

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", "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 and include statements regarding our intentions, beliefs or current expectations concerning, among other things, our strategy of transitioning to e-commerce and wholesale sales, future sales through our e-commerce and wholesale channels, our results of operations, financial condition, liquidity and prospects, and the impact of the COVID-19 pandemic and other geopolitical conditions on the global macroeconomic environment.

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 our Form 10-K filed with the SEC on April 29, 2022.

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 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 who 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 maintain and enhance our brand image;
- Significant competition within our industry;
- Our ability to obtain quality products from third-party manufacturers and suppliers on a timely basis or in sufficient quantities, in light of supply chain disruptions due to the ongoing COVID-19 pandemic and the war in Ukraine;
- Actual or attempted breaches of data security; 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 2022” are to the Company’s fiscal year ending January 28, 2023. All references to “Fiscal 2021” are to the Company’s fiscal year ended January 29, 2022.

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 January 29, 2022 and the year ending January 28, 2023 both cover a 52-week period.

Overview

The Company offers a selection of high-quality proprietary loose-leaf teas, pre-packaged teas, tea sachets, tea-related accessories, and gifts through its e-commerce platform at www.davidstea.com and the Amazon Marketplace, its wholesale customers which include over 3,800 grocery stores and pharmacies, and 18 Company-owned stores across Canada. The Company offers primarily proprietary tea blends that are exclusive to the Company, as well as traditional single-origin teas and herbs. Our passion for and knowledge of tea permeates our culture and is rooted in an excitement to explore the taste, health and lifestyle elements of tea. With a focus on innovative flavours, wellness-driven ingredients and organic tea, the Company launches seasonally driven “collections” with a mission of making tea fun and accessible to all.

Sales fluctuate from quarter to quarter. Sales are traditionally highest in the fourth fiscal quarter due to the year-end holiday season and tend to be lowest in the second and third fiscal quarters because of lower customer engagement during the summer months.

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. We are focused on effectively optimizing our retail footprint into a more sustainable physical presence that complements a growing online and wholesale business, all supported by a right-sized support organization.

In March 2020, the outbreak of a novel strain of coronavirus (“COVID-19”) was declared a global pandemic by the World Health Organization and on March 17, 2020, in response to the COVID-19 pandemic, the Company announced the temporary closure of all its retail stores in Canada and the United States.

Following a careful review of available options to stem the losses generated primarily from its brick-and-mortar footprint, our 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 announced that it was implementing a restructuring plan (the “Restructuring Plan”) under the Companies’ Creditors Arrangement Act (Canada) (the “CCAA”) in order to accelerate its transition to predominantly 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 and the Amazon Marketplace as well as its wholesale distribution channel. On August 21, 2020, the Company re-opened 18 stores across Canada and permanently closed 164 stores in Canada and all 42 stores in the United States.

At a creditors’ meeting held on June 11, 2021, the Company’s Plan of Arrangement was approved by the requisite majorities of creditors of DAVIDsTEA Inc. and its subsidiary DAVIDsTEA (USA) Inc., respectively, in accordance with the CCAA, that is, a simple majority of creditors of DAVIDsTEA Inc. and of DAVIDsTEA (USA) Inc., voting separately, whose claims were affected by the Plan of Arrangement, representing in each case at least two-thirds in dollar value of all such claims duly filed in accordance with the CCAA proceedings.

The approved Plan of Arrangement required that DAVIDsTEA Inc. distribute an aggregate amount of \$17.6 million to its creditors and those of DAVIDsTEA (USA) Inc. in full and final settlement of all claims affected by the Plan of Arrangement on June 18, 2021.

On September 9, 2021, the Monitor filed a Certificate of Termination with the Québec Superior Court in accordance with paragraph 24 of the Sanction Order and declared the CCAA proceedings were terminated without further act or formality.

The Company emerged from the Restructuring Plan a smaller and more invigorated organization, with a renewed sense of purpose and confidence as we continue building a high-performing, future-ready winning culture, driven by purpose. We were founded on a spirit of innovation and of embracing unconventional ideas with a desire to create a North American experience around

tea. We removed the boundaries that kept tea in the cupboards of only those in-the-know. We experimented and took risks, attracted passionate employees and as customers became friends, we embraced our brand purpose; a desire to share “positivitea” with all, and use our platform to do good - for business and for the lives of all with whom we interact.

