

## 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 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", "intend", "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 Restructuring Plan, 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, and 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 filed with the SEC on June 16, 2020, as well as the additional Risk Factors set out in our Form 10-Q filed with the SEC on July 31, 2020, as well as the additional Risk Factor set out in our Form 10-Q filed with the SEC on September 21, 2020.*

*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:*

- The effects of our Restructuring Plan pursuant to the CCAA in Canada and recognition of the CCAA proceedings in the United States under Chapter 15 of the United States Bankruptcy Code;*
- Our ability to successfully pivot our business to a digital-first strategy, supported by our wholesale distribution capabilities and our retail operations, including our ability to attract and retain employees that are instrumental to growing our online and wholesale channel businesses;*
- The duration and impact of the global COVID-19 pandemic, which has disrupted the Company's business and has adversely affected the Company's financial condition and operating results, and may further impact our workforce and operations, the operations of our customers, and those of our respective vendors, suppliers, and partners;*
- Our ability to avoid the delisting of the Company's common stock by Nasdaq due to the Restructuring Plan or our inability to maintain compliance with Nasdaq listing requirements;*
- Our ability to manage significant changes to our leadership team;*
- Our ability to maintain and enhance our brand image;*
- Significant competition within our industry;*
- The effect of a decrease in customer traffic where our stores are located;*
- Our ability to attract and retain employees that embody our entrepreneurial culture;*
- 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, in particular in light of supply chain disruption due to the COVID-19 pandemic;*
- The impact of weather conditions, natural disasters and man-made 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, 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 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. 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 2020” are to the Company’s fiscal year ending January 30, 2021. All references to “Fiscal 2019” are to the Company’s fiscal year ended February 1, 2020.

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 2019 and 2020 both cover a 52-week period.

### **Overview**

We are a branded retailer and growing mass wholesaler of specialty tea, offering a differentiated selection of proprietary loose-leaf teas, pre-packaged teas, tea sachets and tea-related gifts and accessories through our e-commerce platform at [www.davidstea.com](http://www.davidstea.com) and in 18 Company-owned and operated retail stores in Canada. A selection of DAVIDsTEA products is also available in more than 2,500 grocery stores and pharmacies across Canada. The Company is headquartered in Montréal, Canada.

We believe that our proprietary loose-leaf tea assortment and related product suite differentiates us from competitors in North America and resonates with our target customer base. Our strategy is to stabilize our business from unfavorable trend lines by playing to our core strengths and strengthening our business by focusing on how to grow our product portfolio. This includes migrating sales to a virtual experience and best-in-class customer service execution. Our Restructuring Plan is focused on effectively optimizing our retail footprint to emerge as a leaner, more sustainable physical presence that complements a growing world-class online and grocery business, all supported by a right-sized support organization.

On March 17, 2020, we closed all of our stores in North America, as subsequently mandated by the governments in both Canada and the United States in light of the COVID-19 pandemic. Due to the degree of uncertainty in connection with the scope and extent of the COVID-19 pandemic and the resulting impact to our business, and considering that significant losses were historically incurred in our brick-and-mortar operations which are anchored by commercial leases that are difficult to modify, we concluded that our transformation objectives would be better achieved through a formal restructuring process.

On July 8, 2020, the Company announced that it was implementing the Restructuring Plan under the CCAA in order to accelerate its transition to an online retailer and wholesaler of high-quality tea and accessories and that during the restructuring process, the Company would continue to operate its online business through its e-commerce platform at [www.davidstea.com](http://www.davidstea.com) and its wholesale distribution channel, through which it sells a selection of DAVIDsTEA products in grocery stores and pharmacies across Canada. Following a careful

review of available options to stem the losses from its brick-and-mortar footprint, the Company's management and Board of Directors determined that a formal restructuring process was the best option in the context of an increasingly challenging retail environment, further exacerbated by the COVID-19 pandemic.

On July 8, 2020, the Company obtained the Initial Order pursuant to the CCAA from the Québec Superior Court in order to implement the Restructuring Plan. Among other things, the Initial Order provided for the appointment of PwC as Monitor in the CCAA proceedings.

