

---

---

# FORM 10-Q

---

## UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

---

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.**

For the quarterly period ended November 3, 2018.

OR

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.**

For the transition period from \_\_\_\_\_ to \_\_\_\_\_  
Commission file number 001-37404

---

**DAVIDsTEA**  
**DAVIDsTEA Inc.**

(Exact name of registrant as specified in its charter)

---

**Canada**  
(State or other jurisdiction of  
incorporation or organization)

**98-1048842**  
(I.R.S. Employer  
Identification No.)

**5430 Ferrier**  
**Town of Mount-Royal, Québec, Canada, H4P 1M2**  
(Address of principal executive offices) (zip code)

**(888) 873-0006**  
(Registrant's telephone number, including area code)

**Not Applicable**  
(Former name, former address and former fiscal year, if changed since last report)

---

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES  NO

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES  NO

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12-b2 of the Exchange Act.

Large accelerated filer

Accelerated filer

Emerging growth company

Non-accelerated filer

Smaller reporting company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES  NO

As of December 10, 2018, 26,007,757 common shares of the registrant were outstanding.

---

---

**DAVIDsTEA Inc.**

**TABLE OF CONTENTS**

**PART I. FINANCIAL INFORMATION**

Item 1. Consolidated Financial Statements	3
Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations	19
Item 3. Quantitative and Qualitative Disclosures About Market Risk	30
Item 4. Controls and Procedures	30

**PART II. OTHER INFORMATION**

Item 1. Legal Proceedings	32
Item 1A. Risk Factors	32
Item 2. Unregistered Sales of Equity Securities	32
Item 3. Defaults Upon Senior Securities	32
Item 4. Mine Safety Disclosures	32
Item 5. Other Information	33
Item 6. Exhibits	33

DAVIDsTEA Inc. (the “Company”), a corporation incorporated under the *Canada Business Corporations Act*, qualifies as a foreign private issuer in the United States for purposes of the Securities Exchange Act of 1934, as amended (the “Exchange Act”). As a foreign private issuer, the Company has chosen to file annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K with the United States Securities and Exchange Commission (“SEC”) instead of filing the reporting forms available to foreign private issuers, although the Company is not required to do so.

In this quarterly report, unless otherwise specified, all monetary amounts are in Canadian dollars, all references to “\$”, “C\$”, “CAD”, “CND\$”, “Canadian dollars” and “dollars” mean Canadian dollars and all references to “U.S. dollars,” “US\$” and “USD” mean U.S. dollars.

On December 7, 2018, the noon buying rate certified for customs purposes by the U.S. Federal Reserve Bank of New York was US\$1.00 = C\$1.3302.

Part I. FINANCIAL INFORMATION

Item 1. Consolidated Financial Statements

DAVIDsTEA Inc.

Incorporated under the laws of Canada

INTERIM CONSOLIDATED BALANCE SHEETS

Unaudited and in thousands of Canadian dollars

	As at	
	November 3, 2018	February 3, 2018
	\$	\$
<b>ASSETS</b>		
<b>Current</b>		
Cash	18,714	63,484
Accounts and other receivables	4,007	3,131
Inventories	44,408	24,450
Income tax receivable	4,808	2,968
Prepaid expenses and deposits	9,476	7,712
<b>Total current assets</b>	<b>81,413</b>	101,745
Property and equipment	31,698	36,558
Intangible assets	7,392	4,439
Deferred income tax assets	8,962	5,194
<b>Total assets</b>	<b>129,465</b>	147,936
<b>LIABILITIES AND EQUITY</b>		
<b>Current</b>		
Trade and other payables	16,096	14,392
Deferred revenue	4,966	5,186
Current portion of provisions	4,658	4,693
Derivative financial instruments	—	229
<b>Total current liabilities</b>	<b>25,720</b>	24,500
Deferred rent and lease inducements	8,829	8,608
Provisions	14,434	13,460
<b>Total liabilities</b>	<b>48,983</b>	46,568
<b>Equity</b>		
Share capital	112,499	111,692
Contributed surplus	1,230	2,642
Deficit	(34,696)	(14,721)
Accumulated other comprehensive income	1,449	1,755
<b>Total equity</b>	<b>80,482</b>	101,368
	<b>129,465</b>	147,936

See accompanying notes

DAVIDsTEA Inc.

Incorporated under the laws of Canada

INTERIM CONSOLIDATED STATEMENTS OF LOSS

AND COMPREHENSIVE LOSS

Unaudited and in thousands of Canadian dollars, except share and per share information

		For the three months ended		For the nine months ended	
		November 3, 2018 \$	October 28, 2017 \$	November 3, 2018 \$	October 28, 2017 \$
<b>Sales</b>	[Note 14]	<b>43,656</b>	42,997	<b>129,609</b>	137,353
Cost of sales		<b>25,275</b>	24,625	<b>71,193</b>	74,594
<b>Gross profit</b>		<b>18,381</b>	18,372	<b>58,416</b>	62,759
Selling, general and administration expenses	[Note 11]	<b>29,119</b>	27,035	<b>84,865</b>	79,004
<b>Results from operating activities</b>		<b>(10,738)</b>	(8,663)	<b>(26,449)</b>	(16,245)
Finance costs		<b>80</b>	327	<b>237</b>	615
Finance income		<b>(122)</b>	(149)	<b>(574)</b>	(420)
<b>Loss before income taxes</b>		<b>(10,696)</b>	(8,841)	<b>(26,112)</b>	(16,440)
Recovery of income tax		<b>(1,635)</b>	(2,356)	<b>(5,851)</b>	(4,030)
<b>Net loss</b>		<b>(9,061)</b>	(6,485)	<b>(20,261)</b>	(12,410)
<b>Other comprehensive income (loss)</b>					
Items to be reclassified subsequently to income (loss):					
Cumulative translation adjustment		<b>(62)</b>	1,872	<b>(473)</b>	95
Items that may be reclassified subsequently to income (loss):					
Unrealized net gain on forward exchange contracts	[Note 15]	—	824	<b>794</b>	79
Realized net (gain) on forward exchange contracts reclassified to inventory		<b>(425)</b>	(714)	<b>(565)</b>	(46)
Provision for income tax (recovery) on forward exchange contracts		<b>113</b>	589	<b>(62)</b>	(303)
<b>Other comprehensive income (loss), net of tax</b>		<b>(374)</b>	2,571	<b>(306)</b>	(175)
<b>Total comprehensive loss</b>		<b>(9,435)</b>	(3,914)	<b>(20,567)</b>	(12,585)
<b>Net loss per share:</b>					
Basic	[Note 12]	<b>(0.35)</b>	(0.25)	<b>(0.78)</b>	(0.48)
Fully diluted	[Note 12]	<b>(0.35)</b>	(0.25)	<b>(0.78)</b>	(0.48)
<b>Weighted average number of shares outstanding</b>					
— basic	[Note 12]	<b>25,992,339</b>	25,829,090	<b>25,862,086</b>	25,659,164
— fully diluted	[Note 12]	<b>25,992,339</b>	25,829,090	<b>25,862,086</b>	25,659,164

See accompanying notes

DAVIDsTEA Inc.

Incorporated under the laws of Canada

INTERIM CONSOLIDATED STATEMENTS OF CASH FLOWS

Unaudited and in thousands of Canadian dollars

	<u>For the three months ended</u>		<u>For the nine months ended</u>	
	<u>November 3, 2018</u>	<u>October 28, 2017</u>	<u>November 3, 2018</u>	<u>October 28, 2017</u>
	<u>\$</u>	<u>\$</u>	<u>\$</u>	<u>\$</u>
<b>OPERATING ACTIVITIES</b>				
Net loss	(9,061)	(6,485)	(20,261)	(12,410)
Items not affecting cash:				
Depreciation of property and equipment	1,785	2,138	5,193	6,316
Amortization of intangible assets	377	494	905	1,248
Loss on disposal of property and equipment	—	18	14	48
Impairment of property and equipment	725	2,658	3,285	4,971
Deferred rent	74	174	(17)	377
Provision (recovery) for onerous contracts	3,414	(46)	5,306	(1,573)
Stock-based compensation expense	91	362	(7)	1,738
Amortization of financing fees	21	19	61	59
Accretion on provisions	60	307	177	558
Deferred income taxes (recovery)	(2,575)	(227)	(3,921)	203
	<u>(5,089)</u>	<u>(588)</u>	<u>(9,265)</u>	<u>1,535</u>
Net change in other non-cash working capital balances related to operations	<u>(12,948)</u>	<u>(15,546)</u>	<u>(28,316)</u>	<u>(21,511)</u>
<b>Cash flows related to operating activities</b>	<u>(18,037)</u>	<u>(16,134)</u>	<u>(37,581)</u>	<u>(19,976)</u>
<b>FINANCING ACTIVITIES</b>				
Proceeds from issuance of common shares pursuant to exercise of stock options	8	90	82	1,696
<b>Cash flows related to financing activities</b>	<u>8</u>	<u>90</u>	<u>82</u>	<u>1,696</u>
<b>INVESTING ACTIVITIES</b>				
Additions to property and equipment	(1,752)	(2,770)	(3,420)	(7,501)
Additions to intangible assets	(1,128)	(728)	(3,851)	(1,794)
<b>Cash flows related to investing activities</b>	<u>(2,880)</u>	<u>(3,498)</u>	<u>(7,271)</u>	<u>(9,295)</u>
Decrease in cash during the period	(20,909)	(19,542)	(44,770)	(27,575)
<b>Cash, beginning of period</b>	<u>39,623</u>	<u>56,407</u>	<u>63,484</u>	<u>64,440</u>
<b>Cash, end of period</b>	<u>18,714</u>	<u>36,865</u>	<u>18,714</u>	<u>36,865</u>
<b>Supplemental Information</b>				
Cash paid for:				
Income taxes (classified as operating activity)	7	165	9	877
Cash received for:				
Interest	120	146	563	433
Income taxes (classified as operating activity)	—	—	—	26

See accompanying notes

DAVIDsTEA Inc.

