

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

This Quarterly Report on Form 10-Q/A includes statements that express our opinions, expectations, beliefs, plans, objectives, assumptions or projections regarding future events or future results and there 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/A and include statements regarding our intentions, beliefs or current expectations concerning, among other things, our results of operations, financial condition, liquidity, prospects, competitive strengths and differentiators, strategy, long-term Adjusted EBITDA margin potential, dividend policy, impact of the macroeconomic environment, properties, outcome of litigation and legal proceedings, use of cash and operating and capital expenditures, impact of new accounting pronouncements, impact of improvements to internal control and financial reporting.

While we believe these expectations and projections are based on reasonable assumptions, such forward-looking statements are inherently subject to risks, uncertainties and assumptions about us, including the risk factors listed under Item 1A. Risk Factors, as well as other cautionary language in Form 10-K for the fiscal year ended February 2, 2019, filed with the SEC on May 2, 2019.

Actual results may differ materially from those in the forward-looking statements as a result of various factors, including but not limited to, the following:

- *Our ability to manage significant changes to our Board of Directors and leadership team;*
- *Our efforts to expand beyond retail stores;*
- *Our ability to maintain our brand image;*
- *Significant competition within our industry;*
- *The effect of a decrease in customer traffic to the shopping malls, centers and street locations where our stores are located;*
- *The results of our transfer pricing audit;*
- *Our ability to attract and retain employees that embody our culture, including Tea Guides and store and district managers and regional directors;*
- *Changes in consumer preferences and economic conditions affecting disposable income;*
- *Our ability to source, develop and market new varieties of teas, tea accessories, food and beverages;*
- *Our reliance upon the continued retention of key personnel;*
- *The impact from real or perceived quality or safety issues with our teas, tea accessories, food and beverages;*
- *Our ability to obtain quality products from third-party manufacturers and suppliers on a timely basis or in sufficient quantities;*
- *The impact of weather conditions, natural disasters and manmade disasters on the supply and price of tea;*
- *Actual or attempted breaches of data security;*
- *The costs of protecting and enforcing our intellectual property rights and defending against intellectual property claims brought by others;*
- *Fluctuations in exchange rates; and*

- *The seasonality of our business.*

All forward-looking statements should be evaluated with the understanding of their inherent uncertainty. These statements are based upon information available to us as of the date of this Form 10-Q/A, and while we believe such information forms a reasonable basis for such statements, such information may be limited or incomplete, and our statements should not be read to indicate that we have conducted an exhaustive inquiry into, or review of, all potentially-available relevant information. In light of these risks, uncertainties and assumptions, the forward-looking events discussed in this Quarterly Report on Form 10-Q/A might not occur, and investors are cautioned not to unduly rely upon these statements.

Forward-looking statements speak only as of the date of this Form 10-Q/A. 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/A, 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/A 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.

Restatement of Condensed Interim Consolidated Financial Statements

We have restated our unaudited condensed interim consolidated financial statements for (i) the quarterly period ended May 4, 2019 and (ii) the quarterly period ended August 3, 2019, including applicable notes as reflected in this Form 10-Q/A, to reflect our restatement resulting from accounting errors identified in the assessment of impairment indicators upon completing the store impairment analysis under IAS 36, subsequent to the adoption of IFRS 16. Additionally upon further review, management determined that, pursuant to IFRS standards, its financial statements would be more relevant had they applied IAS 36 as of the date of initial adoption, instead of applying an available practical expedient. For additional information about the restatement, please see the Explanatory Note immediately preceding Part I, Item 1 of this Form 10-Q/A and Note 3 to the interim condensed consolidated financial statements, “Changes in Accounting Policies and Restatement of Previously-Issued Financial Statements” in Part I, Item 1 of this Form 10-Q/A.

The following discussion and analysis of our financial condition and results of operations incorporates the restated amounts.

Accounting Periods

All references to “Fiscal 2019” are to the Company’s fiscal year ending February 1, 2020. All references to “Fiscal 2018” are to the Company’s fiscal year ended February 2, 2019.

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. The year ended February 2, 2019 and year ending February 1, 2020 both cover a 52-week 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 233 company-operated DAVIDsTEA stores as of August 3, 2019, and through our online store at www.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.

Factors Affecting Our Performance

We believe that our performance and future success depend on a number of factors that present significant opportunities for us and may pose risks and challenges, as discussed in the “Risk Factors” section of Form 10-K filed with the SEC and on SEDAR and available at www.sec.gov and www.sedar.com, respectively.

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, our online store and from our wholesale distribution channel. 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 quarter because of lower customer traffic in our locations in 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. Sales also include gift card breakage income.

Comparable Sales. Comparable sales refer to period-over-period comparison information for comparable stores. 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 our locations in which we operate;
- the number of customer transactions and average ticket 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.

Gross Profit. Gross profit is equal to our sales less our cost of sales. Cost of sales includes product costs, freight costs, certain 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, including ROU assets and provision (recovery) for onerous contracts. Store operating expenses consist of all store expenses excluding certain 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, depreciation of property, plant and equipment, amortization of intangible, amortization of right-of-use assets 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 on page 6 of this Quarterly Report on Form 10-Q/A.

