DIAMOND ESTATES WINES & SPIRITS INC.

MANAGEMENT DISCUSSION AND ANALYSIS

THREE MONTHS ENDED JUNE 30, 2023 AND 2022

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The following management discussion and analysis ("MD&A") of Diamond Estates Wines & Spirits Inc. ("Diamond" or "the Company") provides a review of corporate developments, results of operations and financial position for the three months ended June 30, 2023 and 2022 ("Q1 2024 and "Q1 2023" respectively). This discussion is prepared as of August 28, 2023 and should be read in conjunction with (i) the unaudited interim condensed consolidated financial statements and the accompanying notes for the three months ended June 30, 2023 and 2022, and (ii) both the audited consolidated financial statements and MD&A for the fiscal years ended March 31, 2023 and 2022. Additional information regarding Diamond is available on Diamond's SEDAR profile at www.sedar.com. The results reported in this MD&A have been prepared in accordance with International Financial Reporting Standards ("IFRS") and are presented in Canadian dollars, which is the Company's functional currency.

FORWARD-LOOKING STATEMENTS

This MD&A contains forward-looking statements. Forward-looking statements can often be identified by the use of words such as "plans", "expects" or "does not expect", "is expected", "estimates", "intends", "anticipates" or "does not anticipate", or "believes", or variations of such words and phrases or state that certain actions, events or results "may", "could", "would", "might" or "will" be taken, occur or be achieved. Forward-looking statements involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of the Company to be materially different from any future results, performance or achievements expressed or implied by the forward-looking statements. Actual results and developments are likely to differ, and may differ materially, from those expressed or implied by the forward-looking statements contained in this MD&A. Such forward-looking statements are based on a number of assumptions which may prove to be incorrect, including, but not limited to, the ability of the Company to obtain necessary financing, the economy generally, the Covid-19 pandemic, conditions in the target market of the Company, consumer interest in the services and products of the Company, competition and anticipated and unanticipated costs. Such statements could also be materially affected by environmental regulation, liquor regulation, taxation policies, competition, the lack of available and qualified personnel or management, stock market volatility and the ability to access sufficient capital from internal or external sources. Actual results, performance or achievement could differ materially from those expressed herein. While the Company anticipates that subsequent events and developments may cause its views to change, the Company specifically disclaims any obligation to update these forward-looking statements, except as required by applicable law. These forward-looking statements should not be relied upon as representing the Company's views as of any date subsequent to the date of this MD&A. Although the Company has attempted to identify important factors that could cause actual actions, events or results to differ materially from those described in forward-looking statements, there may be other factors that cause actions, events or results not to be as anticipated, estimated or intended. Readers should not place undue reliance on forward-looking statements. The factors identified above are not intended to represent a complete list of the factors that could affect the Company.

Detailed information on risks and uncertainties is provided in the "Uncertainties and Principal Risk Factors" section of the annual MD&A for the year ended March 31, 2023.

COMPANY OVERVIEW

Diamond Estates Wines and Spirits Inc. is a producer of high-quality wines and ciders as well as a sales agent for over 120 beverage alcohol brands across Canada. The Company operates five wineries, four in Ontario and one in British Columbia, that produce predominantly VQA wines under such well-known brand names as 20 Bees, Creekside, EastDell, Lakeview Cellars, Mindful, Queenston Mile, Shiny Apple Cider, Fresh, Proud Pour, Red Tractor, Seasons, Serenity, Persona and Backyard Vineyards.

Through its commercial division, Trajectory Beverage Partners, the Company is the sales agent for many leading international brands in all regions of the country as well as being a distributor in the western provinces. These recognizable brands include Josh wines from California, Fat Bastard, Meffre, and Pierre Chavin wines from France, Brimincourt Champagne from France, Merlet and Larsen Cognacs from France, Kaiken wines from Argentina, Blue Nun and Erben wines from Germany, Calabria Family Estate Wines from Australia, Saint Clair Family Estate Wines from New Zealand, Redemption Bourbon and Rye whiskies from the U.S., Gray Whale Gin from California, Storywood and Cofradia Tequilas from Mexico, Magnum Cream Liqueur from Scotland, Talamonti and Cielo wines from Italy, Catedral and Cabeca de Toiro wines from Portugal, Waterloo Beer & Radlers from Canada, Landshark Lager from the USA, Edinburgh Gin, Tamdhu, Glengoyne and Smokehead single-malt Scotch whiskies from Scotland, Islay Mist, Grand MacNish and Waterproof whiskies from Scotland, C. Mondavi & Family wines including C.K. Mondavi & Charles Krug from Napa, Wize Spirits and Hounds Vodka from Canada, Bols Vodka from Amsterdam, Koyle Family Wines from Chile and Pearse Lyons whiskies and gins from Ireland.

