The Second Cup Ltd.

Unaudited Condensed Interim Financial Statements

For the 13 and 39 weeks ended September 30, 2017 and September 24, 2016

Notice to Reader

The management of The Second Cup Ltd. ("Second Cup" or the "Company") is responsible for the preparation of the accompanying condensed interim financial statements. The condensed interim financial statements have been prepared in accordance with International Financial Reporting Standards and are considered by management to present fairly the financial position, financial performance and cash flows of Second Cup.

These condensed interim financial statements have not been reviewed by an auditor. These condensed interim financial statements are unaudited and include all adjustments, consisting of normal and recurring items that management considers necessary for a fair presentation of the financial position, financial performance and cash flows.

(Signed)

Garry Macdonald
Interim President and Chief Executive Officer, The Second Cup Ltd.

(Signed)

Ba Linh Le
Chief Financial Officer, The Second Cup Ltd.

November 2, 2017

The Second Cup Ltd.

Condensed Interim Statements of Financial Position

(Unaudited, expressed in thousands of Canadian dollars)

	September 30, 2017	December 31, 2016
ASSETS		
Current assets		
Cash and cash equivalents	$ 3,264	$ 3,004
Restricted cash (note 11)	1,592	1,947
Trade and other receivables	2,529	3,023
Notes and leases receivable	60	139
Inventories	136	200
Prepaid expenses and other assets	133	251
Income tax receivable	-	532
	7,714	9,096
Non-current assets		
Notes and leases receivable	98	173
Property and equipment	2,362	3,434
Intangible assets	32,457	32,611
Total assets	$ 42,631	$ 45,314
LIABILITIES		
Current liabilities		
Accounts payable and accrued liabilities	$ 3,817	$ 3,700
Provisions	1,025	1,598
Other liabilities	239	217
Gift card liability	2,768	3,484
Deposits from franchisees	935	1,243
	8,784	10,242
Non-current liabilities		
Provisions	291	530
Other liabilities	188	267
Long-term debt (note 5)	-	7,181
Deferred income taxes	3,376	3,818
Total liabilities	12,639	22,038
SHAREHOLDERS' EQUITY	29,992	23,276
Total liabilities and shareholders' equity	$ 42,631	$ 45,314

Contingencies, commitments and guarantees (note 12).
See accompanying notes to the unaudited condensed interim financial statements.

Approved by the Directors on November 2, 2017

Michael Bregman, Director Rael Merson, Director

The Second Cup Ltd.

Condensed Interim Statements of Loss and Comprehensive Loss

(Unaudited, expressed in thousands of Canadian dollars, except per share amounts)

	13 weeks ended		39 weeks ended	
	September 30, 2017	**September 24, 2016**	**September 30, 2017**	**September 24, 2016**
Revenue (note 6)				
Company-owned cafés and product sales	$ 1,692	$ 3,629	$ 6,849	$ 11,453
Franchise revenue	3,647	4,027	10,702	11,398
	5,339	7,656	17,551	22,851
Operating costs and expenses (note 7)				
Company-owned cafés and cost of product sales	1,902	3,857	7,531	12,272
Franchise	1,131	1,888	4,023	6,097
General and administrative	1,504	1,403	4,803	4,276
Loss/(gain) on disposal of assets	(3)	151	99	309
Depreciation and amortization	369	382	1,112	1,183
	4,903	7,681	17,568	24,137
Income/(loss) from operations	436	(25)	(17)	(1,286)
Interest and financing costs (notes 5, 8)	3,394	62	3,902	159
Loss before income taxes	(2,958)	(87)	(3,919)	(1,445)
Income taxes	4	(12)	(167)	(323)
Net loss and comprehensive loss for the period	$ (2,962)	$ (75)	$ (3,752)	$ (1,122)
Basic and diluted loss per share (note 9)	$ (0.19)	$ (0.01)	$ (0.28)	$ (0.09)

See accompanying notes to the unaudited condensed interim financial statements.

The Second Cup Ltd.