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 on page 7 of this Quarterly Report on Form 10-Q/A.

Finance Costs. Finance costs consist of cash and imputed non-cash charges related to our credit facility, accretion expense on the provisions for onerous contracts and interest expense from lease liabilities.

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 ROU assets, 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 on page 7 of this Quarterly Report on Form 10-Q/A.

Selected Operating and Financial Highlights

Results of Operations

The Company has adopted IFRS 16 as at February 3, 2019. As fully described in Note 3 of our unaudited condensed consolidated interim financial statements for the first quarter of 2019, IFRS 16 provides a single model for leases abolishing the current distinction between finance and operating leases, with most leases being recognized on the consolidated balance sheet. The adoption of IFRS 16 had a significant impact as the Company recognized 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. Comparative figures for the first half of 2019 have not been restated and continue to be reported under IAS 17, Leases and Related interpretations.

As a result, operating lease payments which were previously included in cost of sales on the consolidated statement of loss are replaced with depreciation expenses (included in selling, general and administrative expenses) from the right-of-use asset and interest expense (included under finance costs) from the lease liability. For analysis purposes only, this MD&A also shows where applicable, amounts for the first half of 2019 as if the Company continued to report under IAS 17, Leases and Related interpretations, and did not adopt IFRS 16, other than for differences related to testing long-lived assets for impairment and accounting for onerous store leases pursuant to the guidance of IAS 37, *Provisions*, which could have had an impact on the EBITDA and net loss of the Company under accounting standards applicable prior to February 3, 2019.

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

| | For the three months ended | | | For the six months ended | | |
|--|--|--------------------------------|-------------------|--|--------------------------------|--------------------|
| | August 3, 2019 | | | August 3, 2019 | | |
| | August 3, 2019 (Restated - Note 3) | Excluding impact of IFRS 16 | August 4, 2018 | August 3, 2019 (Restated - Note 3) | Excluding impact of IFRS 16 | August 4, 2018 |
| Consolidated statement of loss data: | | | | | | |
| Sales | \$ 39,167 | \$ 39,167 | \$ 40,167 | \$ 83,432 | \$ 83,432 | \$ 85,953 |
| Cost of sales | 17,362 | 23,161 | 22,824 | 35,291 | 46,913 | 45,918 |
| Gross profit | 21,805 | 16,006 | 17,343 | 48,141 | 36,519 | 40,035 |
| Selling, general and administration expenses | 31,563 | 28,449 | 31,350 | 59,583 | 53,367 | 55,746 |
| Results from operating activities | (9,758) | (12,443) | (14,007) | (11,442) | (16,848) | (15,711) |
| Finance costs | 1,781 | — | 78 | 3,608 | — | 157 |
| Finance income | (195) | (195) | (215) | (386) | (386) | (452) |
| Loss before income taxes | (11,344) | (12,248) | (13,870) | (14,664) | (16,462) | (15,416) |
| Provision for income tax recovery | — | — | (3,872) | — | — | (4,216) |
| Net loss | \$ (11,344) | \$ (12,248) | \$ (9,998) | \$ (14,664) | \$ (16,462) | \$ (11,200) |
| Percentage of sales: | | | | | | |
| Sales | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% |
| Cost of sales | 44.3% | 59.1% | 56.8% | 42.3% | 56.2% | 53.4% |
| Gross profit | 55.7% | 40.9% | 43.2% | 57.7% | 43.8% | 46.6% |
| Selling, general and administration expenses | 80.6% | 72.6% | 78.0% | 71.4% | 64.0% | 64.9% |
| Results from operating activities | (24.9%) | (31.8%) | (34.9%) | (13.7%) | (20.2%) | (18.3%) |
| Finance costs | 4.5% | 0.0% | 0.2% | 4.3% | 0.0% | 0.2% |
| Finance income | (0.5%) | (0.5%) | (0.5%) | (0.5%) | (0.5%) | (0.5%) |
| Loss before income taxes | (29.0%) | (31.3%) | (34.5%) | (17.6%) | (19.7%) | (17.9%) |
| Provision for income tax recovery | 0.0% | 0.0% | (9.6%) | 0.0% | 0.0% | (4.9%) |
| Net loss | (29.0%) | (31.3%) | (24.9%) | (17.6%) | (19.7%) | (13.0%) |
| Other financial and operations data: | | | | | | |
| Adjusted EBITDA ⁽¹⁾ | \$ 361 | \$ (5,438) | \$ (5,564) | \$ 3,630 | \$ (7,992) | \$ (5,964) |
| Adjusted EBITDA as a percentage of sales | 0.9% | (13.9%) | (13.9%) | 4.4% | (9.6%) | (6.9%) |
| Number of stores at end of period | 233 | 233 | 239 | 233 | 233 | 239 |
| Comparable sales decline for period ⁽²⁾ | (9.4%) | (9.4%) | (14.8%) | (7.7%) | (7.7%) | (10.8%) |