Incorporated under the laws of Canada

INTERIM CONSOLIDATED STATEMENTS OF EQUITY (DEFICIT)

Unaudited and in thousands of Canadian dollars

	Share Capital \$	Contributed Surplus \$	Deficit \$	Accumulated Other Comprehensive Income			Total Equity \$
				Accumulated Derivative Financial Instrument Adjustment \$	Accumulated Foreign Currency Translation Adjustment \$	Accumulated Other Comprehensive Income \$	
Balance, January 28, 2017	263,828	8,833	(142,398)	333	2,854	3,187	133,450
Net loss for the nine months ended October 28, 2017	—	—	(12,410)	—	—	—	(12,410)
Other comprehensive loss	—	—	—	128	(303)	(175)	(175)
Total comprehensive loss	—	—	(12,410)	128	(303)	(175)	(12,585)
Issuance of common shares	2,546	(850)	—	—	—	—	1,696
Common shares issued on vesting of restricted stock units	912	(1,652)	184	—	—	—	(556)
Stock-based compensation expense	—	1,738	—	—	—	—	1,738
Income tax impact associated with stock options	—	(133)	—	—	—	—	(133)
Reduction of stated capital	(155,947)	—	155,947	—	—	—	—
Balance, October 28, 2017	111,339	7,936	1,323	461	2,551	3,012	123,610
<b>Balance, February 3, 2018</b>	<b>111,692</b>	<b>2,642</b>	<b>(14,721)</b>	<b>(167)</b>	<b>1,922</b>	<b>1,755</b>	<b>101,368</b>
Net loss for the nine months ended November 3, 2018	—	—	(20,261)	—	—	—	(20,261)
Other comprehensive income (loss)	—	—	—	167	(473)	(306)	(306)
Total comprehensive income (loss)	—	—	(20,261)	167	(473)	(306)	(20,567)
Issuance of common shares	164	(82)	—	—	—	—	82
Common shares issued on vesting of restricted stock units	643	(1,322)	286	—	—	—	(393)
Stock-based compensation expense	—	(7)	—	—	—	—	(7)
Income tax impact associated with stock options	—	(1)	—	—	—	—	(1)
Balance, November 3, 2018	112,499	1,230	(34,696)	—	1,449	1,449	80,482

See accompanying notes

## DAVIDsTEA Inc.

### NOTES TO CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

For the three and nine-month periods ended November 3, 2018 and October 28, 2017

Unaudited and in thousands of Canadian dollars except share and per share amounts

#### 1. CORPORATE INFORMATION

The unaudited condensed interim consolidated financial statements of DAVIDsTEA Inc. and its subsidiary (collectively, the “Company”) for the three and nine-month periods ended November 3, 2018 were authorized for issue in accordance with a resolution of the Board of Directors on December 13, 2018. The Company is incorporated and domiciled in Canada and its shares are publicly traded on the NASDAQ Global Market under the symbol “DTEA”. The registered office is located at 5430 Ferrier St., Town of Mount-Royal, Québec, Canada, H4P 1M2.

The Company is engaged in the retail and online sale of tea, tea accessories and food and beverages in Canada and the United States. The results of operations for the interim period are not necessarily indicative of the results of operations for the full year. Sales fluctuate from quarter to quarter. Sales are traditionally higher in the fourth fiscal quarter due to the year-end holiday season, and tend to be lowest in the second and third fiscal quarters because of lower customer traffic during the summer months.

#### 2. STATEMENT OF COMPLIANCE AND BASIS OF PREPARATION

These unaudited condensed interim consolidated financial statements have been prepared in accordance with IAS 34, “Interim Financial Reporting” as issued by the International Accounting Standards Board (“IASB”). Accordingly, these financial statements do not include all of the financial statement disclosures required for annual financial statements and should be read in conjunction with the Company’s audited consolidated financial statements for the year ended February 3, 2018, which have been prepared in accordance with International Financial Reporting Standards (“IFRS”) as issued by the IASB. In management’s opinion, the unaudited condensed interim consolidated financial statements reflect all the adjustments that are necessary for a fair presentation of the results for the interim period presented. These unaudited condensed interim consolidated financial statements have been prepared using the accounting policies and methods of computation as outlined in note 3 of the consolidated financial statements for the year ended February 3, 2018 on Form 10-K filed with the SEC on April 19, 2018.

#### 3. CHANGES IN ACCOUNTING POLICIES

As of February 4, 2018, the Company adopted IFRS 9, “Financial Instruments” (“IFRS 9”). IFRS 9 replaces IAS 39 Financial Instruments: Recognition and Measurement for annual periods beginning on or after January 1, 2018, bringing together all three aspects of the accounting for financial instruments: classification and measurement; impairment; and hedge accounting.

With the exception of hedge accounting, which the Company applied prospectively, the Company has applied IFRS 9 retrospectively, with the initial application date of February 4, 2018.

Overall, there was no material impact on the Company’s consolidated financial statements.

- a) *Classification and measurement.* The Company did not identify any material impact on its consolidated financial statements in applying the classification and measurement requirements of IFRS 9. The following table presents the carrying amount of financial assets held by the Company at February 3, 2018 and their measurement category under IAS 39 and the new model under IFRS 9.

	February 3, 2018		February 3, 2018	
	IAS 39		IFRS 9	
	Measurement category	Carrying Value \$	Measurement category	Carrying Value \$
Cash	FVTPL	63,484	FVTPL	63,484
Credit card cash clearing receivables	Amortized cost	1,291	Amortized cost	1,291
Other receivables	Amortized cost	1,840	Amortized cost	1,840
Derivative financial instruments	FVTPL	229	FVTPL	229

There has been no impact caused by the new classification of financial assets under IFRS 9. The classification of all financial liabilities as financial liabilities at amortized cost remains unchanged as well as their measurement resulting from their classification.

- b) *Impairment.* IFRS 9 requires the Company to record expected credit losses on all of its debt securities, loans and trade receivables, either on a 12-month or lifetime basis. The Company applied the simplified approach and records lifetime expected losses on all trade receivables. The Company performed a detailed analysis that considered all reasonable and supportable information, including forward-looking elements to determine the extent of the impact. The Company's IFRS 9 expected credit loss model did not have a material impact on its consolidated financial statements.
- c) *Hedge accounting.* The Company believes that all existing hedge relationships that are currently designated in effective hedging relationships still qualify for hedge accounting under IFRS 9. As IFRS 9 does not change the general principles of how an entity accounts for effective hedges, the adoption of IFRS 9 did not have a material impact on the Company's hedge accounting.

As of February 4, 2018, the Company adopted IFRS 15, "Revenue from Contracts with Customers" ("IFRS 15"). IFRS 15 replaces IAS 11, "Construction Contracts", and IAS 18, "Revenue", as well as various interpretations regarding revenue. This standard introduces a single model for recognizing revenue that applies to all contracts with customers, except for contracts that are within the scope of standards on leases, insurance and financial instruments. This standard also requires enhanced disclosures. Adoption of IFRS 15 is mandatory and is effective for annual periods beginning on or after January 1, 2018. The implementation of IFRS 15 impacts the allocation of revenue that is deferred in relation to the Company's customer loyalty award programs. Prior to adoption, revenue was allocated to the customer loyalty awards using the residual fair value method. Under IFRS 15, consideration is allocated between the loyalty program awards and the goods on which the awards were earned, based on their relative stand-alone selling prices. The change in allocation of revenue that is deferred in relation to the Company's customer loyalty program does not have a material impact on retained earnings as at February 4, 2018. Overall, there was not a material impact on the Company's consolidated financial statements.

As of February 4, 2018, the Company adopted International Financial Reporting Interpretations ("IFRIC") 22, "Foreign Currency Transactions and Advance Consideration" ("IFRIC 22"). In December 2016, the IASB issued IFRIC 22, which addresses how to determine the date of the transaction for the purpose of determining the exchange rate to use on initial recognition of the related asset, expense or income (or part of it) and on the derecognition of a non-monetary asset or non-monetary liability arising from the payment or receipt of advance consideration in a foreign currency. IFRIC 22 is effective for annual periods beginning on or after January 1, 2018. There was no material impact on the Company's consolidated financial statements.

Information on significant new accounting standards and amendments issued but not yet adopted is described below.

IFRS 16, "Leases" ("IFRS 16") replaces IAS 17, "Leases". This standard provides a single model for leases abolishing the current distinction between finance and operating leases, with most leases being recognized on the balance sheet. Certain exemptions will apply for short-term leases and leases of low value assets. The new standard will be effective for annual periods beginning on or after January 1, 2019 with early application permitted. The Company has performed a preliminary assessment of the potential impact of the adoption of IFRS 16 on its consolidated financial

statements. The Company expects the adoption of IFRS 16 will have a significant impact as the Company will recognize new assets and liabilities for its operating leases of retail stores. In addition, the nature and timing of expenses related to those leases will change as IFRS 16 replaces the straight-line operating lease expense with a depreciation charge for right-of-use assets and interest expense on lease liabilities. The Company has not yet determined which transition method it will apply or whether it will use the optional exemptions or practical expedients under the standard. The Company expects to disclose additional detailed information, including its transition method, any practical expedients elected and estimated quantitative financial effects, before the adoption of IFRS 16.

IFRIC 23, “Uncertainty over Income Tax Treatments”, was issued by the IASB in June 2017. IFRIC 23 provides guidance on the accounting for current and deferred tax liabilities and assets in circumstances in which there is uncertainty over income tax treatments. IFRIC 23 is effective for annual periods beginning on or after January 1, 2019. Earlier application is permitted. IFRIC 23 requires an entity to:

- Contemplate whether uncertain tax treatments should be considered separately, or together as a group, based on which approach provides better predictions of the resolution;
- Reflect an uncertainty in the amount of income tax payable (recoverable) if it is probable that it will pay (or recover) an amount for the uncertainty; and
- Measure a tax uncertainty based on the most likely amount or expected value depending on whichever method better predicts the amount payable (recoverable).

The Company does not expect a material impact from the adoption of IFRIC 23 on its consolidated financial statements.

#### 4. SIGNIFICANT ACCOUNTING JUDGMENTS, ESTIMATES AND ASSUMPTIONS

The preparation of condensed interim consolidated financial statements requires management to make estimates and assumptions using judgments that affect the application of accounting policies and the reported amounts of assets and liabilities, income and expense during the reporting period. Estimates and other judgments are continually evaluated and are based on management’s experience and other factors, including expectations about future events that are believed to be reasonable under the circumstances. Actual results may differ from those estimates.

In preparing these unaudited condensed interim consolidated financial statements, critical judgments made by management in applying the Company’s accounting policies and the key sources of estimation uncertainty were the same as those referred to in note 5 of the consolidated financial statements for the year ended February 3, 2018 on Form 10-K filed with the SEC on April 19, 2018.

#### 5. INVENTORIES

	November 3, 2018	February 3, 2018
	\$	\$
Finished goods	36,510	17,600
Goods in transit	2,784	4,608
Packaging	5,114	2,242
	<u>44,408</u>	<u>24,450</u>

#### 6. PROPERTY AND EQUIPMENT

For the three and nine months ended November 3, 2018, an assessment of impairment indicators was performed which caused the Company to review the recoverable amount of the property and equipment for certain cash generating units (“CGUs”) with an indication of impairment. CGUs reviewed included stores performing below the Company’s expectations.