Our actions are driven by the fervent desire to become the world’s most innovative tea company; one that inspires greater wellness and sustainability through ethical and sustainable tea sourcing, compostable and regenerative packaging, and caring for our community. Our digital-first strategy is built to respond to consumer demand - meeting consumers where they are, driving loyalty with the ability to scale the business, without borders. We are focused on building a winning culture that is fueled by delighting consumers and driven to overcome challenging operational and market conditions. We are focused on revenue growth, attaining profitability and positive cash-flow, and with an unwavering sense of passion, purpose and commitment to our customers and our stakeholders.

Factors Affecting Our Performance

We believe that our performance and future success depend on several 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” in our 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 are generated from our online stores, 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. Several factors influence the level of consumer spending, including economic conditions and the level of disposable consumer income, consumer debt, interest rates, the rate of inflation and consumer confidence that can affect purchases of our products.

As we have transitioned to generating sales primarily from our online stores, 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 and tea accessories; and
- our ability to obtain, process 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 asset impairment 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.

Results from Operating Activities. Results from operating activities consist of our gross profit less our selling, general and administration expenses, and in respect of Fiscal 2021, Restructuring Plan activities, net.

Finance Costs. Finance costs consist of interest expense on lease liabilities.

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

Selected Operating and Financial Highlights

Results of Operations

Sales during the third quarter of Fiscal 2022 decreased by \$6.0 million or 27.1% to \$16.2 million from the prior year quarter due mainly to a decrease in e-commerce sales of \$4.3 million and a decrease in brick-and-mortar and wholesale sales of \$1.8 million.

Sales of \$51.7 million in the year-to-date period ended October 29, 2022 decreased by \$12.5 million from the prior year period or 19.5% due to a decrease in e-commerce sales of \$16.2 million, partially offset by an increase in sales of \$3.7 million from brick-and-mortar and wholesale.

The Company recorded a Net loss of \$4.7 million in the third quarter compared to a Net loss of \$1.9 million in the prior year quarter. Excluding adjustments noted herein, Adjusted net loss ⁽¹⁾ for the third quarter was \$3.3 million compared to an Adjusted net loss ⁽¹⁾ of \$1.8 million in the prior year quarter. Adjusted EBITDA ⁽¹⁾ in the third quarter of Fiscal 2022 was a loss of \$2.0 million compared to a loss of \$0.3 million in the prior year quarter.

The Company recorded a Net Loss of \$11.5 million in the year-to-date period compared to a Net income of \$76.8 million in the prior year period. Excluding adjustments noted herein, Adjusted net loss ⁽¹⁾ for the year-to-date period was \$8.0 million compared to an Adjusted net loss ⁽¹⁾ of \$2.4 million in the prior year period. Adjusted EBITDA ⁽¹⁾ in the year-to-date period of Fiscal 2022 was a loss of \$4.1 million compared to income of \$1.6 million in the prior year period.

Sales and operating results have been materially impacted by changes in overall economic conditions in North America and the impact these conditions have had on consumer confidence and discretionary spending. Continuing inflationary pressures have resulted in an increase in our cost of goods, transportation, and labour costs. Fears of a looming recession, increases in interest rates, the rate of inflation, uncertainty surrounding the COVID-19 pandemic, continuing supply chain disruptions, increased input costs, and shortage of technical and skilled labour are expected to have a continuing significant impact on economic conditions that could materially affect our financial condition, results of operations and cash flows.

As COVID-19 restrictions loosened in Fiscal 2022, consumer spending shifted to out-of-home and we saw a shift away from online to brick-and mortar. We believe this decline in e-commerce revenue is temporary as we continue to build on the wellness trend for healthier beverages with our target audiences.

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 29, 2022	October 30, 2021	October 29, 2022	October 30, 2021
Consolidated statement of operations data:				
Sales	\$ 16,176	\$ 22,203	\$ 51,670	\$ 64,195
Cost of sales	9,894	13,587	30,116	36,816
Gross profit	6,282	8,616	21,554	27,379
Selling, general and administration expenses	10,925	10,242	32,784	28,521
Restructuring plan activities, net	—	195	—	(76,964)
Results from operating activities	(4,643)	(1,821)	(11,230)	75,822
Finance costs	194	71	532	104
Finance income	(120)	(28)	(236)	(118)
Net income (loss) before income taxes	(4,717)	(1,864)	(11,526)	75,836
Recovery of income taxes	—	—	—	(1,000)
Net (loss) income	\$ (4,717)	\$ (1,864)	\$ (11,526)	\$ 76,836
Percentage of sales:				
Sales	100.0%	100.0%	100.0%	100.0%
Cost of sales	61.2%	61.2%	58.3%	57.4%
Gross profit	38.8%	38.8%	41.7%	42.6%
Selling, general and administration expenses	67.5%	46.1%	63.4%	44.4%
Net (loss) income	(29.2)%	(8.4)%	(22.3)%	119.7%
Other financial and operations data:				
Adjusted EBITDA ⁽¹⁾	\$ (2,004)	\$ (308)	\$ (4,043)	\$ 1,555
Adjusted EBITDA as a percentage of sales ⁽¹⁾	(12.4)%	(1.4)%	(7.8)%	2.4%
Adjusted SG&A ⁽¹⁾	\$ 9,525	\$ 10,359	\$ 29,304	\$ 29,780
Adjusted results from operating activities ⁽¹⁾	\$ (3,243)	\$ (1,743)	\$ (7,750)	\$ (2,401)
Adjusted net loss ⁽¹⁾	\$ (3,317)	\$ (1,786)	\$ (8,046)	\$ (2,387)

