315
Repayment	(144,756)	-	-	-	(144,756)
Conversion	-	(17,560)	-	-	(17,560)
Accretion	67,222	213,182	-	-	280,404
Dec. 31, 2018	\$ 1,287,000	\$ 4,224,086	\$ -	\$ -	\$ 5,511,086
Proceeds	123,877	1,850,254	5,923,413	198,604	8,096,148
Repayment	(187,050)	-	-	(41,824)	(228,874)
Conversion	-	(391,671)	-	-	(391,671)
Accretion	73,215	252,058	128,862	-	454,135
Foreign exchange	-	-	(168,272)	-	(168,272)
Dec. 31, 2019	\$ 1,297,042	\$ 5,934,727	\$ 5,884,003	\$ 156,780	\$ 13,272,552

As Presented	December 31, 2019	December 31, 2018
Current portion	\$ 196,341	\$ 194,100
Non-current portion	13,076,211	5,316,986
	\$ 13,272,552	\$ 5,511,086

¹ Included in proceeds for the year ended December 31, 2019 is \$138,350 of lease liabilities recognized as at January 1, 2019 upon the adoption of IFRS 16 (note 3(m)).

(a) Western Innovation Initiative loan:

	Loan	Discount	Net Book Value
December 31, 2017	\$ 1,600,000	\$ (321,317)	\$ 1,278,683
Proceeds	117,832	(31,981)	85,851
Repayment	(144,756)	-	(144,756)
Amortization	-	67,222	67,222
December 31, 2018	\$ 1,573,076	\$ (286,076)	\$ 1,287,000
Proceeds	170,021	(46,144)	123,877
Repayment	(187,050)	-	(187,050)
Amortization	-	73,215	73,215
December 31, 2019	\$ 1,556,047	\$ (259,005)	\$ 1,297,042

On June 20, 2014, the Company entered into a Western Innovation Initiative Agreement with Western Economic Diversification Canada ("WINN"). The WINN agreement provides the Company with an interest-free, repayable loan of \$1,600,000 from the government.

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8. Loans and financing (continued):

(a) Western Innovation Initiative loan (continued):

The loan was to be repaid monthly over five years commencing November 1, 2017 in 60 consecutive instalments of \$26,667. On October 31, 2017, the Company re-negotiated the repayment term to commence on June 1, 2018. At December 31, 2019, the undiscounted balance of the first WINN loan was \$1,268,194.

As the funds were advanced, the Company recognized a gain and discounted the first WINN loan by \$480,070 as a result of the imputed interest benefit received from the interest-free WINN loan.

On August 7, 2018, the Company entered into a second WINN agreement. The second WINN agreement provides the Company with an interest-free, repayable contribution from the government not to exceed \$850,000 towards total project cost estimated at \$1,750,000. The project funds are directed at the Company's development and commercialization of its new non-toxic high-heat bioplastic food containers for the grocery, take-out and consumer markets. Such funds are to be repaid monthly over five years commencing October 1, 2021. The claim period for shared project costs commenced April 1, 2018.

The Company received loan proceeds of \$170,021 under the second WINN agreement during the year ending December 31, 2019 (Year ending December 31, 2018 - \$117,832). The Company recognized a gain and discounted the second WINN loan by \$78,125 as a result of the imputed interest benefit received from the interest-free loan using a discount rate of 8.2%.

The total amount of undiscounted future cash flows required to settle the WINN loans at December 31, 2019 was \$1,556,047 (December 31, 2018 - \$1,573,076). The future cash flows have been discounted using a rate of 8.20%. The remaining repayments for the years ending December 31 are 2020 - \$ 120,000; 2021 - \$603,494; 2022 - \$616,670; 2023 - \$57,576 and beyond 2023 - \$158,307.