Condensed Interim Statements of Changes in Shareholders' Equity

(Unaudited, expressed in thousands of Canadian dollars)

	Share Capital	Warrants	Contributed Surplus	Retained Earnings (Deficit)	Total
Balance - December 26, 2015	$ 8,652	$ -	$ 61,736	$ (46,462)	$ 23,927
Net loss for the period	-	-	-	(1,122)	(1,122)
Stock option plan expense	-	-	49	-	49
Balance - September 24, 2016	$ 8,652	$ -	$ 61,785	$ (47,584)	$ 22,854
Balance - December 31, 2016	$ 8,652	$ 271	$ 61,789	$ (47,436)	$ 23,276
Net loss for the period	-	-	-	(3,752)	(3,752)
Stock option plan expense	-	-	(45)	-	(45)
Warrants (note 5)	-	(106)	-	-	(106)
Shares issued (note 5)	10,619	-	-	-	10,619
Balance - September 30, 2017	$ 19,271	$ 165	$ 61,744	$ (51,188)	$ 29,992

See accompanying notes to the unaudited condensed interim financial statements.

The Second Cup Ltd.

Condensed Interim Statements of Cash Flows

(Unaudited, expressed in thousands of Canadian dollars)

	13 weeks ended		39 weeks ended	
	September 30, 2017	September 24, 2016	September 30, 2017	September 24, 2016
CASH PROVIDED BY (USED IN)				
Operating activities				
Net loss for the period	$ (2,962)	$ (75)	$ (3,752)	$ (1,122)
Items not involving cash				
Depreciation of property and equipment	243	287	774	894
Amortization of intangible assets	114	101	338	306
Share-based compensation expense	(4)	17	(45)	49
Deferred income taxes	(108)	(12)	(366)	(323)
Loss on disposal of capital related items	(4)	151	99	309
Fair value difference on shares issued and other costs (note 5)	3,290	-	3,290	-
Change in fair value of interest rate swap	-	(18)	-	(59)
Changes in non-cash working capital & other (note 10)	(54)	(186)	(59)	(809)
Cash provided by (used in) operating activities	515	265	279	(755)
Investing activities				
Proceeds from disposal of capital related items	59	31	384	113
Cash payments for capital expenditures (note 10)	(74)	(88)	(200)	(292)
Cash payments for intangible assets (note 10)	(31)	(62)	(184)	(276)
Notes receivable repayment	26	38	154	90
Cash provided by (used in) investing activities	(20)	(81)	154	(365)
Financing activities				
Transaction costs	(141)	-	(173)	-
Cash used in financing activities	(141)	-	(173)	-
Increase (decrease) in cash and cash equivalents during the period	354	184	260	(1,120)
Cash and cash equivalents - Beginning of the period	2,910	1,776	3,004	3,080
Cash and cash equivalents - End of the period	$ 3,264	$ 1,960	$ 3,264	$ 1,960

See accompanying notes to the unaudited condensed interim financial statements.
Supplemental cash flow information is provided in note 10.

(Unaudited, expressed in thousands of Canadian dollars, except per share amounts)

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1. Organization and nature of business

The Second Cup Ltd. (the “Company”) is a Canadian specialty coffee retailer with 289 cafés operating under the trade name, Second Cup™, in Canada, of which 15 are Company-operated and the balance are operated by franchisees.

Second Cup owns the trademarks, trade names, operating procedures and systems and other intellectual property used in connection with the operation of Second Cup cafés in Canada.

Second Cup was incorporated under the Business Corporations Act (Ontario) in 2011 and is domiciled in Canada. The address of its registered office is 6303 Airport Road, 2nd Floor, Mississauga, Ontario, L4V 1R8. The Company hereinafter refers to its head office activities as “Coffee Central”. The Company’s website is www.secondcup.com. The common shares of the Company are listed on the Toronto Stock Exchange under the symbol “SCU”.

2. Summary of significant accounting policies

a. Basis of preparation

These unaudited condensed interim financial statements for the 13 and 39 weeks ended September 30, 2017 and September 24, 2016 have been prepared in accordance with International Financial Reporting Standards ("IFRS"), as applicable to condensed interim financial reports including International Accounting Standard (IAS) 34, Interim Financial Reporting ("IAS 34"), and should be read in conjunction with the Company's audited annual financial statements for the year ended December 31, 2016, which have been prepared in accordance with IFRS, as issued by the International Accounting Standards Board ("IASB").

The accounting policies applied in these unaudited condensed interim financial statements are consistent with those of the previous financial year. The accounting policies are based on IFRS issued and outstanding as at November 2, 2017, the date the Board of Directors approved the unaudited condensed interim financial statements.

