# Condensed Consolidated Interim Financial Statements

## For the three and nine months ended May 31, 2021 (Unaudited)

## INDEX



NOTICE TO READER

The accompanying unaudited interim financial statements have been prepared by the Company's management and the Company's independent auditors have not performed a review of these financial statements.

# Condensed Consolidated Interim Statements of Financial Position
(expressed in Canadian Dollars)
(unaudited)

| | May 31, 2021 | August 31, 2020 |
|---|---|---|
| **Assets** | | |
| **Current Assets** | | |
| Cash and cash equivalents | $ 2,711,141 | $ 1,295,723 |
| Other receivables | 159,549 | 263,141 |
| Prepaid expenses and deposits | 508,690 | 118,536 |
| | 3,379,380 | 1,677,400 |
| **Non-Current Assets** | | |
| Exploration and evaluation assets (note 4) | 12,855,613 | 12,083,199 |
| Property, plant and equipment (note 5) | 102,691,109 | 102,836,885 |
| | 115,546,722 | 114,920,084 |
| | $ 118,926,102 | $ 116,597,484 |
| **Liabilities** | | |
| **Current Liabilities** | | |
| Accounts payable | $ 140,501 | $ 153,743 |
| Accrued liabilities | 463,247 | 574,383 |
| Deferred flow-through share premium (note 6) | 96,111 | 136,800 |
| Current portion of lease obligation (note 7) | 189,593 | 178,893 |
| | 889,452 | 1,043,819 |
| **Non-Current Liabilities** | | |
| Lease obligation (note 7) | 545,283 | 688,574 |
| Convertible note payable (note 8) | 3,420,000 | - |
| Derivative liabilities (note 9) | 1,175,600 | 59,827 |
| Site closure and reclamation provisions | 278,600 | 303,600 |
| | 5,419,485 | 1,052,001 |
| | 6,308,937 | 2,095,820 |
| **Shareholders' Equity** | | |
| **Share Capital** (note 10) | 181,475,257 | 179,329,547 |
| **Reserve for Warrants** (note 10c) | 4,336,380 | 4,336,481 |
| **Reserve for Share Based Payments** (note 10d) | 17,455,549 | 17,333,864 |
| **Reserve for Brokers' Compensation Warrants** (note 10e) | 297,113 | 286,000 |
| **Accumulated Deficit** | (90,947,134) | (86,784,228) |
| | 112,617,165 | 114,501,664 |
| | $ 118,926,102 | $ 116,597,484 |

Approved on behalf of the Board

"Donald S. Bubar", Director

"Alan Ferry", Director

## Condensed Consolidated Interim Statements of Comprehensive Loss
## (expressed in Canadian Dollars, except number of shares)
## (unaudited)

| | Three Months Ended | | Nine Months Ended | |
|---|---|---|---|---|
| | May 31, 2021 | May 31, 2020 | May 31, 2021 | May 31, 2020 |
| **Revenue** | | | | |
| Interest | $ 2,064 | $ 3,794 | $ 4,405 | $ 23,733 |
| Management fees (note 5a) | 1,802 | 4,486 | 4,878 | 105,592 |
| | 3,866 | 8,280 | 9,283 | 129,325 |
| **Expenses** | | | | |
| Corporate and administrative (note 11) | 471,299 | 401,568 | 1,455,594 | 1,537,574 |
| General exploration | 8,641 | 23,632 | 42,873 | 104,486 |
| Depreciation (note 5) | 31,822 | 59,236 | 92,735 | 178,770 |
| Share based compensation (note 10d) | 168,667 | 32,069 | 224,670 | 69,002 |
| Interest on lease obligation | 9,568 | 11,712 | 30,366 | 32,337 |
| Financing transaction costs (note 8) | - | - | 1,274,563 | - |
| Foreign exchange loss | 1,653 | 321 | 2,501 | 582 |
| Increase in fair value of convertible redeemable preferred shares | - | - | - | 39,375 |
| Increase (decrease) in fair value of derivative liabilities (note 9) | (1,150,695) | 57,813 | 1,188,826 | 41,615 |
| | (459,045) | 586,351 | 4,312,128 | 2,003,741 |
| **Net Income (Loss) before the Undernoted item** | 462,911 | (578,071) | (4,302,845) | (1,874,416) |
| **Gain on Sale of Property, Plant and Equipment** (note 5a) | - | - | - | 2,373,261 |
| **Net Income (Loss) before Income Taxes** | 462,911 | (578,071) | (4,302,845) | 498,845 |
| **Deferred Income Tax Recoveries** | 78,013 | - | 139,939 | 47,481 |
| **Net Income (Loss) and Total Comprehensive Income (Loss) for the period** | $ 540,924 | $ (578,071) | $ (4,162,906) | $ 546,326 |
| **Income (Loss) per Share - Basic** | $ 0.002 | $ (0.002) | $ (0.012) | $ 0.002 |
| **Income (Loss) per Share - Diluted** | $ (0.001) | $ (0.002) | $ (0.012) | $ 0.002 |
| **Weighted Average Number of Common Shares Outstanding - Basic** | 356,821,191 | 340,695,889 | 351,617,421 | 331,532,228 |
| **Weighted Average Number of Common Shares Outstanding - Diluted** | 360,938,239 | 340,695,889 | 351,617,421 | 333,280,674 |

(expressed in Canadian Dollars, except number of shares)

