CANOPY GROWTH CORPORATION

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

FOR THE THREE AND NINE MONTHS ENDED DECEMBER 31, 2020

FEBRUARY 9, 2021

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Introduction

This Management's Discussion and Analysis ("MD&A") should be read together with other information, including our unaudited condensed interim consolidated financial statements and the related notes to those statements included in Part I, Item 1 of this Quarterly Report (the "Interim Financial Statements"), our consolidated financial statements appearing in our Annual Report on Form 10-K for the year ended March 31, 2020 (as amended, the "Annual Report") and Part I, Item 1A, Risk Factors, of the Annual Report. This MD&A provides additional information on our business, recent developments, financial condition, cash flows and results of operations, and is organized as follows:

- *Part 1 - Business Overview.* This section provides a general description of our business, which we believe is important in understanding the results of our operations, financial condition, and potential future trends.
- *Part 2 - Results of Operations.* This section provides an analysis of our results of operations for the third quarter of fiscal 2021 in comparison to the third quarter of fiscal 2020, and for the nine months ended December 31, 2020 in comparison to the nine months ended December 31, 2019.
- *Part 3 - Financial Liquidity and Capital Resources.* This section provides an analysis of our cash flows and outstanding debt and commitments. Included in this analysis is a discussion of the amount of financial capacity available to fund our ongoing operations and future commitments.

We prepare and report our Interim Financial Statements in accordance with U.S. GAAP. Our Interim Financial Statements, and the financial information contained herein, are reported in thousands of Canadian dollars, except share and per share amounts or as otherwise stated. We have determined that the Canadian dollar is the most relevant and appropriate reporting currency as, despite continuing shifts in the relative size of our operations across multiple geographies, the majority of our operations are conducted in Canadian dollars and our financial results are prepared and reviewed internally by management in Canadian dollars.

Special Note Regarding Forward-Looking Statements

This Quarterly Report contains "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act"), and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act") and other applicable securities laws, which involve certain known and unknown risks and uncertainties. Forward-looking statements predict or describe our future operations, business plans, business and investment strategies and the performance of our investments. These forward-looking statements are generally identified by their use of such terms and phrases as "intend," "goal," "strategy," "estimate," "expect," "project," "projections," "forecasts," "plans," "seeks," "anticipates," "potential," "proposed," "will," "should," "could," "would," "may," "likely," "designed to," "foreseeable future," "believe," "scheduled" and other similar expressions. Our actual results or outcomes may differ materially from those anticipated. You are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date the statement was made.

Forward-looking statements include, but are not limited to, statements with respect to:

- the uncertainties associated with the COVID-19 pandemic, including our ability to continue operations, the ability of our suppliers and distribution channels to continue to operate, the use of our products by consumers, disruptions to the global and local economies due to related stay-at-home orders, quarantine policies and restrictions on travel, trade and business operations and a reduction in discretionary consumer spending;
- laws and regulations and any amendments thereto applicable to our business and the impact thereof, including uncertainty regarding the application of U.S. state and federal law to U.S. hemp (including CBD) products and the scope of any regulations by the U.S. Federal Drug Administration, the U.S. Federal Trade Commission, the U.S. Patent and Trademark Office, the U.S. Department of Agriculture (the "USDA") and any state equivalent regulatory agencies over U.S. hemp (including CBD) products;
- expectations regarding the regulation of the U.S. hemp industry in the U.S., including the promulgation of regulations for the U.S. hemp industry by the USDA;
- expectations regarding the potential success of, and the costs and benefits associated with, our acquisitions, joint ventures, strategic alliances, equity investments and dispositions;
- the amended plan of arrangement with Acreage Holdings, Inc. ("Acreage"), including the satisfaction or waiver of the conditions to closing of such acquisition;
- the plan of arrangement with Canopy Rivers Inc. ("Canopy Rivers"), including the satisfaction or waiver of the conditions to closing of such transaction;

- the grant, renewal and impact of any license or supplemental license to conduct activities with cannabis or any amendments thereof;
- our international activities and joint venture interests, including required regulatory approvals and licensing, anticipated costs and timing, and expected impact;
- the ability to successfully create and launch brands and further create, launch and scale cannabis-based products and U.S. hemp-derived consumer products in jurisdictions where such products are legal and that we currently operate in;
- the benefits, viability, safety, efficacy, dosing and social acceptance of cannabis, including CBD and other cannabinoids;
- the anticipated benefits and impact of the investment in us (the "CBI Group Investments") by Constellation Brands, Inc. ("CBI") and its affiliates (together, the "CBI Group");
- the potential exercise of the warrants held by the CBI Group, pre-emptive rights and/or top-up rights in connection with the CBI Group Investments, including proceeds to us that may result therefrom or the potential conversion of notes held by the CBI Group in connection with the CBI Group Investments;
- expectations regarding the use of proceeds of equity financings, including the proceeds from the CBI Group Investments;
- the legalization of the use of cannabis for medical or recreational in jurisdictions outside of Canada, the related timing and impact thereof and our intentions to participate in such markets, if and when such use is legalized;
- our ability to execute on our strategy and the anticipated benefits of such strategy;
- the ongoing impact of the legalization of cannabis product types and forms for recreational use in Canada, including federal, provincial, territorial and municipal regulations pertaining thereto, the related timing and impact thereof and our intentions to participate in such markets;
- the ongoing impact of developing provincial, territorial and municipal regulations pertaining to the sale and distribution of cannabis, the related timing and impact thereof, as well as the restrictions on federally regulated cannabis producers participating in certain retail markets and our intentions to participate in such markets to the extent permissible;
- the future performance of our business and operations;
- our competitive advantages and business strategies;
- the competitive conditions of the industry;
- the expected growth in the number of customers using our products;
- our ability or plans to identify, develop, commercialize or expand our technology and research and development initiatives in cannabinoids, or the success thereof;
- expectations regarding revenues, expenses and anticipated cash needs;
- expectations regarding cash flow, liquidity and sources of funding;
- expectations regarding capital expenditures;
- the expansion of our production and manufacturing, the costs and timing associated therewith and the receipt of applicable production and sale licenses;
- the expected growth in our growing, production and supply chain capacities;
- expectations regarding the resolution of litigation and other legal proceedings;
- expectations with respect to future production costs;
- expectations with respect to future sales and distribution channels;
- the expected methods to be used to distribute and sell our products;
- our future product offerings;
- the anticipated future gross margins of our operations;
- accounting standards and estimates;
- expectations regarding our distribution network; and
- expectations regarding the costs and benefits associated with our contracts and agreements with third parties, including under our third-party supply and manufacturing agreements.

Certain of the forward-looking statements contained herein concerning the industries in which we conduct our business are based on estimates prepared by us using data from publicly available governmental sources, market research, industry analysis and on assumptions based on data and knowledge of these industries, which we believe to be reasonable. However, although generally indicative of relative market positions, market shares and performance characteristics, such data is inherently imprecise. The industries in which we conduct our business involve risks and uncertainties that are subject to change based on various factors, which are described further below.

The forward-looking statements contained herein are based upon certain material assumptions that were applied in drawing a conclusion or making a forecast or projection, including: (i) management's perceptions of historical trends, current conditions and expected future developments; (ii) our ability to generate cash flow from operations; (iii) general economic, financial market, regulatory and political conditions in which we operate; (iv) the production and manufacturing capabilities and output from our facilities and our joint ventures, strategic alliances and equity investments; (v) consumer interest in our products; (vi) competition;

(vii) anticipated and unanticipated costs; (viii) government regulation of our activities and products including but not limited to the areas of taxation and environmental protection; (ix) the timely receipt of any required regulatory authorizations, approvals, consents, permits and/or licenses; (x) our ability to obtain qualified staff, equipment and services in a timely and cost-efficient manner; (xi) our ability to conduct operations in a safe, efficient and effective manner; (xii) our ability to realize anticipated benefits, synergies or generate revenue, profits or value from our recent acquisitions into our existing operations; (xiii) our ability to continue to operate in light of the COVID-19 pandemic and the impact of the pandemic on demand for, and sales of, our products and our distribution channels; and (xiv) other considerations that management believes to be appropriate in the circumstances. While our management considers these assumptions to be reasonable based on information currently available to management, there is no assurance that such expectations will prove to be correct.

By their nature, forward-looking statements are subject to inherent risks and uncertainties that may be general or specific and which give rise to the possibility that expectations, forecasts, predictions, projections or conclusions will not prove to be accurate, that assumptions may not be correct and that objectives, strategic goals and priorities will not be achieved. A variety of factors, including known and unknown risks, many of which are beyond our control, could cause actual results to differ materially from the forward-looking statements in this Quarterly Report and other reports we file with, or furnish to, the Securities and Exchange Commission (the “SEC”) and other regulatory agencies and made by our directors, officers, other employees and other persons authorized to speak on our behalf. Such factors include, without limitation, changes in laws, regulations and guidelines and our compliance with such laws, regulations and guidelines; the risk that the COVID-19 pandemic may disrupt our operations and those of our suppliers and distribution channels and negatively impact the use of our products; consumer demand for cannabis and U.S. hemp products; our reliance on licenses issued by and contractual arrangements with various federal and provincial governmental authorities; future levels of revenues and the impact of increasing levels of competition; our ability to manage disruptions in credit markets or changes to our credit rating; future levels of capital, environmental or maintenance expenditures, general and administrative and other expenses; the success or timing of completion of ongoing or anticipated capital or maintenance projects; business strategies, growth opportunities and expected investment; the adequacy of our capital resources and liquidity, including but not limited to, availability of sufficient cash flow to execute our business plan (either within the expected timeframe or at all); the potential effects of judicial or other proceedings on our business, financial condition, results of operations and cash flows; volatility in and/or degradation of general economic, market, industry or business conditions; our exposure to risks related to an agricultural business, including wholesale price volatility and variable product quality; compliance with applicable environmental, economic, health and safety, energy and other policies and regulations and in particular health concerns with respect to vaping and the use of cannabis and U.S. hemp products in vaping devices; the anticipated effects of actions of third parties such as competitors, activist investors or federal, state, provincial, territorial or local regulatory authorities, self-regulatory organizations, plaintiffs in litigation or persons threatening litigation; changes in regulatory requirements in relation to our business and products; and the factors discussed under the heading “Risk Factors” in the Annual Report. Readers are cautioned to consider these and other factors, uncertainties and potential events carefully and not to put undue reliance on forward-looking statements.

Forward-looking statements are provided for the purposes of assisting the reader in understanding our financial performance, financial position and cash flows as of and for periods ended on certain dates and to present information about management’s current expectations and plans relating to the future, and the reader is cautioned that the forward-looking statements may not be appropriate for any other purpose. While we believe that the assumptions and expectations reflected in the forward-looking statements are reasonable based on information currently available to management, there is no assurance that such assumptions and expectations will prove to have been correct. Forward-looking statements are made as of the date they are made and are based on the beliefs, estimates, expectations and opinions of management on that date. We undertake no obligation to update or revise any forward-looking statements, whether as a result of new information, estimates or opinions, future events or results or otherwise or to explain any material difference between subsequent actual events and such forward-looking statements, except as required by law. The forward-looking statements contained in this Quarterly Report and other reports we file with, or furnish to, the SEC and other regulatory agencies and made by our directors, officers, other employees and other persons authorized to speak on our behalf are expressly qualified in their entirety by these cautionary statements.

Part 1 - Business Overview

We are a leading cannabis company with operations in countries across the world. We produce, distribute and sell a diverse range of cannabis and hemp-based products and other consumer products for both recreational and medical purposes under a portfolio of distinct brands in Canada pursuant to the *Cannabis Act*, and globally pursuant to applicable international and Canadian legislation, regulations and permits.