On July 9, 2020, the United States Bankruptcy Court for the District of Delaware entered an order in favor of the Company under Chapter 15 of the United States Bankruptcy Code. The order of the United States Bankruptcy Court provisionally recognized the proceedings under the CCAA and enforced the Initial Order, in effect providing protection to the Company from creditor action against its assets in the United States.

As part of its Restructuring Plan and further to obtaining the Initial Order, the Company, on July 10, 2020, sent notices to terminate leases for 82 of its stores in Canada and all 42 of its stores in the United States. These lease terminations were effective on August 9, 2020.

On July 16, 2020, the Company obtained an Amended and Restated Initial Order from the Québec Superior Court, extending to September 17, 2020 the application of the Initial Order. The Amended and Restated Initial Order also dealt with certain administrative matters, particularly with regards to the lease terminations.

On July 30, 2020, the Company sent notices to terminate leases for an additional 82 of its stores in Canada. These lease terminations were effective on August 29, 2020.

On August 21, 2020, the Company re-opened 18 stores across Canada.

On September 17, 2020, the Québec Superior Court extended the stay of all proceedings against the Company to December 15, 2020 and issued a Claims Process Order establishing the claims procedures for the Company's creditors under the CCAA. This Order, among other things set November 6, 2020 as the time by which creditors had to submit their claims to PwC, the Court-appointed Monitor.

Management believes that there is material uncertainty surrounding the Company's ability to execute the strategy necessary to return to profitability in the current environment, including the unpredictability surrounding the recovery from the COVID-19 pandemic, changes in consumer behavior and the ability to successfully emerge from the Restructuring Plan. As a result, these events and conditions indicate that a material uncertainty exists that raises substantial doubt about the Company's ability to continue as a going concern and, therefore, realize its assets and discharge its liabilities in the normal course of business.

### **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 under "Item 1A. Risk Factors" of this Form 10-Q.

### **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 are generated from our online store, retail stores, 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 quarters because of lower customer engagement in both our online store and physical 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.

As we transition to generating sales primarily from our online store, measuring the change in period-over-period comparable same store sales, although still a valid measure within our retail sales channel, loses its significance in the overall evaluation of how our business is performing. Other measures such as sales performance in total and in our e-commerce and wholesale channels begin to influence how we direct resources and evaluate our performance. Factors affecting our performance include:

- 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 online and in our other channels;

- the customer experience we provide online and in our other channels;
- the level of customer traffic to our website and our online presence more generally;
- the number of customer transactions and average ticket online;
- the pricing of our tea, tea accessories; and
- our ability to obtain, manufacture and distribute product efficiently.

*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, assembly and distribution costs.

*Selling, General and Administration Expenses.* Selling, general and administration expenses (“SG&A”) consist of store operating expenses and other general and administration expenses. 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 and equipment, amortization of intangible assets, amortization of right-of-use assets, any store or other asset impairment taken in the normal course of business 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 under “Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations”, of this Form 10-Q (the “MD&A”).

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

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 in our MD&A.

*Finance Costs.* Finance costs consist of cash and imputed non-cash charges related to any credit facility, and interest expense from lease liabilities.

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

*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, non-cash compensation expense, loss on disposal of property and equipment, impairment of property and equipment and right-of-use 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 in our MD&A.

## **Selected Operating and Financial Highlights**

### **Results of Operations**

Our financial results for the third quarter include the impact of our Restructuring Plan which began on July 8, 2020 and July 9, 2020 when we obtained the Initial Order pursuant to the CCAA from the Québec Superior Court and when we received protection from creditor action against our assets in the United States from the United States Bankruptcy Court for the District of Delaware, respectively. On July 10, 2020, we sent notices to terminate leases for 82 of our stores in Canada and all 42 of our stores in the United States. These lease terminations were effective on August 9, 2020. On July 30, 2020, we sent notices to terminate leases for an additional 82 of our stores in Canada. These lease terminations were effective on August 29, 2020. Our retail footprint now includes 18 stores in Canada which we reopened on August 21, 2020.

Sales during the third quarter of \$26.2 million declined by \$13.3 million or 33.6% over the prior year quarter due to the reduction in our retail store footprint. Adjusted EBITDA in the third quarter of Fiscal 2020 was \$3.3 million compared to negative \$2.2 million in the prior year quarter.