As a result, for the three and nine months ended November 3, 2018, an impairment loss of \$725 and \$3,285, respectively, [October 28, 2017 — \$2,658 and \$4,971] related to store leasehold improvements, furniture and equipment, and computer hardware was recorded in the Canada and U.S. segments for \$725 and nil, respectively, for the three months ended November 3, 2018 and \$3,096 and \$189, respectively, for the nine months ended November 3, 2018, respectively [October 28, 2017 — \$595 and \$2,063, respectively, for the three months and \$595 and \$5,242, respectively, for the nine months]. These losses were determined by comparing the carrying amount of the CGU's net assets with their respective recoverable amounts based on value in use. Value in use of nil [October 28, 2017 — \$635] was determined based on management's best estimate of expected future cash flows from use over the remaining lease terms, considering historical experience as well as current economic conditions, and was then discounted using a pre-tax discount rate of 11.9% [October 28, 2017 — 13.4%]. A reversal of impairment occurs when previously impaired CGUs see improved financial results. For the three and nine months ended November 3, 2018, no impairment losses were reversed [October 28, 2017 — \$866 reversed in the U.S. segment, with value in use of \$848]. Impairment losses are reversed only to the extent that the carrying amounts of the CGU's net assets do not exceed the carrying amount that would have been determined, net of depreciation, if no impairment loss had been recognized.

## 7. PROVISIONS

	For the nine months ended November 3, 2018 \$
Opening balance	18,153
Additions	5,894
Reversals	(588)
Utilization	(4,820)
Settlements	(615)
Accretion expense	177
Cumulative translation adjustment	891
<b>Ending balance</b>	<b>19,092</b>
Less: Current portion	(4,658)
Long-term portion of provisions	<u>14,434</u>

Provisions for onerous contracts have been recognized in respect of store leases where the unavoidable costs of meeting the obligations under the lease agreements exceed the economic benefits expected to be received from the contract. The unavoidable costs reflect the present value of the lower of the expected cost of terminating the contract and the expected net cost of operating under the contract.

During the three and nine months ended November 3, 2018, due to changes to assumptions, additions to the onerous provision were recorded in the amount of \$3,743 and \$5,894, respectively, [October 28, 2017 — nil and \$458], while the provisions for other stores were partially or fully reversed by an amount of \$329 and \$588, respectively, [October 28, 2017 — \$46 and \$2,031].

## 8. REVOLVING FACILITY

On June 11, 2018, the Company amended its existing Credit Agreement (the "Amended Credit Agreement"). The Amended Credit Agreement provides for a two-year revolving facility ("Amended Revolving Facility") in the principal amount of \$15.0 million or the equivalent in U.S. dollars, repayable at any time, two years from June 11, 2018, with no accordion feature. Borrowings under the Amended Revolving Facility may not exceed the lesser of the total commitment for the revolving facility and the borrowing base, calculated as 75% of the face value of all eligible receivables plus 50% of the estimated value of all eligible inventory, less any priority payables.

The Amended Credit Agreement subjects the Company to certain financial covenants entered into between the Company and the lender. Without the prior written consent of the lender, the Company's fixed charge coverage ratio

may not be less than 1.10:1.00 and the Company's leverage ratio may not exceed 3.00:1.00. In addition, the Company's net tangible worth may not be less than \$65,000 and the Company's minimum excess availability must not be less than \$15.0 million. The Amended Revolving Facility bears interest based on the Company's adjusted leverage ratio, at the bank's prime rate, U.S. bank rate and LIBOR plus a range from 0.5% to 2.5% per annum. A standby fee range of 0.3% to 0.5% will be paid on the daily principal amount of the unused portion of the Amended Revolving Facility.

The credit facility also contains non-financial covenants that, among other things and subject to certain exceptions, restrict the Company's ability to become guarantor or endorser or otherwise become liable upon any note or other obligation other than in the normal course of business. The Company also cannot make any dividend payments.

As at November 3, 2018 and February 3, 2018, the Company did not have any borrowings under the Amended Revolving Facility. At November 3, 2018, the Company is in breach of its fixed charge coverage ratio and is taking measures to rectify the situation. The Company is in compliance with its other financial and non-financial covenants.

## 9. SHARE CAPITAL

### Authorized

An unlimited number of common shares.

### Issued and outstanding

	November 3, 2018 \$	February 3, 2018 \$
26,007,009 common shares [February 3, 2018 - 25,885,372 shares]	<u>112,499</u>	<u>111,692</u>
	<u>112,499</u>	<u>111,692</u>

During the three and nine-month periods ended November 3, 2018, 10,000 and 88,135 stock options, respectively, were exercised for 88,135 common shares for cash proceeds of \$8 and \$82, respectively, and 36,418 common shares for a non-cash settlement of nil and \$121, respectively [October 28, 2017 — 24,000 and 436,773 stock options, respectively, for cash proceeds of \$90 and \$1,696, respectively]. During the three and nine-month periods ended November 3, 2018, the carrying value of common shares includes \$3 and \$82, respectively [October 28, 2017 — \$22 and \$850, respectively], which corresponds to a reduction in contributed surplus associated with options exercised during the period.

In addition, during the three and nine-month periods ended November 3, 2018, 1,128 and 70,668 common shares, respectively [October 28, 2017 – 19,819 and 75,820 common shares, respectively] were issued in relation to the vesting of restricted stock units ("RSU"), resulting in an increase in share capital of \$7 and \$643, net of tax, respectively [October 28, 2017 – \$208 and \$912, respectively] and a reduction in contributed surplus of \$18 and \$1,322, respectively [October 28, 2017 — \$433 and \$1,652, respectively].

During the nine-month period ended October 28, 2017, the shareholders of the Company approved a resolution to reduce the stated capital maintained in respect of the common shares by an amount of \$155,947, which resulted in a corresponding reduction of the deficit.

### Stock-based compensation

As at November 3, 2018, 842,905 common shares remain available for issuance under the 2015 Omnibus Incentive Plan.

No stock options were granted during the nine-month period ended November 3, 2018. For the nine-month period ended October 28, 2017, the weighted average fair value of options granted of \$2.39 was estimated using the Black Scholes option pricing model, using the following assumptions:

	<u>October 28, 2017</u>
Risk-free interest rate	1.79 %
Expected volatility	27.4 %
Expected option life	4.0 years
Expected dividend yield	0 %
Exercise price	\$ 9.76

Expected volatility was estimated using historical volatility of similar companies whose share prices were publicly available.

A summary of the status of the Company's stock option plan and changes during the nine-month period is presented below.

	<u>For the nine months ended</u>			
	<u>November 3, 2018</u>		<u>October 28, 2017</u>	
	Options outstanding #	Weighted average exercise price \$	Options outstanding #	Weighted average exercise price \$
<b>Outstanding, beginning of period</b>	<b>447,779</b>	<b>7.18</b>	933,195	5.63
Issued	—	—	161,980	9.76
Exercised	<b>(88,135)</b>	<b>2.76</b>	(436,773)	3.88
Forfeitures	<b>(220,791)</b>	<b>8.92</b>	(135,135)	8.31
<b>Outstanding, end of period</b>	<b>138,853</b>	<b>7.23</b>	523,267	7.67
<b>Exercisable, end of period</b>	<b>75,837</b>	<b>4.84</b>	315,909	5.74

For the nine-month period ended November 3, 2018, the weighted average share price at the date of exercise for stock options exercised was \$4.47 [October 28, 2017 — \$8.68].

A summary of the status of the Company's RSU plan and changes during the nine-month period is presented below.

	<u>For the nine months ended</u>			
	<u>November 3, 2018</u>		<u>October 28, 2017</u>	
	RSUs outstanding #	Weighted average fair value per unit (1) \$	RSUs outstanding #	Weighted average fair value per unit (1) \$
<b>Outstanding, beginning of period</b>	<b>289,416</b>	<b>9.70</b>	252,233	12.42
Granted	<b>476,450</b>	<b>4.48</b>	298,897	8.59
Forfeitures	<b>(327,479)</b>	<b>6.45</b>	(34,864)	10.19
Vested	<b>(70,668)</b>	<b>9.08</b>	(75,820)	12.21
Vested, withheld for tax	<b>(69,017)</b>	<b>8.91</b>	(65,342)	11.40
<b>Outstanding, end of period</b>	<b>298,702</b>	<b>5.26</b>	375,104	9.80

(1) Weighted average fair value per unit as at date of grant.

During the three and nine-month periods ended November 3, 2018, the Company recognized stock-based compensation expense and a net reversal of stock-based compensation of \$91 and \$7, respectively [October 28, 2017 — stock-based compensation expense of \$362 and \$1,738, respectively].

## 10. INCOME TAXES

Income tax expense is recognized based on management's best estimate of the weighted average annual income tax rate expected for the full fiscal year.

A reconciliation of the statutory income tax rate to the effective tax rate is as follows:

	For the three months ended				For the nine months ended			
	November 3, 2018		October 28, 2017		November 3, 2018		October 28, 2017	
	%	\$	%	\$	%	\$	%	\$
<b>Income tax recovery — statutory rate</b>	<b>26.9</b>	<b>(2,873)</b>	26.8	(2,368)	<b>26.9</b>	<b>(7,015)</b>	26.8	(4,404)
Increase (decrease) in provision for income tax (recovery) resulting from:								
Non-deductible items	<b>(0.4)</b>	<b>38</b>	(0.4)	38	<b>0.1</b>	<b>(31)</b>	(2.3)	385
Provision for uncertain tax position	<b>(8.8)</b>	<b>940</b>	—	—	<b>(3.6)</b>	<b>940</b>	—	—
Other	<b>(2.4)</b>	<b>260</b>	0.3	(26)	<b>(1.0)</b>	<b>255</b>	0.1	(11)
<b>Income tax provision (recovery) — effective tax rate</b>	<b>15.3</b>	<b>(1,635)</b>	26.7	(2,356)	<b>22.4</b>	<b>(5,851)</b>	24.6	(4,030)

A breakdown of the income tax provision (recovery) on the interim consolidated statement of loss is as follows:

	For the three months ended		For the nine months ended	
	November 3, 2018	October 28, 2017	November 3, 2018	October 28, 2017
	\$	\$	\$	\$
Income tax provision (recovery)				
Current	<b>940</b>	(2,129)	<b>(1,930)</b>	(4,233)
Deferred	<b>(2,575)</b>	(227)	<b>(3,921)</b>	203
	<b>(1,635)</b>	(2,356)	<b>(5,851)</b>	(4,030)

## 11. SELLING, GENERAL AND ADMINISTRATION EXPENSES

	For the three months ended		For the nine months ended	
	November 3, 2018	October 28, 2017	November 3, 2018	October 28, 2017
	\$	\$	\$	\$
Wages, salaries and employee benefits	<b>16,767</b>	15,012	<b>49,031</b>	47,113
Depreciation of property and equipment	<b>1,785</b>	2,138	<b>5,193</b>	6,316
Amortization of intangible assets	<b>377</b>	494	<b>905</b>	1,248
Loss on disposal of property and equipment	—	18	<b>14</b>	48
Impairment of property and equipment	<b>725</b>	2,658	<b>3,285</b>	4,971
Provision (recovery) for onerous contracts	<b>3,414</b>	(46)	<b>5,306</b>	(1,573)
Utilization for onerous contracts	<b>(2,126)</b>	(1,092)	<b>(4,820)</b>	(2,340)
Stock-based compensation	<b>91</b>	362	<b>(7)</b>	1,738
Executive separation costs related to salary	<b>123</b>	1,070	<b>840</b>	1,882
Strategic review and proxy contest costs	<b>27</b>	—	<b>3,538</b>	—
Other selling, general and administration	<b>7,936</b>	6,421	<b>21,580</b>	19,601
	<b>29,119</b>	27,035	<b>84,865</b>	79,004

## 12. EARNINGS PER SHARE

Basic earnings per share (“EPS”) amounts are calculated by dividing the net income (loss) for the period attributable to ordinary equity holders by the weighted average number of ordinary shares outstanding during the period. Diluted EPS amounts are calculated by dividing the net income (loss) attributable to ordinary equity holders (after adjusting for dividends) by the weighted average number of ordinary shares outstanding during the period plus the weighted average number of ordinary shares that would be issued on conversion of all the dilutive potential ordinary shares into ordinary shares, unless these would be anti-dilutive.

