

The Second Cup Ltd.

Management's Discussion and Analysis

CAUTION REGARDING FORWARD-LOOKING STATEMENTS

Certain statements in this Management's Discussion and Analysis ("MD&A") may constitute forward-looking statements within the meaning of applicable securities legislation. The terms the "Company", "Second Cup", "we", "us", or "our" refer to The Second Cup Ltd. Forward-looking statements include words such as "may", "will", "should", "expect", "anticipate", "believe", "plan", "intend" and other similar words. These statements reflect current expectations regarding future events and financial performance and speak only as of the date of this MD&A. The MD&A should not be read as a guarantee of future performance or results and will not necessarily be an accurate indication of whether or not those results will be achieved. Forward-looking statements are based on a number of assumptions and are subject to known and unknown risks, uncertainties and other factors, many of which are beyond Second Cup's control that may cause Second Cup's actual results, performance or achievements, or those of Second Cup cafés, or industry results to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. The following are some of the factors that could cause actual results to differ materially from those expressed in the underlying forward-looking statements: competition; availability of premium quality coffee beans; the ability to attract qualified franchise partners; the location of Second Cup cafés; the closure of Second Cup cafés; loss of key personnel; compliance with government regulations; food safety; potential litigation; the ability to exploit and protect the Second Cup trademarks; changing consumer preferences and discretionary spending patterns including, but not restricted to, the impact of weather and economic conditions on such patterns; reporting of system sales by franchise partners; and the financial performance and financial condition of Second Cup. The foregoing list of factors is not exhaustive, and investors should refer to the risks described under "Risks and Uncertainties" below and in Second Cup's Annual Information Form, which is available at www.sedar.com.

Although the forward-looking statements contained in this MD&A are based on what management believes are reasonable assumptions, there can be no assurance that actual results will be consistent with these forward-looking statements and, as a result, the forward-looking statements may prove to be incorrect.

As these forward-looking statements are made as of the date of this MD&A, Second Cup does not undertake to update any such forward-looking statements whether as a result of new information, future events or otherwise. Additional information about these assumptions and risks and uncertainties is contained in the Company's filings with securities regulators. These filings are also available on the Company's website at www.secondcup.com.

INTRODUCTION

The following MD&A has been prepared as of July 31, 2015 and is intended to assist in understanding the financial performance and financial condition of The Second Cup Ltd. ("Second Cup" or the "Company") for the 13 weeks (the "Quarter") and 26 weeks ended June 27, 2015, and should be read in conjunction with the Unaudited Condensed Interim Financial Statements of the Company for the 13 and 26 weeks ended June 27, 2015 and June 28, 2014, the Audited Financial Statements of the Company for the 52 weeks ended December 27, 2014, and the Annual Information Form, which are available at www.sedar.com. Past performance may not be indicative of future performance. All amounts are presented in thousands of Canadian dollars, except number of cafés, per share amounts or unless otherwise indicated and have been prepared in accordance with International Financial Reporting Standards ("IFRS"). The Company also reports certain non-IFRS measures such as System sales of cafés, Same café sales, Operating income, EBITDA, Adjusted EBITDA, and Adjusted earnings per share that are discussed in the "Definitions and discussion of certain non-GAAP financial measures" in this MD&A.

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CORE BUSINESS, STRATEGY, AND PERFORMANCE DRIVERS

Core business

Second Cup is a Canadian specialty coffee retailer with 337 cafés operating under the trade name Second Cup™ in Canada, of which 47 are Company-operated and the balance are operated by franchisees who are selected and trained to retail Second Cup's product offering. Further discussion of the Company's core business was described in the 2014 annual MD&A.

Strategic imperatives and key performance drivers

Second Cup's new vision of being the coffee brand most passionately committed to quality and innovation will drive management's strategies and actions going forward. Coffee will be at the core of the offering and the brand will win customers' hearts through more "personalized experiences".

In Q2, innovation was the focus in both our product offering and our café design. We reached a key milestone in our transformation with the roll-out of our successful café of the future design to three new locations. The pilot location at King & John streets in Toronto continues to exceed expectations with sales up 40% over Q2 last year and for the 26 weeks ended June 27th.

The loyalty program, Second Cup Coffee Co.™ Rewards, which was launched nationally in April, has surpassed the Company's aggressive internal registration targets and is moving forward with personalized experiences and offers to surprise and delight customers.

This quarter, the Company has also proven its coffee expertise with two innovative summertime launches: its espresso-based Frappé and the Iced Red Eye, both unique offerings within the marketplace.

CAPABILITIES

This section documents factors that affect the Company's capabilities to execute strategies, manage key performance drivers and deliver results. This section is qualified by the section "Caution Regarding Forward-Looking Statements" at the beginning of this MD&A.

The Company's capabilities specific to the Second Cup brand, café of the future, our people, product, locations, competition, and technology were discussed in the 2014 annual MD&A.

Liquidity, capital resources and management of capital

The Company's objectives relating to the management of its capital structure are discussed in the 2014 MD&A. During the period ended June 27, 2015, the Company was in compliance with all financial and other covenants of the Company's term loan and operating credit facility.