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

Non-IFRS Financial Measures and Ratios

The Company uses certain non-IFRS financial measures and ratios for purposes of comparison to prior periods, to prepare annual operating budgets, and for the development of future projections. These measures and ratios 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 and ratios 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 present the following non-IFRS financial measures;

- “Adjusted selling, general and administration expenses” is presented 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 are non-recurring by nature or which vary from period to period.
- “Adjusted results from operating activities” is presented 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 are non-recurring by nature or which vary from period to period.

- (c) “Adjusted net (loss) income” is presented 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 are non-recurring by nature or which vary from period to period.
- (d) “Adjusted EBITDA” is presented 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 are non-recurring by nature or which 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, stock-based compensation and certain non-recurring expenses. This measure also functions as a benchmark to evaluate our operating performance.

We also present the following non-IFRS ratios:

- (a) “Adjusted net (loss) income per common share” for purposes of evaluating underlying business performance relative to our performance based on our results under IFRS, while isolating the effects of some items that vary from period to period.
- (b) Adjusted EBITDA as a percentage of sales is calculated by dividing adjusted EBITDA as defined above by the sales figures for a period.

The use of non-IFRS financial measures and ratios provides complementary information that excludes items that do not reflect our core performance or where their exclusion would assist users in understanding our results for the period. For these reasons, a significant number of users of our MD&A analyze our results based on these financial measures. Management believes these measures help users of our MD&A to better analyze results, enabling better comparability of our results from one period to another and with peers.

Management believes that these non-IFRS financial measures and ratios in addition to IFRS measures and ratios provide users of our financial reports with enhanced understanding of our results and related trends and increases the transparency and clarity of the core results of our business.

We believe that although 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 (loss) income 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 (loss) income 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 and ratios 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 29, 2022	October 30, 2021	October 29, 2022	October 30, 2021
Selling, general and administration expenses	\$ 10,925	\$ 10,242	\$ 32,784	\$ 28,521
Software implementation and configuration costs (a)	(1,142)	(641)	(3,222)	(3,095)
Government emergency wage and rent subsidy (b)	—	758	—	4,354
Impairment of property and equipment and right-of-use assets (c)	(258)	—	(258)	—
Adjusted selling, general and administration expenses	\$ 9,525	\$ 10,359	\$ 29,304	\$ 29,780

- (a) Represents costs related to implementation and configuration of software solutions.
- (b) Represents the wage and rent subsidies received from the Canadian government under the COVID-19 Economic Response Plan.
- (c) Represents costs related to impairment of property and equipment and right-of-use assets within our retail stores.

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

	For the three-months ended		For the nine-months ended	
	October 29, 2022	October 30, 2021	October 29, 2022	October 30, 2021
Results from operating activities	\$ (4,643)	\$ (1,821)	\$ (11,230)	\$ 75,822
Software implementation and configuration costs (a)	1,142	641	3,222	3,095
Restructuring plan activities, net (b)	—	195	—	(76,964)
Government emergency wage and rent subsidy (c)	—	(758)	—	(4,354)
Impairment of property and equipment and right-of-use assets (d)	258	—	258	—
Adjusted results from operating activities	\$ (3,243)	\$ (1,743)	\$ (7,750)	\$ (2,401)

- (a) Represents costs related to implementation and configuration of software solutions.
- (b) Represents the net gain related to the Restructuring Plan activities which were completed in Fiscal 2021.
- (c) Represents the wage and rent subsidies received from the Canadian government under the COVID-19 Economic Response Plan.
- (d) Represents costs related to impairment of property and equipment and right-of-use assets for within our retail stores.