On October 17, 2018, the *Cannabis Act* came into effect in Canada, regulating both the medical and recreational cannabis markets in Canada and providing provincial, territorial and municipal governments the authority to prescribe regulations regarding the distribution and sale of recreational cannabis. On October 17, 2019, the second phase of recreational cannabis products, specifically, ingestible cannabis, cannabis extracts and cannabis topical products (referred to as “Cannabis 2.0”), were legalized pursuant to certain amendments to the regulations under the *Cannabis Act*. We began selling our cannabis-infused chocolates, cannabis-infused beverage offerings, vape pen power sources and pod-based vape devices across Canada in the fourth quarter of fiscal 2020, with these products complementing our existing flower, oil and softgel products. Our 510-threaded vape cartridges began shipping into the market in April 2020, with product availability varying based on provincial and territorial regulations. Our recreational cannabis products are predominantly sold to provincial and territorial agencies under a "business-to-business" wholesale model, with those provincial and territorial agencies then being responsible for the distribution of our products to brick-and-mortar stores and for online retail sales. We have also opened a network of Tweed and Tokyo Smoke retail stores across Canada, where permissible, to promote brand awareness and drive consumer demand under a "business-to-consumer" model.

Our Spectrum Therapeutics medical division is a global leader in medical cannabis. Spectrum Therapeutics produces and distributes a diverse portfolio of medical cannabis products to healthcare practitioners and medical customers in Canada, and in several other countries where it is federally permissible to do so. In April 2019, we acquired C^3 Cannabinoid Compound Company ("C^3"), Europe's largest cannabinoid-based pharmaceuticals company and a leading manufacturer of dronabinol, a registered active pharmaceutical ingredient in Germany and certain other European countries. The addition of dronabinol has allowed us to expand our portfolio of medical cannabis offerings for our customers in countries where permissible.

Subsequent to the passage of the U.S. Agricultural Improvement Act of 2018 in December 2018, we began building our hemp supply chain in the United States through our investment in hemp growing capability and in processing, extraction and finished goods manufacturing facilities. In September 2020, our Martha Stewart CBD line of premium quality, hemp-derived wellness gummies, oils and softgels was launched in the United States.

In June 2019, we implemented a plan of arrangement pursuant to an arrangement agreement with Acreage, a U.S. multi-state cannabis operator. In September 2020, following receipt of all required approvals, we entered into a second amendment to the arrangement agreement with Acreage and implemented an amended and restated plan of arrangement (the "Acreage Arrangement"). Pursuant to the Acreage Arrangement, following the occurrence or waiver (at our discretion) of changes in U.S. federal law to permit the general cultivation, distribution, and possession of marijuana or to remove the regulation of such activities from the federal laws of the United States (the "Triggering Event") and subject to the satisfaction or waiver of the conditions set out in the arrangement agreement with Acreage, we (i) agreed to acquire approximately 70% of the issued and outstanding shares of Acreage, and (ii) obtained the right to acquire the other approximately 30% of the issued and outstanding shares of Acreage. The acquisition of Acreage, if completed, will provide a pathway into cannabis markets in the United States; however, we and Acreage will continue to operate as independent companies until the acquisition of Acreage is completed.

Our other product offerings, which are sold by our subsidiaries in jurisdictions where it is permissible to do so, include (i) vaporizers sold by Storz & Bickel GmbH & Co. KG ("Storz & Bickel"); (ii) beauty, skincare, wellness and sleep products, some of which have been blended with hemp-derived CBD isolate, sold by This Works Products Limited ("This Works"); and (iii) sports nutrition beverages, mixes, protein, gum and mints, some of which have been infused with hemp-derived CBD isolate, sold by BioSteel.

The majority of our products contain THC, CBD, or a combination of these two cannabinoids which are found in the Cannabis sativa plant species. THC is the primary psychoactive or intoxicating cannabinoid found in cannabis. We also refer throughout this MD&A to "hemp", which is a term used to classify varieties of the Cannabis sativa plant that contain CBD and 0.3% or less THC content (by dry weight). Conversely, the term "marijuana" refers to varieties of the Cannabis sativa plant with more than 0.3% THC content and moderate levels of CBD.

Our licensed operational capacity in Canada includes indoor, greenhouse and outdoor cultivation space; post-harvest processing and cannabinoid extraction capability; advanced manufacturing capability for vape products, softgel encapsulation and pre-rolled joints; a beverage production facility; and a chocolate manufacturing facility. These infrastructure investments allow us to supply the recreational and medical markets with a complimentary balance of flower products and extracted cannabinoid input for our oil, CBD and Cannabis 2.0 products. Additionally, we have built a hemp supply chain in the United States and hold the necessary licenses to cultivate and produce cannabis in Denmark.

We operate in two reportable segments:

- Cannabis, Hemp and Other Consumer Products, which encompasses the production, distribution and sale of a diverse range of cannabis, hemp-based, and other consumer products in Canada and internationally pursuant to applicable international and domestic legislation, regulations and permits; and
- Canopy Rivers, a publicly-traded company in Canada, through which we provide growth capital and strategic support in the global cannabis sector, where federally lawful. Canopy Rivers did not generate net revenue in the three and nine months ended December 31, 2020. Refer to "Recent Developments" below for a description of the plan of arrangement with Canopy Rivers.

Update on the COVID-19 Pandemic

Management has continued to closely monitor the impact of the COVID-19 global pandemic, with a focus on the health and safety of our employees, business continuity and supporting our communities. We established a COVID-19 Management Committee shortly after the declaration of COVID-19 as a global pandemic and implemented various measures to reduce the spread of the virus, as highlighted in the MD&A section of our Annual Report. We have continued to operate under the preventative measures as previously described and have experienced minimal disruption to our production and supply chain. As of the date of the filing of this Quarterly Report, all 33 of our corporate-owned retail stores are open and offering click-and-collect and in-store shopping. Our Canadian medical business, which operates as an e-commerce channel, has continued largely unchanged. Our international medical business operates primarily as a pharmacy model, with pharmacies being deemed essential businesses in Germany and other European countries in which we conduct business. In addition, since our non-production workforce continues to effectively work remotely using various technology tools, we are able to maintain our full operations and internal controls over financial reporting and disclosures.

Given the uncertainties associated with the COVID-19 pandemic, including those related to the use of our products by consumers, disruptions to the global and local economies due to related stay-at-home orders, quarantine policies and restrictions on travel, trade and business operations and a reduction in discretionary consumer spending, we are unable to estimate the impact of the COVID-19 pandemic on our business, financial condition, results of operations, and/or cash flows. The uncertain nature of the impacts of the COVID-19 pandemic may continue to affect our results of operations for the balance of fiscal 2021 and into the beginning of fiscal 2022.

We believe we have sufficient liquidity available from cash and cash equivalents and short-term investments on hand of $825.0 million and $768.6 million, respectively, at December 31, 2020, and from available capacity under our revolving debt facility to enable us to meet our working capital and other operating requirements, fund growth initiatives and capital expenditures, settle our liabilities, and repay scheduled principal and interest payments on debt. Refer to "Part 3 – Financial Liquidity and Capital Resources" for further information.

Recent Developments

Restructuring Actions and Sale of British Columbia Production Facilities

In December 2020, as the partial outcome of an ongoing end-to-end strategic review of our operations, we announced a series of Canadian operational changes designed to streamline our operations and further improve our gross margins. We have ceased operations at our sites in St. John's, Newfoundland and Labrador; Fredericton, New Brunswick; Edmonton, Alberta; Bowmanville, Ontario; as well as our outdoor cannabis grow operations in Saskatchewan. As a result of these restructuring actions, we eliminated approximately 220 full-time positions. Additionally, we (i) completed the sale of our production facilities in Aldergrove and Delta, British Columbia in December 2020 and January 2021, respectively, for combined proceeds of $40.7 million; and (ii) completed our strategy shift in Latin America that we commenced in the fourth quarter of fiscal 2020.

As a result of the restructuring actions described above and adjustments to the net book value of our production facilities in British Columbia in order to reflect their selling prices, we recorded pre-tax charges totaling $400.4 million in the third quarter of fiscal 2021 in asset impairment and restructuring costs, and recorded a write-down of inventory in the amount of $15.6 million in cost of goods sold. These charges are detailed below under "Part 2 – Results of Operations".

Canopy Rivers Arrangement Agreement

In December 2020, we entered into an arrangement agreement (the "Canopy Rivers Arrangement Agreement") with our wholly-owned subsidiary The Tweed Tree Lot Inc. ("Tweed NB"), Canopy Rivers and its wholly-owned subsidiary Canopy Rivers Corporation ("CRC"), pursuant to which we will acquire certain assets from CRC, as set out below, in exchange for cash, common shares in the capital of Canopy Growth and the surrender of all shares in the capital of Canopy Rivers held by us by way of a plan of arrangement under the *Business Corporations Act* (Ontario) (the "Arrangement").

Pursuant to the Arrangement, we will increase our conditional ownership interest in TerrAscend Corp. ("TerrAscend") through the acquisition of (i) 19,445,285 exchangeable shares in the capital of TerrAscend; (ii) 2,225,714 common share purchase warrants in the capital of TerrAscend with an exercise price of $5.95 per share; (iii) 333,723 common share purchase warrants in the capital of TerrAscend with an exercise price of $6.49 per share; and (iv) a $13.2 million loan receivable owing by TerrAscend Canada Inc. ("TerrAscend Canada") to CRC. The securities in the capital of TerrAscend are not currently convertible or exercisable, and will not be convertible or exercisable until federal laws in the United States with respect to marijuana are amended. Subject to certain rights of first refusal, pursuant to the Arrangement, we will also acquire all of the common shares and Class A preferred shares in the capital of

Les Serres Vert Cannabis Inc. (“Vert Mirabel”) held by CRC. In addition, all of the obligations of Tweed NB owing to CRC pursuant to a royalty agreement between the parties will be terminated.

We currently own 36,468,318 Class B multiple voting shares and 15,223,938 Class A subordinate voting shares in the capital of Canopy Rivers. Pursuant to the Arrangement, all of the shares held by us will be repurchased by Canopy Rivers for cancellation on a cashless basis. We will not have any equity, debt or other interest in Canopy Rivers following completion of the Arrangement.

As additional consideration for the assets being transferred and the termination of the royalty agreement, we will make a cash payment to CRC of $115.0 million and issue an aggregate of up to 3,750,000 common shares.

The Arrangement remains subject to approval by the shareholders of Canopy Rivers at a special shareholder meeting expected to be held on February 16, 2021. The Arrangement does not require the approval of our shareholders. In addition to Canopy Rivers shareholder approval, the Arrangement is subject to applicable approvals by the Ontario Superior Court of Justice and certain other closing conditions.

PharmHouse

PharmHouse Inc. (“PharmHouse”), a joint venture formed on May 7, 2018, between Canopy Rivers and 2615975 Ontario Limited (the “PharmHouse JV Partner”), is a company licensed to cultivate cannabis under the Cannabis Act.

<u>CCAA Proceedings</u>

During the nine months ended December 31, 2020, PharmHouse determined that the previously anticipated timeline to generate cash flows from its offtake agreements with Canopy Growth and TerrAscend Canada would not be met, and the ultimate timing and receipt of cash inflows pursuant to these agreements became uncertain. As a result of this, as well as broader sector-wide challenges impacting the Canadian cannabis industry, PharmHouse did not have sufficient liquidity and capital resources to meet its business objectives and became unable to meet its financial obligations as they became due.

Accordingly, on September 15, 2020, PharmHouse obtained an order (the “Initial Order”) from the Ontario Superior Court of Justice (the “Court”) granting PharmHouse creditor protection under the Companies’ Creditors Arrangement Act (“CCAA”) (the “CCAA Proceedings”). The Court appointed an independent professional services firm to act as the Monitor of PharmHouse in the CCAA Proceedings while PharmHouse explores a restructuring of its business and operations (the “Restructuring”).

On October 29, 2020, PharmHouse received approval from the Court to commence its Sale and Investor Solicitation Process (“SISP”). The SISP is intended to solicit interest in, and opportunities for, a sale of, or investment in, all or part of PharmHouse’s assets or business. This may include a restructuring, recapitalization, or other form of reorganization of PharmHouse’s business and affairs. Phase one of the SISP concluded on November 30, 2020, and a number of non-binding offers were received. PharmHouse, with the assistance of the Monitor and the SISP advisor, selected a number of parties to bring forward to the next phase of the SISP, and binding offers for phase two of the SISP are due on or about February 16, 2021.