| | Share Capital | | Reserves | | | | |
|---|---|---|---|---|---|---|---|
| | Number of Shares | Amount | Warrants | Share Based Payments | Brokers' Compensation Warrants | Accumulated Deficit | Total |
| Balance at September 1, 2019 | 314,652,449 | $ 177,802,700 | $ 4,330,037 | $ 17,225,482 | $ 286,000 | $ (81,416,964) | $ 118,227,255 |
| Conversion of redeemable preferred shares | 23,706,725 | 997,499 | - | - | - | - | 997,499 |
| Conversion of note payable | 2,846,254 | 116,667 | - | - | - | - | 116,667 |
| Share based compensation | - | - | - | 77,590 | - | - | 77,590 |
| Net income for the nine month period | - | - | - | - | - | 546,326 | 546,326 |
| Balance at May 31, 2020 | 341,205,428 | $ 178,916,866 | $ 4,330,037 | $ 17,303,072 | $ 286,000 | $ (80,870,638) | $ 119,965,337 |
| Equity offerings | 6,000,000 | 396,000 | 7,200 | - | - | - | 403,200 |
| Conversion of note payable | 1,207,729 | 58,333 | - | - | - | - | 58,333 |
| Share based compensation | - | - | - | 30,792 | - | - | 30,792 |
| Share issuance costs - cash | - | (41,652) | (756) | - | - | - | (42,408) |
| Net loss for the three month period | - | - | - | - | - | (5,913,590) | (5,913,590) |
| Balance at August 31, 2020 | 348,413,157 | $ 179,329,547 | $ 4,336,481 | $ 17,333,864 | $ 286,000 | $ (86,784,228) | $ 114,501,664 |
| Equity offerings | 2,500,000 | 400,750 | - | - | - | - | 400,750 |
| Issued for deposit on business acquisition | 1,000,000 | 219,200 | - | - | - | - | 219,200 |
| Conversion of note payable | 1,308,139 | 180,000 | - | - | - | - | 180,000 |
| Exercise of warrants | 6,487,500 | 1,189,175 | - | - | - | - | 1,189,175 |
| Reserve transferred on exercise of warrants | - | 101 | (101) | - | - | - | - |
| Exercise of options | 2,635,000 | 294,700 | - | - | - | - | 294,700 |
| Reserve transferred on exercise of options | - | 113,163 | - | (113,163) | - | - | - |
| Redeemed | (955,949) | (200,750) | - | - | - | - | (200,750) |
| Compensation warrants issued on equity offerings | - | - | - | - | 11,113 | - | 11,113 |
| Share issuance costs - cash | - | (39,516) | - | - | - | - | (39,516) |
| Share issuance costs - compensation warrants issued | - | (11,113) | - | - | - | - | (11,113) |
| Share based compensation | - | - | - | 234,848 | - | - | 234,848 |
| Net loss for the nine month period | - | - | - | - | - | (4,162,906) | (4,162,906) |
| Balance at May 31, 2021 | 361,387,847 | $ 181,475,257 | $ 4,336,380 | $ 17,455,549 | $ 297,113 | $ (90,947,134) | $ 112,617,165 |

## Condensed Consolidated Interim Statements of Cash Flows
## (expressed in Canadian Dollars)
## (unaudited)

| | Three Months Ended | | Nine Months Ended | |
|---|---|---|---|---|
| | May 31, 2021 | May 31, 2020 | May 31, 2021 | May 31, 2020 |
| **Operating Activities** | | | | |
| Cash paid to employees | $ (321,259) | $ (389,355) | $ (846,297) | $ (1,228,775) |
| Cash paid to suppliers | (309,460) | (196,746) | (754,953) | (523,171) |
| Interest received | 2,064 | 3,794 | 4,405 | 23,733 |
| Management fees received | 2,042 | 8,815 | 5,731 | 112,375 |
| Cash Used by Operating Activities | (626,613) | (573,492) | (1,591,114) | (1,615,838) |
| **Financing Activities** | | | | |
| Net proceeds from equity offerings | 468,501 | - | 458,993 | - |
| Net proceeds from issuance of note payable | - | - | - | - |
| (transaction costs paid) (note 8) | (14,451) | - | 2,882,434 | - |
| Proceeds from exercise of stock options | 131,200 | - | 294,700 | - |
| Proceeds from exercise of warrants | 343,875 | - | 559,125 | - |
| Common share redemption (note 10b) | (200,750) | - | (200,750) | - |
| Lease payments paid | (23,062) | (53,095) | (31,138) | (153,968) |
| Cash Provided (Used) by Financing Activities | 705,313 | (53,095) | 3,963,364 | (153,968) |
| **Investing Activities** | | | | |
| Exploration and evaluation assets | (525,257) | (6,719) | (724,080) | (519,478) |
| Property, plant and equipment | (17,622) | (6,735) | (30,251) | (99,388) |
| Deposits paid for business acquisition | (200,000) | - | (200,000) | - |
| Proceeds from sale of property, plant and equipment (note 5a) | - | - | - | 1,778,408 |
| Cash Provided (Used) by Investing Activities | (742,879) | (13,454) | (954,311) | 1,159,542 |
| **Change in Cash and Cash Equivalents** | (664,179) | (640,041) | 1,417,919 | (610,264) |
| **Foreign Exchange Effect on Cash** | (1,653) | (321) | (2,501) | (582) |
| **Cash and Cash Equivalents - beginning of period** | 3,376,973 | 1,911,357 | 1,295,723 | 1,881,841 |
| **Cash and Cash Equivalents - end of period** | $ 2,711,141 | $ 1,270,995 | $ 2,711,141 | $ 1,270,995 |

Supplemental Cash Flow Information (note 14)

## 1. Nature of Operations and Going Concern Uncertainty

Avalon Advanced Materials Inc. ("Avalon") is a publicly listed company incorporated in Canada and continued under the *Canada Business Corporations Act*. Avalon's common shares are listed on the Toronto Stock Exchange (the "TSX") (TSX: AVL), on the OTCQB® Venture Market (OTCQB: AVLNF), and the Frankfurt Stock Exchange in Germany. The registered address, principal address and records office of Avalon is located at 130 Adelaide Street West, Suite 1901, Toronto, Ontario, Canada, M5H 3P5.

Avalon, together with its subsidiaries (collectively, the "Company") is principally engaged in the acquisition, exploration, evaluation and development of specialty metal and mineral properties, located principally in Canada. To date, the Company has not earned any significant revenues.

The realization of amounts shown for its development asset – the Nechalacho Rare Earth Elements Project (the "Nechalacho REE Project") and its exploration and evaluation assets is dependent upon the discovery of economically recoverable reserves (where not already identified), the ability of the Company to obtain the necessary financing to develop these assets, and future profitable production or proceeds of disposition from these assets.

These unaudited condensed consolidated interim financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") applicable to a going concern, which assumes the Company will continue to meet its obligations and discharge its liabilities in the normal course of business for the foreseeable future. Different bases of measurement may be appropriate when a company is not expected to continue operations for the foreseeable future. The Company is in the exploration and development stage and raises funds in the equity markets to conduct its business activities. The Company has incurred losses in the current and prior periods, with a net loss of $4,162,906 for the nine months ended May 31, 2021 (the "Period") and an accumulated deficit of $90,947,134 as at May 31, 2021. The Company's cash and cash equivalents balance at May 31, 2021 was $2,711,141, and the working capital was $2,489,928. Excluding the deferred flow-through share premium of $96,111, the Company's adjusted working capital as at May 31, 2021 was $2,586,039 (calculated by adding back the deferred flow-through share premium of $96,111 to the working capital of $2,489,928).

The outbreak of the novel strain of coronavirus, specifically identified as "COVID-19", has resulted in governments worldwide enacting emergency measures to combat the spread of the virus. These measures, which include the implementation of travel bans, self-imposed quarantine periods and social distancing, have caused material disruption to businesses globally resulting in an economic slowdown. Global equity markets have experienced significant volatility and weakness. Governments and central banks have reacted with significant monetary and fiscal interventions designed to stabilize economic conditions. The duration and impact of the COVID-19 outbreak is unknown at this time, as is the efficacy of the government and central bank interventions. It is not possible to reliably estimate the length and severity of these developments, and the impact on the Company's ability to raise capital, its financial results or its financial condition.