(b) Convertible debentures:

	Debtenture	Equity component	Issuance Cost	Net Book Value
December 31, 2017	\$ -	\$ -	\$ -	\$ -
Proceeds (i)	5,049,000	(672,122)	(348,414)	4,028,464
Conversion	(20,000)	2,440	-	(17,560)
Amortization	-	140,592	72,590	213,182
December 31, 2018	\$ 5,029,000	\$ (529,090)	\$ (275,824)	\$ 4,224,086
Proceeds (ii)	2,740,000	(686,000)	(203,746)	1,850,254
Conversion	(425,000)	33,329	-	(391,671)
Amortization	-	164,950	87,108	252,058
December 31, 2019	\$ 7,344,000	\$ (1,016,811)	\$ (392,462)	\$ 5,934,727

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8. Loans and financing (continued):

(b) Convertible debentures (continued):

i) February 2018 Issue

On February 28, 2018, the Company completed a convertible debenture offering of 5,049 units ("Units") for gross proceeds of \$5,049,000. Each Unit is comprised of one \$1,000 principal amount unsecured 10% convertible debenture ("Debenture") of the Company due February 28, 2022 (the "Maturity Date") and 1,500 common share purchase warrants. The Company issued a total of 7,573,500 Warrants to the debenture subscribers. Related party participation in the private placement totaled 209 units.

The convertible debentures are considered to be compound financial instruments in which the host debt instruments have been determined to be financial liabilities with an embedded equity instrument. The Company initially measured the liability component at fair value, with the residual amount assigned to the equity components. The Company used an effective interest rate of 13.2% resulting in \$672,122 assigned to the conversion feature and warrants.

Each Debenture is convertible, at the option of the holder, at any time prior to the close of business on the last business day immediately preceding the Maturity Date, into that number of common shares computed on the basis of the principal amount of the Debentures divided by the conversion price of \$0.15 per common share. During the Year ending December 31, 2019, \$425,000 of Debentures were converted into 2,833,330 common shares (Year ending December 31, 2018 \$20,000 converted into 133,332 common shares).

The Debentures are subject to an acceleration right exercisable by the Company, which will force the conversion of the Debentures into common shares at the \$0.15 conversion price. This right is exercisable if the Company's common shares trade at or above a volume-weighted average trade price of \$0.15 on the TSX Venture Exchange ("TSX-V") on any 20 consecutive trading days and on cumulative 20-day trading volume of at least 1,000,000 common shares. If the acceleration right is exercised by the Company, the conversion of the Debentures into common shares will occur immediately.

The Debentures are also subject to a redemption right at the Company's option, to redeem at any time on or after the first anniversary of the issue date any part of the February 2018 Debentures then outstanding at such date at a redemption price equal to 105% of the aggregate Principal Amount of the Debentures to be redeemed together with all interest accrued and remaining unpaid.

Subsequent to the year-end, the Company redeemed \$3,215,000 of the February 2018 Debentures resulting in a total payment for principal, redemption premium and accrued interest of \$3,510,584.

Each Warrant entitles the holder to purchase one common share of the Company for a period of 48 months after February 28, 2018 at a price of \$0.10 per Warrant. The Warrants are subject to an acceleration right if on any 20 consecutive or non-consecutive trading days following the closing date, the Company's common shares trade at greater than a volume-weighted average trading price of \$0.20 on the TSX-V.

GOOD NATURED PRODUCTS INC.

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8. Loans and financing (continued):

(b) Convertible debentures (continued):

The interest on the Debentures is payable in cash on a semi-annual basis in arrears (February 28 and August 28).

Pursuant to the offering, the Company paid cash commissions, legal and other related issuance fees totaling \$348,414. The Company also issued non-transferable broker warrants to acquire 2,239,867 common shares from treasury at a price of \$0.15 per common share, exercisable at any time within the 36-month period following February 28, 2018. The fair value at grant date of the broker warrants issued was \$128,344 based on the Black-Scholes pricing model and was recorded as a Debenture discount. The inputs used in the measurement of the fair value at the grant dates follows: risk-free rate of 1.25%; expected life of 3.0 years; volatility factor of 106%; and fair value of \$0.10 per share at issuance date.