<u>PharmHouse Recoverability Assessment</u>

As a result of the CCAA Proceedings and the Restructuring, we determined that there were indicators of impairment present for its investments in various PharmHouse-related financial assets. These investments are described below.

We performed impairment testing for the various PharmHouse-related financial assets by estimating the fair value of PharmHouse en bloc. Due to the lack of profitable operating history for PharmHouse as a cannabis entity, we estimated the fair value of PharmHouse en bloc using an asset-based approach to value PharmHouse’s assets under an orderly liquidation scenario where cannabis operations are not continued at PharmHouse’s facility and the greenhouse is sold for purposes other than cannabis cultivation. This amount was then compared to the carrying values of the various PharmHouse-related financial instruments held by Canopy Growth, in sequence based on the priority of claims on PharmHouse’s assets (the “PharmHouse Recoverability Assessment”). The significant components of this fair value analysis included PharmHouse’s greenhouse facility and retrofits, separable machinery and equipment, saleable inventory, and cash. Significant unobservable inputs used to determine the fair value of PharmHouse’s assets include the selling price per square foot for PharmHouse’s greenhouse facility; the recoverability percentage on the liquidation of PharmHouse’s property, plant and equipment; the selling price per gram of PharmHouse’s existing cannabis inventory; and adjustments for the risk of fair value changes and liquidity. Based on the foregoing, we estimated the recoverable value of PharmHouse’s assets in an orderly liquidation scenario to be approximately $57.5 million. The impact of the PharmHouse Recoverability Assessment on Canopy Growth’s various PharmHouse-related financial instruments is described below.

PharmHouse Financial Guarantee

Prior to December 31, 2020, PharmHouse had entered into a syndicated credit agreement (as amended, the "PharmHouse Credit Agreement") with a number of Canadian banks (the "Lenders") to provide PharmHouse with a committed, non-revolving credit facility (the "PharmHouse Credit Facility") with a maximum principal amount of $90.0 million, which was fully drawn. The obligations of PharmHouse under the PharmHouse Credit Facility are secured by guarantees of Canopy Rivers and CRC, and a pledge by CRC of all of the shares of PharmHouse held by it (the "PharmHouse Financial Guarantee"). Accordingly, if PharmHouse is not able to generate sufficient cash flows to service its obligations pursuant to the PharmHouse Credit Facility, we may be required to compensate the Lenders for their loss incurred on the PharmHouse Credit Facility. The PharmHouse Credit Agreement also contains other covenants applicable to Canopy Rivers and CRC.

Based on the PharmHouse Recoverability Assessment described above, we determined that the fair value of PharmHouse's assets under an orderly liquidation scenario where the facility is not used for cannabis operations may be less than the principal amount owed by PharmHouse pursuant to the PharmHouse Credit Facility. Accordingly, we estimated that we have a financial liability related to the PharmHouse Financial Guarantee, reflecting the estimated shortfall between the recoverable amount of PharmHouse en bloc and our exposure to the PharmHouse Credit Facility.

As at December 31, 2020, we estimated the current expected credit loss related to its contingent obligation under the PharmHouse Financial Guarantee to be $32.5 million, and recognized a financial liability for this amount in the consolidated balance sheet (March 31, 2020 – $nil). During the three and nine months ended December 31, 2020, we recognized associated current expected credit losses of $7.5 million and $32.5 million, in net income (loss) for the three and nine months ended December 31, 2020, respectively (three and nine months ended December 31, 2019 – $nil).

Other financial assets, including loans receivable

As at December 31, 2020, CRC had advanced $40.0 million of secured debt financing pursuant to a shareholder loan agreement with PharmHouse (March 31, 2020 – $40.0 million). The shareholder loan has a three-year term and an annual interest rate of 12%, with interest calculated monthly (effective as at the date principal is advanced) and payable quarterly upon the achievement of certain sales-related milestones.

As at December 31, 2020, CRC had advanced $2.5 million to PharmHouse pursuant to a secured demand promissory note (March 31, 2020 – $2.5 million). The secured demand promissory note is non-interest bearing both before and after demand or default. Based on the terms of the secured demand promissory note, we had recognized the secured demand promissory note as a financial asset initially recorded at fair value and subsequently measured at amortized cost.

On August 4, 2020, CRC entered into an unsecured demand promissory note agreement with PharmHouse, pursuant to which it made total advances of $1.2 million between August 4, 2020, and September 8, 2020. The unsecured promissory note bears interest at a rate of 12% per annum, calculated and compounded monthly, and is payable on the demand date. Based on the terms of the unsecured demand promissory note, we recognized the instrument as a financial asset initially recorded at fair value and subsequently measured at amortized cost.

Pursuant to the Initial Order, CRC entered into an agreement to provide a super-priority, debtor-in-possession ("DIP") interim, non-revolving credit facility up to a maximum principal amount of $7.2 million (the "DIP Financing") to enable PharmHouse to continue its day-to-day operations throughout the anticipated Restructuring. The DIP Financing, which is subordinate to PharmHouse's obligations to the Lenders under the PharmHouse Credit Facility, bears interest at a rate of 8% per annum, calculated and compounded monthly and payable on the maturity date, which is the earlier of December 29, 2020, and the date the CCAA Proceedings are terminated. On December 15, 2020, the DIP Financing agreement entered into between CRC and PharmHouse was amended. As a result of this amendment, the maximum principal amount available to be drawn by PharmHouse pursuant to the DIP Financing increased from $7.2 million to $9.7 million, and the maturity date was extended from December 29, 2020 to February 28, 2021. On December 18, 2020, the Court approved the DIP Financing amendment and extended the stay of proceedings in respect of PharmHouse until February 28, 2021, inclusively. As at December 31, 2020, CRC had advanced $8.3 million pursuant to the DIP Financing.

As a result of the PharmHouse Recoverability Assessment described above, we recognized current expected credit losses of $7.5 million and $32.5 million for the three and nine months ended December 31, 2020, respectively, related to the contingent obligation under the PharmHouse Financial Guarantee. We also concluded that the following amounts may not be recoverable: (i) $8.3 million advanced pursuant to DIP Financing, of which $6.2 million was advanced in the three months ended December 31, 2020; (ii) $40.0 million advanced under the shareholder loan agreement; (iii) $2.5 million advanced under the secured demand promissory note; (iv) $1.2 million advanced under the unsecured demand promissory note; and (v) $9.0 million in interest receivable in relation to the aforementioned financial instruments. Additionally, it was determined that certain advances in the amount of $15.0 million provided to PharmHouse by Canopy Growth may not be recoverable. Accordingly, we recorded expected credit losses on financial assets and related charges of $13.7 million and $108.5 million for the three and nine months ended December 31, 2020, respectively (three and nine months ended December 31, 2019 – $nil).

PharmHouse equity method investment

As at December 31, 2020, CRC owned 10,998,660 common shares of PharmHouse (March 31, 2020 – 10,998,660 common shares), representing a 49% equity interest on a non-diluted basis. CRC has not yet received any distributions on account of its common share investment in PharmHouse. As a result of the PharmHouse Recoverability Assessment described above, we determined that there was an other-than-temporary-impairment and recognized an impairment charge for the full amount of its equity method investment of $32.4 million in the second quarter of fiscal 2021.

Refer to “Canopy Rivers Arrangement Agreement” above for a description of the plan of arrangement with Canopy Rivers.

TerrAscend Option Agreement

On January 13, 2021, we entered into an option agreement to acquire 1,072,450 common shares of TerrAscend for US$10.5 million, conditional upon the occurrence or waiver of amendments to federal laws of the United States to permit the general cultivation, distribution and possession of marijuana or to remove the regulation of such activities from the federal laws of the United States.

Part 2 - Results of Operations

Discussion of Third Quarter of Fiscal 2021 Results of Operations

(in thousands of Canadian dollars, except share amounts and where otherwise indicated)	Three months ended December 31, 2020	Three months ended December 31, 2019	Change	% Change
Selected financial information:				
Net revenue	$ 152,528	$ 123,764	$ 28,764	23%
Gross margin percentage	16%	31%	-	(15%)
Net loss	$ (829,251)	$ (109,634)	$ (719,617)	(656%)
Net loss attributable to Canopy Growth Corporation	$ (904,380)	$ (91,354)	$ (813,026)	(890%)
Loss per share - basic and diluted[1]	$ (2.43)	$ (0.26)	$ (2.17)	(835%)

[1]For the three months ended December 31, 2020, the weighted average number of outstanding common shares, basic and diluted, totaled 372,908,767. For the three months ended December 31, 2019, the weighted average number of outstanding common shares, basic and diluted, totaled 348,530,622.

Revenue

Revenue by Channel *(in thousands of Canadian dollars)*	Three months ended December 31, 2020	Three months ended December 31, 2019	$ Change	% Change
Recreational net revenue				
Business-to-business[1]	$ 43,129	$ 42,997	$ 132	-
Business-to-consumer	20,224	15,242	4,982	33%
	63,353	58,239	5,114	9%
Medical net revenue				
Canadian[2]	13,947	13,440	507	4%
International	21,505	18,701	2,804	15%
	35,452	32,141	3,311	10%
Cannabis net revenue	98,805	90,380	8,425	9%
Other revenue	53,723	33,384	20,339	61%
Net revenue	$ 152,528	$ 123,764	$ 28,764	23%

[1] Reflects excise taxes of $15,977 and other revenue adjustments, representing our determination of returns and pricing adjustments, of $3,750 for the three months ended December 31, 2020 (three months ended December 31, 2019 - excise taxes of $10,457 and other revenue adjustments of $5,343).

[2] Reflects excise taxes of $1,402 for the three months ended December 31, 2020 (three months ended December 31, 2019 - $1,325).

Revenue by Form	Three months ended December 31,			
(in thousands of Canadian dollars)	2020	2019	$ Change	% Change
Recreational revenue by form				
Dry bud[1]	$ 66,210	$ 69,283	$ (3,073)	(4%)
Oils and softgels[1]	7,292	4,756	2,536	53%
Cannabis 2.0 products	9,578	-	9,578	-
Other revenue adjustments	(3,750)	(5,343)	1,593	30%
Excise taxes	(15,977)	(10,457)	(5,520)	(53%)
	63,353	58,239	5,114	9%
Medical revenue by form				
Dry bud	9,000	9,243	(243)	(3%)
Oils and softgels	26,951	24,223	2,728	11%
Cannabis 2.0 products	903	-	903	-
Excise taxes	(1,402)	(1,325)	(77)	(6%)
	35,452	32,141	3,311	10%
Cannabis net revenue	98,805	90,380	8,425	9%
Other revenue	53,723	33,384	20,339	61%
Net revenue	$ 152,528	$ 123,764	$ 28,764	23%

[1] Excludes the impact of other revenue adjustments.

Net revenue in the third quarter of fiscal 2021 was $152.5 million, as compared to $123.8 million in the third quarter of fiscal 2020. The year-over-year increase is primarily attributable to growth in other revenue, the Canadian recreational business-to-consumer channel, and revenue from C^3.

Recreational

Canadian recreational net revenue in the third quarter of fiscal 2021 was $63.4 million, as compared to $58.2 million in the third quarter of fiscal 2020.

Net revenue from the business-to-business channel in the third quarter of fiscal 2021 was $43.1 million, consistent with the $43.0 million generated in the third quarter of fiscal 2020. Our business-to-business gross revenue improved year-over-year due primarily to (i) the overall increase in demand resulting from the opening of 305 new retail stores across Canada in the third quarter of fiscal 2021 (nearly 170 of which were in Ontario); and (ii) the introduction of our Cannabis 2.0 products. However, these improvements were partially offset by an unfavorable product mix due primarily to an increase in the volume of value-priced dried flower product sold compared to the prior year.

Revenue from the business-to-consumer channel in the third quarter of fiscal 2021 was $20.2 million, as compared to $15.2 million in the third quarter of fiscal 2020. The year-over-year increase is primarily attributable to (i) the benefit of holiday promotional campaigns held in the third quarter of fiscal 2021, and the continuing broadening of our brand and product offerings at our retail locations, including the introduction of new value-priced dried flower products, vapes, and cannabis-infused beverages; and (ii) the build-out of our retail store platform across Canada. At December 31, 2020, we operated 33 corporate-owned Tweed and Tokyo Smoke retail stores, an increase from 22 stores at December 31, 2019.