The following reflects the loss and share data used in the basic and diluted EPS computations:

	For the three months ended		For the nine months ended	
	November 3, 2018	October 28, 2017	November 3, 2018	October 28, 2017
	\$	\$	\$	\$
<b>Net loss for basic EPS</b>	<b>(9,061)</b>	<b>(6,485)</b>	<b>(20,261)</b>	<b>(12,410)</b>
<b>Weighted average number of shares outstanding — basic and fully diluted</b>	<b>25,992,339</b>	<b>25,829,090</b>	<b>25,862,086</b>	<b>25,659,164</b>

As a result of the net loss during the three and nine-month periods ended November 3, 2018, the stock options and RSUs disclosed in Note 9 are anti-dilutive.

## 13. RELATED PARTY DISCLOSURES

Other than the reimbursement of third-party costs described below incurred in connection with the proxy contest which culminated at the Company’s annual meeting held on June 14, 2018, (the “2018” Annual Meeting”), there have been no significant changes in related party transactions from those disclosed in the Company’s audited annual consolidated financial statements for the year ended February 3, 2018.

During the three and nine months ended November 3, 2018, the Company purchased merchandise and services from a company controlled by one of its executive employees amounting to \$125 and \$222, respectively [October 28, 2017 — nil].

During the three and nine months ended November 3, 2018, the Company reimbursed Rainy Day Investments Ltd. (“Rainy Day Investments”), a controlling shareholder, nil and \$957, respectively, for third-party costs incurred by it in connection with the proxy contest, as approved by the independent members of the Board of Directors of the Company. This amount is included in selling, general and administration expenses.

## 14. SEGMENT INFORMATION

An operating segment is a component of the Company that engages in business activities from which it may earn revenues and incur expenses. The Company has reviewed its operations and determined that each of its retail stores represents an operating segment. However, because its retail stores have similar economic characteristics, sell similar products, have similar types of customers, and use similar distribution channels, the Company has determined that these operating segments can be aggregated at a geographic level. As a result, the Company has concluded that it has two reportable segments, Canada and the U.S., that derive their respective revenues from the retail and online sale of tea, tea accessories and food and beverages. The Company’s Interim Chief Executive Officer (the chief operating decision maker or “CODM”) makes decisions about resource allocation and assesses performance at the country level, and for which discrete financial information is available.

The Company derives revenue from the following products:

	For the three months ended		For the nine months ended	
	November 3, 2018	October 28, 2017	November 3, 2018	October 28, 2017
	\$	\$	\$	\$
Tea	31,348	30,098	92,167	93,958
Tea accessories	8,478	8,636	25,979	30,315
Food and beverages	3,830	4,263	11,463	13,080
	<u>43,656</u>	<u>42,997</u>	<u>129,609</u>	<u>137,353</u>

Property and equipment and intangible assets by country are as follows:

	November 3, 2018	February 3, 2018
	\$	\$
Canada	35,342	37,234
US	3,748	3,763
<b>Total</b>	<u>39,090</u>	<u>40,997</u>

During the fourth quarter of Fiscal 2017, the Company changed the measure of profit used by the CODM in measuring performance. Management believes that the new measure, being results from operating activities before corporate expenses by country, excluding intercompany profit, is the most relevant in evaluating results. The Company has retroactively revised the results by segment for the three and nine-month periods ended October 28, 2017. Results from operating activities before corporate expenses per country are as follows:

	For the three months ended			For the nine months ended		
	November 3, 2018			November 3, 2018		
	Canada	US	Consolidated	Canada	US	Consolidated
	\$	\$	\$	\$	\$	\$
<b>Sales</b>	34,709	8,947	43,656	103,091	26,518	129,609
Cost of sales	19,520	5,755	25,275	55,060	16,133	71,193
<b>Gross profit</b>	15,189	3,192	18,381	48,031	10,385	58,416
Selling, general and administration expenses (allocated)	13,872	4,513	18,385	40,794	12,907	53,701
Impairment of property and equipment	725	—	725	3,096	189	3,285
Impact of onerous contracts	133	1,155	1,288	1,129	(643)	486
<b>Results from operating activities before corporate expenses</b>	459	(2,476)	(2,017)	3,012	(2,068)	944
Selling, general and administration expenses (non-allocated)			8,721			27,393
<b>Results from operating activities</b>			(10,738)			(26,449)
Finance costs			80			237
Finance income			(122)			(574)
<b>Loss before income taxes</b>			<u>(10,696)</u>			<u>(26,112)</u>

	For the three months ended			For the nine months ended		
	October 28, 2017			October 28, 2017		
	Canada	US	Consolidated	Canada	US	Consolidated
	\$	\$	\$	\$	\$	\$
<b>Sales</b>	35,495	7,502	42,997	112,803	24,550	137,353
Cost of sales	19,475	5,150	24,625	59,046	15,548	74,594
<b>Gross profit</b>	16,020	2,352	18,372	53,757	9,002	62,759
Selling, general and administration expenses (allocated)	12,414	4,319	16,733	37,806	13,265	51,071
Impairment of property and equipment	595	2,063	2,658	595	4,376	4,971
Impact of onerous contracts	(150)	(988)	(1,138)	(101)	(3,812)	(3,913)
<b>Results from operating activities before corporate expenses</b>	3,161	(3,042)	119	15,457	(4,827)	10,630
Selling, general and administration expenses (non-allocated)			8,782			26,875
<b>Results from operating activities</b>			(8,663)			(16,245)
Finance costs			327			615
Finance income			(149)			(420)
<b>Income before income taxes</b>			(8,841)			(16,440)

## 15. FINANCIAL RISK MANAGEMENT

The Company's activities expose it to a variety of financial risks, including risks related to foreign exchange, interest rate, liquidity and credit.

### Currency risk — foreign exchange risk

Currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. Given that some of its purchases are denominated in U.S. dollars, the Company is exposed to foreign exchange risk. The Company's foreign exchange risk is largely limited to currency fluctuations between the Canadian and U.S. dollars. The Company is exposed to currency risk through its cash, accounts receivable and accounts payable denominated in U.S. dollars.

Assuming that all other variables remain constant, a revaluation of these monetary assets and liabilities due to a 5% rise or fall in the Canadian dollar against the U.S. dollar would have resulted in an increase or decrease to net income (loss) in the amount of \$32.

The Company's foreign exchange exposure is as follows:

	November 3, 2018 US\$	February 3, 2018 US\$
Cash	1,963	5,686
Accounts receivable	1,639	882
Accounts payable	4,247	2,555

The Company's U.S. subsidiary's transactions are denominated in U.S. dollars.

In order to protect itself from the risk of losses should the value of the Canadian dollar decline in relation to the U.S. dollar, the Company entered into forward contracts to fix the exchange rate of 80% to 90% of its expected U.S. dollar inventory purchasing requirements, through September 2018. A forward foreign exchange contract is a contractual agreement to buy a specific currency at a specific price and date in the future. The Company designated the forward contracts as cash flow hedging instruments under IFRS 9. This has resulted in mark-to-market foreign exchange adjustments, for qualifying hedged instruments, being recorded as a component of other comprehensive income (loss) for the three and nine-month periods ended November 3, 2018.

The Company had no foreign exchange contracts outstanding as at November 3, 2018.

The nominal and contract values of foreign exchange contracts outstanding as at October 28, 2017 are as follows:

	Contractual exchange rate	Nominal value US\$	Nominal value C\$	Term	Unrealized gain C\$
<b>Purchase contracts</b>					
U.S. dollar	1.2221 - 1.3098	35,400	44,796	November 2017 to September 2018	628

### Market risk — interest rate risk

Interest rate risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market interest rates. Financial instruments that potentially subject the Company to cash flow interest rate risk include financial assets with variable interest rates and consists of cash. The Company is exposed to cash flow risk on its Amended Revolving Facility which bears interest at variable interest rates (Note 8). As at November 3, 2018, the Company did not have any borrowings under the Amended Revolving Facility.

### Liquidity risk

Liquidity risk is the risk that the Company will encounter difficulty in meeting obligations associated with financial liabilities. The Company's approach to managing liquidity risk is to ensure, to the extent possible, that it will always have sufficient liquidity to meet liabilities when due. The Company's liquidity follows a seasonal pattern based on the timing of inventory purchases and capital expenditures. The Company is exposed to this risk mainly in respect of its trade and other payables.

As at November 3, 2018, the Company had \$18,714 in cash.

The Company expects to finance its growth in store base, its store renovations and infrastructure investments through cash flows from operations and cash on hand. The Company expects that its trade and other payables will be discharged within 90 days.

### Credit risk

The Company is exposed to credit risk resulting from the possibility that counterparties may default on their financial obligations to the Company. The Company's maximum exposure to credit risk at the reporting date is equal to the carrying value of accounts receivable and derivative financial instruments. Accounts receivable primarily consist of receivables from retail customers who pay by credit card, recoveries of credits from suppliers for returned or damaged products, and receivables from other companies for sales of products, gift cards and other services. Credit card payments have minimal credit risk and the limited number of corporate receivables is closely monitored. The terms of foreign currency forward contracts included in derivative financial instruments have been negotiated to match the terms of the forecasted inventory purchase transactions. Both contractual parties have fully cash-collateralized the foreign currency forward contracts, and therefore, effectively eliminated any credit risk associated with the contracts (both the counterparty's and the Company's own credit risk).