Given the continuation of weak investor sentiment and capital market conditions in the junior resource sector, there exists an uncertainty as to the Company's ability to raise additional funds on favorable terms. These conditions indicate the existence of a material uncertainty that raises substantial doubt about the Company's ability to continue as a going concern. As at May 31, 2021, the Company is required to incur additional Canadian exploration expenses ("CEE") of $484,187 by December 31, 2022. The Company's expenditures on other discretionary exploration and development activities have some scope for flexibility in terms of amount and timing, which can be adjusted accordingly. Management intends to finance these expenditures over the next twelve months with funds currently on hand, and through planned equity financings and other sources of non-dilutive capital.

## 1. Nature of Operations and Going Concern Uncertainty (continued)

These unaudited condensed consolidated interim financial statements do not reflect the adjustments to the carrying values of assets and liabilities and the reported expenses and statement of financial position classifications that would be necessary should the going concern assumption be inappropriate, and those adjustments could be material.

These unaudited condensed consolidated interim financial statements have been reviewed and approved by the Company's Audit Committee and the Board of Directors (the "Board") on July 13, 2021.

## 2. Basis of Presentation

### a) *Statement of Compliance and Basis of Presentation*

These unaudited condensed consolidated interim financial statements, including comparatives, have been prepared in accordance with International Accounting Standards ("IAS") 34 *Interim Financial Reporting*, as issued by IASB.

These unaudited condensed consolidated interim financial statements do not contain all disclosures required by IFRS and accordingly should be read in conjunction with the Company's consolidated annual financial statements for the year ended August 31, 2020.

These unaudited condensed consolidated interim financial statements have been prepared on a going concern basis using the historical cost basis, except for certain financial instruments which are measured at fair value in accordance with the policies disclosed in Note 3 of the Company's consolidated annual financial statements for the year ended August 31, 2020.

### b) *Basis of Consolidation*

These unaudited condensed consolidated interim financial statements include the accounts of the Company and the entities controlled by the Company. Control exists when the Company is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

These unaudited condensed consolidated interim financial statements include the accounts of the Company and its wholly-owned subsidiaries, 8110131 Canada Inc., Nolava Minerals Inc. ("Nolava"), and Avalon Rare Metals Ltd. ("ARML"). Nolava and ARML are incorporated in the United States of America ("USA").

ARML has not carried on any significant operations since its inception. During the year ended August 31, 2012, 8110131 Canada Inc. acquired certain net smelter returns ("NSR") royalty interests in the Company's properties which were held by third parties. Nolava had held certain mining claims in Utah, USA and had conducted exploration work on those mining claims during fiscal year 2011 to fiscal year 2014. All intercompany transactions and balances have been eliminated on consolidation of the accounts.

The Company also has a 50% interest in NWT Rare Earths Ltd. ("NWTREL"), with an unrelated third party owning the other 50%, which was created during the year ended August 31, 2020 to hold the exploration permits and related authorizations pertaining to the Nechalacho REE Project, in order to assist each party's development of their respective projects. NWT Rare Earths Ltd. has not carried on any significant operations since its inception and no equity earnings/losses have been allocated to the Company.

## 3. Summary of Significant Accounting Policies

These unaudited condensed consolidated interim financial statements have been prepared using the same accounting policies, significant accounting judgments and estimates, and methods of computation as the annual consolidated financial statements of the Company as at and for the year ended August 31, 2020.

## 4. Exploration and Evaluation Assets

| | September 1, 2020 | Expenditures | Impairment Loss | May 31, 2021 |
|---|---|---|---|---|
| **For the Period** | | | | |
| Separation Rapids Lithium Project (a) | $ 12,025,329 | $ 668,629 | $ - | $ 12,693,958 |
| Lilypad Cesium-Tantalum Project (b) | 42,870 | 100,735 | - | 143,605 |
| Other (d) | 15,000 | 3,050 | - | 18,050 |
| | $ 12,083,199 | $ 772,414 | $ - | $ 12,855,613 |

| | September 1, 2019 | Expenditures | Impairment Loss | August 31, 2020 |
|---|---|---|---|---|
| **For the Year Ended August 31, 2020** | | | | |
| Separation Rapids Lithium Project (a) | $ 11,522,138 | $ 503,191 | $ - | $ 12,025,329 |
| Lilypad Cesium-Tantalum Project (b) | 24,488 | 18,382 | - | 42,870 |
| East Kemptville Tin-Indium Project (c) | 5,503,577 | 83,633 | (5,587,210) | - |
| Other (d) | 15,000 | - | - | 15,000 |
| | $ 17,065,203 | $ 605,206 | $ (5,587,210) | $ 12,083,199 |

a) Separation Rapids Lithium Project, Ontario

The Company owns a 100% interest in certain mineral claims and a mining lease in the Kenora area of Ontario.

b) Lilypad Cesium-Tantalum Project, Ontario

The Company owns a 100% interest in certain mineral claims in the Lilypad Cesium-Tantalum property, located 150 km northeast of the Pickle Lake area of Ontario.

c) East Kemptville Tin-Indium Project, Nova Scotia

The Company held a special exploration licence (the “Special Licence”) to search and prospect for all minerals except for coal, salt, potash and uranium at the closed mine site in the East Kemptville area of Yarmouth, Nova Scotia, where the surface rights were held by the original mine developer.

The Special Licence had a term of three years which began February 2, 2015 and was renewable for an additional two one-year periods, which extended the Special Licence until February 1, 2020, after which it was converted to a regular exploration licence following regulatory policy change.

## 4. Exploration and Evaluation Assets (continued)

The Company completed a preliminary economic assessment during fiscal 2018 with a development model of utilizing the existing tailings management area ("TMA") and had been in negotiation with the surface rights owner to secure full tenure to the project site. Agreement in principle was reached in Fiscal 2019, however, the surface rights owner subsequently refused to sign the agreement after putting on hold any new work on TMAs on all of its closed minesites. Not having access to the existing unused tailings ponds severely limits the possibilities for economic re-development of the site. This realization coupled with the continuing difficulties in getting surface access to the project site, caused the Company to decide to withdraw its lease application and to write off the costs incurred to-date of $5,587,210 as an impairment loss during the year ended August 31, 2020.

d) Other Resource Properties

The Company has a 100% interest in a mining lease in the Warren Township Anorthosite Project, located near Foleyet, Ontario, a 2.0% NSR interest in certain claims of the East Cedartree Gold Property located near Kenora, Ontario, and a 2.4% NSR interest in the Wolf Mountain Platinum-Palladium Project located near Thunder Bay, Ontario.