The Company's mission is to build lasting, mutually beneficial relationships with channel partners, growers, suppliers and employees. To meet this goal, the Company is undertaking significant investments in winemaking, brand marketing, sales programming, performance management and back-office infrastructure, including information systems which will support growth in an efficient, profitable manner. Based on its analysis of the market, the Company believes that the growth prospects for the domestic and import beverage alcohol markets in Canada are positive. The Company continues to be a participant in the export market and has been successfully expanding its focus beyond China. Canadian wines and particularly Icewine enjoy a premium product positioning with international consumers.

The Company is committed to achieving its sales objectives through its distribution network, which is focused on the provincial liquor boards, licensed restaurants and bars, grocery chains, Diamond's five retail locations, direct-to-consumer and export channels. This distribution network is supported by enhanced sales, marketing and promotional programs. To ensure the Company strives to maintain an adequate level of liquidity, including compliance with future debt covenants, the Company continues to maintain a strategic review process that engages in actions designed to reduce the cost structure, improve productivity and enhance future cash flow. In addition, the Company is also focused on maintaining on-going funding support from BMO, shareholders and non- strategic assets to fund future operations.

RECENT EVENTS AND Q1 2024 HIGHLIGHTS

- Revenue for Q1 2024 was $7.9 million, an increase of $0.4 million from $7.5 million in Q1 2023. The largest contribution to the increase in sales year-over-year came from the Winery division contributing $0.3 million and the Agency division contributed $0.1 million. The increase experienced at the Winery division came from $0.8 million in bulk wine sales at Backyard Vineyards and the moderate increase from the Agency came from several brands.
- Gross margin[1] for Q1 2024 was $2.9 million, a decrease of $0.1 million from $3.0 million in Q1 2023, while gross margin as a percentage of revenue was 36.8% for Q1 2024 compared to 40.3% in Q1 2023. The decline is gross is attributed to the Winery division which experienced a decrease in gross margins because of a significant one-time sale in bulk wine and a general increase in cost of goods across all channels. When accounting for the depletion of the EWG inventory, gross margins decreased by 10.2% from 46.6% in Q1 2023 to 36.4% in Q1 2024 and when removing the bulk wine sale gross margin decreases to 42.3% in Q1 2024.
- EBITDA[1] remained flat at negative $0.9 million in Q1 2024 relative to Q1 2023; however, when adjusting for the fair value of EWG inventories sold, Adjusted EBITDA[1] decreased from a negative $0.7 million in Q1 2023 to a negative $0.9 million in Q1 2024.
- On August 16, 2023, the Company entered into a non-binding term sheet which would consist of the issuance of 20 million common shares to a related company at an issuance price per share of $0.45. The related party would subscribe for the shares by paying approximately $8.25 million in cash, and converting the $750,000 loan detailed immediately below.
- On May 31, 2023, the Company's primary lender consented in writing to waive the Company's requirement to comply with the fixed charge coverage ratio "(FCCR") covenant for the rolling twelve month period ended June 30, 2023.
- On May 30, 2023, the Company received a loan of $750,000 from a related party.
- On June 29, 2022, the Canadian government announced the Wine Sector Support Program ("WSSP") to provide non-repayable grants to licensed Canadian wineries based on the production of bulk wine fermented in Canada from domestic and/or imported grapes. The Government has budgeted up to $166M over a two-year period and will review further annual funding in the near future. The Company had applied for this support program and received $1.5 million in Q4 2023.
- The Government of Canada has repealed the federal excise duty exemption of 100% Canadian wines effective June 30, 2022 and is subject to an excise tax of $0.69 per litre. As part of the transition provisions, any 100% Canadian wine packaged prior to June 30, 2022 could continue to be sold under the previous exemption. In the first quarter of fiscal 2024 there was a $0.2 million reduction in sales resulting from the repeal of the federal excise duty exemption.

[1] *See definition of selected terms under the heading "Non-IFRS Financial Measures" (see page 12)*

GOING CONCERN

The accompanying consolidated financial statements have been prepared using International Financial Reporting Standards ("IFRS") (as issued by the International Accounting Standard Board ("IASB")) applicable to a going concern.