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

	For the three months ended		For the nine months ended	
	October 31, 2020	November 2, 2019	October 31, 2020	November 2, 2019
<b>Consolidated statement of income (loss) data:</b>				
Sales	\$ 26,225	\$ 39,493	\$ 81,497	\$ 122,925
Cost of sales	15,399	18,139	47,409	53,430
Gross profit	10,826	21,354	34,088	69,495
Selling, general and administration expenses	7,120	30,670	35,883	90,254
Restructuring plan activities, net	(10,743)	—	24,017	—
<b>Results from operating activities</b>	<b>14,449</b>	<b>(9,316)</b>	<b>(25,812)</b>	<b>(20,759)</b>
Finance costs	35	1,699	3,260	5,305
Finance income	(53)	(185)	(361)	(570)
<b>Net income (loss)</b>	<b>\$ 14,467</b>	<b>\$ (10,830)</b>	<b>\$ (28,711)</b>	<b>\$ (25,494)</b>
<b>Percentage of sales:</b>				
Sales	100.0%	100.0%	100.0%	100.0%
Cost of sales	58.7%	45.9%	58.2%	43.5%
Gross profit	41.3%	54.1%	41.8%	56.5%
Selling, general and administration expenses	27.1%	77.7%	44.0%	73.4%
Restructuring plan activities, net	(41.0%)	0.0%	29.5%	0.0%
Results from operating activities	55.1%	(23.6%)	(31.7%)	(16.9%)
Finance costs	0.1%	4.3%	4.0%	4.3%
Finance income	(0.2%)	(0.5%)	(0.4%)	(0.5%)
Net income (loss)	55.2%	(27.4%)	(35.2%)	(20.7%)
<b>Other financial and operations data:</b>				
Adjusted EBITDA <sup>(1)</sup>	\$ 3,304	\$ (2,241)	\$ 4,265	\$ 1,387
Adjusted EBITDA as a percentage of sales	12.6%	(5.7%)	5.2%	1.1%
Adjusted SG&A <sup>(1)</sup>	\$ 8,566	\$ 28,619	\$ 36,767	\$ 83,178
Adjusted results from operating activities <sup>(1)</sup>	\$ 2,260	\$ (7,265)	\$ (2,679)	\$ (13,661)
Adjusted net income (loss) <sup>(1)</sup>	\$ 2,278	\$ (8,779)	\$ (5,578)	\$ (18,396)

- (1) For a reconciliation of Adjusted EBITDA, Adjusted SG&A, Adjusted results from operating activities, and Adjusted net income (loss), to the most directly comparable measure calculated in accordance with IFRS, see “Non-IFRS financial measures” below.

### Non-IFRS financial measures

The Company uses certain non-IFRS financial measures for purposes of comparison to prior periods, to prepare annual operating budgets, and for the development of future projections. These measures are not recognized measures under IFRS, do not have a standardized meaning prescribed by IFRS and therefore may not be comparable to similarly titled measures presented by other companies. Rather, these measures are provided as additional information to complement those IFRS measures by providing further understanding of our results of operations from management’s perspective. Accordingly, they should not be considered in isolation nor as a substitute for analysis of our financial information reported under IFRS. We use non-IFRS financial measures to provide supplemental measures of our operating performance and thus highlight trends in our business that may not otherwise be apparent when relying solely on IFRS financial measures. These non-IFRS financial measures include; Adjusted SG&A, Adjusted results from operating activities, Adjusted net income (loss), Adjusted EBITDA and Adjusted fully diluted net income (loss) per common share.

We believe that these non-IFRS financial measures provide investors with useful information with respect to our historical operations and are frequently used by securities analysts, lenders and others in their evaluation of companies, they have limitations as an analytical tool. Some of these limitations are:

- Adjusted selling, general and administration expenses, Adjusted results from operating activities, Adjusted net income (loss) and Adjusted EBITDA 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 income (loss) and Adjusted EBITDA do not reflect the cash requirements necessary to fund capital expenditures; 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, these non-IFRS financial measures 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 provide reconciliations of our non-IFRS financial measures to the most directly comparable measure calculated in accordance with IFRS:

*Reconciliation of Selling, general and administration expenses to Adjusted selling, general and administration expenses*