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

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

Non-IFRS Financial Measures

Adjusted selling, general and administration expenses, Adjusted results from operating activities, Adjusted net loss and Adjusted EBITDA, before and after adjustments for the impact of IFRS 16, are not a presentation made in accordance with IFRS, and the use of the terms Adjusted selling, general and administration expenses, Adjusted results from operating activities, Adjusted net loss and Adjusted EBITDA, before and after adjustments for the impact of IFRS 16, may differ from similar measures reported by other companies. We believe that Adjusted selling, general and administration expenses, Adjusted results from operating activities, Adjusted net loss and Adjusted EBITDA, before and after adjustments for the impact of IFRS 16, provides investors with useful information with respect to our historical operations. Adjusted selling, general and administration expenses, Adjusted results from operating activities, Adjusted net loss 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, Adjusted net loss 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, Adjusted net loss and Adjusted EBITDA, before and after adjustments for the impact of IFRS 16, do not reflect changes in, or cash requirements for, our working capital needs;
- Adjusted selling, general and administration expenses, Adjusted results from operating activities, Adjusted net loss and Adjusted EBITDA, before and after adjustments for the impact of IFRS 16, 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, before and after adjustments for the impact of IFRS 16, does not reflect any cash requirements for such replacements.

Because of these limitations, Adjusted selling, general and administration expenses, Adjusted results from operating activities, Adjusted net loss and Adjusted EBITDA before and after adjustments for the impact of IFRS 16, 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, Adjusted net loss and Adjusted EBITDA before and after adjustments for the impact of IFRS 16, to our Net loss determined in accordance with IFRS:

Reconciliation of Adjusted selling, general and administration expenses

| | For the three months ended | | | For the six months ended | | |
|---|--|--|-------------------|--|--|-------------------|
| | August 3, 2019 (Restated - Note 3) | August 3, 2019 Excluding impact of IFRS 16 | August 4, 2018 | August 3, 2019 (Restated - Note 3) | August 3, 2019 Excluding impact of IFRS 16 | August 4, 2018 |
| Selling, general and administration expenses | \$ 31,563 | \$ 28,449 | \$ 31,350 | \$ 59,583 | \$ 53,367 | \$ 55,746 |
| Executive separation costs related to salary (a) | — | — | (717) | — | — | (717) |
| Impairment of property, equipment and right-of-use assets (b) | (5,025) | (5,025) | (2,560) | (5,025) | (5,025) | (2,560) |
| Impact of onerous contracts (c) | — | — | (714) | — | — | 802 |
| Strategic review and proxy contest costs (d) | — | — | (2,717) | — | — | (3,511) |
| Adjusted selling, general and administration expenses | \$ 26,538 | \$ 23,424 | \$ 24,642 | \$ 54,558 | \$ 48,342 | \$ 49,760 |

- Executive separation costs represent mainly salary owed to certain former executives as part of their separation of employment from the Company.
- Represent costs related to impairment of property, equipment and right-of use assets for stores.
- Represents provision, 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.
- Represents costs related to the corporate strategic review process as well as costs related to the proxy contest.

Reconciliation of Adjusted results from operating activities

| | For the three months ended | | | For the six months ended | | |
|---|---------------------------------------|--|-------------------|---------------------------------------|--|-------------------|
| | August 3, 2019 (Restated - Note 3) | August 3, 2019 Excluding impact of IFRS 16 | August 4, 2018 | August 3, 2019 (Restated - Note 3) | August 3, 2019 Excluding impact of IFRS 16 | August 4, 2018 |
| Results from operating activities | \$ (9,758) | \$ (12,443) | \$ (14,007) | \$ (11,442) | \$ (16,848) | \$ (15,711) |
| Executive separation costs related to salary (a) | — | — | 717 | — | — | 717 |
| Impairment of property, equipment and right-of-use assets (b) | 5,025 | 5,025 | 2,560 | 5,025 | 5,025 | 2,560 |
| Impact of onerous contracts (c) | — | — | 714 | — | — | (802) |
| Strategic review and proxy contest costs (d) | — | — | 2,717 | — | — | 3,511 |
| Adjusted results from operating activities | \$ (4,733) | \$ (7,418) | \$ (7,299) | \$ (6,417) | \$ (11,823) | \$ (9,725) |

- (a) Executive separation costs represent mainly salary owed to certain former executives as part of their separation of employment from the Company.
- (b) Represent costs related to impairment of property, equipment and right-of use assets for stores.
- (c) Represents provision, 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 the corporate strategic review process as well as costs related to the proxy contest.