On June 11, 2019, the Company secured a \$10 million USD loan facility from BDC Capital Inc. ("BDC" and the "BDC Financing") (see Note 8(c)). Obtaining the BDC Financing required approval of the holders of the Debentures (the "Debenture Holders"). As part of obtaining Debenture Holder consent, the Company agreed to amend the terms of the Debentures and, indirectly, the warrants that were issued as part of a unit with the Debentures.

The amended terms included: (a) in the event of any failure to pay amounts due, or other event of default under the BDC Financing (or any other senior debt facility), the interest payments on the Debentures will be temporarily suspended; (b) the price at which the Debentures can be forced to convert into common shares of the Company is increased to \$0.25 from \$0.15; and (c) each warrant certificate held by a Debenture Holder (to the extent not previously expired or exercised) will be deemed to have been amended, so that the number of common shares that are subject to purchase under the warrant certificate is increased by 122.22%. As a result, 8,568,975 additional warrants at a price of \$0.10 per warrant were issued to Warrant Holders. The fair value at grant date of the additional warrants issued was \$340,154 based on the Black-Scholes pricing model and was recorded as a BDC Financing issuance cost. The inputs used in the measurement of the fair value at the grant dates follows: risk-free rate of 1.50%; expected life of 1.4 years; volatility factor of 73.4%; and fair value of \$0.115 per share at issuance date.

ii) December 2019 Issue

On December 30, 2019, the Company completed a first tranche of convertible debenture units ("Unit") for gross proceeds of \$2,740,000. Each Unit is comprised of one \$1,000 principal amount unsecured 10% convertible debenture ("Debenture") of the Company due December 30, 2024 (the "Maturity Date") and 938 common share purchase warrants. The Company issued a total of 2,570,120 Warrants to the debenture subscribers. Related party participation in the private placement totaled 25 units.

The convertible debentures are considered to be compound financial instruments in which the host debt instruments have been determined to be financial liabilities with an embedded equity instrument. The Company initially measured the liability component at fair value, with the residual amount assigned to the equity components. The Company used an effective interest rate of 15.0% resulting in \$686,000 assigned to the conversion feature and warrants.

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8. Loans and financing (continued):

(b) Convertible debentures (continued):

Each Debenture is convertible, at the option of the holder, at any time prior to the close of business on the last business day immediately preceding the Maturity Date, into that number of common shares computed on the basis of the principal amount of the Debentures divided by the conversion price of \$0.23 per common share.

The Debentures are subject to an acceleration right exercisable by the Company, which will force the conversion of the Debentures into common shares at the \$0.23 conversion price. This right is exercisable if the Company's common shares trade at or above a volume-weighted average trade price of \$0.33 on the TSX Venture Exchange ("TSX-V") on any 20 consecutive trading days. If the acceleration right is exercised by the Company, the conversion of the Debentures into common shares will occur upon delivering a notice to the Debenture holder specifying the accelerated conversion date and concurrently issuing a press release to such effect.

The Debentures are also subject to a redemption right, at the Company's option, to redeem at any time on or after the first anniversary of the issue date, but prior to the Maturity Date, the whole or any part of the Debentures then outstanding at such date at a redemption price equal to 105% of the aggregate Principal Amount of the Debentures to be redeemed together with all interest accrued and remaining unpaid.

Each Warrant entitles the holder to purchase one common share of the Company for a period of 24 months after December 30, 2019 at a price of \$0.16 per Warrant. The Warrants are subject to an acceleration right if on any 20 consecutive or non-consecutive trading days following the closing date, the Company's common shares trade at greater than a volume-weighted average trading price of \$0.20 on the TSX-V.

The interest on the Debentures is payable in cash on a semi-annual basis in arrears (May 31 and November 30).

Pursuant to the offering, the Company paid cash commissions, legal and other related issuance costs totaling \$203,746. The Company also issued non-transferable broker warrants to acquire 708,940 common shares from treasury at a price of \$0.16 per common share, exercisable at any time within the 24-month period following December 30, 2019. The assigned value at grant date of the broker warrants issued was \$40,128 based on the Black-Scholes pricing model. Expected volatility was determined based on comparable publicly listed companies. The inputs used in the measurement of the fair values at the grant date follows: risk-free rate of 1.71%; expected life of 1.5 years; volatility factor of 77.73%; and fair value of \$0.17 per share at issuance date.