	For the three months ended		For the nine months ended	
	October 31,	November 2,	October 31,	November 2,
	2020	2019	2020	2019
<b>Selling, general and administration expenses</b>	\$ 7,120	\$ 30,670	\$ 35,883	\$ 90,254
Impairment of property and equipment and right-of-use assets	—	(2,051)	(2,561)	(7,076)
Government emergency wage subsidy	1,446	—	3,445	—
<b>Adjusted selling, general and administration expenses</b>	\$ 8,566	\$ 28,619	\$ 36,767	\$ 83,178

*Reconciliation of Results from operating activities to Adjusted results from operating activities*

	For the three months ended		For the nine months ended	
	October 31,	November 2,	October 31,	November 2,
	2020	2019	2020	2019
<b>Results from operating activities</b>	\$ 14,449	\$ (9,316)	\$ (25,812)	\$ (20,759)
Impairment of property and equipment and right-of-use assets	—	2,051	2,561	7,076
Loss on disposal of property and equipment and right-of-use assets	—	—	—	22
Restructuring plan activities, net	(10,743)	—	24,017	—
Government emergency wage subsidy	(1,446)	—	(3,445)	—
<b>Adjusted results from operating activities</b>	\$ 2,260	\$ (7,265)	\$ (2,679)	\$ (13,661)

*Reconciliation of Net income (loss) to Adjusted EBITDA*

	For the three months ended		For the nine months ended	
	October 31,	November 2,	October 31,	November 2,
	2020	2019	2020	2019
<b>Net income (loss)</b>	\$ 14,467	\$ (10,830)	\$ (28,711)	\$ (25,494)
Finance costs	35	1,699	3,260	5,305
Finance income	(53)	(185)	(361)	(570)
Depreciation and amortization	846	4,768	6,166	14,522
<b>EBITDA</b>	\$ 15,295	\$ (4,548)	\$ (19,646)	\$ (6,237)
Additional adjustments :				
Stock-based compensation expense	198	256	778	526
Impairment of property and equipment and right-of-use assets	—	2,051	2,561	7,076
Loss on disposal of property and equipment	—	—	—	22
Restructuring plan activities, net	(10,743)	—	24,017	—
Government emergency wage subsidy	(1,446)	—	(3,445)	—
<b>Adjusted EBITDA</b>	\$ 3,304	\$ (2,241)	\$ 4,265	\$ 1,387



*Reconciliation of Net income (loss) to Adjusted net income (loss)*

	For the three months ended		For the nine months ended	
	October 31,	November 2,	October 31,	November 2,
	2020	2019	2020	2019
<b>Net income (loss)</b>	\$ 14,467	\$ (10,830)	\$ (28,711)	\$ (25,494)
Impairment of property and equipment and right-of-use assets	—	2,051	2,561	7,076
Loss on disposal of property and equipment	—	—	—	22
Restructuring plan activities, net	(10,743)	—	24,017	—
Government emergency wage subsidy	(1,446)	—	(3,445)	—
<b>Adjusted Net income (loss)</b>	\$ 2,278	\$ (8,779)	\$ (5,578)	\$ (18,396)

*Reconciliation of fully diluted net income (loss) per common share to Adjusted fully diluted net income (loss) per common share*

	For the three months ended		For the nine months ended	
	October 31,	November 2,	October 31,	November 2,
	2020	2019	2020	2019
<b>Weighted average number of shares outstanding, fully diluted</b>	26,767,470	26,068,435	26,143,963	26,048,239
<b>Net income (loss)</b>	\$ 14,467	(10,830)	\$ (28,711)	\$ (25,494)
<b>Adjusted net income (loss)</b>	\$ 2,278	(8,779)	\$ (5,578)	\$ (18,396)
<b>Net income (loss) per share, fully diluted</b>	\$ 0.54	(0.42)	\$ (1.10)	\$ (0.98)
<b>Adjusted Net income (loss) per share, fully diluted</b>	\$ 0.09	(0.34)	\$ (0.21)	\$ (0.71)

*Three Months Ended October 31, 2020 compared to Three Months Ended November 2, 2019*