Reconciliation of Net loss to Adjusted EBITDA

| | For the three months ended | | | For the six months ended | | |
|---|---------------------------------------|---|--------------------|---------------------------------------|---|--------------------|
| | August 3, 2019 (Restated - Note 3) | August 3, 2019 Excluding impact of IFRS 16 ⁽¹⁾ | August 4, 2018 | August 3, 2019 (Restated - Note 3) | August 3, 2019 Excluding impact of IFRS 16 ⁽¹⁾ | August 4, 2018 |
| Net loss | \$ (11,344) | \$ (12,248) | \$ (9,998) | \$ (14,664) | \$ (16,462) | \$ (11,200) |
| Finance costs | 1,781 | — | 78 | 3,608 | — | 157 |
| Finance income | (195) | (195) | (215) | (386) | (386) | (452) |
| Depreciation and amortization | 4,929 | 1,815 | 2,068 | 9,755 | 3,539 | 3,936 |
| Recovery of income tax | — | — | (3,872) | — | — | (4,216) |
| EBITDA | \$ (4,829) | \$ (10,628) | \$ (11,939) | \$ (1,687) | \$ (13,309) | \$ (11,775) |
| Additional adjustments : | | | | | | |
| Stock-based compensation expense (a) | 143 | 143 | (393) | 270 | 270 | (98) |
| Executive separation costs related to salary (b) | — | — | 717 | — | — | 717 |
| Impairment of property, equipment and right-of-use assets (c) | 5,025 | 5,025 | 2,560 | 5,025 | 5,025 | 2,560 |
| Impact of onerous contracts (d) | — | — | 714 | — | — | (802) |
| Deferred rent (e) | — | — | 46 | — | — | (91) |
| Loss on disposal of property and equipment | 22 | 22 | 14 | 22 | 22 | 14 |
| Strategic review and proxy contest costs (f) | — | — | 2,717 | — | — | 3,511 |
| Adjusted EBITDA | \$ 361 | \$ (5,438) | \$ (5,564) | \$ 3,630 | \$ (7,992) | \$ (5,964) |

⁽¹⁾ Adjusted EBITDA for August 3, 2019 excluding impact of IFRS 16 assumes the Company continued to report under IAS 17, Leases and did not adopt IFRS 16. Under IFRS 16, the nature and timing of expenses related to operating leases have changed as the straight-line operating leases expenses have been replaced with a depreciation charge for right-of-use assets and interest expense on lease liabilities. Accordingly, for the three months and six months ended August 3, 2019, IFRS 16 had a favourable impact of approximately \$5.8 million and \$11.6 million respectively, on adjusted EBITDA as operating lease expenses have been replaced with depreciation and interest expense, which are not included in the calculation of adjusted EBITDA.

- (a) Represents non-cash stock-based compensation expense.
- (b) Executive separation costs represent mainly salary owed to certain former executives as part of their separation of employment from the Company.
- (c) Represent costs related to impairment of property, equipment and right-of use assets for stores.
- (d) Represents provision, 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 our annual rent expense has been above or below our cash rent payments.
- (f) Represents costs related to the corporate strategic review process as well as costs related to the proxy contest.

Reconciliation of reported results to Adjusted net loss

| | For the three months ended | | | For the six months ended | | |
|---|----------------------------|-----------------------------|-------------------|--------------------------|-----------------------------|-------------------|
| | August 3, 2019 | August 3, 2019 | August 4, 2018 | August 3, 2019 | August 3, 2019 | August 4, 2018 |
| | (Restated - Note 3) | Excluding impact of IFRS 16 | | (Restated - Note 3) | Excluding impact of IFRS 16 | |
| Net loss | \$ (11,344) | \$ (12,248) | \$ (9,998) | \$ (14,664) | \$ (16,462) | \$ (11,200) |
| Executive separation costs related to salary (a) | — | — | 717 | — | — | 717 |
| Impairment of property, equipment and right-of-use assets (b) | 5,025 | 5,025 | 2,560 | 5,025 | 5,025 | 2,560 |
| Impact of onerous contracts (c) | — | — | 714 | — | — | (802) |
| Strategic review and proxy contest costs (d) | — | — | 2,717 | — | — | 3,511 |
| Adjusted net loss | <u>\$ (6,319)</u> | <u>\$ (7,223)</u> | <u>\$ (3,290)</u> | <u>\$ (9,639)</u> | <u>\$ (11,437)</u> | <u>\$ (5,214)</u> |

- (a) Executive separation costs represent mainly salary owed to certain former executives as part of their separation of employment from the Company.
- (b) Represent costs related to impairment of property, equipment and right-of use assets for stores.
- (c) Represents provision, 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 the corporate strategic review process as well as costs related to the proxy contest.

Reconciliation of fully diluted loss per common share to adjusted fully diluted loss per common share

| | For the three months ended | | | For the six months ended | | |
|--|----------------------------|-----------------------------|----------------|--------------------------|-----------------------------|----------------|
| | August 3, 2019 | August 3, 2019 | August 4, 2018 | August 3, 2019 | August 3, 2019 | August 4, 2018 |
| | (Restated - Note 3) | Excluding impact of IFRS 16 | | (Restated - Note 3) | Excluding impact of IFRS 16 | |
| Weighted average number of shares outstanding, fully diluted | 26,056,520 | 26,056,520 | 25,910,086 | 26,038,128 | 26,038,128 | 25,878,982 |
| Adjusted weighted average number of shares outstanding, fully diluted | 26,056,520 | 26,056,520 | 25,910,086 | 26,038,128 | 26,038,128 | 25,878,982 |
| Net loss | \$ (11,344) | \$ (12,248) | \$ (9,998) | \$ (14,664) | \$ (16,462) | \$ (11,200) |
| Adjusted net loss | \$ (6,319) | \$ (7,223) | \$ (3,290) | \$ (9,639) | \$ (11,437) | \$ (5,214) |
| Net loss per share, fully diluted | \$ (0.44) | \$ (0.47) | \$ (0.39) | \$ (0.56) | \$ (0.56) | \$ (0.43) |
| Adjusted net loss per share, fully diluted | \$ (0.24) | \$ (0.28) | \$ (0.13) | \$ (0.37) | \$ (0.37) | \$ (0.20) |