Medical

Medical cannabis net revenue in the third quarter of fiscal 2021 was $35.5 million, as compared to $32.1 million in the third quarter of fiscal 2020. Canadian medical net revenue in the third quarter of fiscal 2021 was $13.9 million, as compared to $13.4 million in the third quarter of fiscal 2020. The year-over-year increase is due primarily to the continued broadening of our brand and medical cannabis product offerings available on the Spectrum Therapeutics online store in response to customer demand, including the introduction of pre-rolled joints, vapes and cannabis-infused chocolates, and holiday promotions.

International medical revenue in the third quarter of fiscal 2021 was $21.5 million, as compared to $18.7 million in the third quarter of fiscal 2020. C^3 contributed revenue of $17.6 million in the third quarter of fiscal 2021, a year-over-year increase of $2.9 million due primarily to growth in our customer base relative to the prior year. Our German medical business contributed revenue of $3.9 million in the third quarter of fiscal 2021, consistent with the comparative period.

Other

Other revenue is comprised of revenue related to (i) vaporizers sold by Storz & Bickel; (ii) beauty, skincare, wellness and sleep products, some of which have been blended with hemp-derived CBD isolate, sold by This Works; (iii) sports nutrition beverages, mixes, protein, gum and mints, some of which have been infused with hemp-derived CBD isolate, sold by BioSteel; (iv) our United States CBD business; and (v) other strategic revenue sources such as our clinic partners.

Other revenue in the third quarter of fiscal 2021 was $53.7 million, as compared to $33.4 million in the third quarter of fiscal 2020. The year-over-year increase of $20.3 million is primarily due to the continued strong performance by Storz & Bickel, revenue improvement at BioSteel, growth in our United States CBD business, and revenue growth at This Works.

Revenue from Storz & Bickel was $24.1 million in the third quarter of fiscal 2021, a year-over-year increase of $8.3 million due primarily to the expansion of our distribution network in the United States. Additionally, This Works contributed revenue totaling $10.9 million in the third quarter of fiscal 2021, a year-over-year increase of $2.6 million due primarily to the expansion of distribution to both direct-to-consumer and third-party e-commerce channels, and new product launches.

Cost of Goods Sold and Gross Margin

(in thousands of Canadian dollars except where indicated)	Three months ended December 31, 2020	Three months ended December 31, 2019	$ Change	% Change
Net revenue	$ 152,528	$ 123,764	$ 28,764	23%
Cost of goods sold	$ 127,943	$ 85,556	$ 42,387	50%
Gross margin	24,585	38,208	(13,623)	(36%)
Gross margin percentage	16%	31%	-	(15%)

Cost of goods sold in the third quarter of fiscal 2021 was $127.9 million, as compared to $85.6 million in the third quarter of fiscal 2020. Our gross margin in the third quarter of fiscal 2021 was $24.6 million, or 16% of net revenue, as compared to a gross margin of $38.2 million and gross margin percentage of 31% of net revenue in the third quarter of fiscal 2020. The year-over-year decrease in the gross margin percentage was primarily attributable to:

- Restructuring charges totaling $15.6 million recorded in the third quarter of fiscal 2021, relating primarily to the closure of several of our production facilities in Canada as described above in “Recent Developments”.
- Operating costs relating to facilities not yet cultivating or producing cannabis, not yet producing cannabis-related products or having under-utilized capacity. In the third quarter of fiscal 2021, these costs amounted to $13.9 million and primarily related to start-up costs associated with our gummy production facility in Smiths Falls and our facilities in the United States, and under-utilized capacity associated with our indoor facility in Newfoundland prior to its closure in early December, as discussed in “Recent Developments” above. Comparatively, our gross margin percentage in the third quarter of fiscal 2020 was impacted by operating costs of $8.1 million relating to facilities not yet cultivating or processing cannabis, not yet producing cannabis-related products or having under-utilized capacity, primarily related to start-up costs associated with our advanced manufacturing and beverage facilities in Smiths Falls, our greenhouse in Denmark, and under-utilized capacity associated with our KeyLeaf extraction facility in Saskatchewan.

Operating Expenses

(in thousands of Canadian dollars)	Three months ended December 31, 2020	2019	$ Change	% Change
Operating expenses				
General and administrative	$ 52,125	$ 67,812	$ (15,687)	(23%)
Sales and marketing	53,682	63,382	(9,700)	(15%)
Research and development	13,957	20,808	(6,851)	(33%)
Acquisition-related costs	3,095	3,256	(161)	(5%)
Depreciation and amortization	21,219	13,652	7,567	55%
Selling, general and administrative expenses	144,078	168,910	(24,832)	(15%)
Share-based compensation	18,315	56,763	(38,448)	(68%)
Share-based compensation related to acquisition milestones	1,648	4,916	(3,268)	(66%)
Share-based compensation expense	19,963	61,679	(41,716)	(68%)
Expected credit losses on financial assets and related charges	13,735	-	13,735	-
Asset impairment and restructuring costs	400,422	-	400,422	-
Total operating expenses	$ 578,198	$ 230,589	$ 347,609	151%

Selling, general and administrative expenses

Selling, general and administrative expenses in the third quarter of fiscal 2021 were $144.1 million, as compared to $168.9 million in the third quarter of fiscal 2020.

General and administrative expense in the third quarter of fiscal 2021 was $52.1 million, as compared to $67.8 million in the third quarter of fiscal 2020. The year-over-year decrease is due primarily to a reduction in costs attributable to the restructuring actions initiated in the fourth quarter of fiscal 2020, resulting from an organizational and strategic review of our business. Accordingly, as we exited non-strategic geographies and began streamlining our operations, we realized reductions related to (i) compensation costs for finance, information technology, legal and other administrative functions; (ii) facilities and insurance costs; (iii) scaling-back on our expansion and business development initiatives; and (iv) other professional consulting fees.

Sales and marketing expense in the third quarter of fiscal 2021 was $53.7 million, as compared to $63.4 million in the third quarter of fiscal 2020. In the comparative prior period we incurred costs attributable to product marketing and brand awareness advertising and media campaigns largely in support of the launch and penetration of our Cannabis 2.0 portfolio of products in Canada. These costs did not recur to the same extent in the third quarter of fiscal 2021. This decrease was partially offset by (i) an increase in sponsorship fees relating to BioSteel's partnerships deals with the Toronto Raptors and Dallas Mavericks, and promotional and sales and marketing staff compensation costs supporting BioSteel's launch of ready-to-drink beverages across the United States through their distribution network; and (ii) increased brand and advertisement agency spending in support of our United States CBD business.

Research and development expense in the third quarter of fiscal 2021 was $14.0 million, as compared to $20.8 million in the third quarter of fiscal 2020. The year-over-year decrease is primarily attributable to a reduction in costs due to the restructuring actions initiated in the fourth quarter of fiscal 2020 and continuing throughout fiscal 2021. As we rationalized our research and development activities, we realized reductions in compensation costs and curtailed certain research and development projects for which we had incurred costs in the third quarter of fiscal 2020.

Acquisition-related costs in the third quarter of fiscal 2021 were $3.1 million, relatively consistent with $3.3 million in the third quarter of fiscal 2020. In the third quarter of fiscal 2021, costs were incurred in relation to the Canopy Rivers Arrangement Agreement, as described in "Recent Developments" above, and evaluating other potential acquisition opportunities. Comparatively, in the third quarter of fiscal 2020, we completed the acquisitions of BioSteel and the unowned interest in Beckley Canopy Therapeutics ("BCT"), and the transaction to launch More Life Growth Company ("More Life").

Depreciation and amortization expense in the third quarter of fiscal 2021 was $21.2 million, as compared to $13.7 million in the third quarter of fiscal 2020. The year-over-year increase is primarily attributable to the growth in our network of corporate-owned

Tweed and Tokyo Smoke retail stores, the implementation of information technology software projects, and the growth in our business through acquisitions.

Share-based compensation expense

Share-based compensation expense in the third quarter of fiscal 2021 was $18.3 million, as compared to $56.8 million in the third quarter of fiscal 2020. The year-over-year decrease is primarily attributable to:

- The significant number of stock options that were granted in previous years at relatively higher exercise prices, which impacted share-based compensation expense more significantly in previous periods. We granted 22.1 million stock options in fiscal 2019 at a weighted average price of $51.49 per option, as compared to 9.5 million options in fiscal 2020 at a weighted average price of $33.87. The decrease in the number of stock option grants from fiscal 2019 to fiscal 2020 was due to the modification of our share-based compensation program in fiscal 2020; only 433,199 options were granted in the nine months ended December 31, 2020, as compared to 8.3 million in the comparative period; and
- The forfeiture or cancellation of 5.9 million stock options in fiscal 2020 and the forfeiture of another 7.3 million stock options in the nine months ended December 31, 2020 resulting primarily from restructuring actions commenced in the fourth quarter of fiscal 2020. These forfeitures and cancellations also contributed to a year-over-year reduction in share-based compensation expense.

As a result of the changes described above to our share-based compensation program leading to a reduction in the number of stock option grants, stock option exercises and the forfeiture of stock options in recent quarters, 22.5 million stock options were outstanding at December 31, 2020, as compared to 33.6 million at December 31, 2019.

Share-based compensation expense related to acquisition milestones in the third quarter of fiscal 2021 was $1.6 million, as compared to $4.9 million in the third quarter of fiscal 2020. The year-over-year decrease is primarily related to the restructuring of our operations in Colombia in the fourth quarter of fiscal 2020, which resulted in the acceleration of share-based compensation expense related to the unvested milestones associated with the acquisitions of Spectrum Colombia S.A.S. (“Spectrum Colombia”) and Canindica Capital Ltd. (“Canindica”). As a result, there is no remaining share-based compensation expense to be recognized in association with the Spectrum Colombia acquisition, and only a minimal amount of remaining share-based compensation expense to be recognized in association with the Canindica acquisition.

Expected credit losses on financial assets and related charges

In the third quarter of fiscal 2021, we recorded expected credit losses on financial assets and related charges in the amount of $13.7 million, in relation to our equity investment in PharmHouse, as discussed in “Recent Developments” above.

Asset impairment and restructuring costs

Asset impairment and restructuring costs recorded in operating expenses in the third quarter of fiscal 2021 were $400.4 million.

Due to the restructuring actions resulting in the closure of certain of our sites in Canada in the third quarter of fiscal 2021 as described in “Recent Developments” above, we abandoned or impaired certain of our production facilities and intangible assets. A loss totaling $352.6 million was recognized in the third quarter of fiscal 2021 representing the difference between the net book value of the long-lived assets and their estimated salvage value or fair value. Of this loss, $298.2 million related to property, plant and equipment and $54.4 million related to facility licenses and other intangible assets. The losses related to property, plant and equipment were primarily attributable to buildings and greenhouses, production and warehouse equipment, and right-of-use assets. Additionally, we recognized contractual and other settlement obligations of $13.1 million and employee-related and other restructuring costs of $1.9 million.

Additionally, as a result of the sale of our production facilities in Aldergrove and Delta, British Columbia in December 2020 and January 2021, respectively, and the completion of our strategy shift in Latin America that we commenced in the fourth quarter of fiscal 2020, we recognized a loss totaling $28.4 million in the third quarter of fiscal 2021 representing the difference between the net book value of the long-lived assets and their selling prices. Additionally, we recognized costs totaling $4.4 million related to contractual and other settlement obligations, employee-related costs, and other restructuring costs associated with the remediation of damages caused by the fire at the Delta facility in November, the closure of the facilities in British Columbia, and their sale.

Other

(in thousands of Canadian dollars)	Three months ended December 31, 2020	2019	$ Change	% Change
Loss from equity method investments	$ (671)	$ (2,664)	$ 1,993	75%
Other income (expense), net	(290,567)	57,963	(348,530)	(601%)
Income tax recovery	15,600	27,448	(11,848)	(43%)

Loss from equity method investments

The loss from equity method investments in the third quarter of fiscal 2021 was $0.7 million, as compared to $2.7 million in the third quarter of fiscal 2020. The year-over-year decrease in the loss is primarily attributable to (i) the impairment of our equity investment in PharmHouse in the second quarter of fiscal 2021, as no further equity method losses were recognized in respect of this equity investment in the third quarter of fiscal 2021; and (ii) improved performance by CanapaR prior to its sale by Canopy Rivers in late December 2020.