**Sales.** Sales for the three months ended October 31, 2020 decreased 33.6%, or \$13.3 million, to \$26.2 million from \$39.5 million in the prior year quarter. On March 17, 2020, in response to the COVID-19 pandemic, the Company temporarily closed all its retail stores in Canada and the United States, and subsequently, as part of its formal Restructuring Plan, exited all of its brick and mortar stores except for 18 Canadian stores which were reopened on August 21, 2020. Accordingly, brick and mortar sales for the quarter declined when compared to the prior year quarter by \$26.4 million or 86.5% to \$4.1 million. Sales from e-commerce and wholesale channels increased by \$13.1 million or 145.5% to \$22.1 million, from \$9.0 million in the prior year quarter. E-commerce and wholesale sales represented 84.3% of sales compared to 22.8% of sales in the prior year quarter.

**Gross profit.** Gross profit of \$10.8 million for the three months ended October 31, 2020 decreased by \$10.5 million or 49.3% from the prior year quarter due primarily to a decline in sales during the period. As the Company pivots to a digital-first strategy, the cost of delivery and distribution that is included in arriving at gross profit will compare unfavorably to prior periods that were predominantly focused on retail sales distribution. The significant increase in e-commerce sales resulted in an increase of \$4.2 million in delivery and distribution costs, thereby negatively impacting gross profit percentage. As a result, gross profit as a percentage of sales declined to 41.3% for the three-month period ended October 31, 2020 from 54.1% in the prior year quarter. We expect that the increased cost to deliver online purchases will be less than the selling expenses incurred in a brick and mortar environment that have been historically included as part of Selling, general and administration expenses.

**Selling, general and administration expenses.** Selling, general and administration expenses decreased by \$23.6 million or 76.8% to \$7.1 million in the three months ended October 31, 2020 from the prior year quarter. Excluding the impact of the \$1.4 million wage subsidy received under the Canadian government COVID-19 Economic Response Plan in Fiscal 2020, and the impact in Fiscal 2019 of the impairment of property and equipment and right-of use assets amounting to \$2.1 million, Adjusted SG&A decreased by \$20.1 million. In connection with our Restructuring Plan, we terminated the leases for all of our stores in North America except for 18 Canadian stores which reopened on August 21, 2020. As a result, wages, salaries and employee benefits were reduced by \$12.2 million, and we realized a reduction of \$3.8 million in amortization expenses due to a lower right-of-use asset value at the beginning of the period. Adjusted SG&A as a percentage of sales in the quarter decreased to 32.7% from 72.5% in the prior year quarter.

*Results from operating activities.* Income from operating activities was \$14.4 million compared to a loss of \$9.3 million in the prior year quarter. Excluding the impact of the Restructuring Plan announced on July 8, 2020, the wage subsidy received from the Canadian government under the COVID-19 Economic Response Plan, the impact of the impairment of property and equipment and right-of-use assets and the loss on disposal of property and equipment, Adjusted results from operating activities amounted to \$2.3 million in the three-month period ended October 31, 2020 compared to a loss of \$7.3 million in the prior year quarter. This resulting improvement of \$9.6 million is explained by a reduction in wages, salaries and employee benefits from stores and head office, amounting to \$12.2 million, a reduction of \$3.8 million in amortization expense due to a lower right-of-use asset value at the beginning of the period, and a reduction of other brick and mortar selling expenses of \$3.5 million, partially offset by the reduction of gross profit of \$10.5 million.

*Finance costs.* Finance costs amounted to almost nil in the three months ended October 31, 2020, a decrease of \$1.7 million from the prior year quarter. The interest expense relates to lease liabilities and has decreased slightly from the prior year quarter.

*Finance income.* Finance income of \$0.1 million is derived mainly from interest on cash on hand and has decreased slightly from the prior year quarter.

*EBITDA.* EBITDA was \$15.3 million in the quarter ended October 31, 2020 compared to a negative \$4.5 million in the prior year quarter, representing an increase of \$19.8 million over the prior year quarter. Adjusted EBITDA for the quarter ended October 31, 2020, which excludes the impact of stock-based compensation expense, Restructuring plan activities, the subsidy received from the Canadian government under the COVID-19 Economic Response Plan, and the impairment of property and equipment and right-of-use assets amounted to \$3.3 million compared to negative \$2.2 million in the prior year quarter. As the Company pivots to a digital-first strategy, we are seeing an improvement in EBITDA driven from our focus on e-commerce and wholesale channels. In this quarter, EBITDA also improved as a result of a reduced general and administrative infrastructure to support the on-going business.