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FINANCIAL HIGHLIGHTS

The following table sets out selected IFRS and certain non-GAAP financial measures of the Company and should be read in conjunction with the Unaudited Condensed Interim Financial Statements of the Company for the 13 and 26 weeks ended June 27, 2015 and June 28, 2014.

(in thousands of Canadian dollars, except same café sales, number of cafés, per share amounts, and number of common shares.)	13 weeks ended		26 weeks ended	
	June 27, 2015	June 28, 2014	June 27, 2015	June 28, 2014
System sales of cafés ¹	\$43,715	\$45,829	\$86,890	\$89,759
Same café sales ¹	(3.2%)	(5.0%)	(2.2%)	(5.9%)
Number of cafés - end of period	337	357	337	357
Total revenue	\$9,420	\$6,435	\$18,434	\$13,059
Operating costs and expenses	\$9,427	\$6,824	\$18,372	\$13,221
Operating income (loss) ¹	(\$7)	(\$389)	\$62	(\$162)
EBITDA ¹	\$334	(\$113)	\$753	\$380
Net loss and comprehensive loss	(\$72)	(\$390)	(\$148)	(\$334)
Basic and diluted loss per share as reported	(\$0.01)	(\$0.04)	(\$0.01)	(\$0.03)
Total assets - end of period	\$50,457	\$74,434	\$50,457	\$74,434
Number of common shares issued and outstanding - end of period	12,830,945	9,903,045	12,830,945	9,903,045

¹See the section "Definitions and discussion on certain non-GAAP financial measures" for further analysis.

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OPERATIONAL REVIEW

Seasonality of System sales of cafés

The following table shows the percentage of annual System sales of cafés achieved, on average, in each fiscal reporting quarter over the last three years:

% of annual System sales of cafés	2012	2013	2014	Average
First quarter	24.2	24.5	24.0	24.2
Second quarter	24.4	24.9	25.1	24.8
Third quarter	23.9	23.5	23.9	23.8
Fourth quarter	27.5	27.1	27.0	27.2
	100.0	100.0	100.0	100.0

Historically, System sales of cafés have been higher in the fourth quarter, which includes the holiday sales periods of November and December. Because of this seasonality, the results for any quarter are not necessarily indicative of what may be achieved for any other quarter or year.

Café network

	13 weeks ended		26 weeks ended	
	June 27, 2015	June 28, 2014	June 27, 2015	June 28, 2014
Number of cafés - beginning of period	344	357	347	356
Cafés opened	-	2	2	7
Cafés closed	(7)	(2)	(12)	(6)
Number of cafés - end of period	337	357	337	357

The Company ended the quarter with forty-seven (2014 - fourteen) Company-operated cafés.

Second Quarter

System sales of cafés

System sales of cafés for the 13 weeks ended June 27, 2015 were \$43,715, compared to \$45,829 for the 13 weeks ended June 28, 2014, representing a decrease of \$2,114 or 4.6%. The decrease is attributable to decreased same café sales and to the smaller store network.

Same café sales

During the quarter, same café sales declined by 3.2%, compared to a decline of 5.0% in the comparable quarter of 2014.

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Analysis of revenue

Total revenue for the Quarter was \$9,420 (2014 - \$6,435), consisting of Company-owned café and product sales, royalty revenue, and franchise fees and other revenue.

Company-owned cafés and product sales for the Quarter were \$5,634 (2014 - \$1,745). The increase in revenue of \$3,889 is attributable to additional company owned cafés, as well as growth of the product sales segment of the business.

Franchise revenue was \$3,786 for the Quarter (2014 - \$4,690). The decrease in franchise revenue of \$904 is primarily driven by the new royalty incentive introduced in August 2014, lower café sales, and the increase in corporately owned cafés.

Operating costs and expenses

Operating costs and expenses include the costs of Company-owned cafés and product sales, franchise related expenses, general and administrative expenses, the loss/gain on disposal of assets, and depreciation and amortization. Total operating costs and expenses for the Quarter were \$9,427 (2014 - \$6,824), an increase of \$2,603.

Company-owned cafés and product sales

Company-owned cafés and product related expenses for the Quarter were \$5,622 (2014 - \$1,927), an increase of \$3,693. This increase in costs is caused by additional Company-owned cafés.

Franchise

The Company incurred franchise related expenses of \$1,968 (2014 - \$1,413). The increase of \$555 is driven mainly by the costs of launching the Second Cup Coffee Co.™ Rewards loyalty program.

General and administrative

General and administrative expenses were \$1,584 for the Quarter (2014 - \$3,187). Prior year general and administrative costs included restructuring expenses of \$1,607.

Gain and loss on disposal

A gain on disposal of \$88 was recognized in the Quarter (2014 - \$21 loss). The gain related to the resale of Company-owned cafés.

Depreciation and amortization

Depreciation and amortization expense was \$341 (2014 - \$276).

EBITDA

EBITDA for the Quarter was \$334, compared to a loss of \$113 last year.