Net loss and comprehensive loss for Q1 2024 was $2.5 million (Q1 2023 - $1.6 million). Additionally, the Company reported negative cash flow from operations (before changes in non-cash working capital) of $1.7 million in Q1 2024 (Q1 2023 - $1.0 million). As at June 30, 2023, the Company had an accumulated deficit of $24.5 million (March 31, 2023 - $22.1 million). As at June 30, 2023, the Company had a working capital deficiency of $3.7 million (March 31, 2023 - $8.0 million).

The operations and net loss for the rolling twelve-month period ended September 30, 2022 had resulted in the Company being in breach of its quarterly fixed charge covenant under the terms of its current credit agreement with Bank of Montreal ("BMO"), its primary lender. However, on October 24, 2022, the Company entered into an amendment for which the Company received a waiver on its fixed charge coverage ratio ("FCCR") covenant until March 31, 2023. On May 31, 2023, BMO consented in writing to waive the Company's requirement to comply with the FCCR covenant for the rolling twelve month period ended June 30, 2023. The Company has debt repayment requirements of $31.5 million over the next twelve months, including all its bank indebtedness that matures on January 2, 2024, the loan payable - related party, the current portion of its lease liabilities, and the principal amount of the debentures payable plus accrued interest due by November 2, 2023, as well as annual seasonal grape purchase commitments in the fall of 2023. These circumstances lend significant doubt as to the ability of the Company to continue as a going concern and, accordingly, the appropriateness ultimately of the use of accounting principles applicable to the going concern assumption.

In response to the recurring operating losses and negative cash flows from operating activities, the Company is taking a number of actions to enhance its financial flexibility, to meet its obligations and to fund its ongoing business operations, as evidenced by the restructured credit agreement and debenture financing arranged in November, 2022, the assets held for sale as of June 30, 2023 and the related party loan received in May, 2023 *(see further discussions in "Liquidity and Capital Resources" section below)* and the August, 2023 financing *(see further discussions in "Subsequent Events" section below)*. To ensure the Company maintains an adequate level of liquidity, including compliance with debt covenants, the Company continues to maintain a strategic review process that engages in actions designed to reduce the cost structure, improve productivity and enhance future cash flow.

The Company's ability to meet the covenant measurements under the terms of its credit agreements with its lenders is still dependent upon profitable commercial operations, divestiture of non-strategic assets, continued funding support from BMO and shareholders, and new equity and debt placements. However, there can be no assurance that management will be successful in this regard. These consolidated financial statements do not include any adjustments to the carrying value of assets or liabilities, to the recoverable amounts or the reported expenses and consolidated statement of financial position classifications that would be necessary if the going concern assumption were inappropriate, and these adjustments could be material.

QUARTERLY PERFORMANCE

The following table highlights certain key quarterly financial highlights. Commentary on the selected highlights is included under "Results of Operations" and "Liquidity and Capital Resources".

	Jun-2023 Q1 2024	Mar-2023 Q4 2023	Dec-2022 Q3 2023	Sep-2022 Q2 2023	Jun-2022 Q1 2023	Mar-2022 Q4 2022	Dec-2021 Q3 2022	Sep-2021 Q2 2022
	$	$	$	$	$	$	$	$
Balance sheet								
Working capital surplus (deficiency)	(3,745,468)	(7,983,033)	19,150,127	(2,842,434)	(1,920,390)	(696,908)	23,401,723	(1,641,158)
Term debt, lease liabilities and debentures payable	30,778,356	32,380,546	30,653,735	27,879,579	29,747,827	28,707,858	28,683,046	27,121,527
Total equity	19,909,461	22,890,793	26,526,485	27,588,963	28,811,355	30,313,267	33,431,936	17,135,698
Income statement								
Revenue	7,911,196	5,916,596	9,109,426	9,216,140	7,480,778	7,074,715	8,394,161	7,144,174
Gross margin	2,909,116	247,367	3,780,582	3,570,345	3,012,205	2,046,886	3,195,982	2,719,618
EBITDA	(925,361)	(2,878,434)	(220,846)	(443,814)	(921,920)	(1,601,211)	(325,714)	(208,338)
Adjusted EBITDA	(895,430)	(919,279)	(73,846)	(223,815)	(701,920)	(1,111,102)	(21,865)	(267,986)
Net income (loss)	(2,464,079)	(4,367,725)	(1,177,624)	(1,366,434)	(1,613,872)	(3,101,092)	2,017,681	(1,035,479)
Basic income (loss) per share	(0.09)	(0.16)	(0.04)	0.05	(0.06)	(0.11)	0.08	(0.04)