Three Months Ended August 3, 2019 restated Compared to Three Months Ended August 4, 2018

Sales. Sales for the three months ended August 3, 2019 decreased 2.5%, or \$1.0 million, to \$39.2 million from \$40.2 million in the prior year quarter. Sales from our e-commerce and wholesale channels increased \$2.8 million, or by 52.8%, driven primarily by greater online adoption as well as by increased demand in our grocery distribution channel. Offsetting this was a decline in retail sales of \$3.8 million and a decline of \$2.9 million, or 9.4%, in comparable store sales.

Gross Profit. Gross profit increased by 25.7%, or \$4.5 million, to \$21.8 million for the three months ended August 3, 2019, from the prior year quarter. IFRS 16 replaces the straight-line operating lease expense with a depreciation charge for right-of-use assets and interest expense on lease liabilities. Accordingly, straight-line operating lease expense is no longer included in cost of sales in arriving at gross profit. Prior to the adoption of IFRS 16, straight-line operating lease expense amounting to \$5.8 million would have been included in arriving at gross profit. Excluding the impact of IFRS 16, gross profit decreased by \$1.3 million to \$16.0 million, representing a gross profit of 40.9% for the three months ended August 3, 2019, a decrease of 2.3% from the prior year quarter resulting from a shift in product sales mix and the deleveraging of fixed costs due to negative comparable store sales.

Selling, General and Administration Expenses. Selling, general and administration expenses (“SG&A”) remained stable at \$31.6 million in the three months ended August 3, 2019 compared to the prior year quarter. Under IFRS 16, SG&A includes \$3.1 million of depreciation in connection with our right-of-use assets. Excluding the impact of IFRS 16, SG&A would have amounted to \$28.4 million, a decrease of \$2.9 million, or 9.3%, from the prior year quarter and as a percentage of sales would have amounted to 72.6% representing a decrease of 5.4% over the prior year quarter. Excluding the impact of IFRS 16 and the impairment of property, equipment and right-of-use assets for the three months ended August 3, 2019 and the impact of onerous contracts, impairment of property, equipment and right-of-use assets, executive separation cost related to salary and costs related to the strategic review and proxy contest for the three months ended August 4, 2018, Adjusted SG&A decreased by \$1.2 million for the three months ended August 3, 2019. As a percentage of sales and excluding the impact of IFRS 16, Adjusted SG&A decrease to 59.8% from 61.3%.

Results from Operating Activities. Loss from operating activities was \$9.8 million as compared to a loss of \$14.0 million in the prior year quarter. Excluding the impact of IFRS 16 and impairment of property, equipment and right-of-use assets, loss from operating activities would have amounted to \$7.4 million, a decrease of \$0.2 million from the prior year quarter. This decrease is mainly explained by the absence of executive separation cost related to salary, the impact of onerous contracts, and costs related to the strategic review and proxy contest of incurred in the same period of 2018 offset by the increase of the impairment of property, equipment and right-of-use assets. Adjusted results from operating activities, which excludes any impact of executive separation cost related to salary, impairment of property, equipment and right-of-use assets, impact from onerous contracts, and costs related to the strategic review and proxy contest, was \$7.4 million compared to \$7.3 million in the prior year quarter.

Finance Costs. Finance costs amounted to \$1.8 million in the three months ended August 3, 2019, an increase of \$1.7 million from the prior year quarter. Finance costs under IFRS 16 includes interest expense from lease liabilities measured at the present value of lease payments to be made over the lease term. The Company recognized a lease liability of \$102.2 million on initial application of IFRS 16. Excluding the impact of IFRS 16, interest expense would have been nil in the current year quarter.

Finance Income. Finance income of \$0.2 million is derived primarily from interest on cash on hand and has decreased slightly from prior year quarter.

EBITDA and Adjusted EBITDA. EBITDA, which excludes non-cash and other items in the current and prior periods, was negative \$4.8 million in the quarter ended August 3, 2019 compared to a negative \$11.9 million in the prior year quarter. Excluding the impact of IFRS 16, EBITDA would have amounted to a negative \$10.6 million, representing an increase of \$1.3 million over the prior year quarter. Adjusted EBITDA for the quarter amounted to \$0.4 million compared to a negative \$5.6 million in the prior year quarter. Excluding the impact of IFRS 16, stock-based compensation and the impairment of property, equipment and right-of-use assets for the three months ended August 3, 2019 and the impact of stock-based compensation, executive separation costs related to salary, impairment of property, equipment and right-of-use assets, onerous contracts, deferred rent and costs related to the strategic review and proxy contest for the three months ended August 4, 2018, Adjusted EBITDA increased by \$0.1 million.