Reconciliation of Net (loss) income to Adjusted net loss

	For the three-months ended		For the nine-months ended	
	October 29, 2022	October 30, 2021	October 29, 2022	October 30, 2021
Net (loss) income	\$ (4,717)	\$ (1,864)	\$ (11,526)	\$ 76,836
Software implementation and configuration costs (a)	1,142	641	3,222	3,095
Restructuring plan activities, net (b)	—	195	—	(76,964)
Government emergency wage and rent subsidy (c)	—	(758)	—	(4,354)
Recovery of income taxes (d)	—	—	—	(1,000)
Impairment of property and equipment and right-of-use assets (e)	258	—	258	—
Adjusted net loss	\$ (3,317)	\$ (1,786)	\$ (8,046)	\$ (2,387)

- (a) Represents costs related to implementation and configuration of software solutions.
- (b) Represents the net gain related to the Restructuring Plan activities which were completed in Fiscal 2021.
- (c) Represents the wage and rent subsidies received from the Canadian government under the COVID-19 Economic Response Plan.
- (d) Represents the reversal of the previously accrued estimate of income tax liabilities that were compromised by the Restructuring Plan.
- (e) Represents costs related to impairment of property and equipment and right-of-use assets within our retail stores.

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

	For the three-months ended		For the nine-months ended	
	October 29, 2022	October 30, 2021	October 29, 2022	October 30, 2021
Weighted average number of shares outstanding, fully diluted	26,566,441	26,359,969	26,493,484	27,584,128
Adjusted weighted average number of shares outstanding, fully diluted	26,566,441	26,359,969	26,493,484	26,300,289
Net (loss) income	\$ (4,717)	\$ (1,864)	\$ (11,526)	\$ 76,836
Adjusted net loss	\$ (3,317)	\$ (1,786)	\$ (8,046)	\$ (2,387)
Net (loss) earnings per common share, fully diluted	\$ (0.18)	\$ (0.07)	\$ (0.44)	\$ 2.79
Adjusted net loss per common share, fully diluted	\$ (0.12)	\$ (0.07)	\$ (0.30)	\$ (0.09)

Reconciliation of Net (loss) income to Adjusted EBITDA

	For the three-months ended		For the nine-months ended	
	October 29, 2022	October 30, 2021	October 29, 2022	October 30, 2021
Net (loss) income	\$ (4,717)	\$ (1,864)	\$ (11,526)	\$ 76,836
Finance costs	194	71	532	104
Finance income	(120)	(28)	(236)	(118)
Depreciation and amortization	884	1,043	2,644	3,019
Recovery of income taxes	—	—	—	(1,000)
EBITDA	\$ (3,759)	\$ (778)	\$ (8,586)	\$ 78,841
Additional adjustments:				
Stock-based compensation expense (a)	355	392	1,063	937
Software implementation and configuration costs (b)	1,142	641	3,222	3,095
Restructuring plan activities, net (c)	—	195	—	(76,964)
Government emergency wage and rent subsidy (d)	—	(758)	—	(4,354)
Impairment of property and equipment and right-of-use assets (e)	258	—	258	—
Adjusted EBITDA	\$ (2,004)	\$ (308)	\$ (4,043)	\$ 1,555

(a) Represents non-cash stock-based compensation expense.

(b) Represents costs related to implementation and configuration of software solutions.

(c) Represents the net gain related to the Restructuring Plan activities which were completed in Fiscal 2021.

(d) Represents the wage and rent subsidies received from the Canadian government under the COVID-19 Economic Response Plan.

(e) Represents costs related to impairment of property and equipment and right-of-use assets within our retail stores.

Operating results for the three-months ended October 29, 2022, compared to the operating results for the three-months ended October 30, 2021

Sales. Sales decreased 27.1%, or \$6.0 million, to \$16.2 million in the quarter ended October 29, 2022, compared to \$22.2 million in the prior year quarter. Sales in Canada of \$12.9 million, representing 79.7% of total revenues, decreased \$5.0 million or 28.1% compared to the prior year quarter. U.S. sales of \$3.3 million decreased by \$1.0 million or 23.0% compared to the prior year quarter. Sales from e-commerce decreased by \$4.3 million or 29.5% to \$10.2 million from \$14.5 million in the prior year quarter. Sales from our wholesale channel decreased \$1.1 million or 41.8% to \$1.6 million from \$2.7 million in the prior year quarter. This decrease is explained primarily by discounting on older formats as we transitioned to our new individually wrapped sachets. Brick-and-mortar sales for the quarter of \$4.4 million were impacted by reduced consumer traffic, decreasing \$0.6 million or 12.5% compared to the prior year quarter. E-commerce, wholesale, and brick-and-mortar sales represented 62.9%, 9.8% and 27.3% of sales, respectively compared to 65.0%, 12.2% and 22.8%, respectively in the prior year quarter.