Second Cup's fiscal year is such that each quarter will consist of 13 weeks and will end on the Saturday closest to the calendar quarter end. The fiscal year is made up of 52 or 53-week periods ending on the last Saturday of December. Fiscal 2017 is a 52-week period (2016 – 53-week period).

b. Segmented information and reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the Chief Executive Officer. The Company substantially operates and is managed as one reportable segment. Operating revenues are comprised of royalties, the sale of goods from Company-operated cafés, the sale of goods through retail and other ancillary channels, and other service fees.

c. Reclassification

Certain comparable figures have been reclassified to conform to the current period's financial statement presentation. The change in the restricted cash balance in the previous year cash flow has been reclassified from investing activities to operating activities. This reclassification has been made to enhance the presentation of the company's activities and the financial statements.

3. Changes in accounting policies

The accounting policies adopted in the preparation of these unaudited condensed interim financial statements are consistent with those followed in the preparation of the Company's audited financial statements for the year ended December 31, 2016.

In May 2014, the IASB issued IFRS 15, a new comprehensive model for entities to use accounting for revenue arising from contracts with customers. In September 2015, the IASB deferred adoption of the new standard by one year. Several updates have been issued since to clarify the implementation guidance. The new guidance supersedes the most current revenue recognition guidance, including industry-specific guidance, enhances revenue recognition disclosures, and is now effective commencing in 2018. The guidance allows for either a full retrospective or modified retrospective transition method. We currently expect to apply the modified retrospective transition method.

We are performing a preliminary analysis of the impact of the new revenue recognition guidance and are developing a comprehensive plan for implementation. The project plan includes analyzing the impact on our current revenue streams, comparing our historical accounting policies to the new guidance, and identifying potential differences from applying the requirements of the new guidance to our contracts. Under current accounting guidance, we recognize initial franchise fees when we have performed all material obligations and services, which generally occurs when the franchised café opens. As required under the new guidance, we anticipate deferring the initial franchise fees and recognizing revenue over the term of the related franchise agreement.

We anticipate that the new guidance will also change our reporting of the Co-op Fund contributions from franchisees and the related advertising and promotional expenditures, which are currently reported on a net basis in our Statements of Financial Position. Under the new guidance, Co-op Fund contributions from franchisees and advertising and promotional expenditures will be reported on a gross basis.

In addition, we anticipate that the estimated breakage income on gift cards will be recognized as gift cards are utilized instead of our current policy of recognizing on a pro rata basis based on historical gift card redemption patterns.

We do not believe this guidance will materially impact our recognition of revenue from Company-owned cafes and product sales or our recognition of franchise revenue.

In January 2016, the IASB issued an amendment to IAS 7, Statement of Cash Flows ("IAS 7"). The amendment requires an entity to provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes. Other than the aforementioned additional disclosures, which will be included in the 2017 annual financial statements, the application of the amendments to IAS 7 did not result in any changes to the presentation of the unaudited condensed interim statements of cash flows.

In February 2016, the IASB issued an amendment to IAS 12, Income Taxes – Deferred Tax. The amendment clarifies the requirements for recognizing deferred tax assets on unrealized losses. Further, the amendment clarifies the accounting for deferred tax where an asset is measured at fair value and that fair value is below the asset's tax base. Certain other aspects of accounting for deferred tax assets are also clarified. The adoption of this standard had no impact on the unaudited condensed interim financial statements.

(Unaudited, expressed in thousands of Canadian dollars, except per share amounts)

4. Provisions

Provisions for café leases are estimates for costs to be incurred by the Company as a result of closure of cafés and franchisee failure to make payment of occupancy costs.

An expense of $122 (September 24, 2016 – expense of $430) was recognized in the 39 weeks ended September 30, 2017 and was reflected in the franchise operating costs and expenses line on the unaudited condensed interim statements of loss and comprehensive loss.

5. Long-term debt

	September 30, 2017	December 31, 2016
Face value of borrowings	$ -	$ 8,000
Unamortized transaction costs	-	(819)
	$ -	$ 7,181

On August 10, 2017, the Company issued 4,210,528 common shares and 300,000 warrants of Second Cup to the four shareholders of SPE Finance LLC (SPE), an affiliate of Serruya Private Equity. The Company also extinguished its $8,000 debt to SPE and cancelled 600,000 of old warrants. These transactions resulted in one-time, non-cash financing charges of $3,290. These charges consist of the difference between the share price of $2.60 on the issuance date and the agreed-to share price of $1.90, and the write-off of the unamortized portion of deferred transaction costs related to the debt.