*Net income (loss).* Net income was \$14.5 million in the quarter ended October 31, 2020 compared to a Net loss of \$10.8 million in the prior year quarter. Adjusted net loss, which excludes the Restructuring plan activities, the subsidy received from the Canadian Government under the COVID-19 Economic Response Plan, and the impairment of property and equipment and right-of-use assets amounted to \$2.3 million compared to a loss of \$8.8 million in the prior year quarter. This \$11.1 million improvement is driven by the same reasons mentioned above in “Results from operating activities”.

*Fully diluted income (loss) per common share.* Fully diluted income per common share was \$0.54 compared to a loss of \$0.42 in the third quarter of Fiscal 2019. Adjusted fully diluted income per common share, which is adjusted net income (loss) on a fully diluted weighted average shares outstanding basis, was \$0.09 per share compared to a loss of \$0.34 per share.

#### *Nine Months Ended October 31, 2020 compared to Nine Months Ended November 2, 2019*

*Sales.* Sales for the nine months ended October 31, 2020 decreased 33.7%, or \$41.4 million, to \$81.5 million from \$122.9 million in the same period in the prior year. On March 17, 2020, in response to the COVID-19 pandemic, the Company announced the temporary closures of all its retail stores in Canada and the United States, and subsequently, as part of its Restructuring Plan, exited all of its brick and mortar stores except for 18 Canadian stores which were reopened on August 21, 2020. Accordingly, brick and mortar sales declined by \$78.9 million or 80.3% when compared to the same period in the prior year. Sales from our e-commerce and wholesale channels increased \$37.5 million or 152.0% to \$62.1 million, from \$24.7 million in the same period in prior year as we shifted to a digital first strategy to address consumers changing shopping habits. For the nine-month period ended October 31, 2020, e-commerce and wholesale sales represented 76.2% of total sales as opposed to 20.1% in the same period in the prior year.

*Gross profit.* Gross profit of \$34.1 million for the nine-month period ended October 31, 2020 decreased by \$35.4 million or 50.9% from the same period of the prior year due primarily to a decline in sales during the period. Gross profit as a percentage of sales declined to 41.8% for the nine-month period ended October 31, 2020 from 56.5% in the same period in the prior year. As the Company pivots to a digital first strategy, the cost of delivery and distribution that is included in arriving at gross profit will compare unfavorably to prior periods that were predominantly focused on retail sales distribution. The significant increase in e-commerce sales during the period ended October 31, 2020 resulted in an increase of \$9.3 million in delivery and distribution costs. Our margins were also impacted by an increase in inventory obsolescence of \$2.6 million in Fiscal 2020 caused by the consolidation of merchandise from our closed retail stores during the first quarter and the permanent closure of the majority of our stores.

*Selling, general and administration expenses.* SG&A decreased by \$54.4 million or 60.2%, to \$35.9 million in the nine months ended October 31, 2020 from the same period in the prior year. Excluding the impact of the impairment of property and equipment and right-of-use assets, and the wage subsidy received from the Canadian Government under the COVID-19 Economic Response Plan in the nine-month period ended October 31, 2020 which amounted to \$0.9 million, Adjusted SG&A decreased by \$46.4 million for the nine months ended October 31, 2020. This is mostly explained by the temporary closure of our stores effective March 17, 2020 and the reopening of 18 stores on August 21, 2020. As a result, wages, salaries and employee benefits were reduced by \$31.1 million and we realized a reduction of \$8.5 million in amortization expense due to a lower right-of-use asset value at the beginning of Fiscal 2020. As a

percentage of sales, Adjusted SG&A decreased to 45.1% from 67.7% due to lower selling expenses resulting from the now permanent closure of our 206 stores effective March 17, 2020 and the reopening of 18 stores on August 21, 2020.