Gross Profit. Gross profit of \$6.3 million for the three-months ended October 29, 2022 decreased by \$2.3 million or 27.1% from the prior year quarter due to a decline in sales during the period, partially offset by lower delivery and distribution costs, compared to the prior year quarter. Gross profit as a percentage of sales was 38.8% for the quarter, consistent with the prior year quarter.

Selling, General and Administration Expenses. Selling, general and administration expenses (“SG&A”) increased \$0.7 million or 6.7% to \$10.9 million in the third quarter compared to the prior year quarter. Excluding the impact of software implementation and configuration costs, the impact of the wage and rent subsidies received under the Canadian government COVID-19 Economic Response Plan, and the impairment of property and equipment and right-of-use assets, Adjusted SG&A decreased by \$0.8 million or 8.1% to \$9.5 million in the quarter. The drop in SG&A expenses is primarily due to a decrease in marketing expenses and credit card fees partially offset by increases in IT ongoing expenses as the Company continues its transformation to an omnichannel organization. Adjusted SG&A as a percentage of sales in the quarter increased to 58.9% from 46.7% in the prior year quarter.

Results from Operating Activities. Loss from operating activities during the quarter was \$4.6 million compared to a loss of \$1.8 million in the prior year quarter. Excluding the impact of the Restructuring plan activities, net, the wage and rent subsidies received from the Canadian government under the COVID-19 Economic Response Plan, and software implementation and configuration costs, and the impairment of property and equipment and right-of-use assets, Adjusted operating loss amounted to \$3.2 million in the third quarter compared to an Adjusted operating loss of \$1.7 million in the prior year quarter. The increased Adjusted operating loss results primarily from a decline in sales, lower gross profit and increased SG&A expenses in pursuit of the ongoing transformation to become a digital first organization.

Finance Costs. Finance costs amounted to \$194 thousand in the three-months ended October 29, 2022 and compares unfavorably to the prior year period due primarily to the interest expense on our right-of-use assets.

Finance Income. Finance income of \$120 thousand, which is derived mainly from interest on cash on hand, decreased slightly from the prior year quarter.

Net loss. Net loss was \$4.7 million in the quarter compared to a Net loss of \$1.9 million in the prior year quarter. Adjusted net loss, which excludes the impact of Restructuring plan activities, net, the wage and rent subsidies received from the Canadian government under the COVID-19 Economic Response Plan, software implementation and configuration costs, and the impairment of property and equipment and right-of-use assets, amounted to a Net loss of \$3.3 million compared to a Net loss of \$1.8 million in the prior year quarter.

Fully diluted loss per common share. Fully diluted loss per common share was \$0.18 in the quarter ended October 29, 2022 compared to a fully diluted loss per common share of \$0.07 in the prior year quarter. Adjusted fully diluted loss per common share was \$0.12 in the quarter ended October 29, 2022 compared to an Adjusted fully diluted loss per common share of \$0.07 in the prior year quarter.

EBITDA and Adjusted EBITDA. EBITDA, which excludes non-cash and other items in the current and prior periods, was negative \$3.8 million in the quarter ended October 29, 2022 compared to negative \$0.8 million in the prior year quarter representing a decrease of \$3.0 million over the prior year quarter. Adjusted EBITDA for the quarter ended October 29, 2022 was negative \$2.0 million compared to negative \$0.3 million for the same period in the prior year. The decrease in Adjusted EBITDA of \$1.7 million reflects the impact of a sales decline of \$6.0 million, lower gross profit and increased SG&A expenses.

Operating results for the nine-months ended October 29, 2022, compared to the operating results for the nine-months ended October 30, 2021

Sales. Sales for the nine-months ended October 29, 2022 decreased by 19.5% or \$12.5 million, to \$51.7 million from \$64.2 million in the prior year period. Sales in Canada of \$42.3 million, representing 81.9% of total revenues, decreased \$8.8 million or 17.3% over the prior year period. U.S. sales of \$9.4 million decreased by \$3.7 million or 28.3% over the prior year period. Sales from e-commerce decreased by \$16.2 million or 34.1% to \$31.3 million from \$47.5 million in the prior year period as we transition from last year's pandemic-fueled surge of online sales to serving consumers throughout our omni-channel capabilities. Sales from our wholesale channel increased by \$1.8 million or 33.5% to \$7.0 million from \$5.2 million in the prior year period. Brick-and-mortar sales increased by \$1.9 million or 16.8% to \$13.3 million from \$11.4 million in the prior year period. E-commerce, wholesale, and brick-and-mortar sales represented 60.7%, 13.5% and 25.8% of sales, respectively compared to 74.1%, 8.1% and 17.8% of sales, respectively in the prior year period.