During the Period, the Company entered into a binding letter of intent (the "LOI") to purchase ownership of 2333382 Ontario Inc. ("2333382"), a private Ontario corporation which owns four industrial minerals properties and a demonstration-scale processing plant located at Matheson, Ontario. Among the industrial minerals property assets owned by 2333382 is an asset transfer agreement giving 2333382 the right to acquire full title to the Cargill Carbonatite Complex near Kapuskasing, Ontario. The total purchase price to be paid by the Company will be $16 million, payable in a combination of cash and common shares of Avalon over a period of two years. The initial payment of $200,000 in cash and the issuance of 1,000,000 common shares were paid during the quarter ended May 31, 2021 (the "Quarter"). The balance of the purchase price will be made in four instalments on the following schedule:

i) on or before August 15, 2021, $900,000 in cash, of which 50% can be paid in common shares at the Company's discretion;
ii) on or before February 15, 2022, $3 million in cash;
iii) on or before August 15, 2022, $3 million in cash; and
iv) on or before February 15, 2023, $8,700,000 in cash.

The Company will also assume responsibility for managing all of 2333382's ongoing operations upon posting of a Letter of Credit in the amount of $23.7 million with the Ontario government to meet current closure plan financial assurance requirements at the Cargill site. Discussions are in progress with a number of lenders and surety providers toward securing the required Letter of Credit.

During the Period, the Company staked certain mineral claims in close proximity to the Cargill Carbonatite Complex.

## 5. Property, Plant and Equipment

| | Nechalacho REE Project (a) | Airstrip | Office, Computer and Office Equipment (b) | Land and Building | Exploration Equipment | Leasehold Improvements | Total |
|---|---|---|---|---|---|---|---|
| **Cost** | | | | | | | |
| As at September 1, 2019 | $ 101,474,299 | $ 646,860 | $ 201,137 | $ 90,905 | $ 695,532 | $ 101,614 | $ 103,210,347 |
| Additions | 30,340 | - | 18,575 | - | 1,300 | 5,140 | 55,355 |
| IFRS 16 adjustments | - | - | 1,045,810 | - | - | - | 1,045,810 |
| Disposals | - | - | (30,283) | - | - | - | (30,283) |
| As at August 31, 2020 | 101,504,639 | 646,860 | 1,235,239 | 90,905 | 696,832 | 106,754 | 104,281,229 |
| Additions | 32,470 | - | - | - | - | - | 32,470 |
| As at May 31, 2021 | $ 101,537,109 | $ 646,860 | $ 1,235,239 | $ 90,905 | $ 696,832 | $ 106,754 | $ 104,313,699 |
| **Accumulated Depreciation** | | | | | | | |
| As at September 1, 2019 | $ - | $ 286,070 | $ 174,289 | $ 14,558 | $ 658,890 | $ 94,702 | $ 1,228,509 |
| Depreciation expense | - | 18,974 | 210,352 | 4,191 | 11,025 | 1,576 | 246,118 |
| Disposals | - | - | (30,283) | - | - | - | (30,283) |
| As at August 31, 2020 | - | 305,044 | 354,358 | 18,749 | 669,915 | 96,278 | 1,444,344 |
| Depreciation expense | - | 13,092 | 154,141 | 3,143 | 6,057 | 1,813 | 178,246 |
| As at May 31, 2021 | $ - | $ 318,136 | $ 508,499 | $ 21,892 | $ 675,972 | $ 98,091 | $ 1,622,590 |
| **Net Book Value** | | | | | | | |
| As at August 31, 2020 | $ 101,504,639 | $ 341,816 | $ 880,881 | $ 72,156 | $ 26,917 | $ 10,476 | $ 102,836,885 |
| As at May 31, 2021 | $ 101,537,109 | $ 328,724 | $ 729,740 | $ 69,013 | $ 20,860 | $ 8,663 | $ 102,691,109 |

## 5. Property, Plant and Equipment (continued)

a) Nechalacho REE Project, Northwest Territories

The Company owns a 100% interest the resources below a depth of 150 metres above sea level (the "Basal Zone Resources") in eight mining leases located at Thor Lake in the Mackenzie Mining District of the Northwest Territories.

These eight contiguous mining leases total 5,786 hectares (14,297 acres), after three mining claims totalling 332 hectares on the southwest side of the original five leases were converted to mining leases. The original five leases are subject to one independently owned 2.5% Net Smelter Returns ("NSR") royalty agreement. Avalon has the contractual right to buy out this royalty on the basis of a fixed formula, which is currently approximately $1.6 million, and which will increase at a rate equal to the Canadian prime rate until the royalty is bought out.

During the year ended August 31, 2020, the Company disposed of the resources above a depth of 150 metres above sea level ("Upper Zone Resources") to a third party for a total cash consideration of $5.0 million and recognized a net gain on sale of $2,373,261. Advance payments totaling $3.2 million had been received by August 31, 2019 and the balance of $1.8 million was received during the year ended August 31, 2020.

The Company retained a 3.0% NSR royalty (the "3.0% NSR Royalty") and continue to have access to the property for development and mining of its Basal Zone resources. The Company has also agreed to waive the 3.0% NSR Royalty for the third party for the first five years of commercial production and to grant the third party the option to pay the Company $2.0 million within eight years of the transaction closing to extend the waiver of this royalty in perpetuity. The third party has the option to purchase the Company's option in the 2.5% NSR Royalty, provided that, upon exercising the option, it extinguishes this royalty. Avalon and the third party have formed a jointly-owned corporation to hold the exploration permits and related authorizations related to their projects and have also entered into a co-ownership agreement governing each party's activities and management at site.

During the Period, the Company generated net management fees of $4,878 (2020 - $105,592) for services provided to the third party to manage its exploration activities on the property.

At May 31, 2021, the amount of the net assets of the Company is more than its market capitalization, IAS 36 – *Impairment of Assets* considers that an indicator of impairment is present based on external sources of information. The Company completed an impairment test on the Nechalacho Project as at May 31, 2021 and determined that the Project was not impaired. The main assumptions used to determine the recoverable amount related to Nechalacho were long-term commodity prices, changes in cost estimates, discount rates, foreign exchange rates and years to commencement of production.

b) Depreciation of $63,201 (net of $83,866 in rent forgiveness under the Canada Emergency Commercial Rent Assistance and rent subsidy under the Canada Emergency Rent Subsidy programs) was recognized relating to the right of use ("ROU") asset during the Period (2020 - $147,067), and the carrying balance of the ROU asset was $702,653 as at May 31, 2021 (August 31, 2020 - $849,720).