6. Revenue

	13 weeks ended		39 weeks ended	
	September 30, 2017	September 24, 2016	September 30, 2017	September 24, 2016
Franchise Revenue				
Royalties	$ 2,499	$ 2,428	$ 7,489	$ 7,446
Services and other	1,148	1,599	3,213	3,952
	3,647	4,027	10,702	11,398
Company-owned cafés and product sales	1,692	3,629	6,849	11,453
	$ 5,339	$ 7,656	$ 17,551	$ 22,851

Royalties
Royalty revenue from franchised cafés is based on agreed percentage royalty rates of the franchise location sales. Revenue is recognized on an accrual basis in accordance with the substance of the relevant agreement, provided that it is probable that the economic benefits will flow to the Company and the amount of revenue can be measured reliably.

(Unaudited, expressed in thousands of Canadian dollars, except per share amounts)

Services and other

Services and other consist of initial franchise fees, renewal fees, transfer fees earned on the sale of cafés from one franchisee to another, construction administration fees, purchasing coordination fees, licensing fees and other ancillary fees (such as IT support and training fees).

Company-owned cafés and product sales

Company owned cafés and product sales revenue includes the sale of goods from Company-owned cafés, as well as products sold in grocery stores through wholesale distribution channels and third party licensing agreements.

7. Operating costs and expenses

	13 weeks ended		39 weeks ended	
	September 30, 2017	**September 24, 2016**	**September 30, 2017**	**September 24, 2016**
Company-owned cafés and cost of product sales				
Cost of product sales	$ 642	$ 1,495	$ 2,536	$ 4,594
Labour and related expenses	603	1,147	2,436	3,796
Occupancy and other	657	1,215	2,559	3,882
Depreciation of property and equipment	74	95	233	306
Loss/(gain) on disposal of assets	(3)	151	99	309
	1,973	4,103	7,863	12,887
Franchise				
Labour and related expenses	857	1,037	2,846	3,279
Travel and franchisee meetings	68	103	269	550
Professional fees and other	206	748	908	2,268
	1,131	1,888	4,023	6,097
General and administrative				
Labour and related expenses	459	502	1,691	1,504
Professional fees and other	933	791	2,764	2,438
Occupancy	112	110	348	334
	1,504	1,403	4,803	4,276
Other				
Depreciation and amortization	295	287	879	877
	295	287	879	877
	$ 4,903	$ 7,681	$ 17,568	$ 24,137

(Unaudited, expressed in thousands of Canadian dollars, except per share amounts)

8. Interest and financing costs

	13 weeks ended		39 weeks ended	
	September 30, 2017	September 24, 2016	September 30, 2017	September 24, 2016
Fair value difference on shares issued and other costs	$ 3,290	$ -	$ 3,290	$ -
Interest expense	92	64	505	164
Amortization of deferred financing costs	24	6	139	19
Interest income	(12)	(8)	(32)	(24)
	$ 3,394	$ 62	$ 3,902	$ 159

On August 10, 2017, the Company issued 4,210,528 common shares and 300,000 warrants of Second Cup to the four shareholders of SPE Finance LLC (SPE), an affiliate of Serruya Private Equity. The Company also extinguished its $8,000 debt to SPE and cancelled 600,000 of old warrants. These transactions resulted in one-time, non-cash financing charges of $3,290. These charges consist of the difference between the share price of $2.60 on the issuance date and the agreed-to share price of $1.90, and the write-off of the unamortized portion of deferred transaction costs related to the debt.

9. Basic and diluted loss per share

Loss per share is based on the weighted average number of shares outstanding during the period. Basic and diluted loss per share is determined as follows:

	13 weeks ended		39 weeks ended	
	September 30, 2017	September 24, 2016	September 30, 2017	September 24, 2016
Net loss	$ (2,962)	$ (75)	$ (3,752)	$ (1,122)
Weighted average number of shares issued and outstanding	15,236,961	12,830,945	13,632,590	12,830,945
Basic and diluted loss per share	$ (0.19)	$ (0.01)	$ (0.28)	$ (0.09)

(Unaudited, expressed in thousands of Canadian dollars, except per share amounts)