Other income (expense), net

Other income (expense), net in the third quarter of fiscal 2021 was an expense amount of $290.6 million, as compared to an income amount of $58.0 million in the third quarter of fiscal 2020. The year-over-year change of $348.5 million from an income amount to an expense amount is primarily attributable to:

- Change of $276.5 million related to fair value changes on the warrant derivative liability associated with the Tranche B Warrants held by CBI, from an income amount of $82.5 million in the third quarter of fiscal 2020 to an expense amount of $194.0 million in the third quarter of fiscal 2021. The increase of $194.0 million in the fair value of the warrant derivative liability (resulting in non-cash expense) in the third quarter of fiscal 2021 is primarily attributable to an increase of approximately 64% in our share price from October 1, 2020 to December 31, 2020, partially offset by changes during the quarter in certain other assumptions used to value the liability, including the risk-free interest rate. Comparatively, the decrease of $82.5 million in the fair value of the warrant derivative liability in the third quarter of fiscal 2020 was attributable to a decline of approximately 5% in our share price from October 1, 2019 to December 31, 2019.
- Increase in non-cash expense of $273.0 million related to the fair value changes on the liability arising from the Acreage Arrangement, from $30.0 million in the third quarter of fiscal 2020 to $303.0 million in the third quarter of fiscal 2021. On a quarterly basis, we determine the fair value of the liability arising from the Acreage Arrangement using a probability-weighted expected return model, incorporating several potential scenarios and outcomes associated with the Acreage Arrangement. The current quarter expense amount, associated with an increase in the liability arising from the Acreage Arrangement, is primarily attributable to an increase of approximately 64% in our share price from October 1, 2020 to December 31, 2020, relative to an increase of approximately 2% in Acreage's share price during that same period. As a result, the model in the third quarter of fiscal 2021 reflects a higher estimated value of the Canopy Growth shares expected to be issued at the exchange ratio of 0.3048 upon a Triggering Event, relative to the estimated value of the Acreage shares expected to be acquired at that time. Comparatively, the expense amount of $30.0 million in the third quarter of fiscal 2020 was primarily attributable to overall declines, in that quarter, in both Canopy Growth's and Acreage's share prices.
- Change of $82.2 million related to the non-cash fair value changes on our senior convertible notes, from an income amount of $6.7 million in the third quarter of fiscal 2020 to an expense amount of $75.5 million in the third quarter of fiscal 2021. The year-over-year change is primarily due to the increase of approximately 64% in our share price from October 1, 2020 to December 31, 2020, as compared to a decline of approximately 5% in our share price in the third quarter of fiscal 2020.
- In the third quarter of fiscal 2020, we recognized gains of $61.8 million in relation to (i) our acquisition of the unowned interest in BCT, which increased our total ownership to 100% of BCT's issued and outstanding shares ($39.5 million); and (ii) our disposal of a previously-consolidated subsidiary in conjunction with the transaction completed to launch More Life ($22.3 million). No such transactions resulting in gains occurred in the third quarter of fiscal 2021.
- Change of $358.7 million related to non-cash fair value changes on our other financial assets, from an expense amount of $77.3 million in the third quarter of fiscal 2020 to an income amount of $281.4 million in the third quarter of fiscal 2021. The current quarter income amount is primarily attributable to fair value increases relating to our investments in the TerrAscend exchangeable shares ($210.0 million), and the TerrAscend Canada secured debenture and TerrAscend warrants (totaling $86.4 million), driven largely by an increase of approximately 120% in TerrAscend's share price from October 1 to December 31, 2020 and a re-assessment of the probability and timing of changes in federal laws in the United States regarding the permissibility of the cultivation, distribution or possession of marijuana. Partially offsetting these year-over-year fair value increases was a fair value decrease of $15.0 million representing the difference between the loan advanced to a wholly-owned subsidiary of Acreage ("Acreage Hempco") and the debenture's estimated fair value measured using a discounted cash flow model. Comparatively, in the third quarter of fiscal 2020 the expense amount was primarily driven by a decrease of $42.0

million in the fair value of our exchangeable shares in TerrAscend, primarily attributable to a decline in TerrAscend's share price during the quarter, and fair value decreases for several of our other investments which were in-line with the broader decline in the Canadian cannabis market at that time.

Income tax recovery

Income tax recovery in the third quarter of fiscal 2021 was $15.6 million, compared to income tax recovery of $27.4 million in the third quarter of fiscal 2020. In the third quarter of fiscal 2021, the income tax recovery consisted of a deferred income tax recovery of $16.6 million (compared to a recovery of $33.9 million in the third quarter of fiscal 2020) and current income tax expense of $1.0 million (compared to an expense of $6.5 million in the third quarter of fiscal 2020).

The decrease of $17.3 million in the deferred income tax recovery is primarily a result of (i) recording a reduction in deferred tax liabilities that arose in connection with the required revaluation of the accounting carrying value, but not the tax basis, of property, plant and equipment, intangible assets, and other financial assets; and (ii) the recognition of losses carried forward net of the use of losses carried forward from prior years for which a deferred tax asset had been recorded. In connection with certain deferred tax assets, mainly in respect of losses for tax purposes, where the accounting criteria for recognition of an asset has yet to be satisfied and it is not probable that they will be used, the deferred tax asset has not been recognized.

The decrease of $5.5 million in the current income tax expense arose primarily in connection with acquired legal entities that generated income for tax purposes during prior periods that could not be reduced by the group's tax attributes but whose current period income will now be reduced by the group's tax attributes.

Net Loss

The net loss in the third quarter of fiscal 2021 was $829.3 million, as compared to a net loss of $109.6 million in the third quarter of fiscal 2020. The year-over-year increase in the net loss is primarily attributable to the year-over-year change in other income (expense), net, the asset impairment and restructuring costs recognized in the third quarter of fiscal 2021, and the other variances described above.

Segmented Analysis

In the third quarters of fiscal 2021 and fiscal 2020, all of our revenue was earned by the Cannabis, Hemp and Other Consumer Products segment. Canopy Rivers contributed net income of $101.7 million in the third quarter of fiscal 2021, of which $27.5 million was attributable to Canopy Growth. In the third quarter of fiscal 2020, Canopy Rivers contributed a net loss of $5.1 million, of which $1.4 million was attributable to Canopy Growth. The change from a net loss to net income is primarily attributable to fair value increases relating to Canopy Rivers' investments in the TerrAscend exchangeable shares, for the reasons noted above. Refer to "Recent Developments" above for a description of the Canopy Rivers Arrangement Agreement.

Adjusted EBITDA (Non-GAAP Measure)

Our "Adjusted EBITDA" is a non-GAAP measure used by management that is not defined by U.S. GAAP and may not be comparable to similar measures presented by other companies. Management calculates Adjusted EBITDA as the reported net loss, adjusted to exclude income tax recovery (expense); other income (expense), net; loss on equity method investments; share-based compensation expense; depreciation and amortization expense; asset impairment and restructuring costs; expected credit losses on financial assets and related charges; restructuring costs recorded in cost of goods sold; and charges related to the flow-through of inventory step-up on business combinations, and further adjusted to remove acquisition-related costs. Accordingly, management believes that Adjusted EBITDA provides meaningful and useful financial information as this measure demonstrates the operating performance of businesses.

The following table presents Adjusted EBITDA for the three months ended December 31, 2020 and 2019:

	Three months ended December 31,			
(in thousands of Canadian dollars)	2020	2019	$ Change	% Change
Net loss	$ (829,251)	$ (109,634)	$ (719,617)	656%
Income tax recovery	(15,600)	(27,448)	11,848	43%
Other (income) expense, net	290,567	(57,963)	348,530	601%
Loss on equity method investments	671	2,664	(1,993)	(75%)
Share-based compensation[1]	19,963	61,679	(41,716)	(68%)
Acquisition-related costs	3,095	3,256	(161)	(5%)
Depreciation and amortization[1]	32,385	30,464	1,921	6%
Asset impairment and restructuring costs	400,422	-	400,422	-
Expected credit losses on financial assets and related charges	13,735	-	13,735	-
Restructuring costs recorded in cost of goods sold	15,637	-	15,637	-
Adjusted EBITDA[2]	$ (68,376)	$ (96,982)	$ 28,606	29%

[1] From Condensed Interim Consolidated Statements of Cash Flows.

[2]Adjusted EBITDA is a non-GAAP measure and is calculated as the reported net loss, adjusted to exclude income tax (expense) recovery; other income (expense), net; loss on equity method investments; share-based compensation expense; depreciation and amortization expense; asset impairment and restructuring costs; expected credit losses on financial assets and related charges; restructuring costs recorded in cost of goods sold; and charges related to the flow-through of inventory step-up on business combinations, and further adjusted to remove acquisition-related costs.

The Adjusted EBITDA loss in the third quarter of fiscal 2021 was $68.4 million, as compared to the Adjusted EBITDA loss of $97.0 million in the third quarter of fiscal 2020. The year-over-year decrease in the Adjusted EBITDA loss is primarily attributable to the year-over-year reduction in our selling, general and administrative expense, as discussed above.

Discussion of Results of Operations for the Nine Months Ended December 31, 2020

(in thousands of Canadian dollars, except share amounts and where otherwise indicated)	Nine months ended December 31, 2020	2019	Change	% Change
Selected financial information:				
Net revenue	$ 398,210	$ 290,859	$ 107,351	37%
Gross margin percentage	14%	21%	-	(7%)
Net loss	$ (1,054,125)	$ (61,035)	$ (993,090)	(1627%)
Net loss attributable to Canopy Growth Corporation	$ (1,044,942)	$ (18,305)	$ (1,026,637)	(5609%)
Loss per share - basic and diluted[1]	$ (2.83)	$ (0.05)	$ (2.78)	(5560%)

[1]For the nine months ended December 31, 2020, the weighted average number of outstanding common shares, basic and diluted, totaled 369,418,037. For the nine months ended December 31, 2019, the weighted average number of outstanding common shares, basic and diluted, totaled 346,877,660.

Revenue

Revenue by Channel *(in thousands of Canadian dollars)*	Nine months ended December 31, 2020	2019	$ Change	% Change
Recreational net revenue				
Business-to-business[1]	$ 120,286	$ 90,732	$ 29,554	33%
Business-to-consumer	48,263	38,980	9,283	24%
	168,549	129,712	38,837	30%
Medical net revenue				
Canadian[2]	41,745	38,090	3,655	10%
International	59,170	47,287	11,883	25%
	100,915	85,377	15,538	18%
Cannabis net revenue	269,464	215,089	54,375	25%
Other revenue	128,746	75,770	52,976	70%
Net revenue	$ 398,210	$ 290,859	$ 107,351	37%

[1] Reflects excise taxes of $37,423 and other revenue adjustments, representing our determination of returns and pricing adjustments, of $10,900 for the nine months ended December 31, 2020 (nine months ended December 31, 2019 - excise taxes of $29,824 and other revenue adjustments of $46,070).

[2] Reflects excise taxes of $4,190 for the nine months ended December 31, 2020 (nine months ended December 31, 2019 - $3,875).

Revenue by Form	Nine months ended December 31,			
(in thousands of Canadian dollars)	2020	2019	$ Change	% Change
Recreational revenue by form				
Dry bud[1]	$ 170,234	$ 189,177	$ (18,943)	(10%)
Oils and softgels[1]	22,034	16,429	5,605	34%
Cannabis 2.0 products	24,604	-	24,604	-
Other revenue adjustments	(10,900)	(46,070)	35,170	76%
Excise taxes	(37,423)	(29,824)	(7,599)	(25%)
	168,549	129,712	38,837	30%
Medical revenue by form				
Dry bud	28,147	26,029	2,118	8%
Oils and softgels	75,012	63,223	11,789	19%
Cannabis 2.0 products	1,946	-	1,946	-
Excise taxes	(4,190)	(3,875)	(315)	(8%)
	100,915	85,377	15,538	18%
Cannabis net revenue	269,464	215,089	54,375	25%
Other revenue	128,746	75,770	52,976	70%
Net revenue	$ 398,210	$ 290,859	$ 107,351	37%

[1] Excludes the impact of other revenue adjustments.