RESULTS OF OPERATIONS

	Q1 2024	Q1 2023
Revenue	$ 7,911,196	$ 7,480,778
Cost of sales	5,002,080	4,468,573
Gross margin	2,909,116	3,012,205
Gross margin (% of revenue)	36.8%	40.3%
Selling, general and administration expenses	3,834,477	3,934,125
SG&A expenses (% of revenue)	48.5%	52.6%
EBITDA	(925,361)	(921,920)
Interest and accretion	957,063	294,189
Depreciation and amortization	437,855	313,524
Financing costs	9,408	26,655
Loss from operations	(2,329,687)	(1,556,288)
Change in fair value of derivative liability	(82,681)	-
Gain on disposition of right-of-use assets	32,036	54,376
Share based compensation	(83,747)	(111,960)
Net loss and comprehensive loss	$ (2,464,079)	$ (1,613,872)

See definition of selected terms under the heading "Non-IFRS Financial Measures" (see page 12)

Revenue for Q1 2024 was $7.9 million, an increase of $0.4 million from $7.5 million in Q1 2023. The largest contribution to the increase in sales year-over-year came from the Winery division contributing $0.3 million and the Agency division contributed $0.1 million. The increase experienced at the Winery division came from $0.8 million in bulk wine sales at Backyard Vineyards and the moderate increase from the Agency came from several brands. There continued to be softness experienced in the export market when comparing Q1 to the prior year with revenue remaining constant at $0.1 million. The Winery division also incurred approximately $0.2 million in excise taxes for the quarter

Gross margin for Q1 2024 was $2.9 million, a decrease of $0.1 million from $3.0 million in Q1 2023, while gross margin as a percentage of revenue was 36.8% for Q1 2024 compared to 40.3% in Q1 2023. The decline is gross is attributed to the Winery division which experienced a decrease in gross margins from 41.3% in Q1 2023 to 35.8% in Q1 2024 because of a significant one-time sale in bulk wine and a general increase in cost of goods across all channels. When accounting for the depletion of the EWG inventory, gross margins decreased by 10.2% from 46.6% in Q1 2023 to 36.4% in Q1 2024, and when removing the bulk wine sale gross margin decreases to 42.3% in Q1 2024. The gross margins at the Agency was consistent year over year at $1.3 million, but decreased as a percentage of sales from 39.0% in Q1 2023 to 38.1% in Q1 2024.

Total SG&A expenses for Q1 2024 were $3.8 million, a decrease of $0.1 million from $3.9 million in Q1 2023. Employee compensation remained constituent at approximately $1.8 million and decreased as a percentage of sales from 24.2% in Q1 2023 to 23.5% in Q1 2024. General and administrative expenses remained flat year over year at $1.9 million and decrease as a percentage of sales from 14.6% in Q1 2023 to 13.7% in Q1 2024. The remainder of the change is mostly attributable to (i) a decrease in advertising and promotion of $0.2 million and (ii) an increase in delivery and warehousing expense of $0.1 million.

Interest expense for Q1 2024 was $1.0 million, an increase of $0.7 million compared to $0.3 million in Q1 2023. The increase is a result of increase in year-over-year interest rates since Q1 2023 and the addition of the $4.9 million of convertible debentures issued in November 2022. Depreciation and amortization expense for Q1 2024 was $0.4 million compared to $0.3 million in Q1 2023.

EBITDA remained flat at negative $0.9 million in Q1 2024 relative to Q1 2023; however, when adjusting for the fair value of EWG inventories sold, adjusted EDITDA decreased from a negative $0.7 million in Q1 2023 to a negative $0.9 million in Q1 2024.

Loss from operations for Q1 2024 was $2.3 million compared to $1.6 million in Q1 2023, a decrease in profitability of $0.7 million. The lower level of profitability is a direct result of the increase in interest expense year over year. The net loss and comprehensive loss further decreases by $0.9 million from a negative $1.6 million to $2.5 million mostly due to the change in fair value of derivative liability of $0.1 million.