Net Loss. Net loss was \$11.3 million in the quarter ended August 3, 2019 compared to a net loss of \$10.0 million in the prior year quarter. Excluding the impact of IFRS 16, Net loss would have amounted to \$12.2 million, representing a decrease of \$2.2 million in net loss over the prior year quarter. Adjusted net loss, which excludes the impact from executive separation cost related to salary, impairment of property plant, equipment and right-of-use assets, impact of onerous contracts and costs related to strategic review and proxy contest, was \$7.2 million compared to \$3.3 million in the prior year quarter.

Fully diluted loss per common share. Fully diluted loss per common share was \$0.44 compared to \$0.39 in the second quarter of Fiscal 2018. Adjusted fully diluted loss per common share, which is adjusted net loss on a fully diluted weighted average shares outstanding basis, was \$0.24 per share compared to \$0.13 per share.

Six Months Ended August 3, 2019 restated Compared to Six Months Ended August 4, 2018

Sales. Sales for the six months ended August 3, 2019 decreased 2.9%, or \$2.5 million, to \$83.4 million from \$85.9 million in the same period in the prior year. Sales from our e-commerce and wholesale channels increased \$3.2 million, or by 28.2%, driven primarily by greater online adoption as well as by increased demand in our grocery distribution channel. Offsetting this was a decline in retail sales of \$5.7 million and a decline of \$5.8 million, or 9.7%, in comparable store sales.

Gross Profit. Gross profit increased by 20.2%, or \$8.1 million, to \$48.1 million for the three months ended August 3, 2019, from the same period in the prior year. IFRS 16 replaces the straight-line operating lease expense with a depreciation charge for right-of-use assets and interest expense on lease liabilities. Accordingly, straight-line operating lease expense is no longer included in cost of sales in arriving at gross profit. Prior to the adoption of IFRS 16, straight-line operating lease expense amounting to \$11.6 million would have been included in arriving at gross profit. Excluding the impact of IFRS 16, gross profit decreased by \$3.5 million to \$36.5 million, representing a gross profit of 43.8% for the six months ended August 3, 2019, a decrease of 2.8% compare to the six months ended August 4, 2018 driven by a shift in product sales mix and the deleveraging of fixed costs due to negative comparable store sales.

Selling, General and Administration Expenses. SG&A increased by 6.9%, or \$3.8 million, to \$59.6 million in the six months ended August 3, 2019 from the same period in the prior year. Under IFRS 16, SG&A includes \$6.2 million of depreciation in connection with our right-of-use assets. Excluding the impact of IFRS 16, SG&A would have amounted to \$53.4 million, a decrease of \$2.4 million, or 4.3%, from the prior year quarter and as a percentage of sales would have amounted to 64.0% representing a decrease of 0.9% over the prior year quarter. Excluding the impact of IFRS 16 and impairment of property, equipment and right-of-use assets for the six months ended August 3, 2019 and the impact of executive separation cost related to salary, impairment of property, equipment and right-of-use assets, onerous contracts and costs related to the strategic review and proxy contest for the six months ended August 4, 2018, Adjusted SG&A decreased by \$1.4 million for the six months ended August 3, 2019. As a percentage of sales, Adjusted SG&A stayed stable at 57.9%.

Results from Operating Activities. Loss from operating activities was \$11.4 million as compared to a loss of \$15.7 million in the same period in 2018. Excluding the impact of IFRS 16, loss from operating activities would have amounted to \$16.8 million, a decrease of \$1.1 million from the same period in 2018. This is mainly due to the absence of costs related to executive separation costs related to salary, the impact of onerous contracts and the costs related to the strategic review and proxy contest incurred in the period in 2018 partially offset by the increase in the impairment of property, equipment and right-of-use assets. Adjusted results from operating activities, which excludes any impact from executive separation costs related to salary, impairment of property, equipment and right-of-use assets, onerous contracts, and costs related to the strategic review and proxy contest, was negative \$11.8 million compared to negative \$9.7 million in the same period in the prior year.

Finance Costs. Finance costs amounted to \$3.6 million in the six months ended August 3, 2019, an increase of \$3.5 million from the same period in 2018. Finance costs under IFRS 16 includes interest expense from lease liabilities measured at the present value of lease payments to be made over the lease term. The Company recognized a lease liability of \$102.2 million on initial application of IFRS 16. Excluding the impact of IFRS 16, interest expense would have been nil in the current six-month period.

Finance Income. Finance income of \$0.4 million is derived primarily from interest on cash on hand and has decreased slightly from the same period in the prior year.