Gross Profit. Gross profit decreased by 21.3% or \$5.8 million to \$21.6 million in the nine-month period ended October 29, 2022 in comparison to the prior period due primarily to a decline in sales and a lower gross margin, partially offset by lower delivery and distribution costs and lower retail lease expense compared to the prior year period. Gross profit as a percentage of sales decreased to 41.7% for the nine-month period ended October 29, 2022 from 42.6% in the prior year period.

Selling, General and Administration Expenses. SG&A increased by \$4.3 million or 14.9% to \$32.8 million in the nine-month period ended October 29, 2022 from the same period in the prior year. Excluding the impact of non-recurring software implementation and configuration costs, the impact of the wage and rent subsidies received under the Canadian government COVID-19 Economic Response Plan, and the impairment of property and equipment and right-of-use assets, Adjusted SG&A decreased by \$0.5 million to \$29.3 million in the nine-month period ended October 29, 2022. Adjusted SG&A as a percentage of sales increased to 56.7% from 46.4% in the prior year period.

Restructuring plan activities, net. Restructuring plan activities, net was \$nil for the nine-month period ended October 29, 2022 compared to a gain of \$76.9 million in the prior year period.

Results from Operating Activities. Results from operating activities during the nine-month period ended October 29, 2022 was negative \$11.2 million compared to \$75.8 million in the prior year period. Excluding the impact of the Restructuring Plan, the wage and rent subsidies received from the Canadian government under the COVID-19 Economic Response Plan, non-recurring software implementation costs, and the impairment of property and equipment and right-of-use assets, Adjusted operating loss amounted to \$7.8 million in the nine-month period ended October 29, 2022, compared to an Adjusted operating loss of \$2.4 million in the prior year period. The increase in Adjusted operating loss results from a decrease in sales of \$12.5 million, partially offset by a reduction in operating costs.

Finance Costs. Finance costs amounted to \$0.5 million in the nine-month period ended October 29, 2022, an increase of \$0.4 million from the prior year period. The interest expense relates to the accounting for lease liabilities.

Finance Income. Finance income of \$236 thousand is derived mainly from interest on cash on hand and has increased \$118 thousand from \$118 thousand in the prior year period.

Net income (loss). Net loss was \$11.5 million in the nine-month period ended October 29, 2022 compared to a Net income of \$76.8 million in the prior year period. Adjusted net loss, which excludes the Restructuring plan activities, net, the wage and rent subsidies received from the Canadian government under the COVID-19 Economic Response Plan, non-recurring software implementation costs, recovery of income taxes, and the impairment of property and equipment and right-of-use assets, amounted to \$8.0 million compared to a Net loss of \$2.4 million in the prior year period.

Fully diluted net (loss) earnings per common share. Fully diluted net loss per common share was \$0.44 in nine-month period ended October 29, 2022 compared to fully diluted net earnings of \$2.79 per common share in the same period in the prior year. Adjusted fully diluted loss per common share, which is Adjusted net loss on a fully diluted weighted average shares outstanding basis, was \$0.30, compared to a loss of \$0.09 in the prior year period.

EBITDA and Adjusted EBITDA. EBITDA, which excludes non-cash and other items in the current and prior periods, was negative \$8.6 million in the nine-month period October 29, 2022 compared to \$78.8 million in the prior year period representing a decrease of \$87.4 million over the prior year period. Adjusted EBITDA for the nine-months ended October 29, 2022, which excludes the impact of stock-based compensation expense, the impairment of property and equipment and right-of-use assets, the Restructuring Plan activities, net, the wage and rent subsidies received from the Canadian government under the COVID-19 Economic Response Plan, non-recurring software implementation costs, and the impairment of property and equipment and right-of-use assets, was negative \$4.0 million compared to \$1.6 million in the prior year period. The decrease in Adjusted EBITDA of \$5.6 million is explained by a decrease in Gross profit of \$5.8 million offset by a decrease in Adjusted SG&A expenses.

Summary of quarterly results

Due to seasonality and the timing of holidays, the results of operations for any quarter are not necessarily indicative of the results of operations for the fiscal year. The table below presents selected consolidated financial data for the eight most recently completed quarters.