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8. Loans and financing (continued):

(c) BDC Capital Inc. Financing:

	Loan	Equity component	Issuance Cost	Net Book Value
December 31, 2018	\$ -	\$ -	\$ -	\$ -
Proceeds	6,965,737	(340,154)	(702,170)	5,923,413
Amortization	-	42,053	86,809	128,862
Foreign exchange restatement to period end spot rate	(168,272)	-	-	(168,272)
December 31, 2019	\$ 6,797,465	\$ (298,101)	\$ (615,361)	\$ 5,884,003

On June 11, 2019, the Company secured a \$10 million USD loan facility from BDC Capital Inc. ("BDC" and the "BDC Financing"). The BDC Financing will be drawn down in up to three tranches. The first tranche of \$5 million USD will be used for working capital to further accelerate organic growth. The remaining \$5 million USD may be advanced at a later date for use in funding acquisition opportunities. The maturity date of the loan facility is May 1, 2025.

The loan facility bears interest at BDC Capital's floating base rate plus 6% per year and is payable monthly (7.05% at date of signing; 5.1% at April 1, 2020). Principal repayment of the outstanding loan commences on June 1, 2021 by way of 48 monthly instalments of \$93,750 USD and a balloon payment of \$500,000 USD on May 1, 2025. The loan facility is secured in a subordinate position on all assets of the Company except for the Company's intellectual property where BDC's security interest shall rank first.

The loan facility also bears non-compounding interest of 8% per year payable on the maturity date. The rate may be reduced by up to 1% upon achievement of certain milestones.

The loan facility requires maintenance of minimum coverage ratio and earning levels along with other customary covenants such as limitations on, among other things, additional debt, liens, investments, acquisitions and capital expenditures, future dividends and asset sales. As at December 31, 2019, the Company was in compliance with all covenants under the BDC Financing.

(d) Other Loans:

Other Loans includes capitalized office lease liability and long-term customer financing of custom packaging molds. The Company recorded the remaining three years of lease payments for its office space as a lease liability of \$138,350. Lease liability was measured at the present value of the remaining lease payments discounted at the incremental borrowing rate of 6.45% as at January 1, 2019. Customer financing totaled \$60,255 is repayable over 2 years on a minimum per unit sold basis. In the event that total payments made over the 2 year term do not equal the financed amount, the balance outstanding is due at maturity.

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8. Loans and financing (continued):

(e) Undiscounted repayment commitment:

The required undiscounted annual repayments of the Company's long-term debt for the years ending December 31 follow:

2020	\$ 196,341
2021	1,340,184
2022	6,345,670
2023	1,182,576
2024 and beyond	6,789,523
	<hr/>
	\$ 15,854,294

9. Share capital and share-based payments:

(a) Common and preferred share capital:

Authorized and issued:

Unlimited number of common shares without par value.

Unlimited number of preferred shares without par value, issuable in series.

As at December 31, 2019, 105,797,873 common shares were issued and outstanding (December 31, 2018 - 94,350,686).

Shares for acquisition consideration:

On December 23, 2016, the Company completed the acquisition of Lindar Corporation's ("Lindar") bioplastic book of business, which was subject to finalization of an outsourcing agreement and approval from the TSX Venture Exchange. The common shares to be issued to Lindar were recorded with a value of \$591,500 as consideration and reflected as shares issuable.

On March 21, 2019, the Company finalized the outsourcing agreement with Lindar and received approval from the TSX Venture Exchange to release the common share consideration for the acquisition. The Company originally agreed to issue 4,225,000 shares with a value of \$591,500 on December 23, 2016. Pursuant to the agreement finalization and share release approval, the Company agreed to increase the number of shares to 5,382,000.

Shares for debt settlement:

During the year ended December 31, 2018, the Company issued 150,000 shares at a price of \$0.11 per share and 52,500 shares at a price of \$0.10 to settle outstanding indebtedness of \$21,750.