Net revenue in the nine months ended December 31, 2020 was $398.2 million, as compared to $290.9 million in the nine months ended December 31, 2019. The year-over-year increase is primarily attributable to growth in other revenue, growth across both the Canadian recreational business-to-business and business-to-consumer channels, and growth in C^3 revenue due both to strong performance and a full nine months of revenue contribution.

Recreational

Canadian recreational net revenue in the nine months ended December 31, 2020 was $168.5 million, as compared to $129.7 million in the nine months ended December 31, 2019.

Net revenue from the business-to-business channel in the nine months ended December 31, 2020 was $120.3 million, as compared to $90.7 million in the nine months ended December 31, 2019. Net revenue in the nine months ended December 31, 2019 was impacted by other revenue adjustments in the amount of $46.7 million related to our determination, primarily in the first two quarters of fiscal 2020, of returns and pricing adjustments associated primarily to the risk of over-supply of certain oil and softgel products. We also benefited in the current period from (i) an overall increase in demand resulting from the opening of over 620 new retail stores across Canada in the nine months ended December 31, 2020; and (ii) the introduction of our portfolio of Cannabis 2.0 product offerings. These favorable year-over-year variances were partially offset by lower sales of our dry bud products. We took steps to reposition our product offerings in the value-priced dried flower category in the first quarter of fiscal 2021, the effect of which began contributing to year-over-year improvement in our sales in this category in the second quarter of fiscal 2021. However, increased competition in that particular category of the recreational market – in the form of the number of competitive offerings, particularly those with higher THC potency, and aggressive pricing strategies adopted by some market participants – impacted sales of our dry bud products in the first quarter of fiscal 2021. Additionally, we were impacted by an unfavorable product mix due primarily to an increase in the volume of value-priced dried flower product sold compared to the prior year.

Revenue from the business-to-consumer channel in the nine months ended December 31, 2020 was $48.3 million, as compared to $39.0 million in the nine months ended December 31, 2019. The year-over-year increase is primarily attributable to (i) increased traffic and ticket size at our retail stores, due largely to the broadening of our brand and product offerings at our retail locations, including the introduction of new value-priced dried flower products, vapes, and cannabis-infused beverages; and (ii) the build-out of our retail store platform across Canada to 33 corporate-owned Tweed and Tokyo Smoke retail stores at December 31, 2020, an increase from 22 stores at December 31, 2019. Partially offsetting this increase was the adverse impact, predominantly in the first quarter of fiscal 2021, of the temporary closure of our retail stores in response to the COVID-19 pandemic and their re-opening, beginning in mid-April, with reduced hours and under a “click-and-collect” model with curbside pickup or delivery.

Medical

Medical cannabis net revenue in the nine months ended December 31, 2020 was $100.9 million, as compared to $85.4 million in the nine months ended December 31, 2019. Canadian medical net revenue in the nine months ended December 31, 2020 was $41.7 million, as compared to $38.1 million in the nine months ended December 31, 2019. The year-over-year increase is due primarily to (i) the continued broadening of our brand and medical cannabis product offerings available on the Spectrum Therapeutics online store in response to medical customer demand, including the introduction pre-rolled joints, vapes and cannabis-infused chocolates; and (ii) the convenience of our trusted medical cannabis e-commerce channel, which has been benefitting from the slower-than-expected opening of recreational retail stores in Ontario in fiscal 2021.

International medical revenue in the nine months ended December 31, 2020 was $59.2 million, as compared to $47.3 million in the nine months ended December 31, 2019. C^3 (acquired in April 2019) contributed revenue totaling $46.6 million in the current period, a year-over-year increase of $9.0 million. In addition to the full nine months of revenue contribution in the current period, revenue growth was driven by an expansion of C^3's customer base relative to the prior year. Our German medical business contributed revenue of $12.6 million, resulting in year-over-year growth of $2.9 million primarily attributable to the resolution of supply constraints we had experienced early in the prior fiscal year, and which were largely associated with the opening of the recreational cannabis market in Canada.

Other

Other revenue in the nine months ended December 31, 2020 was $128.7 million, as compared to $75.8 million in the nine months ended December 31, 2019. The year-over-year increase of $53.0 million is primarily due to an increase in revenue from Storz & Bickel, a full nine months of revenue contribution from both This Works (acquired in May 2019) and BioSteel (acquired in October 2019), and the growth in our United States CBD business.

Revenue from Storz & Bickel was $63.1 million in the nine months ended December 31, 2020, a year-over-year increase of $26.6 million due primarily to an expansion of our distribution network in the United States. Additionally, This Works contributed a full period of revenue totaling $24.8 million in the nine months ended December 31, 2020, a year-over-year increase of $8.4 million due primarily to one incremental month of contribution in the nine months ended December 31, 2020, the expansion of distribution to both direct-to-consumer and third-party e-commerce channels, and new product launches. These factors were only partially offset by the impact of the temporary closure of brick-and-mortar retail stores and measures in relation to the COVID-19 pandemic, largely in the first quarter and late in the third quarter of fiscal 2021.

Cost of Goods Sold and Gross Margin

	Nine months ended December 31,			
(in thousands of Canadian dollars except where indicated)	2020	2019	$ Change	% Change
Net revenue	$ 398,210	$ 290,859	$ 107,351	37%
Cost of goods sold	$ 341,050	$ 230,718	$ 110,332	48%
Gross margin	57,160	60,141	(2,981)	(5%)
Gross margin percentage	14%	21%	-	(7%)

Cost of goods sold in the nine months ended December 31, 2020 was $341.1 million, as compared to $230.7 million in the nine months ended December 31, 2019. Our gross margin in the nine months ended December 31, 2020 was $57.2 million, or 14% of net revenue, as compared to a gross margin of $60.1 million and gross margin percentage of 21% of net revenue in the nine months ended December 31, 2019. The year-over-year decrease in the gross margin percentage was primarily attributable to:

- Restructuring charges totaling $15.6 million recorded in the third quarter of fiscal 2021, relating primarily to the closure of several of our production facilities in Canada as described above in “Recent Developments”.
- The impact of operating costs relating to facilities not yet cultivating or producing cannabis, not yet producing cannabis-related products or having under-utilized capacity. In the nine months ended December 31, 2020, these costs amounted to $50.8 million and primarily related to (i) start-up costs associated with our gummy production facility in Smiths Falls, our facilities in the United States, and our greenhouse in Denmark; and (ii) under-utilized capacity associated with our chocolate, beverage and vape production facilities in Smiths Falls, and our indoor facility in Newfoundland prior to its closure in early December, as discussed in “Recent Developments” above; and
- Lower production output, particularly in the first quarter of fiscal 2021 in Canada, to align with market demand at that time and expected market demand. Lower production output, coupled with (i) our fixed costs representing a high proportion of our overall cultivation and manufacturing cost structure; and (ii) the gradual reduction of our variable costs late in the first quarter

of fiscal 2021, resulted in the under-absorption of these fixed and variable costs and an adverse impact on gross margin in the current period. In connection with these changes to our production strategy we also adjusted our cannabis production profile to focus on higher-potency strains which are more in-demand, resulting in additional inventory charges in the first quarter of fiscal 2021.

Comparatively, our gross margin percentage in the nine months ended December 31, 2019 was impacted by (i) charges of $19.8 million for excess finished recreational cannabis inventory recorded primarily in connection with our evaluation of the estimated on-hand provincial and territorial inventory levels at that time; (ii) the impact on gross margin of $9.2 million reflecting the returns and pricing adjustments relating primarily to the over-supply of certain oil and softgel products; and (iii) other adjustments related to the net realizable value of inventory. Additionally, we incurred operating costs of $34.9 million relating to facilities not yet cultivating or processing cannabis, not yet producing cannabis-related products or having under-utilized capacity, primarily related to start-up costs associated with our advanced manufacturing and beverage facilities in Smiths Falls, our greenhouse in Denmark, and under-utilized capacity associated with our KeyLeaf extraction facility.

Operating Expenses

	Nine months ended December 31,			
(in thousands of Canadian dollars)	2020	2019	$ Change	% Change
Operating expenses				
General and administrative	$ 186,507	$ 225,328	$ (38,821)	(17%)
Sales and marketing	134,824	176,018	(41,194)	(23%)
Research and development	41,782	41,233	549	1%
Acquisition-related costs	7,961	19,000	(11,039)	(58%)
Depreciation and amortization	55,649	34,579	21,070	61%
Selling, general and administrative expenses	426,723	496,158	(69,435)	(14%)
Share-based compensation	66,775	217,611	(150,836)	(69%)
Share-based compensation related to acquisition milestones	5,857	24,311	(18,454)	(76%)
Share-based compensation expense	72,632	241,922	(169,290)	(70%)
Expected credit losses on financial assets and related charges	108,480	-	108,480	-
Asset impairment and restructuring costs	459,579	-	459,579	-
Total operating expenses	$ 1,067,414	$ 738,080	$ 329,334	45%

Selling, general and administrative expenses

Selling, general and administrative expenses in the nine months ended December 31, 2020 were $426.7 million, as compared to $496.2 million in the nine months ended December 31, 2019.

General and administrative expense in the nine months ended December 31, 2020 was $186.5 million, as compared to $225.3 million in the nine months ended December 31, 2019. The year-over-year decrease is primarily attributable to:

- A reduction in costs attributable to the restructuring actions initiated in the fourth quarter of fiscal 2020, as described above in our analysis of our results of operations for the third quarter of fiscal 2021. Partially offsetting these cost reductions were a year-over-year increase in third-party professional fees associated with the organizational and strategic review of our business, and the growth in our business through the acquisitions of C^3, This Works and BioSteel in fiscal 2020 that contributed a full nine months to our operating results in fiscal 2021.
- Losses recorded in the second quarter of fiscal 2020 of $10.8 million related to a legal dispute with a third-party supplier, and $8.8 million associated with additional reserves on onerous lease obligations. These losses did not recur in the current period.

Sales and marketing expense in the nine months ended December 31, 2020 was $134.8 million, as compared to $176.0 million in the nine months ended December 31, 2019. In the comparative period we incurred costs attributable to (i) creative design, brand insights and product marketing campaigns in preparation for the launch of our Cannabis 2.0 portfolio of products; (ii) staffing costs associated with servicing our Canadian and United States markets in the areas of creative design and advertising, brand insights and launch support, and brand management; and (iii) media and advertisement placement campaigns to drive brand awareness and educate consumers in support of our recreational brands at the onset of the opening of the Canadian recreational market in October 2018. These costs did not recur to the same extent in the nine months ended December 31, 2020, as we rationalized our Canadian marketing organization in April 2020, delayed or cancelled various product and brand marketing initiatives across our business due to measures established to contain the spread of COVID-19, and incurred significantly reduced travel costs due to travel restrictions. The above factors were partially offset by higher compensation costs related to our marketing and sales capabilities servicing (i) the United States market, where initiatives continue to commercialize and drive brand and product awareness for our United States CBD business; and (ii) the growth in our business as compared to the prior period resulting in a full nine months of contributions to our operating results from the acquisitions of C^3 in April 2019, This Works in May 2019 and BioSteel in October 2019.

Research and development expense in the nine months ended December 31, 2020 was $41.8 million, consistent with $41.2 million in the nine months ended December 31, 2019.

Acquisition-related costs in the nine months ended December 31, 2020 were $8.0 million, as compared to $19.0 million in the nine months ended December 31, 2019. The year-over-year decrease is primarily attributable to more mergers and acquisitions activity in the nine months ended December 31, 2019, which included entering into and implementing the arrangement agreement with Acreage, closing the acquisitions of C^3, This Works, BioSteel and the unowned interest in BCT, and the transaction to launch More Life. Additionally, costs were incurred in relation to evaluating other potential acquisition opportunities. Comparatively, in the nine months ended December 31, 2020, our primary mergers and acquisitions activity related to (i) entering into, and implementing the Acreage Arrangement, and (ii) entering into the Canopy Rivers Arrangement Agreement.