	Fiscal Year 2022				Fiscal Year 2021			Fiscal Year 2020
	Third Quarter	Second Quarter	First Quarter	Fourth Quarter	Third Quarter	Second Quarter	First Quarter	Fourth Quarter
	\$	\$	\$	\$	\$	\$	\$	\$
Sales	16,176	15,207	20,287	39,878	22,203	18,743	23,249	40,189
Net (loss) income	(4,717)	(4,835)	(1,974)	1,291	(1,863)	75,477	3,221	(27,222)
EBITDA ¹	(3,759)	(3,851)	(976)	2,613	(778)	75,493	4,126	(25,918)
Adjusted EBITDA ¹	(2,004)	(2,128)	89	3,696	(308)	(641)	2,505	5,384
Net (loss) earnings per share:								
Basic	(0.18)	(0.18)	(0.07)	0.05	(0.07)	2.87	0.12	(1.04)
Fully diluted	(0.18)	(0.18)	(0.07)	0.05	(0.07)	2.75	0.12	(1.00)
Adjusted fully diluted ¹	(0.12)	(0.13)	(0.05)	0.13	(0.01)	(0.07)	0.05	0.15
Weighted average number of shares outstanding:								
Basic	26,566,441	26,487,933	26,426,055	26,393,118	26,359,969	26,299,094	26,296,690	26,228,206
Fully diluted	26,566,441	26,487,933	26,426,055	27,614,734	26,359,969	27,455,005	27,400,840	27,140,065
Cash	16,131	19,048	22,680	25,107	13,367	12,051	31,321	30,197
Accounts receivable	3,937	2,497	3,197	3,209	4,602	6,986	6,625	6,157
Prepaid expenses and depositions	6,137	5,172	4,479	4,142	4,835	5,580	11,578	14,470
Inventories	29,985	30,234	28,359	31,048	39,802	38,055	29,258	23,468
Trade and other payables	14,445	11,701	8,966	12,300	13,958	12,533	6,154	4,152

Liquidity and Capital Resources

As at October 29, 2022, the Company had \$16.1 million of cash held by major Canadian financial institutions.

Working capital was \$33.7 million as at October 29, 2022 compared to \$43.4 million as at January 29, 2022. The decrease in working capital of \$9.7 million is explained by a decrease in current assets of \$7.3 million and an increase in current liabilities of \$2.4 million.

Working capital requirements are for the purchase of inventory, payment of payroll and other operating costs, including software purchases and implementation costs. Working capital requirements fluctuate during the year, rising in the second and third fiscal quarters as the Company take title to increasing quantities of inventory in anticipation of our peak selling season in the fourth fiscal quarter. The Company funds its operating, capital and working capital requirements from a combination of cash on hand and cash provided by operating activities.

On August 23, 2022, a revolving line of credit on demand with the Bank of Nova Scotia was established for up to \$15.0 million, less a reserve of \$0.5 million for credit cards based on eligible accounts receivable and inventory balances and subject to financial covenants required to be calculated and met starting January 28, 2023. The credit facility will bear interest at the prime rate plus 1%, renewable annually at the lender's option. In addition, Investissement Québec has provided a loan loss guarantee under its "Loan Loss Program", securing 50% of any loss incurred by the Bank of Nova Scotia with respect to the recovery of indebtedness under the line of credit.

As at October 29, 2022, the Company has financial commitments in connection with the purchase of goods and services that are enforceable and legally binding on the Company, amounting to \$8.3 million, net of \$659 thousand of advances, which are expected to be discharged within 12 months.

Cash Flows

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

	<u>For the three-months ended</u>		<u>For the nine-months ended</u>	
	<u>October 29,</u> <u>2022</u>	<u>October 30,</u> <u>2021</u>	<u>October 29,</u> <u>2022</u>	<u>October 30,</u> <u>2021</u>
	<u>\$</u>	<u>\$</u>	<u>\$</u>	<u>\$</u>
Cash flows used in:				
Operating activities	(2,164)	1,553	(6,577)	(16,219)
Financing activities	(753)	(237)	(2,271)	(559)
Investing activities	—	—	(128)	(52)
Decrease in cash	(2,917)	1,316	(8,976)	(16,830)

Three-months ended October 29, 2022 compared to three-months ended October 30, 2021

Cash flows used in operating activities. Net cash used in operating activities amounted to \$2.2 million for the quarter ended October 29, 2022, representing a change of \$3.7 million from the net cash used in operations of \$1.5 million in the prior year quarter. The decrease is primarily due to the loss reported this quarter.

Cash flows used in financing activities. Net cash flows used in financing activities of \$753 thousand during the quarter ended October 29, 2022 represents an increase of \$516 thousand compared to the prior year quarter due to an increase in lease repayments.