Shares for debenture conversion:

During the year ended December 31, 2019, the Company issued 2,833,330 shares at a price of \$0.15 per share pursuant to the conversion of \$425,000 of outstanding debentures (December 31, 2018 – 133,332 shares; \$20,000) (Note 8 (b)).

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9. Share capital and share-based payments (continued):

(b) Share options:

The change in the number of the Company's stock options follows:

	Options	Weighted average exercise price
Outstanding as at December 31, 2017	7,188,794	\$ 0.18
Issuance of options	560,000	0.11
Forfeiture of options	(845,000)	0.15
Outstanding as at December 31, 2018	6,903,794	0.18
Issuance of options	281,000	0.13
Forfeiture of options	(45,000)	0.10
Outstanding as at December 31, 2019	7,139,794	\$ 0.18
Exercisable as at December 31, 2019	5,741,064	\$ 0.18

Information about the Company's stock options outstanding and exercisable as at December 31, 2019 follows:

Expiry date	Options outstanding	Options exercisable	Exercise price	Weighted average remaining contractual life (in years)
April 2020	500,000	500,000	\$ 0.25	0.25
January 2023	46,630	46,630	0.25	3.01
October 2023	11,658	11,658	0.25	3.78
September 2024	29,144	29,144	0.25	4.68
September 2024	142,857	142,857	0.18	4.72
April 2025	104,918	104,918	0.25	5.26
April 2025	61,924	61,924	0.28	5.31
July 2025	1,100,000	1,100,000	0.20	5.55
August 2025	350,000	350,000	0.19	5.59
February 2026	1,305,000	1,293,570	0.20	6.16
May 2027	2,736,663	1,767,454	0.15	7.35
July 2028	100,000	100,000	0.15	8.53
November 2026	370,000	184,996	0.10	6.92
January 2027	100,000	47,913	0.10	7.03
July 2027	85,000	-	0.15	7.50
September 2027	60,000	-	0.15	7.72
October 2027	36,000	-	0.13	7.84
	7,139,794	5,741,064	\$ 0.18	6.12

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9. Share capital and share-based payments (continued):

(b) Share options (continued):

The fair values of options granted were measured based on the Black-Scholes pricing model. Expected volatility was determined based on comparable publicly listed companies. The inputs used in the measurement of the fair values at the modification and grant dates follows:

	Year ended December 31 2019	Year ended December 31 2018
Risk-free interest rate	1.53 - 2.16%	1.53 – 2.16%
Dividend yield	0.00%	0.00%
Expected life (years)	2 - 4	2 -10
Volatility	61.9 - 126.8%	72.3 – 126.8%
Forfeiture rate	0.0%	0.0%
Fair value at grant date	\$0.10 - \$0.16	\$0.10 - \$0.15

(c) Share purchase warrants:

The following table summarizes information about the Company's share purchase warrants:

	Warrants	Weighted average exercise price
Outstanding at December 31, 2017	46,335,221	\$ 0.21
Issuance of warrants	7,573,500	0.10
Issuance of warrants to brokers	2,239,867	0.15
Exercise of warrants	(562,500)	0.10
Expiry of warrants	(25,711,123)	0.25
Outstanding at December 31, 2018	29,874,965	\$ 0.14
Issuance of warrants	11,139,095	0.11
Issuance of warrants to brokers	708,940	0.16
Exercise of warrants	(3,231,857)	0.13
Expiry of warrants	(18,034,172)	0.15
Outstanding at December 31, 2019	20,456,971	\$ 0.12

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9. Share capital and share-based payments (continued):

(c) Share purchase warrants (continued):

Expiry date	Warrants outstanding	Exercise price	Weighted average remaining contractual life (in years)
October 20, 2021	52,231	\$ 0.19	1.81
February 28, 2021	2,239,867	0.15	1.16
February 28, 2022	14,885,813	0.10	2.16
December 30, 2021	3,279,060	0.16	2.00
	20,456,971	\$ 0.12	1.81

10. Related party transactions

The following table sets forth the remuneration of directors and key management personnel:

	Year ended December 31	
	2019	2018
Salaries, management, consulting and director fees	\$ 896,020	\$ 821,181
Share based payments ⁽ⁱ⁾	36,901	95,096
	\$ 932,921	\$ 916,277

⁽ⁱ⁾ Share-based payments are the fair value of options granted to directors and key management personnel on an accrual basis.