## 6. Deferred Flow-Through Share Premium

A summary of the changes in the deferred flow-through share premium amount is set out below:

| | |
|---|---|
| Balance – September 1, 2019 | $ 47,481 |
| Increase relating to flow-through common shares issued | 136,800 |
| Decrease relating to CEE incurred | (47,481) |
| Balance – August 31, 2020 | 136,800 |
| Increase relating to flow-through common shares issued | 99,250 |
| Decrease relating to CEE incurred | (139,939) |
| Balance – May 31, 2021 | $ 96,111 |

## 7. Lease Obligation

The Company had the following future commitment relating to the lease contract for its office premises:

| | |
|---|---|
| 2021 | $ 55,297 |
| 2022 | 222,556 |
| 2023 | 229,181 |
| 2024 | 233,563 |
| 2025 | 63,280 |
| Total future lease payments as at May 31, 2021 | 803,877 |
| Amounts representing interest | 68,999 |
| Present value of future lease payments | 734,878 |
| Current portion of lease obligation | 189,593 |
| Non-current portion of lease obligation | $ 545,285 |

## 8. Convertible Note Payable

On January 29, 2021, the Company issued a convertible note payable in the amount of $3,000,000 to an entity managed by the Lind Partners ("Lind") (the "Note"). The Note has a term of two years with a maturity date of January 29, 2023 and accrued an interest amount of $600,000 on the date of issuance, resulting in the Note to bear a face value of $3,600,000 at issuance.

Lind is entitled to convert any outstanding amount of the face value of the Note into common shares commencing on May 30, 2021 at a conversion price equal to 85% of the five day trailing value weighted average price ("VWAP") of the common shares prior to the date of conversion (the "Conversion Feature"). The Company has the right to repurchase the Note at the outstanding face value at any time (the "Buyback Option"), subject to the holder's option to convert up to one third of the original value into common shares prior to the Company's repurchase.

In conjunction with the issuance of the Note, Lind received a closing fee of $90,000 and 9,800,000 common share purchase warrants. Each warrant entitles the holder to purchase one common share of the Company at a price of $0.18 per common share until January 29, 2025.

The Note is a hybrid instrument that contains multiple embedded derivatives including the Conversion Feature and Buyback Option.

## 8. Convertible Note Payable (continued)

The economic characteristics and risks of the Conversion Feature are different from that of the host contract (the "Note") in that it allows Lind to convert the Note (a debt instrument) into the Company's common shares (an equity instrument) at a price per share equal to 85% of the five day trailing VWAP of the shares prior to the date of conversion, thus the Conversion Option can be measured separately from the Note. In addition, the number of common shares to be issued upon conversion is variable and does not meet the "a fixed amount of cash for a fixed number of equity instruments" requirement to be classified as an equity instrument. As such, the Company had designated the entire hybrid contract (the Note and all of the embedded derivatives) as a financial liability at FVTPL and are re-measured at each financial statement reporting date, with the resulting change in value being recorded as increase or decrease in fair value of convertible note payable in the consolidated statement of comprehensive loss.

As the Company has the Buyback Option to repurchase the Note at the outstanding face value, the total fair value of the Note is therefore equal the face value, and is $3,600,000 at issuance.

The exercise price of the warrant is subject to adjustment from time to time in the event of certain common share rights offering, such that the exercise of the warrants does not result in a fixed number of common shares being issued for a fixed amount of cash. As a result, the warrants had been classified as a financial liability at FVTPL and re-measured at each financial statement reporting date using the Black-Scholes pricing model, with the resulting change in value being recorded as increase or decrease in fair value of derivative liabilities in the consolidated statement of comprehensive loss.

The fair value of the warrants was estimated at $556,997 at issuance, and this amount was allocated to the warrant component of this private placement. The fair value of the warrants was estimated using the Black-Scholes pricing model, with the following assumptions: expected dividend yield of Nil; risk free interest rate of 0.37%; expected life of 4.0 years; and expected volatility of 35%.

The fair values of the Note and the warrants at issuance totaled $4,156,997 and the excess of this amount over the gross proceeds ($3,000,000) of $1,156,997 had been recorded as a financing transaction cost in the Statement of Comprehensive Loss.

A summary of the changes in the convertible note payable amount during the Period is set out below:

| | |
|---|---|
| Balance – August 31, 2020 | $ - |
| Issued | 3,000,000 |
| Interest | 600,000 |
| Converted to common shares | (180,000) |
| Balance – May 31, 2021 | $ 3,420,000 |

The number of common shares to be issued would be 23,123,732 if the entire Note had been converted into common shares based on the five day trailing VWAP of the Company's common shares on the TSX of $0.1739 on May 31, 2021.

## 9. Derivative Liabilities

The derivative liabilities consist of the warrants denominated in foreign currency, and certain warrants with exercise prices that are subject to adjustment from time to time in the event of certain common share rights offering (collectively referred to as "liability classified warrants").

## 9. Derivative Liabilities (continued)

The following table summarizes information concerning the derivative liabilities as at the beginning and end of the respective reporting periods:

| | Number of Warrants | Amount |
|---|---|---|
| **Warrants denominated in foreign currency** | | |
| Balance – September 1, 2019, August 31, 2020 and May 31, 2021 | 6,466,513 | $ 1 |
| **Other warrants subject to potential price adjustment** | | |
| Balance – September 1, 2019 | 21,475,000 | 27,068 |
| Increase in fair value | - | 32,758 |
| Balance – August 31, 2020 | 21,475,000 | 59,826 |
| Issued | 9,800,000 | 556,997 |
| Exercised | (6,450,000) | (630,050) |
| Increase in fair value | - | 1,188,826 |
| Balance – May 31, 2021 | 24,825,000 | 1,175,599 |
| **Total derivative liabilities** | | $ 1,175,600 |

## 10. Share Capital

### *a) Authorized*

The Company is presently authorized to issue an unlimited number of common shares without par value. The Company is also authorized to issue up to 25,000,000 preferred shares without par value, of which 950 have been issued and none are outstanding as at May 31, 2021.

### *b) Common Shares*

Common shares issued, redeemed and cancelled during the Period are as follows:

i) In May 2021, the Company completed a private placement and issued 2,500,000 flow-through common shares at $0.20 per share for gross proceeds of $500,000.