Nine-months ended October 29, 2022 compared to nine-months ended October 30, 2021

Cash flows used in operating activities. Net cash used in operating activities amounted to \$6.6 million for the nine-month period ended October 29, 2022, representing a change of \$9.6 million from the net cash used in operations of \$16.2 million in the prior year period. The decrease is primarily due to decrease in inventory over the prior period, offset by an increase in the net loss.

Cash flows used in financing activities. Net cash flows used in financing activities of \$2.3 million during the nine-month period ended October 29, 2022 represents an increase of \$1.7 million compared to the prior year period due to an increase in lease repayments.

Off-Balance Sheet Arrangements

Other than certain operating lease obligations and purchase commitments disclosed elsewhere, we have no other off-balance sheet obligations.

Contractual Obligations and Commitments

In the normal course of business, we enter into contractual arrangements that will require us to disburse cash over future periods. All commitments have been recorded in our consolidated balance sheets, except for the purchase of goods and services that are expected to be received in future periods. As of October 29, 2022, the Company had financial commitments in connection with the purchase of goods and services that are enforceable and legally binding on the Company, exclusive of additional amounts based on sales, taxes and other costs amounting to \$8.3 million, net of \$659 thousand of advances (January 29, 2022 - \$11.3 million, net of \$542 thousand of advances). These contractual obligations and commitments are expected to be discharged within 12 months.

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 5 to our consolidated financial statements for the year ended January 29, 2022 included in our Annual Report on Form 10-K dated April 29, 2022. There have been no material changes to the critical accounting policies and estimates since January 29, 2022.

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 April 29, 2022.

We are exposed to foreign currency exchange risk on purchases of our teas and tea accessories.

A significant portion of our tea and tea accessory purchases are in U.S. dollars as is our revenue from U.S. e-commerce customers. As a result, our statement of loss and cash flows could be adversely impacted by changes in exchange rates, primarily between the U.S. dollar and the Canadian dollar.

Item 4. Controls and Procedures

Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive and Brand Officer and our President, Chief Financial and Operating Officer, evaluated the effectiveness of our disclosure controls and procedures as of October 29, 2022. 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 the assessment of our disclosure controls and procedures, our management concluded that our disclosure controls and procedures were effective as of October 29, 2022.

Changes in Internal Control over Financial Reporting

There were no significant changes in our internal control over financial reporting during the quarter ended October 29, 2022 that materially affected, or were reasonably likely to materially affect, our internal control over financial reporting.

Part II. OTHER INFORMATION

Item 1. Legal Proceedings

From time to time, we may become involved in various lawsuits and legal proceedings which arise in the ordinary course of business. Although the outcome of these and other claims cannot be predicted with certainty, management does not believe that the ultimate resolution of any matters in which we are currently involved will have a material adverse effect on our business, financial condition, or operating results. However, litigation is subject to inherent uncertainties, and an adverse result in these or other matters may arise from time to time that may harm our business.

The Company is subject to a claim amounting to \$350,000 from a third-party service provider for which services were rendered prior to July 8, 2020, when the Company announced it was implementing the Restructuring Plan under the Companies' Creditors Arrangement Act. At this stage, it is too early to determine whether the claim has a legal merit and the final amount of settlement, if any.

Item 1A. Risk Factors

Except as set forth below, there have been no material changes to the risk factors previously disclosed in our Form 10-K for the fiscal year ended January 29, 2022.

On October 28, 2022, the Company, received a letter from The Nasdaq Stock Market LLC ("Nasdaq"), notifying the Company that for the past 30 consecutive business days, the closing bid price per share of its common stock was below the \$1.00 minimum bid price requirement for continued listing on The Nasdaq Capital Market, as required by Nasdaq Listing Rule 5550(a)(2) (the "Bid Price Rule"). As a result, the Company was notified by Nasdaq that it is not in compliance with the Bid Price Rule. Nasdaq has provided the Company with 180 calendar days, or until April 26, 2023, to regain compliance with the Bid Price Rule. This notification has no immediate effect on the Company's listing on the Nasdaq Capital Market or on the trading of the Company's common stock.

There can be no assurance that we will be able to regain compliance with Nasdaq's continued listing requirements. The failure to regain compliance prior to April 26, 2023 may result in the Company's common stock being delisted from Nasdaq and it could be more difficult to buy or sell our securities and to obtain accurate quotations, and the price of our common stock could suffer a material decline. In addition, a delisting would impair our ability to raise capital through the public markets, could deter broker-dealers from making a market in or otherwise seeking or generating interest in our securities and might deter certain institutions and persons from investing in our securities at all.

Item 2. Unregistered Sales of Equity Securities

Not applicable.

Item 3. Defaults Upon Senior Securities

Not applicable.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None.