EBITDA and Adjusted EBITDA. EBITDA, which excludes non-cash and other items in the current and prior periods, was negative \$1.7 million in the six-month period ended August 3, 2019 compared to negative \$11.8 million in the same period in the prior year. Excluding the impact of IFRS 16, EBITDA would have amounted to a negative \$13.3 million, representing an increase of \$1.5 million over the same period in the prior year. Adjusted EBITDA for the six-month period amounted to \$3.6 million compared to a negative \$6.0 million in the same period in the prior year. Excluding the impact of IFRS 16, impairment of property, equipment and right-of-use assets and stock-based compensation for the six months ended August 3, 2019 and the impact of stock-based compensation, executive separation costs related to salary, impairment of property, equipment and right-of-use assets, onerous contracts, deferred rent and costs related to the strategic review and proxy contest for the six months ended August 4, 2018, Adjusted EBITDA decreased by \$2.0 million.

Net Loss. Net loss was \$14.7 million in the six-month period ended August 3, 2019 compared to a net loss of \$11.2 million in the same period in the prior year. Excluding the impact of IFRS 16, Net loss would have amounted to \$16.5 million, representing an increase of \$5.3 million in net loss over the same period in the prior year. Adjusted net loss, which excludes the impact from executive separation costs related to salary, impairment of property, equipment and right-of-use assets, onerous contracts and costs related to strategic review and proxy contest, was \$11.4 million compared to \$5.2 million in the prior year period.

Fully diluted loss per common share. Fully diluted loss per common share in the six-month period ended August 3, 2019 was \$0.56 compared to \$0.43 in the same period of Fiscal 2018. Adjusted fully diluted loss per common share, which is adjusted net loss on a fully diluted weighted average shares outstanding basis, was \$0.37 per share compared to \$0.20 per share.

Liquidity and Capital Resources

As at August 3, 2019, we had \$29.7 million of cash primarily held by major Canadian financial institutions. Total current assets less the sum of Trade and other payables and Deferred revenue was \$55,794 and \$65,842, for the periods ended August 3, 2019 and February 2, 2019, respectively.

Our primary source of liquidity is cash on hand. Our primary cash needs are to finance working capital, investments in infrastructure and for capital expenditures related to store renovations.

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

Our primary working capital requirements are for the purchase of store inventory and payment of payroll, rent and other store operating costs. Our working capital requirements fluctuate during the year, rising in the second and third fiscal quarters as we take title to increasing quantities of inventory in anticipation of our peak selling season in the fourth fiscal quarter. We funded our capital expenditures and working capital requirements from cash on hand and net cash provided by our operating activities.

We believe that our cash position, net cash provided by our operating activities will be adequate to finance our planned capital expenditures and working capital requirements for the next twelve months.

Cash Flow

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

| | For the three months ended | | | For the six months ended | | |
|---|----------------------------|--|--------------------|--------------------------|--|--------------------|
| | August 3, 2019 | August 3, 2019 Excluding impact of IFRS 16 | August 4, 2018 | August 3, 2019 | August 3, 2019 Excluding impact of IFRS 16 | August 4, 2018 |
| Cash flows provided by (used in) : | | | | | | |
| Operating activities | \$ 3,083 | \$ (2,716) | \$ (12,438) | \$ 3,443 | \$ (8,179) | \$ (19,544) |
| Financing activities | (5,799) | — | 74 | (11,622) | — | 74 |
| Investing activities | (3,050) | (3,050) | (1,881) | (4,170) | (4,170) | (4,391) |
| Decrease in cash | \$ (5,766) | \$ (5,766) | \$ (14,245) | \$ (12,349) | \$ (12,349) | \$ (23,861) |

Three Months Ended August 3, 2019 Compared to Three Months Ended August 4, 2018

Cash Flows Used in Operating Activities. Net cash provided by operating activities amounted to \$3.1 million for the three months ended August 3, 2019 from net cash used of \$12.4 million for the three months ended August 4, 2018. Excluding the impact of IFRS 16, net cash used in operating activities amounted to \$2.7 million, an improvement of \$9.7 million from the prior year quarter. Net change in other non-cash working capital balances related to operations improved by \$9.1 million primarily from a reduction in cash used for inventories and the collection of account receivables partially offset by a decrease in accounts payable and accrued liabilities, and an increase in prepaid.

Cash Flows Used in Financing Activities. Net cash flows used in financing activities was \$5.8 million for the three months ended August 3, 2019, compared to net cash provided of \$0.1 million for the three months ended August 4, 2018. Excluding the impact of IFRS 16, net cash used in financing activities amounted to nil.

Cash Flows Used in Investing Activities. Cash flows used in investing activities was \$3.1 million for the three months ended August 3, 2019, compared to \$1.9 million for the three months ended August 4, 2018. The increase in net cash used in investing activities relates to the loan advance made during the period, partially offset by the decrease in capital expenditures.

Six Months Ended August 3, 2019 Compared to Six Months Ended August 4, 2018

Cash Flows Used in Operating Activities. Net cash provided by operating activities amounted to \$3.4 million for the six months ended August 3, 2019 from net cash used of \$19.5 million for the six months ended August 4, 2018. Excluding the impact of IFRS 16, net cash used in operating activities amounted to \$8.2 million, an improvement of \$11.4 million from the same period in the prior year. Net change in other non-cash working capital balances related to operations improved by \$14.8 million primarily from a reduction in inventories, the collection of account receivables partially offset by a decrease in accounts payable and accrued liabilities

Cash Flows Used in Financing Activities. Net cash flows used in financing activities was \$11.6 million for the six months ended August 3, 2019, compared to net cash provided of \$0.1 million for the six months ended August 4, 2018. Excluding the impact of IFRS 16, net cash used in financing activities amounted to nil.