The excess of the cash consideration received over the market price of the Company's shares at the date of the announcement of the flow-through share financing totaling $99,250 was recorded as a deferred flow-through share premium liability on the consolidated statement of financial position on May 14, 2021.

ii) In March 2021, completed its share capital amendment, which involved amending the Company's articles to reflect a 500:1 consolidation of the Company's common shares, immediately followed by a 1:500 split of the Company's post-consolidated common shares on March 15, 2021 (the "Share Capital Amendment"). Shareholders who held less than 500 common shares in the form of a physical certificate immediately prior to March 15, 2021 ("Registered Shareholder") were paid a cash payment in exchange for their shares (the "Cash Payment") equal to the number of common shares they held immediately prior to the Share Capital Amendment multiplied by $0.21, which is the five day VWAP of the common shares on the TSX prior to March 15, 2021. Shareholders holding less than 500 common shares in a brokerage account immediately prior to the March 15, 2021, and who so elected through their intermediary, have been paid the Cash Payment. All other shareholders continued to hold the exact same number of shares after the Share Capital Amendment that they did prior to the Share Capital Amendment.

## 10. Share Capital (continued)

As a result of the Share Capital Amendment, a total of 955,949 common shares had been redeemed and cancelled, of which 932,366 shares were elected by shareholders who held their shares in a brokerage account, and the balance of 23,583 shares were held by Registered Shareholders.

### c) Warrants

The following table reconciles the equity classified warrants outstanding to purchase common shares of the Company at the beginning and end of the respective periods:

| | Number of Warrants | Weighted Average Exercise Price |
|---|---|---|
| Balance – September 1, 2019 | 8,257,500[1] | $ 0.132 |
| Issued pursuant to equity offerings | 3,000,000 | 0.120 |
| Expired | (6,060,000) | 0.136 |
| Balance – August 31, 2020 | 5,197,500[1] | 0.120 |
| Exercised | (37,500) | 0.120 |
| Balance – May 31, 2021 | 5,160,000[1] | $ 0.120 |

[1] Does not include the additional liability classified warrants as disclosed below.

During the Period, the expiry dates for the remaining outstanding warrants (each with an exercise price of $0.12 per share) issued in the November 2018 Private Placement were extended. The expiry date has been extended from November 1, 2020 to November 1, 2021 for 1,900,000 warrants, and the expiry date for the remaining 287,500 warrants has been extended from November 23, 2020 to November 23, 2021. All other terms and conditions of these warrants remain unchanged.

The outstanding equity classified warrants have a weighted average remaining contract life of 0.9 years.

The warrants reserve, included as a component of the consolidated statement of changes in equity, relates to equity settled instruments issued by the Company to various stakeholders.

The Company also has the following liability classified warrants outstanding as at May 31, 2021:

i) 6,466,513 warrants with an adjusted exercise price of US$0.5223 per share ("US$ Warrants") and are exercisable until June 13, 2021. These warrants are subject to certain anti-dilution provisions, which may reduce the exercise price, with a floor of US$0.5095 per share;

ii) 6,900,000 A1 Warrants with an exercise price of $0.23 per share and are exercisable until March 10, 2022;

iii) 6,250,000 B1 Warrants with an exercise price of $0.15 per share and are exercisable until January 15, 2023;

iv) 1,875,000 C1 Warrants with an exercise price of $0.125 per share and are exercisable until June 29, 2023; and

v) 9,800,000 warrants with an exercise price of $0.18 per share and are exercisable until January 29, 2025.

## 10. Share Capital (continued)

The Company is also required to issue 20,000 warrants to the Northwest Territory Métis Nation in two equal installments of 10,000 warrants upon the Nechalacho REE Project meeting certain milestones.

### *d) Share Based Payments*

The shareholders have approved a Stock Option Plan (the "Plan") that provides for the issue of up to 10% of the number of issued and outstanding common shares of the Company to eligible employees, directors and service providers of the Company.

The Plan authorizes the granting of options to purchase common shares of the Company at a price equal to or greater than the closing price of the shares on either the trading day prior to the grant or the day of the grant. The options generally vest over a period of one to four years, and generally have a term of two to five years (but can have a maximum term of up to 10 years).

The following table reconciles the stock options outstanding at the beginning and end of the respective reporting periods:

| | Number of Options | Weighted Average Exercise Price |
|---|---|---|
| Balance – September 1, 2019 | 9,396,250 | $ 0.16 |
| Granted | 7,680,000 | 0.08 |
| Expired | (3,241,250) | 0.21 |
| Forfeited | (290,000) | 0.10 |
| Balance – August 31, 2020 | 13,545,000 | 0.10 |
| Granted | 6,610,000 | 0.19 |
| Exercised | (2,635,000) | 0.11 |
| Expired | (1,285,000) | 0.14 |
| Forfeited | (443,750) | 0.09 |
| Balance – May 31, 2021 | 15,791,250 | $ 0.13 |

As at May 31, 2021, there were 4,353,750 options vested (August 31, 2020 – 5,416,250) with an average exercise price of $0.10 per share (August 31, 2020 - $0.12), that were exercisable.

During the Period, an aggregate of 2,635,000 stock options were exercised at the weighted average exercise price of $0.11 per share, and the weighted average closing market share price on the date preceding the date of exercise was $0.22 per share. No stock options were exercised during the nine months ended May 31, 2020.

The following table summarizes information concerning outstanding and exercisable options as at May 31, 2021:

| Exercise Price Range | Number of Options Outstanding | Number of Options Exercisable | Weighted Average Remaining Contractual Life |
|---|---|---|---|
| $0.21 - $0.26 | 400,000 | - | 4.7 years |
| $0.15 - $0.20 | 5,740,000 | 565,000 | 4.0 years |
| $0.11 - $0.14 | 1,802,500 | 900,000 | 2.7 years |
| $0.08 - $0.10 | 7,848,750 | 2,888,750 | 3.2 years |
| | 15,791,250 | 4,353,750 | |

## 10. Share Capital (continued)

The fair value of each option granted is estimated at the time of grant using the Black-Scholes option-pricing model. The Black-Scholes option-pricing model requires the input of subjective assumptions, including expected life of the option award, share price volatility and other assumptions. The expected life of options granted is derived from historical data on employee exercises and post-vesting employment termination behavior. Expected volatility is based on the historic volatility of the Company's shares. These assumptions involve inherent uncertainties and the application of management judgment. In addition, the Company is required to estimate the expected forfeiture rate and only recognize expense for those options expected to vest.