As at December 31, 2019, \$204,208 (December 31, 2018 - \$177,408) was due to directors and officers of the Company for accrued bonus, management, consulting, director fees and expense reimbursement.

As at December 31, 2019, \$79,000 (December 31, 2018 - \$209,000) was due to directors and officers of the Company for convertible debentures outstanding. During the year ended December 31, 2019, the Company paid debenture interest to the directors and officers of the Company \$21,826 (December 31, 2018 - \$10,364).

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11. Income taxes:

Income tax recovery (expense) differs from the amount that would result from applying the Canadian federal and provincial tax rate to loss before income taxes as follows:

	Year ended December 31	
	2019	2018
Loss before income taxes	\$ (3,473,821)	\$ (3,287,799)
Expected income tax recovery at 27.0% (2017 - 27.0%)	(937,932)	(887,706)
Permanent differences and other	96,123	48,714
Change in deferred tax assets not recognized	564,747	657,519
	\$ (277,062)	\$ (181,473)

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes.

The Company has recognized deferred taxes in respect of the following:

	December 31, 2019	December 31, 2018
Deferred tax assets:		
Net operating loss carry forwards	\$ 357,748	\$ 142,854
Deferred tax liabilities:		
Long-term debt	(357,748)	(142,854)
	\$ -	\$ -

The Company did not recognize deferred tax assets for the following deductible temporary differences:

	December 31, 2019	December 31, 2018
Net operating loss carry forwards	\$ 16,082,954	\$ 14,199,584
Other deductible temporary differences	5,633,275	4,121,777
	\$ 21,716,229	\$ 18,321,361

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11. Income taxes (continued):

The Company has incurred losses of \$17,407,948 (December 31, 2018 - \$14,728,673) for Canadian tax purposes which are available to reduce future taxable income. Such benefits will be recorded as an adjustment to the tax provision in the year realized. The losses will expire as follows:

2030	\$ 79,091
2031	175,689
2032	381,900
2033	834,303
2034	1,347,768
2035	2,313,584
2036	2,622,263
2037	4,291,145
2038	2,519,251
2039	2,842,955
	<hr/>
	\$ 17,407,948

In addition, the Company has \$632,636 (December 31, 2018 - \$632,636) of SR&ED expenditure pool which is available to reduce future taxable income. This amount carries forward indefinitely.

12. Management of capital:

The Company's objectives when managing capital are to safeguard its ability to continue as a going concern and to have sufficient capital to be able to fund the research and development of its high-performance bioplastics, for the benefit of its shareholders. In the management of capital, the Company includes loans, share capital and contributed surplus.

In order to maintain its capital structure, the Company, is dependent on equity funding and when necessary, raises capital through issuance of equity instruments. The Company manages its capital structure and makes adjustments to it in light of economic conditions. The Company, upon approval from its Board of Directors, will make changes to its capital structure as deemed appropriate under the specific circumstances. To date, no dividends have been paid to the Company's shareholders and none are planned.

The Company is subject to certain covenants on its credit facility and long-term debt. Along with customary covenants such as limitations on, among other things, additional debt, liens, investments, acquisitions and capital expenditures, future dividends and asset sales, the loans require maintenance of minimum coverage ratio and earning levels. Other than these required covenants, the Company is not subject to any externally imposed capital requirements.

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13. Financial risk management and financial instruments:

(a) Overview:

The Company is exposed to risks of varying degrees of significance which could affect its ability to achieve its strategic objectives for growth. The main objectives of the Company's risk management process are to ensure that risks are properly identified and that the capital base is adequate in relation to those risks. The principal financial risks to which the Company is exposed are described below.

(b) Market risk:

Market risk is the risk that changes in market prices, such as fluctuations in the prices of inputs for materials, foreign exchange rates or interest rates, will affect the Company's income or the value of its financial instruments. The Company does not engage in risk management practices such as hedging or derivatives.