### Fair values

Financial assets and financial liabilities are measured on an ongoing basis at fair value or amortized cost, based on the guidance provided in IFRS 9 and as disclosed in Note 3 in these unaudited condensed interim consolidated financial statements for the three and nine-month periods ended November 3, 2018. The fair values of derivative financial instruments have been determined by reference to forward exchange rates at the end of the reporting period and classified in Level 2 of the fair value hierarchy.

The Company enters into its foreign currency forward contracts with financial institutions with investment grade credit ratings. Foreign currency forward contracts are valued using valuation techniques with market observable inputs. The most frequently applied valuation techniques include forward pricing, using present value calculations. The models incorporate various inputs including the credit quality of counterparties, foreign exchange spot and forward rates, yield curves of the respective currencies, currency basis spreads between the respective currencies, interest rate curves and forward rate curves of the underlying commodity. All foreign currency forward contracts are fully cash collateralized, thereby mitigating both the counterparty and the Company's non-performance risk.

There were no transfers between Level 1, Level 2 and Level 3 of the fair value hierarchy during the nine-month period ended November 3, 2018 or the nine-month period ended October 28, 2017.

## **16. COMPARATIVE FIGURES**

Certain comparative figures have been reclassified to conform to the presentation adopted in the current quarter.

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

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

#### Forward-Looking Statements

*Certain statements contained herein include statements that express our opinions, expectations, beliefs, plans, objectives, assumptions or projections regarding future events or future results and are, or may be deemed to be, "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995 (the "Act"). The following cautionary statements are being made pursuant to the provisions of the Act and with the intention of obtaining the benefits of the "safe harbor" provisions of the Act. These forward-looking statements can generally be identified by the use of forward-looking terminology, including the terms "believes", "expects", "may", "will", "should", "could", "seeks", "projects", "approximately", "intends", "plans", "estimates" or "anticipates", or, in each case, their negatives or other variations or comparable terminology. These forward-looking statements include all matters that are not historical facts. They appear in a number of places throughout this Quarterly Report on Form 10-Q and include statements regarding our intentions, beliefs or current expectations concerning, among other things, our results of operations, our turnaround strategy, our store renovation plans, expansion into new sales channels, financial condition, liquidity, prospects, new store opening projections, use of cash and operating and capital expenditures, impact of new accounting pronouncements, and the impact of improvements to internal control and financial reporting. These risks and uncertainties include, but are not limited to, the risks referred to under the section entitled "Risk Factors" elsewhere in this Quarterly Report on Form 10-Q. Forward-looking statements speak only as of the date hereof. Except as required under federal securities laws and the rules and regulations of the SEC, we do not have any intention to update any forward-looking statements to reflect events or circumstances arising after the date of this Form 10-Q, whether as a result of new information, future events or otherwise. As a result of these risks and uncertainties, readers are cautioned not to place undue reliance on the forward-looking statements included in this Form 10-Q or that may be made elsewhere from time to time by, or on behalf of, us. All forward-looking statements attributable to us are expressly qualified by these cautionary statements.*

#### Accounting Periods

All references to "Fiscal 2018" are to the Company's fiscal year ending February 2, 2019. All references to "Fiscal 2017" are to the Company's fiscal year ended February 3, 2018. All references to "Fiscal 2016" are to the Company's fiscal year ended January 28, 2017.

The Company's fiscal year ends on the Saturday closest to the end of January, typically resulting in a 52-week year, but occasionally giving rise to an additional week, resulting in a 53-week year. Fiscal 2017 covers a 53-week fiscal period. Fiscal 2018 and Fiscal 2016 each cover a 52-week fiscal period.

#### Overview

We are a retailer of specialty tea, offering a differentiated selection of proprietary loose-leaf teas, pre-packaged teas, tea sachets and tea-related gifts, accessories and food and beverages, primarily through 238 company-operated DAVIDsTEA stores as of November 3, 2018, and our website, davidstea.com. We are building a brand that seeks to expand the definition of tea with innovative products that consumers can explore in an open and inviting retail environment and online. We strive to make tea a multi-sensory experience in our stores by facilitating interaction with our products through education and sampling so that our customers appreciate the compelling attributes of tea as well as the ease of preparation.

## How we assess our performance

The key measures we use to evaluate the performance of our business and the execution of our strategy are set forth below:

*Sales.* Sales consist primarily of sales from our retail stores and e-commerce site. Our business is seasonal and, as a result, our sales fluctuate from quarter to quarter. Sales are traditionally highest in the fourth fiscal quarter, which includes the holiday sales period, and tend to be lowest in the second and third fiscal quarters because of lower customer traffic in our locations during the summer months.

The specialty retail industry is cyclical, and our sales are affected by general economic conditions. A number of factors that influence the level of consumer spending, including economic conditions and the level of disposable consumer income, consumer debt, interest rates and consumer confidence, can affect purchases of our products. There has been a decline in customer traffic at many malls in which our stores are located. This reduction in foot traffic has had an impact on our sales at such stores.

*Comparable Sales.* Comparable sales refer to period-over-period comparison information for comparable stores and e-commerce. Our stores are added to the comparable sales calculation in the beginning of their thirteenth month of operation. As a result, data regarding comparable sales may not be comparable to similarly titled data from other retailers.

Measuring the change in period-over-period comparable sales allows us to evaluate how our business is performing. Various factors affect comparable sales, including:

- our ability to anticipate and respond effectively to consumer preference, buying and economic trends;
- our ability to provide a product offering that generates new and repeat visits to our stores and online;
- the customer experience we provide in our stores and online;
- the level of customer traffic near the locations in which we operate;
- the number of customer transactions and average ticket amount in our stores and online;
- the pricing of our tea, tea accessories, and food and beverages;
- our ability to obtain and distribute product efficiently;
- our opening of new stores in the vicinity of our existing stores; and
- the opening or closing of competitor stores in the vicinity of our stores.

*Non-Comparable Sales.* Non-comparable sales include sales from stores prior to the beginning of their thirteenth fiscal month of operation and from our wholesale sales channel, which includes sales to groceries, hotels, restaurants and institutions, office and workplace locations and food services, as well as corporate gifting.

*Gross Profit.* Gross profit is equal to our sales less our cost of sales. Cost of sales includes product costs, freight costs, store occupancy costs and distribution costs.

*Selling, General and Administration Expenses.* Selling, general and administration expenses consist of store operating expenses and other general and administration expenses, including store impairments and provision (recovery) for onerous contracts. Store operating expenses consist of all store expenses excluding occupancy related costs (which are included in costs of sales). General and administration costs consist of salaries and other payroll costs, travel, professional fees, stock compensation, marketing expenses, information technology and other operating costs.

General and administration costs, which are generally fixed in nature, do not vary proportionally with sales to the same degree as our cost of sales. We believe that these costs will decrease as a percentage of sales over time. Accordingly, this expense as a percentage of sales is usually higher in lower volume quarters and lower in higher volume quarters.

We present Adjusted selling, general and administration expenses as a supplemental measure because we believe it facilitates a comparative assessment of our selling, general and administration expenses under IFRS, while isolating the effects of some items that vary from period to period. It is reconciled to its nearest IFRS measure beginning on page 23 of this Quarterly Report on Form 10-Q.

*Results from Operating Activities.* Results from operating activities consist of our gross profit less our selling, general and administration expenses.

We present Adjusted results from operating activities as a supplemental performance measure because we believe it facilitates a comparative assessment of our operating performance relative to our performance based on our results under IFRS, while isolating the effects of some items that vary from period to period. It is reconciled to its nearest IFRS measure beginning on page 24 of this Quarterly Report on Form 10-Q.

*Finance Costs.* Finance costs consist of cash and imputed non-cash charges related to our credit, as well as the accretion expense on the provisions for onerous contracts.

*Finance Income.* Finance income consists of interest income on cash balances.

*Provision for Income Tax.* Provision for income tax consists of federal, provincial, state and local current and deferred income taxes.

*Adjusted EBITDA.* We present Adjusted EBITDA as a supplemental performance measure because we believe it facilitates a comparative assessment of our operating performance relative to our performance based on our results under IFRS, while isolating the effects of some items that vary from period to period. Specifically, Adjusted EBITDA allows for an assessment of our operating performance and our ability to service or incur indebtedness without the effect of non-cash charges, such as depreciation, amortization, finance costs, deferred rent, non-cash compensation expense, costs (recovery) related to onerous contracts or contracts where we expect the costs of the obligations to exceed the economic benefit, loss on disposal of property and equipment, impairment of property and equipment, and certain non-recurring expenses. This measure also functions as a benchmark to evaluate our operating performance. It is reconciled to its nearest IFRS measure beginning on page 25 of this Quarterly Report on Form 10-Q.

## Selected Operating and Financial Highlights

### Results of Operations

The following table summarizes key components of our results of operations for the periods indicated:

	<u>For the three months ended</u>		<u>For the nine months ended</u>	
	<u>November 3, 2018</u>	<u>October 28, 2017</u>	<u>November 3, 2018</u>	<u>October 28, 2017</u>
	(unaudited)	(unaudited)	(unaudited)	(unaudited)
<b>Consolidated statement of income (loss) data:</b>				
Sales	\$ 43,656	\$ 42,997	\$ 129,609	\$ 137,353
Cost of sales	25,275	24,625	71,193	74,594
<b>Gross profit</b>	<b>18,381</b>	18,372	<b>58,416</b>	62,759
Selling, general and administration expenses	29,119	27,035	84,865	79,004
<b>Results from operating activities</b>	<b>(10,738)</b>	(8,663)	<b>(26,449)</b>	(16,245)
Finance costs	80	327	237	615
Finance income	(122)	(149)	(574)	(420)
<b>Loss before income taxes</b>	<b>(10,696)</b>	(8,841)	<b>(26,112)</b>	(16,440)
Recovery of income tax	(1,635)	(2,356)	(5,851)	(4,030)
<b>Net loss</b>	<b>\$ (9,061)</b>	\$ (6,485)	<b>\$ (20,261)</b>	\$ (12,410)
<b>Percentage of sales:</b>				
Sales	100.0%	100.0%	100.0%	100.0%
Cost of sales	57.9%	57.3%	54.9%	54.3%
Gross profit	42.1%	42.7%	45.1%	45.7%
Selling, general and administration expenses	66.7%	62.9%	65.5%	57.5%
Results from operating activities	(24.6%)	(20.2%)	(20.4%)	(11.8%)
Finance costs	0.2%	0.7%	0.1%	0.4%
Finance income	(0.3%)	(0.3%)	(0.4%)	(0.3%)
Loss before income taxes	(24.5%)	(20.6%)	(20.1%)	(11.9%)
Recovery of income tax	(3.7%)	(5.5%)	(4.5%)	(2.9%)
Net loss	(20.8%)	(15.1%)	(15.6%)	(9.0%)
<b>Other financial and operations data:</b>				
Adjusted EBITDA (1)	\$ (6,248)	\$ (2,887)	\$ (12,212)	\$ (3,578)
Adjusted EBITDA as a percentage of sales	(14.3%)	(6.7%)	(9.4%)	(2.6%)
Number of stores at end of period	238	236	238	236
Comparable sales decline for period (2)	(4.7%)	(6.8%)	(8.8%)	(4.5%)

(1) For a reconciliation of Adjusted EBITDA to net income see “—Non-IFRS Metrics” below.