LIQUIDITY AND CAPITAL RESOURCES

	June 30, 2023	June 30, 2023	June 30, 2023	March 31, 2023
ASSETS	As reported	Assets held for sale	Adjusted	
Accounts receivable	$ 3,670,064	$ 36,832	$ 3,706,896	$ 3,159,280
Inventory	21,289,455	3,464,124	24,753,579	26,289,426
Prepaid expenses	501,708	59,498	561,206	341,667
Asset held for resale	10,736,020	(10,736,020)	-	-
Biological assets	184,785	-	184,785	-
Total current assets	36,382,032	(7,175,566)	29,206,466	29,790,373
Property, plant and equipment	18,804,470	6,082,044	24,886,514	25,141,085
Right of use assets	1,635,008	896,984	2,531,992	2,554,677
Intangible assets	4,187,976	196,538	4,384,514	4,483,318
Total assets	$ 61,009,486	$ -	$ 61,009,486	$ 61,969,453
LIABILITIES				
Accounts payable and accrued liabilities	$ 7,491,982	$ 402,151	$ 7,894,133	$ 6,708,787
Loan payable - related party	750,000	-	750,000	-
Current portion of term loans payable and lease liabilities	25,232,760	128,858	25,361,618	26,115,050
Debentures payable	4,573,071	-	4,573,071	4,359,242
Derivative liability	673,008	-	673,008	590,327
Liabilities held for sale	1,406,679	(1,406,679)	-	-
Total current liabilities	40,127,500	(875,670)	39,251,830	37,773,406
Lease liabilities, net of current portion	972,525	875,670	1,848,195	1,906,254
Total liabilities	41,100,025	-	41,100,025	39,679,660
SHAREHOLDERS' EQUITY	19,909,461	-	19,909,461	22,289,793
	$ 61,009,486	$ -	$ 61,009,486	$ 61,969,453

The Company has modified the presentation of the statement of financial position as at June 30, 2023 to also include columns to allocate the assets held for sale back to their equivalent presentation as at March 31, 2023. This is presented as a supplementary non-IFRS financial measure to provide users with more meaningful comparative balances and to better illustrate the impact on working capital of the reclassification of assets held for sale.

Liquidity risk is the risk that the Company may encounter difficulty in meeting the obligations associated with its financial liabilities that are settled by delivering cash or another financial asset. The Company's approach to managing liquidity is to ensure, as far as possible, that it will have sufficient liquidity to meet its liabilities when due, under both normal and stress conditions, without incurring unacceptable losses or damage to the Company's reputation. To ensure the Company maintains an adequate level of liquidity, including compliance with debt covenants, the Company maintains a strategic review process that engages in actions designed to reduce the cost structure, improve productivity and enhance future cash flow *(see further discussion in "Going Concern" section above)*;

The working capital deficiency decreased by $4.3 million to negative $3.7 million as at June 30, 2023 from negative $8.0 million as at June 30, 2023, significantly impacted by the reclassification of (net) assets held for sale *(see further discussion below)*. The operations and net loss for the rolling twelve-month period ended September 30, 2022 had resulted in the Company being in breach of its quarterly fixed charge covenant under the terms of its current credit agreement with BMO. However, on October 24, 2022 the Company entered into an amendment for which the Company received a waiver on its fixed charge covenant until March 31, 2023. As the banking agreement expires on January 2, 2024, all term loans payable have been classified as current as of June 30, 2023. On May 31, 2023, BMO consented in writing to waive the Company's requirement to comply with the fixed charge coverage ratio "(FCCR") covenant for the rolling twelve month period ended June 30, 2023.

As at June 30, 2023, the Company has classified certain winery division properties and related operating assets detailed below totalling $9,329,341 as assets held for sale. Management intends to sell these assets within one year of the reporting date. They have commenced an active process to sell these assets, but no agreements of purchase and sale have been entered into as of the date of release of these unaudited interim condensed consolidated financial statements.

Assets held for sale	
Accounts receivable	**$ 36,832**
Inventory	**3,464,124**
Prepaid expenses	**59,498**
Property, plant and equipment	**6,082,044**
Right-of-use assets	**896,984**
Intangible assets	**196,538**
	10,736,020
Liabilities held for sale	
Accounts payable and accrued liability	**402,151**
Lease liability	**1,004,528**
	1,406,679
Net assets held for resale	**$ 9,329,341**

Accounts receivable of $3.7 million as at June 30, 2023 increased by $0.5 million from $3.2 million as at March 31, 2023 as a result an increase in trade receivables.

The inventory balance was $24.8 million as at June 30, 2023, a decrease of $1.5 million from $26.3 million as at March 31, 2023. Bulk wine decreased by $1.4 million from $14.2 million as at March 31, 2023 to $12.8 as at June 30, 2023 million. The decrease was attributable to the significant one-time sale of bulk wine at Backyard Vineyards of approximately $0.7 million and bottlings throughout the period. Finished Goods increased by $1.0 million because of the rate of sales being lower than the rate of bottlings throughout the quarter.

Property, plant and equipment of $24.9 million as at June 30, 2023 decreased by $0.2 million from $25.1 million as at March 31, 2023 due to depreciation taken in the quarter. Right-of-use assets of $2.5 million as at June 30, 2023 remained consistent compared to March 31, 2023, with additions of $0.1 million offset by depreciation of $0.1 million taken in Q1 2024. Intangible assets of $4.4 million as at June 30, 2023 decreased by $0.1 million from $4.5 million as at June 30, 2023 due to depreciation taken during Q1 2024.