*Results from operating activities.* Loss from operating activities was \$25.8 million compared to a loss of \$20.8 million in the same period in Fiscal 2019. Excluding the impact of the impairment of property and equipment and right-of-use assets, the Restructuring plan activities, the wage subsidy received from the Canadian Government under the COVID-19 Economic Response Plan, and the loss on disposal of property and equipment, Adjusted results from operating activities was a loss of \$2.7 million compared to a loss of \$13.7 million in the same period in the prior year. This resulting improvement of \$11.0 million is explained by reduction in wages, salaries and employee benefits, from stores and head office, amounting to \$31.1 million and an \$8.5 million reduction in amortization expense due to a lower right-of-use asset value at the beginning of Fiscal 2020, and a reduction of other selling expenses, partially offset by the reduction of gross profit of \$35.4 million.

*Finance costs.* Finance costs amounted to \$3.3 million in the nine-month period ended October 31, 2020, a decrease of \$2.0 million from the prior year quarter. The interest expense relates to lease liabilities and has decreased from the prior year period due to the store closures.

*Finance income.* Finance income of \$0.4 million is derived mainly from interest on cash on hand and has decreased slightly from the prior year period.

*EBITDA.* EBITDA was negative \$19.6 million in the nine-month period ended October 31, 2020 compared to negative \$6.2 million in the same period in the prior year, representing a decrease of \$13.4 million over Fiscal 2019. Adjusted EBITDA for the nine months ended October 31, 2020, which excludes the impact of stock-based compensation expense, the impairment of property and equipment and right-of-use assets, the Restructuring plan activities, the wage subsidy received from the Canadian Government under the COVID-19 Economic Response Plan, and the loss on disposal of property and equipment amounted to \$4.3 million compared to \$1.4 million in the same period in the prior year. The increase in Adjusted EBITDA, of \$2.9 million, is an outcome of the reduction in SG&A that was partially offset by the decline in gross profit.

*Net loss.* Net loss was \$28.7 million in the nine months ended October 31, 2020 compared to a net loss of \$25.5 million in the same period in prior year. Adjusted net loss, which excludes the impact from the impairment of property and equipment and right-of-use assets, the Restructuring plan activities, the subsidy received from the Canadian Government under the COVID-19 Economic Response Plan, and loss on disposal of property and equipment was \$5.6 million compared to \$18.4 million in the same period in the prior year. This \$12.8 million improvement is driven by the same reasons mentioned above in Results from operating activities.

*Fully diluted loss per common share.* Fully diluted loss per common share was negative \$1.10 compared to negative \$0.98 in the nine months ended October 31, 2020. Adjusted fully diluted loss per common share, which is adjusted net loss on a fully diluted weighted average shares outstanding basis, was negative \$0.21 per share compared to negative \$0.71 per share.

## **Liquidity and Capital Resources**

As at October 31, 2020 we had \$21.9 million of cash primarily held by major Canadian financial institutions. Working capital was negative \$12.2 million as at October 31, 2020, compared to \$36.4 million as at February 1, 2020.

Our primary source of liquidity is cash on hand as we have no access to any form of debt financing. Our primary cash needs are to finance working capital and capital expenditures in connection with enhancing the functions and features of our online store. Our working capital requirements are for the purchase of inventory and payment of payroll and other operating costs. Furthermore, in light of implementing the Restructuring Plan, the Company expects to use cash on hand to pay for professional fees and for the settlement of obligations upon acceptance, if any, of a plan of arrangement that will be presented to creditors. 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 fund our capital expenditures and working capital requirements from a combination of cash on hand and cash provided by operating activities.

## Cash Flow

A summary of our cash flows provided by (used in) operating, investing and financing activities is presented in the following table:

	For the three months ended		For the nine months ended	
	October 31, 2020	November 2, 2019	October 31, 2020	November 2, 2019
<b>Cash flows provided by (used in) :</b>				
Operating activities	\$ (12,016)	\$ 4,786	\$ (19,896)	\$ 8,229
Financing activities	(250)	(5,711)	(5,821)	(17,333)
Investing activities	(94)	(756)	1,304	(4,926)
<b>Decrease in cash</b>	<b>\$ (12,360)</b>	<b>\$ (1,681)</b>	<b>\$ (24,413)</b>	<b>\$ (14,030)</b>

### Three Months Ended October 31, 2020 compared to Three Months Ended November 2, 2019

*Cash flows provided by (used in) Operating activities.* Net cash flows used in Operating activities during the quarter ended October 31, 2020 amounted to \$12.0 million and represented a change of \$16.8 million from the prior year quarter. The change is primarily due to the impact of the Restructuring Plan, wherein cash was used to make vendor deposits for both services and inventory related purchases.