Depreciation and amortization expense in the nine months ended December 31, 2020 was $55.6 million, as compared to $34.6 million in the nine months ended December 31, 2019. The year-over-year increase is primarily attributable to substantial completion of the build-out of our infrastructure across Canada over the past year, the growth in our business over the past year with the acquisitions of C^3, BioSteel and This Works, the growth in our network of corporate-owned Tweed and Tokyo Smoke retail stores, the implementation of information technology software projects, and our investment in our infrastructure in Europe and the United States.

<u>Share-based compensation expense</u>

Share-based compensation expense in the nine months ended December 31, 2020 was $66.8 million, as compared to $217.6 million in the nine months ended December 31, 2019. The year-over-year decrease is primarily attributable to:

- The significant number of stock options that were granted in previous years at relatively higher exercise prices, which impacted share-based compensation expense more significantly in previous periods. We granted 22.1 million stock options in fiscal 2019 at a weighted average price of $51.49 per option, as compared to 9.5 million options in fiscal 2020 at a weighted average price of $33.87. The year-over-year decrease in the number of stock option grants was due to the modification of our share-based compensation program in the first half of fiscal 2020, and only 433,199 options were granted in the nine months ended December 31, 2020; and
- The forfeiture or cancellation of 5.9 million stock options in fiscal 2020 and the forfeiture of another 7.3 million stock options in the nine months ended December 31, 2020 resulting primarily from restructuring actions commenced in the fourth quarter of fiscal 2020. These forfeitures and cancellations also resulted in a year-over-year reduction in share-based compensation expense.

Share-based compensation expense related to acquisition milestones in the nine months ended December 31, 2020 was $5.9 million, as compared to $24.3 million in the nine months ended December 31, 2019. The year-over-year decrease is primarily related to (i) the restructuring of our operations in Colombia in the fourth quarter of fiscal 2020, which resulted in the acceleration of share-based compensation expense related to the unvested milestones associated with the acquisitions of Spectrum Colombia and Canindica (as a result, there is no remaining share-based compensation expense to be recognized in association with the Spectrum Colombia acquisition and only a minimal amount was recognized in connection with the Canindica acquisition in the current period); and (ii) the achievement, in earlier quarters, of major milestones associated with the acquisitions of Spectrum Colombia, Canindica, and Spectrum Denmark, which had resulted in the recognition of share-based compensation expense at that time.

<u>Expected credit losses on financial assets and related charges</u>

In the nine months ended December 31, 2020, we recorded expected credit losses on financial assets and related charges in the amount of $108.5 million, in relation to our equity investment in PharmHouse, as discussed in "Recent Developments" above.

<u>Asset impairment and restructuring costs</u>

Asset impairment and restructuring costs recorded in operating expenses in the nine months ended December 31, 2020 were $459.6 million.

In the first quarter of fiscal 2021, we completed certain of the restructuring actions that had commenced in the fourth quarter of fiscal 2020, including completing the exit of our operations in South Africa and Lesotho, and recorded final adjustments related to changes in certain estimates recorded at March 31, 2020. In addition, we incurred additional costs in the first quarter of fiscal 2021 related primarily to the rationalization of our marketing organization in April 2020.

In the second quarter of fiscal 2021, we recorded (i) adjustments related to changes in the estimated fair value of certain of our Canadian production facilities from March 31, 2020; and (ii) charges related to rationalizing certain research and development activities.

In the third quarter of fiscal 2021, we recorded charges related primarily to (i) the restructuring actions resulting in the closure of certain of our sites in Canada, with losses recognized for the difference between the net book value of the associated property, plant and equipment and intangible assets and their estimated salvage value or fair value, contractual and other settlement obligations; and employee-related and other restructuring costs; (ii) adjustments to the net book value of our production facilities in Aldergrove and Delta, British Columbia in order to reflect their selling prices, and other costs associated with the remediation of damages caused by the fire at the Delta facility in November, the closure of the facilities in British Columbia, and their sale; and (iii) the completion of our strategy shift in Latin America that we commenced in the fourth quarter of fiscal 2020. The restructuring actions in the third quarter of fiscal 2021 and the sale of our production facilities in British Columbia are described above under "Recent Developments".

Other

	Nine months ended December 31,			
(in thousands of Canadian dollars)	2020	2019	$ Change	% Change
Loss from equity method investments	$ (40,851)	$ (6,668)	$ (34,183)	(513%)
Other income (expense), net	(21,106)	600,624	(621,730)	(104%)
Income tax recovery	18,086	22,948	(4,862)	(21%)

Loss from equity method investments

The loss from equity method investments in the nine months ended December 31, 2020 was $40.9 million, as compared to $6.7 million in the nine months ended December 31, 2019. The year-over-year increase in the loss is primarily attributable to (i) impairment charges of $32.4 million recognized in the second quarter of fiscal 2021 relating to our equity method investment in PharmHouse, as discussed in "Recent Developments" above; and (ii) the larger net losses recognized by our investees PharmHouse (prior to its impairment) and Agripharm in the nine months ended December 31, 2020, relative to the comparative period.

Other income (expense), net

Other income (expense), net in the nine months ended December 31, 2020 was an expense amount of $21.1 million, as compared to an income amount of $600.6 million in the nine months ended December 31, 2019. The year-over-year change of $621.7 million from an income amount to an expense amount is primarily attributable to:

- Change of $842.7 million related to fair value changes on the warrant derivative liability associated with the Tranche B Warrants held by CBI, from an income amount of $749.3 million in the nine months ended December 31, 2019 to an expense amount of $93.5 million in the nine months ended December 31, 2020. The increase of $93.5 million in the fair value of the warrant derivative liability (resulting in non-cash expense) in the nine months ended December 31, 2020 is primarily attributable to an increase of approximately 53% in our share price from April 1, 2020 to December 31, 2020, partially offset by a decrease in the risk-free rate and a shorter expected time to maturity of the warrants. Comparatively, the decrease of $749.3 million in the fair value of the warrant derivative liability during the nine months ended December 31, 2019 was primarily attributable to a decline of approximately 49% in our share price from the time the terms of the Tranche B Warrants were amended in late June 2019 to December 31, 2019.
- Change of $310.3 million related to the non-cash fair value changes on our senior convertible notes, from an income amount of $202.6 million in the nine months ended December 31, 2019 to an expense amount of $107.8 million in the nine months ended December 31, 2020. The year-over-year change is primarily due to the increase of approximately 53% in our share price from April 1, 2020 to December 31, 2020, as compared to a decline in our share price of approximately 57% in the nine months ended December 31, 2019.
- In the nine months ended December 31, 2019, we recognized gains of $61.8 million in relation to (i) our acquisition of the unowned interest in BCT, which increased our total ownership to 100% of BCT's issued and outstanding shares ($39.5 million); and (ii) our disposal of a previously-consolidated subsidiary in conjunction with the transaction completed to launch More Life ($22.3 million). No such transactions resulting in gains occurred in the nine months ended December 31, 2020.

- A decrease in interest income of $32.5 million, primarily attributable to the year-over-year decrease in our cash and cash equivalents and short-term investments balances and lower interest rates relative to the prior year.
- Change of $573.3 million related to non-cash fair value changes on our other financial assets, from an expense amount of $188.1 million in the nine months ended December 31, 2019 to an income amount of $385.2 million in the nine months ended December 31, 2020. The income amount recognized in the nine months ended December 31, 2020 is primarily attributable to fair value increases relating to our investments in the TerrAscend exchangeable shares ($277.0 million), and the TerrAscend Canada secured debenture and the TerrAscend warrants (totaling $163.5 million), driven largely by an increase of approximately 410% in TerrAscend's share price from April 1, 2020 to December 31, 2020. Comparatively, in the nine months ended December 31, 2019, the expense amount was primarily driven by decreases of $102.0 million and $35.0 million in the fair value of our exchangeable shares in TerrAscend and warrants in the capital of SLANG Worldwide Inc., respectively, which were attributable primarily to declines in share prices for these two companies during the period. Additionally, the fair values of several of our other investments decreased during the period in-line with the broader decline in the Canadian cannabis market. Partially offsetting these year-over-year fair value increases was a fair value decrease of $38.3 million representing the difference between the loan advanced to Acreage Hempco and the debenture's estimated fair value measured using a discounted cash flow model.
- An increase of $36.7 million in non-cash income related to fair value changes on acquisition related contingent consideration. In fiscal 2019 we acquired ebbu Inc. ("ebbu"), and the consideration paid included contingent consideration related to the achievement, by ebbu, of certain scientific related milestones. The year-over-year change in the fair value of the acquisition related contingent consideration is primarily attributable to changes in our assessment of the probability and timing of ebbu achieving certain of these milestones.
- A decrease in non-cash expense of $15.3 million related the fair value changes on the liability arising from the Acreage Arrangement, from $265.2 million in the nine months ended December 31, 2019 to $249.8 million in the nine months ended December 31, 2020. The current period expense amount, associated with an increase the liability arising from the Acreage Arrangement, is primarily attributable to (i) an increase of approximately 53% in our share price from April 1, 2020 to December 31, 2020, resulting in the estimated value of the Canopy Growth shares expected to be issued upon a Triggering Event to be higher relative to the estimated value of the Acreage shares expected to be acquired at that same time, partially offset by (ii) the implementation of the amended arrangement with Acreage in September 2020, which included a reset of the exchange ratio and resulted in other changes to potential scenarios and outcomes associated with the Acreage Arrangement that had been considered in prior valuation models, and had resulted in higher liability balances at those times. Comparatively, the expense amount of $265.2 million in the nine months ended December 31, 2019 was primarily attributable to overall declines in both Canopy Growth's and Acreage's share prices in the period.

Income tax recovery

Income tax recovery in the nine months ended December 31, 2020 was $18.1 million, compared to income tax recovery of $22.9 million in the nine months ended December 31, 2019. In the nine months ended December 31, 2020, the income tax recovery consisted of a deferred income tax recovery of $19.8 million (compared to a recovery of $37.5 million in the nine months ended December 31, 2019) and current income tax expense of $1.7 million (compared to an expense of $14.6 million in the nine months ended December 31, 2019).

The decrease of $17.7 million in the deferred income tax recovery is primarily a result of (i) recording a reduction in deferred tax liabilities that arose in connection with the required revaluation of the accounting carrying value, but not the tax basis, of property, plant and equipment, intangible assets, and other financial assets; and (ii) the recognition of losses carried forward net of the use of losses carried forward from prior years for which a deferred tax asset had been recorded. In connection with certain deferred tax assets, mainly in respect of losses for tax purposes, where the accounting criteria for recognition of an asset has yet to be satisfied and it is not probable that they will be used, the deferred tax asset has not been recognized.

The decrease of $12.9 million in the current income tax expense arose primarily in connection with acquired legal entities that generated income for tax purposes during prior periods that could not be reduced by the group's tax attributes but whose current period income will now be reduced by the group's tax attributes.

Net Loss

The net loss in the nine months ended December 31, 2020 was $1.1 billion, as compared to a net loss of $61.0 million in the nine months ended December 31, 2019. The increase in the net loss is primarily attributable to the year-over-year change in other income (expense), net; asset impairment and restructuring costs; expected credit losses on financial assets and related charges, and partially offset by year-over-year reductions in our selling, general and administrative expenses and share-based compensation expense.

Segmented Analysis

In the nine months ended December 31, 2020 and 2019, all of our revenue was earned by the Cannabis, Hemp and Other Consumer Products segment. Canopy Rivers contributed net income of $4.6 million in the nine months ended December 31, 2020, of which $1.4 million was attributable to Canopy Growth. In the nine months ended December 31, 2019, Canopy Rivers contributed a net loss of $11.1 million, of which $3.0 million was attributable to Canopy Growth. The decrease in the net loss reflects the fair value increases relating to Canopy Rivers' investments in the TerrAscend exchangeable shares, partially offset by the impairment losses and expected credit losses related to the PharmHouse equity method investment and associated financial assets, as described under "Recent Developments" above. Additionally, refer to "Recent Developments" above for a description of the Canopy Rivers Arrangement Agreement.