A portion of the Company's operations are performed in US dollars, giving rise to exposure to market risks from foreign exchange rates.

(c) Currency risk:

(i) Exposure to currency risk:

The Company is exposed to financial risks as a result of exchange rate fluctuations and the volatility of these rates. At December 31, 2019, total assets include cash of US\$3,601,403 (December 31, 2018 - US\$203,063) and receivables of US\$501,505 (December 31, 2018 - US\$658,611); total liabilities include payables and accruals of US\$1,758,471 (December 31, 2018 - US\$710,890), credit line of US\$500,000 (December 31, 2018 - \$Nil) and undiscounted long-term debt of US\$5,223,561 (December 31, 2018 - \$Nil).

(ii) Sensitivity analysis:

A change of the US dollar against the Canadian dollar as at December 31, 2018 would have increased or decreased comprehensive loss by the amount shown below. The analysis assumes that all other variables remain constant.

	Profit or loss
10% change of the US dollar	\$ 337,912

(d) Liquidity risk:

Liquidity risk is the risk that the Company is not able to meet its financial obligations as they fall due or can do so only at excessive cost. The Company mitigates liquidity risk by holding sufficient cash and cash equivalents to meet its short-term financial obligations. The Company's growth is primarily financed through the issuance of equity and debt. The majority of the Company's financial liabilities recorded in accounts payable and accrued liabilities are due within 60 days.

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13. Financial risk management and financial instruments (continued):

(d) Liquidity risk (continued):

The following are the contractual maturities of financial liabilities.

	Carrying amount	Contractual cash flows	Less than 1 year	Year 2	Years 3-5	More than 5 years
Non-derivative financial liabilities:						
Trade and other payables and accrued liabilities	\$3,039,288	\$ 3,039,288	\$ 3,039,288	\$ -	\$ -	\$ -
Credit line	649,500	649,500	649,500	-	-	-
Loan payable	13,272,552	15,854,293	196,341	1,340,184	8,710,822	5,606,946
	\$16,961,340	\$19,543,081	\$ 3,885,129	\$1,340,184	\$8,710,822	\$ 5,606,946

It is not expected that the cash flows included in the maturity analysis could occur significantly earlier, or at significantly different amounts.

(e) Credit risk:

The Company's exposure to credit risk primarily arises from the possibility that its customers may fail to meet their obligations. The Company has credit evaluation, approval and monitoring processes in place which mitigates these potential credit risks. The Company continually evaluates the collectability of accounts receivable and records an allowance for doubtful accounts if required, which reduces the receivables by the amount of any expected credit losses. The failure of a significant customer could have a material adverse effect on the Company. Total accounts receivable as at December 31, 2017 are \$682,622 (December 31, 2018 - \$915,800). There is no allowance for doubtful accounts against this balance (December 31, 2018 - nil), which management believes adequately reflects the Company's expected credit losses. The provision for allowance for doubtful accounts is recognized within operating expenses, if any.

(f) Fair values of financial instruments:

The Company categorizes its fair value estimates using a fair value hierarchy based on the inputs used to measure fair value. The fair value hierarchy has three levels based on the reliability of the inputs used to determine fair value as follows:

Level 1: Values based upon unadjusted quoted prices in active markets that are accessible at the measurement date for identical assets or liabilities.

Level 2: Values based upon quoted prices in markets that are not active or model inputs that are observable either directly or indirectly for substantially the full term of the asset or liability.

Level 3: Values based upon prices or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement.

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13. Financial risk management and financial instruments (continued):

(f) Fair values of financial instruments (continued):

The carrying value of cash and cash equivalents, trade and other receivables, and accounts payable and accrued liabilities approximate their fair values due to the short-term nature of these instruments. The carrying value of the credit facility and loans, approximates their fair values as the interest rate environment has not changed significantly since the date of issue.

The Company has no financial instruments which are measured at fair value at December 31, 2019 with the exception of cash which is considered Level 2.