*Cash flows used in Financing activities.* Net cash flows used in Financing activities of \$0.3 million compares to \$5.7 million used in the prior year quarter. This net reduction in use of cash was primarily due to the Restructuring Plan and the termination of our store lease agreements.

*Cash flows used in Investing activities.* Cash flows used in Investing activities decreased from \$0.8 million to \$0.1 million for the three months ended October 31, 2020. The decrease is primarily due to the capital expenditures and the loan advance that was made in the prior year quarter. Capital expenditures decreased by \$0.4 million, to \$0.1 million for the three months ended October 31, 2020, from \$0.5 million in the prior year quarter. This decrease was primarily due to lower investment in software enhancements.

### Nine Months Ended October 31, 2020 compared to Nine Months Ended November 2, 2019

*Cash flows (used in) provided by Operating activities.* Net cash flows used in Operating activities during the nine-month period ended October 31, 2020 amounted to \$19.9 million and represented a change of \$28.1 million from the prior year. The change is primarily due to the impact of our Restructuring PlanA, wherein we have used cash to make vendor deposits for both services and purchases of inventory related goods.

*Cash flows used in Financing activities.* Net cash flows used in financing activities of \$5.8 million during the nine-month period ended October 31, 2020 represents a reduction of \$11.5 million compared to the prior year corresponding period and due primarily to the non-payment of lease obligations from April 1, 2020 to July 8, 2020 and the termination of our store lease agreements.

*Cash flows provided by (used in) Investing activities.* Cash flows provided by investing activities of \$1.3 million during the nine-month period ended October 31, 2020 increased by \$6.2 million. The increase is primarily due to the receipt of cash from repayment of the loan from a Company controlled by an executive employee, partially offset by capital expenditures. Capital expenditures decreased by \$2.2 million to \$0.7 million for the nine-month period ended October 31, 2020, from \$2.9 million in the prior year period. This decrease was primarily due to lower investment in both leasehold improvements as well as software enhancements.

## Off-Balance Sheet Arrangements

We have no off-balance sheet obligations.

## Contractual Obligations and Commitments

We enter into contractual obligations and commitments that require us to disburse cash over future periods. All commitments have been recorded in our consolidated balance sheet, except for future purchase obligations. Given the nature of our Restructuring Plan, and as mentioned in Note 7, we anticipate that there will be significant changes to previously reported contractual obligations in future periods and when reasonably estimable, will be recorded through earnings.

## 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 judgment 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 1, 2020 included in our Annual Report on Form 10-K dated June 16, 2020. There have been no material changes to the critical accounting policies and estimates since February 1, 2020, other than those disclosed in Note 4 to our interim consolidated financial statements for the three and nine-month periods ended October 31, 2020.

## 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 June 16, 2020.

## 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 and Operating Officer, evaluated the effectiveness of our disclosure controls and procedures as of October 31, 2020. 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.

Based on an assessment of our disclosure controls and procedures, as a result of the identification of a material weakness in connection with our non-financial asset impairment testing processes identified in the close process for the fourth quarter of Fiscal 2019, as well as the material weakness identified in the Company’s financial statement close process for the quarter ended November 2, 2019 related to accounting errors identified in the assessment of impairment indicators upon the adoption of IFRS 16, “Leases”, our management concluded that, considering the significant extent of change driven largely by the implementation of our Restructuring Plan, remediation efforts continue and our disclosure controls and procedures continue to not be effective as of October 31, 2020.

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

The COVID-19 pandemic could negatively affect our internal controls over financial reporting, including our ongoing process of remediating the material weakness in our disclosure control and procedures, as a portion of our workforce is required to work remotely and standard processes are disrupted. New processes, procedures, and controls, which may increase the overall inherent risk in the business, may be required to ensure an effective control environment.

With the exception of the material weaknesses identified there were no other changes in our internal control over financial reporting during our fiscal quarter ended October 31, 2020 that materially affected, or were reasonably likely to materially affect, our internal control over financial reporting.