The weighted average assumptions for grants during the Period and the year ended August 31, 2020 are as follows:

| | May 31, 2021 | August 31, 2020 |
|---|---|---|
| Exercise price | $0.19 | $0.08 |
| Closing market price on day preceding date of grant | $0.18 | $0.05 |
| Risk-free interest rate | 0.65% | 1.00% |
| Expected life (years) | 4.1 | 3.6 |
| Expected volatility | 88% | 80% |
| Expected dividend yield | Nil | Nil |
| Grant date fair value | $0.11 | $0.02 |
| Forfeiture rate | 13% | 14% |

During the Period, the shareholders approved the Company's Deferred Share Unit ("DSU") Plan and Restricted Share Unit ("RSU") Plan. The maximum number of common shares which may be issued in connection with the redemption of DSUs and/or RSUs, when combined with any other equity compensation arrangement of the Company cannot exceed 10% of the total issued and outstanding common shares from time to time. In addition, the maximum number of common shares which may be issued in connection with the redemption of DSUs granted under the DSU Plan cannot exceed 1,750,000 common shares, or such greater number as may be approved by the shareholders from time to time.

DSUs are awarded to the Company's directors. Under the DSU plan, directors are permitted to elect in each year to receive their respective director's retainer in cash, DSUs or a combination thereof. The number of DSUs granted to a director electing to receive their retainer in DSUs is determined based on the five day VWAP of the Company's common shares prior to the date the DSUs are awarded and vest upon grant. The Board may grant discretionary awards of DSUs to directors of the Company from time to time, subject to such vesting, performance criteria, or other terms and conditions as the Board may prescribe. The Board may elect to issue cash or common share, or any combination thereof to redeem the DSUs within fifteen days of the redemption date.

Under the RSU Plan, the Board may grant discretionary awards of RSUs to directors, senior officers and key employees of the Company from time to time, subject to a restricted period and such vesting, performance criteria, or other terms and conditions as the Board may prescribe. Unless the Board determines otherwise at the time of the award of RSUs, one-third of such award will be restricted until the first anniversary of the grant date, another one-third will be restricted until the second anniversary of the grant date and the remaining one-third will be restricted until the third anniversary of the grant date. The Board may elect to issue cash or common share, or any combination thereof to redeem the RSUs within fifteen days of the redemption date. Where the Board elects to redeem RSUs in cash, the cash payment will be based on the five day VWAP of the Company's common shares prior to the redemption date.

On April 20, 2021, an aggregate of 475,000 DSUs vesting at the grant date were granted to the Company's directors (the "DSU Grant" and a total of 1,475,000 RSUs were granted to the Company's officers and key employees (the "RSU Grant"). One-third of the RSU Grant will vest on each of the first, second and third anniversary of the grant date.

## 10. Share Capital (continued)

The DSU and RSU grants have been accounted for as equity settled share units as the Company does not have a present obligation to settle the DSUs and RSUs in cash at the grant date.

Changes to the number of share units are as follows:

| | DSU Plan (Equity Settled) | RSU Plan (Equity Settled) |
|---|---|---|
| Balance – September 1, 2019 and August 31, 2020 | - | - |
| Granted | 475,000 | 1,475,000 |
| Balance – May 31, 2021 | 475,000 | 1,475,000 |

The share based payments reserve, included as a component of the consolidated statement of changes in equity, relates to equity settled compensation options, DSUs and RSUs issued by the Company to its directors, officers, employees and consultants.

The estimated fair value of options, DSUs and RSUs earned during the Period was $234,848 (2020 – $77,590), of which $67 (2020 - $297) was capitalized to property, plant and equipment, $9,404 (2020 - $6,169) was capitalized as exploration and evaluation assets, $707 (2020 - $2,122) was charged to operations as general exploration expenses, with the balance of $224,670 (2020 – $69,002) charged to operations as share based compensation expense.

### *e) Brokers' Compensation Warrants*

The following table summarizes information concerning outstanding brokers' compensation warrants as at the beginning and end of the respective reporting periods:

| | Number of Compensation Warrants | Weighted Average Exercise Price |
|---|---|---|
| Balance – September 1, 2019 | 420,000 | $ 0.15 |
| Expired | (420,000) | 0.15 |
| Balance – August 31, 2020 | - | - |
| Issued pursuant to equity offering | 150,000 | 0.20 |
| Balance – August 31, 2020 and May 31, 2021 | 150,000 | $ 0.20 |

The brokers' compensation warrants reserve, included as a component of the consolidated statement of changes in equity, relates to equity settled compensation instruments issued by the Company to external service providers.

As at May 31, 2021, the Company has 150,000 compensation warrants outstanding with an exercise price of $0.20 per common share, which are exercisable until May 14, 2023.

## 11. Corporate and Administrative Expenses

Corporate and administrative expenses for the three months and nine months ended May 31, 2021 and May 31, 2020 consist of the following:

| | Three Months Ended | | Nine Months Ended | |
|---|---|---|---|---|
| | May 31, 2021 | May 31, 2020 | May 31, 2021 | May 31, 2020 |
| Salaries and benefits[(1)] | $ 269,535 | $ 217,297 | $ 798,754 | $ 867,631 |
| Directors' fees[(2)] | 2,334 | 1,851 | 8,573 | 11,851 |
| Consulting and professional fees | 80,272 | 94,307 | 306,072 | 279,048 |
| Office, insurance and other expenses | 92,459 | 56,322 | 201,878 | 186,320 |
| Shareholders' communications and filing fees | 25,971 | 20,888 | 137,799 | 131,263 |
| Travel and related costs | 728 | 10,903 | 2,518 | 61,461 |
| | $ 471,299 | $ 401,568 | $ 1,455,594 | $ 1,537,574 |

(1) These figures do not include share based compensation and are net of the Canada Emergency Wage Subsidy ("CEWS") of $51,034 (2020 - $77,840) for the Quarter and $192,563 for the Period (2020 - $77,840). Employees' salaries and benefits including share based compensation expensed for the Quarter and the Period totaled $360,855 (2020 - $231,305) and $946,876 (2020 - $907,112), respectively.

(2) These figures are net of the CEWS of $2,748 for the Quarter (2020 - $3,807) and $9,209 for the Period (2020 - $3,807), respectively.

## 12. Related Party Disclosures

Balances and transactions between the Company and its subsidiaries have been eliminated on consolidation and are not disclosed in this note. Details of the transactions between the Company and other related parties are disclosed below:

### *a) Trading transactions*

There has been no material trading transactions with related parties during each of the nine months ended May 31, 2021 and 2020.

### *b) Compensation of key management personnel*

The remuneration of directors and other key members of the Company's senior management team during each of the three and nine months ended May 31, 2021 and May 31, 2020 are as follows:

| | Three Months Ended | | Nine Months Ended | |
|---|---|---|---|---|
| | May 31, 2021 | May 31, 2020 | May 31, 2021 | May 31, 2020 |
| Salaries, benefits and directors' fees[(1)] | $ 309,061 | $ 275,266 | $ 888,380 | $ 930,307 |
| Share based compensation[(2)] | 142,401 | 24,979 | 176,618 | 57,213 |
| | $ 451,462 | $ 300,245 | $ 1,064,998 | $ 987,520 |

(1) Salaries and benefits of key management personnel capitalized to exploration and evaluation assets and PPE for the Quarter and for the Period totaled $21,048 (2020 - $45,228) and $57,939 (2020 - $188,765), respectively.