Accounts payable and accrued liabilities of $7.9 million as at June 30, 2023 increased by $1.2 million from $6.7 million as at June 30, 2023 as a result of a similar increase in trade account payable.

The BMO credit facilities are governed under the terms of the SARCA and include the BCAP term loan, an existing non-revolving term loan, a revolving operating line, the total of which was $24.9 million as at June 30, 2023, a decrease of $0.8 million from $25.7 million as at June 30, 2023. The decrease resulted from (i) repayments on the non-revolving term loans of $0.3 million and (ii) an increase in utilization of the revolving term loan of $0.5 million.

On October 24, 2022, the Company entered into a further amendment to its SARCA, the major terms of which are outlined below:

Credit limits: The credit limits remained unchanged (i) the revolving term loan of $14.4 million with an accordion feature to fund future growth, and (ii) the non-revolving term loan of $10.8 million.
Maturity dates: The maturity dates remained unchanged with the revolving and non-revolving facilities having a two-year term expiring as at January 2, 2024, including the Business Credit Availability Program ("BCAP") facility.
Interest rates: Under the current amendment, the interest rate increased by 1.00% on each component of the facility as follows:

- prime plus 2.40% under the revolving term facility;
- prime plus 2.65% under the non-revolving term facility; and
- prime plus 2.65% under the BCAP Facility.

Repayment: The repayment terms remained unchanged (i) the non-revolving term loan is repayable in 80 quarterly principal payments of 1.25% of the drawn amount, or $135,000, and (ii) the BCAP loan is repayable in monthly principal payments of $57,292.

Covenants: The Amendment is subject to compliance to the following additional covenants:

- the leverage ratio shall not be less than or equal to 2.00 to 1 for every calendar month and fiscal quarter
- the Company will not permit its forecasted or actual liquidity (as defined under the SARCA) to be less than $Nil.

The adjusted SARCA is still subject to the following major covenants:

- leverage ratio at less than or equal to 2.15 to 1; and
- fixed charges coverage ratio at greater than or equal to 1.25 to 1.

On November 2, 2022, the Company completed a non-brokered private placement of $4.884 million of 10.0% unsecured convertible debentures of the Company. The Company intends to use the net proceeds of the placement for general working capital and investment purposes. Certain insiders of the Company, including Lassonde and a related company controlled by its chairman, subscribed for $3.35 million of the total placement. The debentures mature one year from their date of issuance, being November 2, 2023, unless the holder requests to accelerate the maturity date in the event the Company completes an equity financing within the next 12 months. The debentures are convertible at the holder's option into common shares of the Company from the date of issuance until the maturity date at a conversion price of $0.80. If repayment of the debentures on the maturity date would constitute non-compliance by the Company under its senior borrowing obligations, the holder has the option to convert at the conversion price, or to roll the obligations over into new one-year debentures, on similar terms to be negotiated, subject to TSXV approval.

The convertible debentures have been accounted for as a compound financial instrument under IAS 32 - Financial Instruments, and have both a liability and an embedded derivative component. The convertible debentures were initially recognized on November 2, 2022 with a fair value of $4,884,000 less transaction costs of $77,949 less the fair value of the embedded derivative of $775,591. After recording interest accretion on the debenture payable of $328,782, the carrying value of the debenture as at March 31, 2023 was $4,359,242. After recording further interest accretion on the debenture payable for the three months ended June 30, 2023 of $213,829, the carrying value of the debenture as at June 30, 2023 was $4,573,071. Coupon interest on the debentures in the amount of $121,765 was accrued for the three months ended June 30, 2023, such that a total of $321,140 has been accrued and is included in accounts payable and accrued liabilities at June 30, 2023.

The fair value of the embedded derivative as at June 30, 2023 of $- has increased by $- compared to the fair value as at March 31, 2023 of $-, with the change being recognized as an expense during the three months ended June 30, 2023.

The following table outlines the Company's contractual obligations as at June 30, 2023:

	<1 year	**2-3 years**	**4-5 years**	**>5 years**	**Total**
			$ (000's)		
Accounts payable and accrued liabilities	7,894	-	-	-	7,894
Term loans payable	24,890	-	-	-	24,890
Lease liabilities	471	783	523	601	2,378
Debentures payable	5,372	-	-	-	5,372
Purchase contracts for grapes, packaging and other raw materials	3,654	3,654	-	-	7,308
Total contractual obligations	42,281	4,437	523	601	47,842

The Company's debt to equity ratio increased to 1.67:1 as at June 30, 2023 from 1.48:1 as at June 30, 2023, where debt is defined as total liabilities less accounts payable and accrued liabilities, and equity is defined as shareholders' equity. This increase is due to the loan payable - related party and the loss incurred for Q1 2024.