(2) Comparable sales refer to period-over-period comparison information for comparable stores and e-commerce. Our stores are added to the comparable sales calculation in the beginning of their thirteenth month of operation.

#### Non-IFRS Metrics

Adjusted selling, general and administration expenses, Adjusted results from operating activities and Adjusted EBITDA are not presentations made in accordance with IFRS, and the use of the terms Adjusted selling, general and administration expenses, Adjusted results from operating activities and Adjusted EBITDA may differ from similar measures reported by other companies. We believe that Adjusted selling, general and administration expenses, Adjusted results from operating activities and Adjusted EBITDA provide investors with useful information with respect to our historical operations.

Adjusted selling, general and administration expenses, Adjusted results from operating activities and Adjusted EBITDA are not measurements of our financial performance under IFRS and should not be considered in isolation or as an alternative to net income, net cash provided by operating, investing or financing activities or any other financial statement data presented as indicators of financial performance or liquidity, each as presented in accordance with IFRS. We understand that although Adjusted selling, general and administration expenses, Adjusted results from operating activities and Adjusted EBITDA are frequently used by securities analysts, lenders and others in their evaluation of companies, they have limitations as an

analytical tool, and should not be considered in isolation, or as a substitute for analysis of our results as reported under IFRS. Some of these limitations are:

- Adjusted selling, general and administration expenses, Adjusted results from operating activities and Adjusted EBITDA do not reflect changes in, or cash requirements for, our working capital needs and do not reflect the cash requirements necessary to service interest or principal payments on our debt; and
- Although depreciation and amortization are non-cash charges, the assets being depreciated and amortized will often have to be replaced in the future, and Adjusted EBITDA does not reflect any cash requirements for such replacements.

Because of these limitations, Adjusted selling, general and administration expenses, Adjusted results from operating activities and Adjusted EBITDA should not be considered as discretionary cash available to us to reinvest in the growth of our business or as a measure of cash that will be available to us to meet our obligations.

The following tables present reconciliations of Adjusted selling, general and administration expenses, Adjusted results from operating activities and Adjusted EBITDA to their most comparable IFRS figures.

*Reconciliation of Adjusted selling, general and administration expenses*

(in thousands)	For the three months ended		For the nine months ended	
	November 3, 2018	October 28, 2017	November 3, 2018	October 28, 2017
<b>Selling, general and administration expenses</b>	29,119	27,035	84,865	79,004
Executive separation costs (a)	(123)	(1,112)	(840)	(2,074)
Impairment of property and equipment (b)	(725)	(2,658)	(3,285)	(4,971)
Impact of onerous contracts (c)	(1,288)	1,138	(486)	3,913
Strategic review and proxy contest costs (d)	(27)	—	(3,538)	—
<b>Adjusted selling, general and administration expenses</b>	<b>\$ 26,956</b>	<b>\$ 24,403</b>	<b>\$ 76,716</b>	<b>\$ 75,872</b>

- (a) Executive separation costs represent mainly salary owed to certain former executives as part of their separation of employment from the Company. The three and nine-month periods ended October 28, 2017 include \$42 and \$192, respectively, of non-cash stock-based compensation expenses relating to the vesting of equity awards pursuant to the separation agreements.
- (b) Represents non-cash provisions related to impairment of property and equipment for stores.
- (c) Represents non-cash provisions, non-cash reversals, and utilization related to certain stores where the unavoidable costs of meeting the obligations under the lease agreements are expected to exceed the economic benefits expected to be received from the contract.
- (d) Represents costs related to a corporate strategic review process as well as costs related to the proxy contest which culminated at the 2018 Annual Meeting. Costs for the three and nine months ended November 3, 2018 include nil and \$389, respectively, related to the strategic review process, nil and \$868 for incremental directors' and officers' run-off insurance costs incurred prior to the 2018 Annual Meeting, and \$27 and \$2,281, respectively, for costs incurred in connection with the proxy contest, including nil and \$957, respectively, paid to Rainy Day Investments, a controlling shareholder, for third-party costs incurred by it, as approved by the independent members of the Board of Directors of the Company.

Reconciliation of Adjusted results from operating activities

(in thousands)	For the three months ended		For the nine months ended	
	November 3, 2018	October 28, 2017	November 3, 2018	October 28, 2017
<b>Results from operating activities</b>	(10,738)	(8,663)	(26,449)	(16,245)
Executive separation costs (a)	123	1,112	840	2,074
Impairment of property and equipment (b)	725	2,658	3,285	4,971
Impact of onerous contracts (c)	1,288	(1,138)	486	(3,913)
Strategic review and proxy contest costs (d)	27	—	3,538	—
<b>Adjusted results from operating activities</b>	<b>\$ (8,575)</b>	<b>\$ (6,031)</b>	<b>\$ (18,300)</b>	<b>\$ (13,113)</b>

- (a) Executive separation costs related to salary represent mainly salary owed to the former executives as part of their separation of employment from the Company. The three and nine-month periods ended October 28, 2017 include \$42 and \$192, respectively, of non-cash stock-based compensation expenses relating to the vesting of equity awards pursuant to the separation agreements.
- (b) Represents non-cash provisions related to impairment of property and equipment for stores.
- (c) Represents non-cash provisions, non-cash reversals, and utilization related to certain stores where the unavoidable costs of meeting the obligations under the lease agreements are expected to exceed the economic benefits expected to be received from the contract.
- (d) Represents costs related to a corporate strategic review process as well as costs related to the proxy contest which culminated at the 2018 Annual Meeting. Costs for the three and nine months ended November 3, 2018 include nil and \$389, respectively, related to the strategic review process, nil and \$868 for incremental directors' and officers' run-off insurance costs incurred prior to the 2018 Annual Meeting, and \$27 and \$2,281, respectively, for costs incurred in connection with the proxy contest, including nil and \$957, respectively, paid to Rainy Day Investments, a controlling shareholder, for third-party costs incurred by it, as approved by the independent members of the Board of Directors of the Company.

Reconciliation of Adjusted EBITDA to our net loss

(in thousands)	For the three months ended		For the nine months ended	
	November 3, 2018	October 28, 2017	November 3, 2018	October 28, 2017
<b>Net loss</b>	<b>\$ (9,061)</b>	<b>\$ (6,485)</b>	<b>\$ (20,261)</b>	<b>\$ (12,410)</b>
Finance costs	80	327	237	615
Finance income	(122)	(149)	(574)	(420)
Depreciation and amortization	2,162	2,632	6,098	7,564
Loss on disposal of property and equipment	—	18	14	48
Recovery of income tax	(1,635)	(2,356)	(5,851)	(4,030)
<b>EBITDA</b>	<b>\$ (8,576)</b>	<b>\$ (6,013)</b>	<b>\$ (20,337)</b>	<b>\$ (8,633)</b>
Additional adjustments:				
Stock-based compensation expense (reversal) (a)	91	362	(7)	1,738
Executive separation costs related to salary (b)	123	1,070	840	1,882
Impairment of property and equipment (c)	725	2,658	3,285	4,971
Impact of onerous contracts (reversals) (d)	1,288	(1,138)	486	(3,913)
Deferred rent (e)	74	174	(17)	377
Strategic review and proxy contest costs (f)	27	—	3,538	—
<b>Adjusted EBITDA</b>	<b>\$ (6,248)</b>	<b>\$ (2,887)</b>	<b>\$ (12,212)</b>	<b>\$ (3,578)</b>

- (a) Represents non-cash net stock-based compensation expense (reversal).
- (b) Executive separation costs related to salary represent salary owed to former executives as part of their separation of employment from the Company.
- (c) Represents non-cash provisions related to impairment of property and equipment for stores.

- (d) Represents non-cash provisions, non-cash reversals, and utilization related to certain stores where the unavoidable costs of meeting the obligations under the lease agreements are expected to exceed the economic benefits expected to be received from the contract.
- (e) Represents the extent to which the Company's annual rent expense has been above or below its cash rent payments.
- (f) Represents costs related to a corporate strategic review process as well as costs related to the proxy contest which culminated at the 2018 Annual Meeting. Costs for the three and nine months ended November 3, 2018 include nil and \$389, respectively, related to the strategic review process, nil and \$868 for incremental directors' and officers' run-off insurance costs incurred prior to the 2018 Annual Meeting, and \$27 and \$2,281, respectively, for costs incurred in connection with the proxy contest, including nil and \$957, respectively, paid to Rainy Day Investments, a controlling shareholder, for third-party costs incurred by it, as approved by the independent members of the Board of Directors of the Company.

*Three Months Ended November 3, 2018 Compared to Three Months Ended October 28, 2017*

*Sales.* Sales for the three months ended November 3, 2018 increased 1.6% and \$0.7 million, to \$43.7 million from \$43.0 million for the three months ended October 28, 2017. E-commerce and wholesale channels increased \$2.0 million and 35.1% compared to the three months ended October 28, 2017 driven primarily by greater online adoption in both Canada and the U.S. and our entry into grocery chain distribution earlier this year. Non-comparable sales of \$1.6 million from stores opened for less than thirteen months, helped to partially offset decreases of \$2.9 million and 7.9% in comparable sales.

*Gross Profit.* Gross profit remained consistent at \$18.4 million for both the three months ended November 3, 2018 and the three months ended October 28, 2017. Gross profit as a percentage of sales decreased slightly to 42.1% for the three months ended November 3, 2018 from 42.7% for the three months ended October 28, 2017 respectively, resulting from a shift in product sales mix and a deleveraging of fixed costs due to negative comparable sales.

*Selling, General and Administration Expenses.* Selling, general and administration expenses for the three months ended November 3, 2018 increased by 7.7%, and \$2.1 million, to \$29.1 million from \$27.0 million for the three months ended October 28, 2017. As a percentage of sales, selling, general and administration expenses increased to 66.7% for the three months ended November 3, 2018 compared to 62.9% for the three months ended October 28, 2017. Excluding the impact of executive separation costs, impairment of property and equipment, onerous contracts and costs related to the strategic review and proxy contest for the three months ended November 3, 2018 and October 28, 2017, selling, general and administration expenses increased to \$27.0 million for the three months ended November 3, 2018 from \$24.4 million for the three months ended October 28, 2017. The increase of \$2.6 million and 10.4% was attributable primarily to a \$1.7 million increase in staff compensation, partly attributable to minimum wage increases, and a \$0.8 million increase in foreign currency translation losses. As a percentage of sales, selling, general and administration expenses excluding these items increased to 61.7% from 56.7%, due to deleveraging of fixed costs as a result of the negative comparable sales this quarter.