(2) Fair value of stock options, DSUs and RSUs earned and recognized as share based compensation during the respective reporting period.

## 13. Financial Instruments

IFRS 7 establishes a fair value hierarchy that reflects the significance of inputs used in making fair value measurements as follows:

| | |
|---|---|
| Level 1 | quoted prices in active markets for identical assets or liabilities; |
| Level 2 | inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e., as prices) or indirectly (i.e., from derived prices); and |
| Level 3 | inputs for the asset or liability that are not based upon observable market data. |

Assets are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. The fair values of the Company's warrants denominated in a currency that is not the functional currency of the Company and the warrants with exercise prices that are subject to adjustment from time to time are based on Level 2 inputs that are observable for the liability such as interest rate, dividend yield and historical volatility. The fair value of the Convertible Note Payable is based on Level 3 inputs including the applicable face value of the Note. The Company has the right to buy back the Note at any time for the outstanding face value, as such the fair value of the Note is the outstanding face value of the Note.

### *Fair Values*

Except as disclosed elsewhere in these condensed consolidated interim financial statements, the carrying amounts for the Company's financial instruments approximate their fair values because of the short-term nature of these items.

The Company's risk exposures and the impact on the Company's financial instruments are summarized below:

### *Credit risk*

The Company is not exposed to any significant credit risk as at May 31, 2021. The Company's cash and cash equivalents are either on deposit with a major Canadian Chartered banking group in Canada or invested in bankers' acceptance notes or guaranteed investment certificates issued by a major Canadian Chartered banking group. The Company's receivables primarily consist of Goods and Services Tax/Harmonized Sales Tax receivable, government grants and refundable security deposits with various federal and provincial governments and are therefore not subject to significant credit risk.

### *Liquidity risk*

Liquidity risk is the risk that an entity will not be able to meet its financial obligations as they come due. The Company has in place a planning and budgeting process to assist in determining the funds that are required to support the Company's normal operating requirements on an on-going basis and its plans for exploration and development expenditures. The Company ensures that there are sufficient funds to meet its short-term requirements, taking into account its anticipated cash flows from operations and its holdings of cash and cash equivalents.

As at May 31, 2021, the Company has current assets of $3,379,141 and current liabilities of $889,452. The Company's working capital as at May 31, 2021 was $2,489,928. Excluding the deferred flow-through share premium of $96,111, the Company's adjusted working capital as at May 31, 2021 was $2,586,039, (calculated by adding back the deferred flow-through share premium of $96,111 to the working capital of $2,489,928). As the de-recognition of the deferred flow-through share premium will not require the future out flow of resources by the Company, it is management's belief that the adjusted working capital figure provides useful information in assessing the Company's liquidity risk.

## 13. Financial Instruments (continued)

Repayments due by period as of May 31, 2021:

| | Within 1 Year | 1-3 Years | 4-5 Years | Over 5 Years | Total |
|---|---|---|---|---|---|
| Accounts payable and accrued liabilities | $ 603,748 | $ - | $ - | $ - | $ 603,748 |
| Convertible note payable | - | 3,420,000 | - | - | 3,420,000 |
| Lease obligation | 222,044 | 459,986 | 121,847 | - | 803,877 |
| | $ 825,792 | $ 3,879,986 | $ 121,847 | $ - | $ 4,827,625 |

### *Market risk*

i) Interest rate risk

The Company has cash and cash equivalents balances and it has no interest-bearing debt. The Company's current policy is to invest its excess cash in highly liquid money market investments such as bankers' acceptance notes, treasury bills and GICs. These short term money market investments are subject to interest rate fluctuations.

ii) Foreign currency risk

The Company's functional currency is the Canadian dollar. The majority of the Company's purchases are transacted in Canadian dollars. Other than the US$ Warrants as disclosed in Note 10c, the Company had no other significant financial assets or financial liabilities denominated in foreign currencies as at May 31, 2021.

iii) Price risk

The prices of metals and minerals fluctuate widely and are affected by many factors outside of the Company's control. The prices of metals and minerals and future expectation of such prices have a significant impact on the market sentiment for investment in mining and mineral exploration companies. This in turn may impact the Company's ability to raise equity financing for its long term working capital requirements.

### *Sensitivity analysis*

Considering the Company's budget expenditures for the balance of fiscal 2021 and its current cash and cash equivalents of $2,711,141, with other variables held constant, sensitivity to a plus or minus 25 basis points change in interest rates would not have any significant effect on the Company's net loss for the balance of fiscal 2021.

Other than the US$ Warrants as disclosed in Note 10c, the Company had no other significant financial assets or financial liabilities denominated in foreign currencies as at May 31, 2021, and its anticipated on-going expenditures to be transacted in US dollars for the next three month period is approximately US$50,000. If the Canadian dollar weakens (or strengthens) 5% against the US dollar with other variables held constant, it would not have any significant effect on the Company's expenditures over a three month period.

## 14. Supplemental Cash Flow Information

Non-cash financing and investing transactions not reflected in the Condensed Consolidated Interim Statements of Cash Flows for the three and nine months ended May 31, 2021 and 2020 are as follows:

| | Three Months Ended | | Nine Months Ended | |
|---|---|---|---|---|
| | May 31, 2021 | May 31, 2020 | May 31, 2021 | May 31, 2020 |
| Share based compensation capitalized as property, plant and equipment | $ 24 | $ 111 | $ 67 | $ 297 |
| Share based compensation capitalized as exploration and evaluation assets | 7,514 | 2,165 | 9,404 | 6,169 |
| Depreciation expense capitalized as exploration and evaluation assets | 548 | 1,949 | 1,644 | 5,847 |
| Property, plant and equipment acquired under lease arrangement | | - | - | 1,045,810 |
| Common shares issued for deposit on business acquisition (note 4d) | 219,200 | - | 219,200 | - |
| | $ 227,286 | $ 4,225 | $ 230,315 | $ 1,058,123 |

## 15. Events After the Reporting Period

Subsequent to end of the Period, the Company:

a) granted an aggregate of 700,000 stock options with a weighted exercise price of $0.20 per share to certain employees of the Company. The weighted average contract life of these options at issuance was 5.0 years;

b) issued 125,000 common shares pursuant to the exercise of 125,000 stock options with a weighted average exercise price of $0.08 per share;

c) issued 1,353,383 common shares pursuant to the conversion of $180,000 convertible note payable; and

d) had 6,466,513 warrants with an adjusted exercise price of US$0.5223 per share expire.