SUBSEQUENT EVENTS

Financing

On August 16, 2023, the Company entered into a non-binding term sheet (the "Financing") with a related party which would consist of the issuance of 20 million common shares at an issuance price per share of $0.45. The related party would subscribe for the shares by paying approximately $8.25 million in cash, and converting the $750,000 principal amount (plus interest) owing under the advance agreement between the Company and Lassonde and the related party dated May 30, 2023. The Company intends to use the net proceeds of the Financing to reduce long-term debt and for general working capital and transactional expenses. Concurrently or immediately following the Financing, the related party may elect to convert up to all of the $3.35 million aggregate principal amount of 10.0% unsecured convertible debentures of the Company due November 2023 (together with accrued and unpaid interests thereon) into common shares, at the same conversion price as the issuance price of the common share being issued pursuant to the Financing.

The closing of the Financing is subject to customary shareholder and regulatory approvals.

Supplier

On August 22, 2023 the Company received notification from its largest supplier of import wines that its contract will expire on October 1, 2023 and is not being renewed. As of March 31, 2023, this supplier represented $9.1 million in revenue and $3.1 million in gross margin. The Company is still assessing the impact to its profits in the agency division as well as any mitigating actions that may be undertaken.

CAPITALIZATION

The Company has common shares and other equity instruments outstanding at each reporting date as follows:

	June 30, 2023	June 30, 2023	Change in reporting period
Common shares	27,875,978	27,875,978	-
Stock options	1,735,000	1,735,000	-
Deferred share units	814,758	528,778	285,980
Warrants	5,555,905	5,555,905	-
Total equity instruments	35,981,641	35,695,661	285,980

There were no issuances, exercises or expiries of common shares, options or warrants during Q1 2024. In May, 2023, the Company issued an aggregate of 285,980 DSUs in settlement of $100,093 of previously accrued deferred directors compensation. In July, 2023, the Company issued a further 98,177 DSUs valued at $47,125.

NON-IFRS FINANCIAL MEASURES

Management uses net loss and comprehensive loss as presented in the unaudited interim condensed consolidated statements of net loss and comprehensive loss as well as "gross margin", "EBITDA" and "Adjusted EBITDA" as a measure to assess performance of the Company. The Company defines "gross margin" as gross profit excluding depreciation. EBITDA and "Adjusted EBITDA" are other financial measures and are reconciled to net loss and comprehensive loss below under "Results of Operations".

Gross margin, EBITDA and Adjusted EBITDA are supplemental financial measures to further assist readers in assessing the Company's ability to generate income from operations before considering the Company's financing decisions, depreciation of property, plant and equipment and amortization of intangible assets. EBITDA comprises gross margin less operating costs before financial expenses, depreciation and amortization, non-cash expenses such as share-based compensation, one-time and other unusual items, and income tax. Adjusted EBITDA comprises EBITDA before non-recurring expenses including cost of sales adjustments related to inventory acquired in business combinations, EWG transaction costs expensed, government funding under CEWS and CERS programs, and other non-recurring adjustments included in the calculation of EBITDA. Gross margin is defined as gross profit excluding depreciation on property, plant and equipment used in production. Operating expenses exclude interest, depreciation on property, plant and equipment used in selling and administration, and amortization of intangible assets.

EBITDA does not represent the actual cash provided by the operating activities nor is it a recognized measure of financial performance under IFRS. Readers are cautioned that this measure should not be considered as a replacement for those as per the consolidated financial statements prepared under IFRS. The Company's definitions of this non-IFRS financial measure may differ from those used by other companies.