*Results from Operating Activities.* Losses from operating activities increased by \$2.1 million, to \$10.7 million for the three months ended November 3, 2018 from a loss of \$8.7 million for the three months ended October 28, 2017. Excluding the impact of executive separation costs, impairment of property and equipment, onerous contracts and the strategic review and proxy contest for the three months ended November 3, 2018, losses from operating activities increased by \$2.6 million, to \$8.6 million from a loss of \$6.0 million for the three months ended October 28, 2017.

*Recovery of Income Taxes.* Recovery of income taxes decreased by \$0.7 million, to \$1.6 million for the three months ended November 3, 2018 from \$2.4 million for the three months ended October 28, 2017. The decrease was due primarily to lower operating activities and a provision recorded of \$0.9 million in connection with an uncertainty in the eventual outcome of a tax position the Company has taken. The Company's effective tax rates were 15.3% and 24.7% for the three months ended November 3, 2018 and October 28, 2017, respectively. Adjusting the November 3, 2018

effective tax rate for the provision taken on uncertain tax position, the Company's effective tax rate would have been 26.5%.

#### *Nine Months Ended November 3, 2018 Compared to Nine Months Ended October 28, 2017*

*Sales.* Sales for the nine months ended November 3, 2018 decreased 5.7%, or \$7.8 million, to \$129.6 million from \$137.4 million for the nine months ended October 28, 2017. E-commerce and wholesale channel sales increased \$3.0 million and 19.4% compared to the nine months ended October 28, 2017 driven primarily by greater online adoption in both Canada and the U.S. and our entry into grocery chain distribution. Non-comparable sales of \$2.5 million from stores opened for less than thirteen months, helped to partially offset decreases of \$13.3 million and 11.7% in comparable sales.

*Gross Profit.* Gross profit decreased by 7.0%, or \$4.4 million, to \$58.4 million for the nine months ended November 3, 2018 from \$62.8 million for the nine months ended October 28, 2017. Gross profit as a percentage of sales decreased slightly to 45.1% for the nine months ended November 3, 2018 from 45.7% for the nine months ended October 28, 2017.

*Selling, General and Administration Expenses.* Selling, general and administration expenses increased by 7.4%, or \$5.9 million, to \$84.9 million for the nine months ended November 3, 2018 from \$79.0 million for the nine months ended October 28, 2017. As a percentage of sales, selling, general and administration expenses increased to 65.5% for the nine months ended November 3, 2018 compared to 57.5% for the nine months ended October 28, 2017. Excluding the impact of separation costs, impairment of property and equipment, onerous contracts and costs related to the strategic review and proxy contest for the nine months ended November 3, 2018 and October 28, 2017, selling, general and administration expenses increased to \$76.7 million for the nine months ended November 3, 2018 from \$75.9 million for the nine months ended October 28, 2017. The net increase of \$0.8 million and 1.1% was attributable to a \$1.9 million increase in salaries, partly attributable to minimum wage increases, a \$0.5 million increase in foreign exchange translation losses and a \$1.7 million decrease in non-cash stock-based compensation expense. As a percentage of sales, selling, general and administration expenses excluding the impact of these items increased to 59.2% from 55.2%, due to deleveraging of fixed costs as a result of the negative comparable sales.

*Results from Operating Activities.* Losses from operating activities increased by \$10.2 million, to \$26.4 million for the nine months ended November 3, 2018 from a loss of \$16.2 million for the nine months ended October 28, 2017. Excluding the impact of executive separation costs, impairment of property and equipment, onerous contracts and costs related to the strategic review and proxy contest for the nine months ended November 3, 2018 and October 28, 2017, results from operating activities increased by \$5.2 million, to \$18.3 million from a loss of \$13.1 million for the nine months ended October 28, 2017.

*Recovery of Income Taxes.* Recovery of income taxes increased by \$1.8 million, to a recovery of \$5.9 million for the nine months ended November 3, 2018 from a recovery of \$4.0 million for the nine months ended October 28, 2017. The increase was due primarily to an increase in recovery of income taxes attributable primarily to lower results from operating activities, partially offset by a \$0.9 million tax provision in connection with an uncertainty in the eventual outcome of a tax position the Company has taken. The Company's effective tax rates were 22.4% and 24.6% for the nine months ended November 3, 2018 and October 28, 2017, respectively. Adjusting the November 3, 2018 effective tax rate for the provision taken on uncertain tax position, the Company's effective tax rate would have been 27.0%.

#### **Liquidity and Capital Resources**

As at November 3, 2018, the Company had \$18.7 million of cash primarily held with major Canadian financial institutions. Working capital was \$55.1 million as at November 3, 2018, compared to \$77.2 million as at February 3, 2018.

The Company's primary sources of liquidity are cash on hand and cash flows from operations. The Company's primary cash needs are to support the increase in inventories and for capital expenditures related to new stores, store renovations and infrastructure investments.

Capital expenditures typically vary depending on the timing of new store openings, store renovations and infrastructure-related investments.

The Company's primary working capital requirements are for the purchase of store inventory and payment of payroll, rent and other store operating costs. The Company's working capital requirements fluctuate during the year, rising in the second and third fiscal quarters as the Company takes title to increasing quantities of inventory in anticipation of its peak selling season in the fourth fiscal quarter. The Company funds its capital expenditures and working capital requirements from cash on hand and net cash provided by its operating activities.

The Company believes that its cash position and net cash provided by its operating activities will be adequate to finance its planned capital expenditures and working capital requirements for the foreseeable future.

#### *Cash Flow*

A summary of the Company's cash flows from operating, investing and financing activities is presented in the following table:

	<u>For the three months ended</u>		<u>For the nine months ended</u>	
	<u>November 3,</u>	<u>October 28,</u>	<u>November 3,</u>	<u>October 28,</u>
	<u>2018</u>	<u>2017</u>	<u>2018</u>	<u>2017</u>
<b>Cash flows provided by (used in):</b>				
Operating activities	\$ (18,037)	\$ (16,134)	\$ (37,581)	\$ (19,976)
Investing activities	(2,880)	(3,498)	(7,271)	(9,295)
Financing activities	8	90	82	1,696
<b>Decrease in cash</b>	<b>\$ (20,909)</b>	<b>\$ (19,542)</b>	<b>\$ (44,770)</b>	<b>\$ (27,575)</b>

#### *Cash Flows Provided by (Used in) Operating Activities*

Net cash used in operating activities decreased to \$18.0 million for the three months ended November 3, 2018 from \$16.1 million for the three months ended October 28, 2017. The decrease in the cash flows used in operating activities was due primarily to lower results from operations and to an increase in working capital attributed to prepaid rents, due to the timing of quarter end, and higher investments in inventory to support the sales for the holiday season.

Net cash used in operating activities decreased to \$37.6 million for the nine months ended November 3, 2018 from \$20.0 million for the nine months ended October 28, 2017. The decrease in the cash flows used in operating activities was due primarily to lower results from operations and to an increase in working capital attributed to prepaid rents, due to the timing of quarter end, and higher investments in inventory in comparison to the nine months ended October 28, 2017.

#### *Cash Flows Provided by (Used in) Investing Activities*

Capital expenditures decreased by \$0.6 million, to \$2.9 million for the three months ended November 3, 2018 from \$3.5 million for the three months ended October 28, 2017. The decrease was primarily due to a lower number of new store build-outs and store renovations.

Capital expenditures decreased by \$2.0 million, to \$7.3 million for the nine months ended November 3, 2018 from \$9.3 million for the nine months ended October 28, 2017. The decrease was primarily due to a lower number of new store build-outs and store renovations.

### ***Cash Flows Provided By Financing Activities***

Net cash flows provided by financing activities were \$0.0 million and \$0.1 million for the three and nine months ended November 3, 2018, compared to \$0.1 million and \$1.7 million, respectively, for the three and nine months ended October 28, 2017.

### ***Credit Facility***

In June 2018, the Company entered into a two year revolving credit facility, the Amended Credit Agreement, with a major Canadian financial institution, its lender.

The Amended Credit Agreement subjects the Company to certain financial covenants entered into between the Company and its lender. Without the prior written consent of the lender, the Company's fixed charge coverage ratio may not be less than 1.10:1.00 and the Company's leverage ratio may not exceed 3.00:1.00. In addition, the Company's net tangible worth may not be less than \$65,000 and the Company's minimum excess availability must not be less than \$15.0 million. The Amended Revolving Facility bears interest based on the Company's adjusted leverage ratio, at the lender's prime rate, U.S. bank rate and LIBOR plus a range from 0.5% to 2.5% per annum. A standby fee range of 0.3% to 0.5% will be paid on the daily principal amount of the unused portion of the Amended Revolving Facility.

The Amended Credit Agreement also contains non-financial covenants that, among other things and subject to certain exceptions, restrict the Company's ability to become a guarantor or endorser or otherwise become liable upon any note or other obligation other than in the normal course of business. The Company also cannot make any dividend payments.

As at November 3, 2018 and February 3, 2018, the Company did not have any borrowings under the Amended Revolving Facility.

### **Off-Balance Sheet Arrangements**

Other than operating lease obligations, the Company has no off-balance sheet obligations.

### **Contractual Obligations and Commitments**

There have been no significant changes to the Company's contractual obligations as disclosed in our consolidated financial statements for the fiscal year ended February 3, 2018, other than those which occur in the normal course of business.

### **Critical Accounting Policies and Estimates**

The Company's discussion and analysis of operating results and financial condition are based upon its financial statements. The preparation of financial statements requires the Company to estimate the effect of various matters that are inherently uncertain as of the date of the financial statements. Each of these required estimates varies in regard to the level of judgment involved and its potential impact on the reported financial results. Estimates are deemed critical when a different estimate could have reasonably been used or where changes in the estimates are reasonably likely to occur from period to period, and would materially impact the Company's financial position, changes in financial position or results of operations. The Company's significant accounting policies are discussed under note 3 to its consolidated financial statements for the year ended February 3, 2018 included in the Annual Report on Form 10-K filed with the SEC on April 19, 2018. There have been no material changes to the critical accounting policies and estimates since February 3, 2018, other than as described below.

### **Recently Issued Accounting Standards**

As of February 4, 2018, the Company adopted the new accounting standards described below.