Cash Flows Used in Investing Activities. Cash flows used in investing activities was \$4.2 million for the six months ended August 3, 2019, compared to \$4.4 million for the six months ended August 4, 2018. The decrease in net cash used in investing activities relates to the decrease in capital expenditures partially offset by the loan advance made during the period.

Credit Facility with Bank of Montreal

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 \$15,000 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. 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 \$15,000. The Amended Revolving Facility bears interest based on the Company’s adjusted leverage ratio, at the bank’s prime rate, U.S. bank rate or 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 nonfinancial 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 August 3, 2019, the Company did not have any borrowings under the Amended Revolving Facility.

As at August 3, 2019, the Company is in breach of its fixed charge coverage ratio and certain nonfinancial covenants. BMO has temporarily agreed to forbear from exercising remedies under the Credit Agreement, however the Company cannot borrow under the facility.

The Company is in good faith discussions with BMO to install an asset based lending facility that will provide a revolving facility at commercial reasonable terms.

Off-Balance Sheet Arrangements

We have no off-balance sheet obligations.

Contractual Obligations and Commitments

There have been no significant changes to our contractual obligations as disclosed in our consolidated financial statements for the fiscal year ended February 2, 2019, other than those which occur in the normal course of business.

Critical Accounting Policies and Estimates

Our discussion and analysis of operating results and financial condition are based upon our financial statements. The preparation of financial statements requires us 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 judgement involved and its potential impact on our 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 our financial position, changes in financial position or results of operations. Our significant accounting policies are discussed under Note 3 to our consolidated financial statements for the year ended February 2, 2019 included in our Annual Report on Form 10-K dated May 2, 2019. There have been no material changes to the critical accounting policies and estimates since February 2, 2019, other than with respect to IFRS 16 as described in Note 3 to the interim consolidated financial statements.

Recently Issued Accounting Standards

Refer to Note 3, “Changes in Accounting Policies” for a discussion of recent accounting pronouncements.

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 our Annual Report on Form 10-K dated May 2, 2019.

Item 4. Controls and Procedures

Disclosure Controls and Procedures

Our management, with the participation of our Chairman and Interim Chief Executive Officer and Chief Financial Officer and Chief Operating Officer, evaluated the effectiveness of our disclosure controls and procedures as of August 3, 2019. 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 our disclosure controls and procedures as of August 3, 2019, our Chairman and Interim Chief Executive Officer and Chief Financial Officer and Chief Operating Officer concluded that, as of such date, our disclosure controls and procedures were not effective.

During the course of the Company’s financial statement close process for the quarter ended November 2, 2019, accounting errors were identified in the assessment of impairment indicators upon completing the store impairment analysis under IAS 36, Impairment of Assets (“IAS 36”), subsequent to the adoption of IFRS 16, Leases (“IFRS 16”). When appropriately performing the assessment of impairment indicators with respect to the right-of-use assets (“ROU assets”) as at May 4, 2019 and August 3, 2019, impairment charges of \$13,924 and \$5,025 respectively were identified that would have been required to be recognized in the respective periods under the Company’s accounting policy for transition to IFRS 16, which included the use of the practical expedient for assessing impairment. Upon further review, the Company also determined that, pursuant to IFRS standards, its financial statements would be more relevant had they applied IAS 36 to assess impairment of ROU assets as of the date of initial adoption, instead of applying the available practical expedient. Accordingly, the Company elected to voluntarily change its accounting policy to perform an impairment assessment in accordance with IAS 36 at the date of transition to IFRS 16. The Company believes this change is more

relevant because it more faithfully depicts the performance of the Company. Subsequent to the retrospective application of the change in accounting policy, the impairment charges were nil and \$5,025 for the quarters ended May 4, 2019 and August 3, 2019, respectively.

As a result of the aforementioned analysis, a material weakness in the design of the monitoring of impairment triggers upon completing the store impairment analysis under IAS 36, subsequent to the adoption of IFRS 16 was identified. A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of the Company's annual or interim statements will not be prevented or detected on a timely basis.

Certain remedial efforts were undertaken during the third quarter financial statement close process that resulted in effective design of the monitoring of impairment triggers under IAS 36 subsequent to the adoption of IFRS 16; however, we are unable to conclude that this control was operationally effective due to lack of sufficient extent of samples for testing.

Changes in Internal Control over Financial Reporting

In light of the restatement, our Chief Executive Officer and Chief Financial Officer have reassessed their evaluation of the effectiveness of the design and operation of its disclosure controls over financial reporting as of August 3, 2019 and concluded that the Company did not maintain effective disclosure control and procedures due to a material weakness in the Company's internal control over financial reporting that existed at that date in the monitoring of impairment triggers upon completing a store impairment analysis under IAS 36 subsequent to the adoption of IFRS 16.