The Company calculates gross margin as follows:

	Q1 2024 $	Q1 2023 $
Revenue	**7,911,196**	7,480,778
Cost of sales		
Change in inventories of finished goods and raw materials consumed	**5,002,080**	4,468,573
Depreciation	**161,701**	43,033
Gross profit	**2,747,415**	2,969,172
Exclude depreciation	**161,701**	43,033
Gross margin	**2,909,116**	3,012,205
Gross margin (% of revenue)	**36.8%**	40.3%

The Company calculates EBITDA and Adjusted EBITDA as follows:

	Q1 2024 $	Q1 2023 $
Net loss for period	**(2,464,079)**	(1,613,872)
Interest and accretion	**957,063**	294,189
Financing costs	**9,408**	26,655
Share-based compensation	**83,747**	111,960
Depreciation and amortization	**437,855**	313,524
Change in fair value of derivative liability	**82,681**	-
Gain on disposition of right-of-use assets	**(32,036)**	(54,376)
Recovery of deferred income taxes	**-**	-
EBITDA	**(925,361)**	(921,920)
Cost of goods sold adjustments for fair value of EWG inventories sold	**29,931**	220,000
Adjusted EBITDA	**(895,430)**	(701,920)

STRATEGIC OUTLOOK AND DIRECTION

Diamond is committed to building enduring, high quality beverage alcohol brands that enhance life enjoyment in a socially responsible manner. The Company believes in the development of leading brands that recognize consumers' interests in wine, beer, cider and ready-to-drink beverages and spirits, while addressing their desire to explore many of the Company's exciting offerings. The Company has also added a low alcohol brand Mindful, to its domestic portfolio in addition to low alcohol and no-alcohol beer and wine suppliers to its import portfolio, reflecting consumer interest and demand in those categories. Vertically integrated, Diamond combines modern and efficient production facilities for its Niagara and B.C. wines with a national marketing agency for its broad portfolio of leading international wines and spirits. The Company is well positioned to add to its throughput of wine production and leverage its national sales force to drive growth from existing brands and support new brands secured by the agency without material change to its cost structure.

Over the past three years, the Covid-19 pandemic has had a material impact on the global economy. In the spring of 2023, the pandemic impact has eased significantly and consumers have returned to more normal shopping and consumption behaviour. We anticipate the impact of Covid to continue to ease, but also expect that some volatility will continue both domestically and around the world. We also expect to see continued supply chain challenges, pressure on staffing and recent record setting inflation – further fuelled by the conflict in Ukraine.

We are seeing a return to more normal sales channel development with the return of the on-premise (restaurant and bars) business to near pre Covid levels, the partial return of business to our winery retail stores and significantly improved export sales as countries around the world re-open to import wines and consumers get back to entertaining and dining out. Interest in and appreciation of Canadian Icewine and table wines remains high. Our company continues to successfully expand distribution into several new jurisdictions including Finland, USA, Thailand, Singapore, Vietnam and Taiwan.

Consumers discovered on-line shopping for wine and beer during the pandemic and we see this as a very positive development for our business. This channel is more profitable given tax treatment of direct sales and it allows a more controlled retail interaction with our customers. This provides an additional way to build enduring brand relationships and to turn a first interaction at one of our wineries into an ongoing dialogue and purchasing behaviour. It also provides us with greater ability to manage our inventories as we control what we promote.

The retail modernization of the sale of beverage alcohol in Ontario continues to be a high priority for the provincial government. To date, the government has issued 450 beer licenses and 226 wine licenses to Ontario grocers and has reiterated its commitment to allowing the sale of beer and wine in grocery, big-box and convenience stores during their current mandate, which began in June, 2022. There is an active debate within the beverage alcohol industry and government on how best to influence this modernization program to the benefit of all stakeholders.

Lastly, in response to the recurring operating losses and negative cash flows from operating activities, the Company is taking a number of actions to enhance its financial flexibility, return to profitable commercial operations, divestiture of non-strategic assets, continued funding support from BMO and shareholders, and new equity and debt placements.

RECENTLY ADOPTED AND ISSUED ACCOUNTING PRONOUNCEMENTS

IAS 12 "Income Taxes"

This standard has been amended to require companies to recognize deferred tax on transactions that, on initial recognition, give rise to equal amounts of taxable and deductible temporary differences. The amendments are effective for annual reporting periods beginning on or after January 1, 2023. The Company has not yet assessed the impact of this amendment on the unaudited interim condensed consolidated financial statements.

IAS 1, "Presentation of Financial Statements"

This standard has been amended to clarify the classification of liabilities as current or non-current depending on the rights that exist at the end of the reporting period. Classification is unaffected by the expectations of the entity or events after the reporting date. The amendment also clarifies the meaning of settlement of a liability. This amendment is effective for annual periods beginning on or after January 1, 2023. The standard has also been amended to specify that covenants to be complied with after the reporting date do not affect the classification of debt as current or non-current at the reporting date. Instead, the amendments require a company to disclose information about these covenants in the notes to the financial statements. The amendment are effective for annual reporting periods beginning on or after January 1, 2024, with early adoption permitted. The Company has not yet assessed the impact of this amendment on unaudited interim condensed consolidated financial statements.