14. Segmented information:

The Company carries on business in the plastics and packaging industry and all sales and costs are made in this segment. The vast majority of the Company's operations are performed within the United States and Canada.

Sales in the year ended December 31, 2019 from the top four customers amounted to \$7,464,472 or 74% of total revenue. (Year ended December 31, 2018 - \$4,346,755 or 85%).

The Company had two accounts that accounted for greater than ten percent of accounts receivable for a total of \$375,993 or 55% at December 31, 2019 (December 31, 2018 – three accounts: \$691,313 or 75%).

15. Product development:

Product development expenses are as follows:

	Year ended December 31	
	2019	2018
Product development expenses	\$ 617,888	\$ 313,042
Capitalized product development expenses	(155,914)	(93,997)
	<u>\$ 461,974</u>	<u>\$ 219,045</u>

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16. Selling, general, and administrative:

The following is a breakdown of the Company's selling, general and administrative expenses.

	Year ended December 31	
	2019	2018
Salaries	\$ 1,282,213	\$ 1,163,962
Other selling, general and administrative expenses	972,111	832,620
Outsourced supply chain, freight costs, and fulfillment	2,400,874	1,386,600
	\$ 4,655,198	\$ 3,383,182

17. Supplementary cash flow information:

	Year ended December 31	
	2019	2018
Non-cash financing activities:		
Shares issued for settlement of accounts payable	\$ -	\$ 21,750
Shares issued for conversion of debentures	\$ 425,000	\$ 20,000

18. Subsequent events:

a) Equity Transactions

Subsequent to the year end, the following equity related transactions occurred:

- the Company issued 1,566,661 shares at a price of \$0.15 per share pursuant to the conversion of \$235,000 of outstanding debentures;
- the Company issued 766,665 shares at a price of \$0.10 per share for gross proceeds of \$76,667; and
- the Company issued 108,400 share options to employees of the Company with an option price ranging from \$0.10 per share to \$0.175 per share

On January 23, 2020, the Company closed the final tranche of convertible debenture (Note 8(b)(ii)) units for gross proceeds of \$1,190,000. In total, the Company issued 3,930 units at a price of \$1,000 per unit. Each unit is comprised of a CAD \$1,000 principal amount, 10% subordinated unsecured convertible debentures due sixty months from the closing date and 938 common share purchase warrants. Each debenture is convertible at a conversion price of \$0.23 per common share of the Company. Each warrant entitles its holder to acquire one additional common share at a price of \$0.16 per common share within the 24-month period following the closing date. Proceeds of the debenture placement were used for closing costs and to redeem \$3,214,000 of the Company's existing 10% convertible unsecured debentures due February 2022 (the "2018 Debentures"). The redemption included a 5% premium plus accrued interest.

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18. Subsequent events (continued):

b) Acquisition

On March 3, 2020, the Company entered a definitive agreement to acquire 100% of Shepherd Thermoforming & Packaging Inc., a leading thermoformer with over 35 years' experience and all its real estate assets for CAD\$9.5 million in cash (the "Purchase"). The assets include machinery, molds and a 42,000 square foot manufacturing facility, all located on 2.31 acres of land in the Greater Toronto Area of Brampton, Ontario. The closing of the transaction is expected to be not later than April 30, 2020. In addition to the \$9.5 million payable in cash at closing, the Purchase contemplates an earnout payment of \$2.25 million which may be payable at some point between 42 and 60 months post-closing, upon satisfaction of a condition relating to increase in the value of the real estate purchased as part of the transaction. The Company is completing the final stages of financing required to close the Purchase with its financial partners, including BDC, under the terms and conditions of its previously announced BDC financing from June 2019 (Note 8(c)).

c) Novel Coronavirus ("COVID-19") impact

The Company's operations are deemed an essential business as defined by the US Department of Homeland Security and the Canadian provinces where we manufacture food packaging. Our packaging manufacturers are operational and have implemented enhanced sanitary measures to ensure their ability to continue to produce and deliver products.

Effective March 15, 2020 and to the date of these financials statements, the Company's employees have been working from home in accordance with recommendations to safeguard against COVID-19.