IFRS 9, “Financial Instruments” (“IFRS 9”), replaces IAS 39, “Financial Instruments: Recognition and Measurement” and all previous versions of IFRS 9. IFRS 9 brings together all three aspects of the accounting for financial instruments project: classification and measurement, impairment and hedge accounting. With the exception of hedge accounting, which the Company applied prospectively, it has applied IFRS 9 retrospectively, with the initial application date of February 4, 2018. Overall, there was no material impact on the Company’s consolidated financial statements.

IFRS 15, “Revenue from Contracts with Customers” (“IFRS 15”), replaces IAS 11, “Construction Contracts”, and IAS 18, “Revenue”, as well as various interpretations regarding revenue. This standard introduces a single model for recognizing revenue that applies to all contracts with customers, except for contracts that are within the scope of standards on leases, insurance and financial instruments. This standard also requires enhanced disclosures. Adoption of IFRS 15 is mandatory and is effective for annual periods beginning on or after January 1, 2018. The implementation of IFRS 15 impacts the allocation of revenue that is deferred in relation to the Company’s customer loyalty award programs. Prior to adoption, revenue was allocated to the customer loyalty awards using the residual fair value method. Under IFRS 15, consideration is allocated between the loyalty program awards and the goods on which the awards were earned, based on their relative stand-alone selling prices. The change in allocation of revenue that is deferred in relation to the Company’s customer loyalty program does not have a material impact on retained earnings as at February 4, 2018. Overall, there was not a material impact on the Company’s consolidated financial statements.

IFRIC 22, “Foreign Currency Transactions and Advance Consideration” (“IFRIC 22”). In December 2016, the IASB issued IFRIC 22, which addresses how to determine the date of the transaction for the purpose of determining the exchange rate to use on initial recognition of the related asset, expense or income (or part of it) and on the derecognition of a non-monetary asset or non-monetary liability arising from the payment or receipt of advance consideration in a foreign currency. IFRIC 22 is effective for annual periods beginning on or after January 1, 2018. There was no material impact on the Company’s consolidated financial statements.

Information on significant new accounting standards and amendments issued but not yet adopted is described below.

IFRS 16, “Leases” (“IFRS 16”) replaces IAS 17, “Leases”. This standard provides a single model for leases abolishing the current distinction between finance and operating leases, with most leases being recognized in the statement of financial position. Certain exemptions will apply for short-term leases and leases of low value assets. The new standard will be effective for annual periods beginning on or after January 1, 2019, with early application permitted. The Company has performed a preliminary assessment of the potential impact of the adoption of IFRS 16 on its consolidated financial statements. The Company expects the adoption of IFRS 16 will have a significant impact as the Company will recognize new assets and liabilities for its operating leases of retail stores. In addition, the nature and timing of expenses related to those leases will change as IFRS 16 replaces the straight-line operating lease expense with a depreciation charge for right-of-use assets and interest expense on lease liabilities. The Company has not yet determined which transition method it will apply or whether it will use the optional exemptions or practical expedients under the standard. The Company expects to disclose additional detailed information, including its transition method, any practical expedients elected and estimated quantitative financial effects, before the adoption of IFRS 16.

IFRIC 23, “Uncertainty over Income Tax Treatments”, was issued by the IASB in June 2017. IFRIC 23 provides guidance on the accounting for current and deferred tax liabilities and assets in circumstances in which there is uncertainty over income tax treatments. IFRIC 23 is effective for annual periods beginning on or after January 1, 2019. Earlier application is permitted. IFRIC 23 requires an entity to:

- Contemplate whether uncertain tax treatments should be considered separately, or together as a group, based on which approach provides better predictions of the resolution;
- Reflect an uncertainty in the amount of income tax payable (recoverable) if it is probable that it will pay (or recover) an amount for the uncertainty; and
- Measure a tax uncertainty based on the most likely amount or expected value depending on whichever method better predicts the amount payable (recoverable).

The Company does not expect a material impact from the adoption of IFRIC 23 on its consolidated financial statements.

### **Item 3. Quantitative and Qualitative Disclosures About Market Risk**

There has been no material change in the foreign exchange and interest rate risk discussed in “Management’s Discussion and Analysis of Financial Condition and Results of Operations” included in the Company’s Annual Report on Form 10-K for the year ended February 3, 2018 filed with the SEC on April 19, 2018.

### **Item 4. Controls and Procedures**

#### *Disclosure Controls and Procedures*

The Company’s management, with the participation of the Interim Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of its disclosure controls and procedures as of November 3, 2018. The term “disclosure controls and procedures,” as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (“Exchange Act”), means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company’s management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure. Management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based on the evaluation of the Company’s disclosure controls and procedures as of November 3, 2018, the Interim Chief Executive Officer and Chief Financial Officer concluded that, as of such date, the Company’s disclosure controls and procedures were effective.

#### *Changes in Internal Control over Financial Reporting*

There have been no changes in the Company’s internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) during the three and nine-month period ended November 3, 2018 that have materially affected or are reasonably likely to materially affect the Company’s internal controls over financial reporting.

## **Item 1. Legal Proceedings**

The Company is, from time to time, subject to claims and suits arising in the ordinary course of business. Although the outcome of these and other claims cannot be predicted with certainty, management does not believe that the ultimate resolution of any matters in which the Company is currently involved will have a material adverse effect on its financial position or on its results of operations.

On June 1, 2018, certain investment funds managed by Porchlight Equity Management LLC (the “Porchlight Funds”) filed an Application for declaratory judgment in the Superior Court in the District of Montreal, Province of Québec (the “Initial Action”) against Rainy Day Investments, our controlling shareholder, and Herschel Segal, who controls Rainy Day Investments. The Company and its directors were named as “mis en cause”, also referred to as an impleaded party. The Initial Action related to a 2013 settlement agreement between the Porchlight Funds and Rainy Day Investments. On July 20, 2018, the Initial Action was discontinued.

On July 24, 2018, the Porchlight Funds filed an “Application for declaratory judgment and for the issuance of orders for relief from oppression and to prohibit defendant Herschel Segal from holding the office of director and/or executive chairman and/or chief executive officer of [the Company]” in the Superior Court in the District of Montreal, Province of Québec against Rainy Day Investments and Herschel Segal (the “Second Action”). The Company and its directors were again named as impleaded parties. The allegations contained in the Second Action were similar to those contained in the Initial Action. In October 2018, the Second Action was discontinued.

## **Item 1A. Risk Factors**

In addition to the other information set forth in this Quarterly Report on Form 10-Q, you should carefully consider the factors discussed in Part I, “Item 1A. Risk Factors” in our Annual Report on Form 10-K for the year ended February 3, 2018 and in Part II, “Item 1A. Risk Factors” in our Quarterly Report on Form 10-Q for the quarterly period ended November 3, 2018, as filed with the SEC, which could materially affect our business, financial condition or future results.

If any of such risks actually occurs, our business, prospects, operating results and financial condition could suffer materially, the trading price of our common shares could decline and you could lose all or part of your investment in the Company. Although we believe that we have identified and discussed as referred to above the key risk factors affecting our business, there may be additional risks and uncertainties that are not currently known to us or that are currently deemed immaterial that may adversely affect our business and financial condition.

## **Item 2. Unregistered Sales of Equity Securities**

### **Recent Sales of Unregistered Securities**

Not applicable.

## **Item 3. Defaults Upon Senior Securities**

Not applicable.

## **Item 4. Mine Safety Disclosures**

Not applicable.

## **Item 5. Other Information**

### **Indemnification Agreements**

On December 10, 2018, the Company entered into an Indemnification Agreement with Frank Zitella, the Company's recently appointed Chief Financial Officer. The Company also expects to enter into the Indemnification Agreement with its future officers and directors.

The Indemnification Agreement requires the Company to indemnify these individuals to the fullest extent permitted by the laws of the Province of Québec and the federal laws of Canada applicable in the Province of Québec, for certain liabilities to which they may become subject as a result of their affiliation with the Company.

The foregoing summary description of the material terms of the Indemnification Agreement does not purport to be complete and is subject to, and qualified in its entirety by reference to, the full text of form of Indemnification Agreement, which was attached as Exhibit 10.2 to the Quarterly Report on Form 10-Q filed with the SEC on September 13, 2018 and incorporated herein by reference.

## **Item 6. Exhibits**

(a) Exhibits:

- 31.1 Principal Executive Officer Certification Pursuant to Securities Exchange Act Rules 13a-14 and 15d-14 as Adopted Pursuant to the Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Principal Financial Officer Certification Pursuant to Securities Exchange Act Rules 13a-14 and 15d-14 as Adopted Pursuant to the Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Principal Executive Officer Certification Pursuant to 18 U.S.C. Section 1350 as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Principal Financial Officer Certification Pursuant to 18 U.S.C. Section 1350 as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

## SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

### DAVIDsTEA Inc.

Date: December 13, 2018

By: /s/ Herschel Segal

Name: Herschel Segal

Title: Chairman and Interim Chief Executive Officer  
(principal executive officer)

Date: December 13, 2018

By: /s/ Frank Zitella

Name: Frank Zitella

Title: Chief Financial Officer (principal accounting  
officer and principal financial officer)

**CERTIFICATION PURSUANT TO  
SECURITIES EXCHANGE ACT RULES 13a-14 and 15d-14  
AS ADOPTED PURSUANT TO  
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Herschel Segal, President and Chief Executive Officer, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q for the fiscal quarter ended November 3, 2018 of DAVIDsTEA Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: December 13, 2018

/s/ Herschel Segal  
\_\_\_\_\_  
Herschel Segal  
President and Chief Executive Officer

**CERTIFICATION PURSUANT TO  
SECURITIES EXCHANGE ACT RULES 13a-14 and 15d-14  
AS ADOPTED PURSUANT TO  
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Frank Zitella, Chief Financial Officer, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q for the fiscal quarter ended November 3, 2018 of DAVIDsTEA Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: December 13, 2018

/s/ Frank Zitella  
Frank Zitella  
Chief Financial Officer

**CERTIFICATION PURSUANT TO  
18 U.S.C. SECTION 1350  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of DAVIDsTEA Inc. (the “Company”) on Form 10-Q for the period ended November 3, 2018, as filed with the Securities and Exchange Commission (the “Report”), I, Herschel Segal, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that based on my knowledge:

- 1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- 2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: December 13, 2018

/s/ Herschel Segal

Herschel Segal  
President and Chief Executive Officer

**CERTIFICATION PURSUANT TO  
18 U.S.C. SECTION 1350  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of DAVIDsTEA Inc. (the “Company”) on Form 10-Q for the period ended November 3, 2018, as filed with the Securities and Exchange Commission (the “Report”), I, Howard Tafler, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that based on my knowledge:

- 1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- 2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: December 13, 2018

/s/ Frank Zitella

\_\_\_\_\_  
Frank Zitella  
Chief Financial Officer