Adjusted EBITDA (Non-GAAP Measure)

The following table presents Adjusted EBITDA for the nine months ended December 31, 2020 and 2019:

	Nine months ended December 31,			
(in thousands of Canadian dollars)	2020	2019	$ Change	% Change
Net loss	$ (1,054,125)	$ (61,035)	$ (993,090)	1627%
Income tax recovery	(18,086)	(22,948)	4,862	(21%)
Other (income) expense, net	21,106	(600,624)	621,730	104%
Loss on equity method investments	40,851	6,668	34,183	513%
Share-based compensation[1]	72,632	241,922	(169,290)	(70%)
Acquisition-related costs	7,961	19,000	(11,039)	(58%)
Depreciation and amortization[1]	98,190	76,232	21,958	29%
Asset impairment and restructuring costs	459,579	-	459,579	-
Expected credit losses on financial assets and related charges	108,480	-	108,480	-
Restructuring costs recorded in cost of goods sold	15,637	-	15,637	-
Charges related to the flow-through of inventory step-up on business combinations	1,494	-	1,494	-
Adjusted EBITDA[2]	$ (246,281)	$ (340,785)	$ 94,504	28%

[1] From Condensed Interim Consolidated Statements of Cash Flows.

[2]Adjusted EBITDA is a non-GAAP measure and is calculated as the reported net loss, adjusted to exclude income tax (expense) recovery; other income (expense), net; loss on equity method investments; share-based compensation expense; depreciation and amortization expense; asset impairment and restructuring costs; expected credit losses on financial assets and related charges; restructuring costs recorded in cost of goods sold; and charges related to the flow-through of inventory step-up on business combinations, and further adjusted to remove acquisition-related costs.

The Adjusted EBITDA loss in the nine months ended December 31, 2020 was $246.3 million, as compared to the Adjusted EBITDA loss of $340.8 million in the nine months ended December 31, 2019. The year-over-year decrease in the Adjusted EBITDA loss is primarily attributable to the year-over-year reduction in our selling, general and administrative expense, as discussed above.

Part 3 – Financial Liquidity and Capital Resources

We manage liquidity risk by reviewing, on an ongoing basis, our sources of liquidity and capital requirements. As of December 31, 2020, we had cash and cash equivalents of $825.0 million and short-term investments of $768.6 million, which are predominantly invested in liquid securities issued by the United States and Canadian governments. Additionally, we have capacity of $40.0 million under our revolving debt facility with Farm Credit Canada ("FCC"). In evaluating our capital requirements, including the impact, if any, on our business from the COVID-19 pandemic, and our ability to fund the execution of our strategy, we believe we have adequate available liquidity to enable us to meet our working capital and other operating requirements, fund growth initiatives and capital expenditures, settle our liabilities, and repay scheduled principal and interest payments on debt for at least the next twelve months.

Our objective is to generate sufficient cash to fund our operating requirements and expansion plans. To date, we have incurred net losses on a U.S. GAAP basis and Adjusted EBITDA losses, and our cash and cash equivalents have decreased $478.2 million from March 31, 2020 (and, together with short-term investments, decreased $383.0 million from March 31, 2020), as discussed in the "Cash Flows" section below. However, management anticipates the success and eventual profitability of the business. We have also ensured that we have access to public capital markets through our U.S. and Canadian public stock exchange listings, and continue to review and pursue selected external financing sources to ensure adequate financial resources. These potential sources include, but are not limited to (i) obtaining financing from traditional or non-traditional investment capital organizations; (ii) obtaining funding from the sale of our common shares or other equity or debt instruments; and (iii) obtaining debt financing with lending terms that more closely match our business model and capital needs. There can be no assurance that we will gain adequate market acceptance for our products or be able to generate sufficient positive cash flow to achieve our business plans. In the nine months ended December 31, 2020, our purchases of and deposits on property, plant and equipment totaled $138.0 million, which were funded out of available cash, cash equivalents and short-term investments. Included in our purchase obligations for fiscal 2021, as reflected under the heading "Contractual Obligations and Commitments" in the MD&A section of our Annual Report, are commitments for the purchase of property, plant and equipment totaling $73.2 million in fiscal 2021. We expect to continue funding these purchases with our available cash, cash equivalents and short-term investments. Therefore, we are subject to risks including, but not limited to, our inability to raise additional funds through debt and/or equity financing to support our continued development, including capital expenditure requirements, operating requirements and to meet our liabilities and commitments as they come due.

Cash Flows

	Nine months ended December 31,	
(in thousands of Canadian dollars)	2020	2019
Net cash (used in) provided by:		
Operating activities	$ (367,899)	$ (561,996)
Investing activities	(328,918)	(281,449)
Financing activities	269,140	(71,356)
Effect of exchange rate changes on cash and cash equivalents	(50,539)	(4,365)
Net decrease in cash and cash equivalents	(478,216)	(919,166)
Cash and cash equivalents, beginning of year	1,303,176	2,480,830
Cash and cash equivalents, end of period	$ 824,960	$ 1,561,664

Operating activities

Cash used in operating activities in the nine months ended December 31, 2020 totaled $367.9 million, as compared to cash used of $562.0 million in the nine months ended December 31, 2019. The year-over-year decrease in the cash used in operating activities was primarily due to the year-over-year reduction in our working capital spending on inventory, primarily attributable to the lower production output in the nine months ended December 31, 2020, as described in the "Cost of Goods Sold and Gross Margin" section above, and a year-over-year reduction in our selling, general and administrative expenses as discussed above.

Investing activities

The cash used in investing activities totaled $328.9 million in the nine months ended December 31, 2020, as compared to cash used of $281.4 million in the nine months ended December 31, 2019. In the nine months ended December 31, 2020, we invested $138.0 million, primarily in our production infrastructure in the United States and an expansion of our Storz & Bickel facilities. Comparatively, in the nine months ended December 31, 2019, we invested $610.9 million in expanding our growing capacity, and the construction of advanced manufacturing capability and a bottling plant at our Smiths Falls location. The year-over-year decrease in our purchases of property, plant and equipment reflects the substantial completion of our cultivation and Cannabis 2.0 infrastructure build-out, and the shift in strategy to an asset-light model in certain markets and sustaining and process improvement investments.

In the nine months ended December 31, 2020, we did not complete any acquisitions, whereas in the nine months ended December 31, 2019, cash outflows related to acquisitions totaled $505.2 million, with the most notable outflows relating to our acquisitions of C^3 and This Works. We completed strategic investments totaling $34.2 million in the nine months ended December 31, 2020, made payments of $49.8 million to Acreage shareholders upon implementation of the amended arrangement with Acreage in September 2020, and advanced the loan of $67.0 million to Acreage Hempco. This compares to strategic investments totaling $446.2 million in the nine months ended December 31, 2019, which most notably included the initial $395.2 million investment related to Acreage. Finally, in the nine months ended December 31, 2020, we made payments totaling $15.1 million for acquisition-related liabilities, as compared to $29.8 million in the nine months ended December 31, 2019 as we continue to draw-down on the amounts owing in relation to acquisitions completed in prior years.

Additional cash inflows during the nine months ended December 31, 2020 related to proceeds of $30.9 million from the sale of property, plant and equipment, proceeds of $7.0 million from the sale of equity method investments, proceeds of $18.3 million from the sale of a portfolio of patents in Germany, and $10.0 million related to a recovery of amounts related to construction financing.

Partially offsetting these decreases in cash outflows was the net purchase of short-term investments in the nine months ended December 31, 2020 in the amount of $83.6 million, as compared to the net redemption of short-term investments of $1.3 billion in the nine months ended December 31, 2019. The year-over-year change reflects our investment of the proceeds from CBI exercising their warrants during the quarter (see below) in relatively safe, liquid investments. Comparatively, in the nine months ended December 31, 2020, we redeemed short-term investments primarily for use for the purposes described above.

Financing activities

The cash provided by financing activities totaled $269.1 million in the nine months ended December 31, 2020, as compared to cash used of $71.4 million in the nine months ended December 31, 2019. In the nine months ended December 31, 2020, we received proceeds of $245.0 million in relation to CBI exercising 18.9 million warrants to purchase our common shares. Comparatively, in the nine months ended December 31, 2019, we repaid the Alberta Treasury Board financing in the amount of $95.2 million and made other scheduled debt repayments.

Free Cash Flow (Non-GAAP Measure)

Free cash flow is a non-GAAP measure used by management that is not defined by U.S. GAAP and may not be comparable to similar measures presented by other companies. Management believes that free cash flow presents meaningful information regarding the amount of cash flow required to maintain and organically expand our business, and that the free cash flow measure provides meaningful information regarding our liquidity requirements.

	Three months ended December 31,		Nine months ended December 31,	
(in thousands of Canadian dollars)	2020	2019	2020	2019
Net cash used in operating activities	$ (87,604)	$ (189,911)	$ (367,899)	$ (561,996)
Purchases of and deposits on property, plant and equipment	(47,782)	(170,708)	(137,977)	(610,858)
Free cash flow[1]	$ (135,386)	$ (360,619)	$ (505,876)	$ (1,172,854)

[1]Free cash flow is a non-GAAP measure, and is calculated as net cash provided by (used in) operating activities, less purchases of and deposits on property, plant and equipment.

Free cash flow in the third quarter of fiscal 2021 was an outflow of $135.4 million, as compared to an outflow of $360.6 million in the third quarter of fiscal 2020. The year-over-year decrease in the outflow reflects the decrease in the cash used for operating activities, as described above, and the substantial completion of our cultivation and Cannabis 2.0 infrastructure build-out over the past year and the shift in strategy to an asset-light model in certain markets.

Free cash flow in the nine months ended December 31, 2020 was an outflow of $505.9 million, as compared to an outflow of $1.2 billion in the nine months ended December 31, 2019. The year-over-year decrease in the outflow reflects the decrease in the cash used for operating activities, as described above, and the substantial completion of our infrastructure build-out and shift to a sustaining and process improvement investment strategy.

Debt

Since our formation, we have financed our cash requirements primarily through the issuance of capital stock, including the $5.1 billion investment by CBI in the third quarter of fiscal 2019, and debt. Total debt outstanding as of December 31, 2020 was $632.2 million, as compared to $465.4 million as of March 31, 2020. The total principal amount owing, which excludes fair value adjustments related to our convertible senior notes, was $604.4 million at December 31, 2020, a decrease from the principal amount owing of $615.2 million at March 31, 2020 due primarily to the repayment of the outstanding balance on the revolving debt facility with FCC.

Convertible senior notes

In June 2018, we issued convertible senior notes with an aggregate principal amount of $600.0 million. The notes bear interest at a rate of 4.25% per annum, payable semi-annually on January 15th and July 15th of each year commencing January 15, 2019. The notes mature on July 15, 2023. Holders of the notes may convert the notes at their option at any time from January 15, 2023 to the maturity date. CBI holds $200.0 million of these notes.

Other

On August 13, 2019, we entered into a $40.0 million revolving debt facility with FCC. This facility replaced all previous loans with FCC and is secured by our property on Niagara-on-the-Lake, Ontario. The outstanding balance at December 31, 2020 is $nil million, and the facility bears interest of 3.45%, or the FCC prime rate plus 1.0%, and matures on September 3, 2024. The outstanding balance plus accrued interest was repaid in October 2020.

The revolving debt facility agreement with FCC includes affirmative, negative and financial covenants. As of December 31, 2020, we were in compliance with all covenants in the revolving debt facility agreement.

Further information regarding our debt issuances, including the conversion rights of the senior convertible notes, is included in Note 16 of the Interim Financial Statements.

Contractual Obligations and Commitments

Except for the PharmHouse Financial Guarantee, as described in “Recent Developments” above, there have been no material changes to our contractual obligations and commitments from the information provided in the MD&A section in our Annual Report.

Off-Balance Sheet Arrangements

Except for the PharmHouse Financial Guarantee, as described in “Recent Developments” above, we have no off-balance sheet arrangements that have, or are reasonably likely to have, a material current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that are material to investors.

Critical Accounting Policies and Estimates

There have been no material changes to our critical accounting policies and estimates from the information provided in the MD&A section in our Annual Report.