10. Supplemental cash flow information

	13 weeks ended		39 weeks ended	
	September 30, 2017	**September 24, 2016**	**September 30, 2017**	**September 24, 2016**
Changes in non-cash working capital & other (inflow (outflow)):				
Trade and other receivables	$ (587)	$ 222	$ 494	$ 1,243
Inventories	20	(11)	64	(23)
Prepaid expenses and other assets	322	90	118	204
Accounts payable and accrued liabilities	6	22	117	(932)
Provisions	(206)	(8)	(812)	(608)
Other liabilities	(77)	(145)	97	(257)
Gift card liability	(117)	(92)	(716)	(723)
Deposits from franchisees and restricted cash	140	(340)	47	(371)
Income taxes	445	76	532	658
	$ (54)	$ (186)	$ (59)	$ (809)
Cash payments for capital expenditures				
Cash payments for capital expenditures	$ (74)	$ (88)	$ (200)	$ (292)
Cash payments for intangible assets	(31)	(62)	(184)	(276)
	$ (105)	$ (150)	$ (384)	$ (568)
Supplementary information				
Interest paid	$ 93	$ 72	$ 505	$ 186

(Unaudited, expressed in thousands of Canadian dollars, except per share amounts)

11. Restricted cash

The Company has established certain accounts that have been classified as restricted cash primarily representing: a) deposits from franchisees for the cost of constructing a new café or the renovation of an existing café, b) funds contributed for use in advertising and promotional programs where the Company is acting as an agent on behalf of the Co-op Fund, and c) a deposit held by the Company's bank as security for cash management services.

	September 30, 2017	December 31, 2016
Development Fund	$ 697	$ 1,220
Co-op Fund	655	487
Security Deposit held by bank	240	240
Total Restricted Cash	$ 1,592	$ 1,947

A summary of activities in the Co-op Fund is provided as follows:

	13 weeks ended		39 weeks ended	
	September 30, 2017	September 24, 2016	September 30, 2017	September 24, 2016
Co-op Fund – opening balance	$ 399	$ 422	$ 487	$ 319
Contributions by franchisees	625	509	1,898	1,757
Contributions by Company for Company-owned cafés	83	18	260	172
Other contributions by Company	-	75	-	75
Payments to third party suppliers for goods and services	(452)	(698)	(1,990)	(1,790)
Repayments to Company in respect of promissory notes	-	(88)	-	(295)
Co-op Fund – closing balance	$ 655	$ 238	$ 655	$ 238

(Unaudited, expressed in thousands of Canadian dollars, except per share amounts)

12. Contingencies, commitments and guarantees

The Company has lease commitments for Company-operated cafés and acts as the head tenant on most leases, which it in turn subleases to franchisees. To the extent the Company may be required to make rent payments due to head lease commitments, a provision has been recognized. The Company's lease commitments as at September 30, 2017 are as follows:

	Head lease commitments	Sublease to franchisees	Net
September 29, 2018	$ 15,993	$ 14,503	$ 1,490
September 28, 2019	14,268	12,729	1,539
September 26, 2020	12,051	10,641	1,410
September 25, 2021	10,148	8,847	1,301
September 24, 2022	8,985	7,735	1,250
Thereafter	22,527	19,225	3,302
	$ 83,972	$ 73,680	$ 10,292

The Company believes it will have sufficient resources to meet the net commitment of $10,292 over the term of the leases.

The Company is involved in litigation and other claims arising in the normal course of business. Judgment must be used to determine whether or not a claim has any merit, the amount of the claim and whether to record a provision, which is dependent on the potential success of the claim. It is believed that no significant losses or expenses will be incurred with such claims. However, there can be no assurance that unforeseen circumstances will not result in significant costs. The outcome of these actions is not determinable at this time, and adjustments, if any, will be recorded in the period of settlement.

Contracts are in place with third party companies to purchase the coffee that is sold in all cafés. In terms of these supply agreements, there is a guaranteed minimum volume of coffee purchases of $2,417 (September 24, 2016 - $927) for the subsequent 12 months. The coffee purchase commitment is comprised of two components: unapplied futures commitment contracts and fixed price physical contracts.

Due to the Company acting as the primary coordinator of café construction costs on behalf of its franchisees and for Company-operated cafés, there is $554 (September 24, 2016 - $526) of contractual commitments pertaining to construction costs for new locations and renovations as at the end of the quarter. Construction costs financed for franchise projects are from deposits received from franchisees and for corporate projects from the Company's cash flows.

13. Related parties

Related parties are identified as key management, members of the Board of Directors and shareholders that effectively exercise significant influence over the Company. Such related parties include any entities acting with or on behalf of the aforementioned parties. There were no related party transactions in the reporting period.