Net income

The Company's net loss for the Quarter was \$72 or \$0.01 per share, compared to net loss of \$390 or \$0.04 per share in 2014. The improvement in net income of \$319 or \$0.03 per share was mainly the result of savings due to the FY14 restructuring, partially offset by increased expenses related to additional Company-owned cafés. A reconciliation of net income to EBITDA is provided in the section "Definitions and discussion on certain non-GAAP financial measures".

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Year to date

System sales of cafés

System sales of cafés for the 26 weeks ended June 27, 2015 were \$86,890 compared to \$89,759 for the 26 weeks ended June 28, 2014, representing decrease of \$2,869 or 3.2%. The decrease is attributable to decreased same café sales and to the smaller store network.

Same café sales

During the quarter, same café sales declined by 2.2% for the 26 weeks ended June 27, 2015, compared to a decline of 5.9% for the 26 weeks ended June 28, 2014.

Analysis of revenue

Total revenue for the year to date was \$18,434 (2014 - \$13,059).

Company-owned cafés and product sales were \$10,873 (2014 - \$3,814). The increase of \$7,059 is mainly attributable to additional Company-owned cafés.

Franchise revenue was \$7,561 for the year to date (2014 - \$9,245). The decrease in revenue of \$1,684 is primarily a result of the new royalty incentive introduced in August 2014, lower café sales, and the increase in corporately owned cafés.

Operating costs and expenses

Operating expenses include the costs outlined above in the quarterly comments. Total operating expenses for the year to date were \$18,372 (2014 - \$13,221), an increase of \$5,151.

Company-owned cafés and product sales

Company-owned cafés and product related expenses for the year to date were \$10,845 (2014 - \$4,404), an increase of \$6,441. This increase in costs is caused by additional Company-owned cafés.

Franchise

Franchise related expenses of \$3,905 were incurred year to date (2014 - \$3,152). The increase of \$753 is driven by the costs of launching the Second Cup Coffee Co.™ Rewards loyalty program, as well as the cost of a franchise convention.

General and administrative

General and administrative expenses were \$3,019 for the year to date (2014 - \$5,211). Prior year general and administrative costs included restructuring expenses of \$1,607.

Gain and loss on disposal

A gain on disposal of \$88 was recognized for the year to date (2014 - \$88 gain). The gain related to the resale of company owned cafés.

Depreciation and amortization

Depreciation and amortization expense was \$691 (2014 - \$542).

EBITDA

EBITDA for the year to date was \$753, compared to \$380 last year.

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Net income

The Company's net loss for the year to date is \$148 or \$0.01 per share, compared to net loss of \$334 or \$0.03 per share in 2014. The increase in net income of \$185 or \$0.02 per share was mainly due to Coffee Central expense savings due to the FY14 restructuring, offset partially by an increase in costs relating to corporate café operations.

SELECTED QUARTERLY INFORMATION

(in thousands of Canadian dollars, except Number of cafés, Same café sales, and per share amounts)	Q2 2015	Q1 2015	Q4 2014 ²	Q3 2014
System sales of cafés ¹	\$43,715	\$43,174	\$49,427	\$43,596
Same café sales ¹	(3.2%)	(1.1%)	(3.9%)	(3.3%)
Number of cafés - end of period	337	344	347	349
Total revenue	\$9,420	\$9,014	\$8,427	\$6,686
Operating income (loss) ¹	(\$6)	\$68	(\$521)	(\$30,214)
EBITDA ¹	\$334	\$419	(\$139)	(\$29,866)
Net loss for the period	(\$72)	(\$76)	(\$469)	(\$26,230)
Basic and diluted loss per share	(\$0.01)	(\$0.01)	(\$0.04)	(\$2.65)
Dividends declared per share	-	-	-	-
	Q2 2014	Q1 2014	Q4 2013 ²	Q3 2013
System sales of cafés ¹	\$45,829	\$43,930	\$51,898	\$44,894
Same café sales ¹	(5.0%)	(6.9%)	(4.3%)	(3.7%)
Number of cafés - end of period	357	357	356	351
Total revenue	\$6,435	\$6,623	\$8,038	\$6,268
Operating (loss) income ¹	(\$389)	\$226	\$1,891	\$1,361
EBITDA ¹	(\$113)	\$493	\$2,239	\$1,671
Net (loss) income for the period	(\$390)	\$56	\$1,177	\$918
Basic and diluted (loss) earnings per share	(\$0.04)	\$0.01	\$0.12	\$0.09
Dividends declared per share	-	\$0.085	\$0.085	\$0.085

¹See the section "Definitions and discussion on certain non-GAAP financial measures" for further analysis.

²The Company's fourth quarter System sales of cafés are higher than other quarters due to the seasonality of the business (see "Seasonality of System sales of cafés" above).

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LIQUIDITY AND CAPITAL RESOURCES

Second Cup collects royalties based on the franchisees' portion of System sales of cafés, franchise fees, and other amounts from its franchisees and also generates revenues from its Company-operated cafés. The performance of Second Cup franchisees and Company-operated cafés could impact the ability of the Company to declare and pay dividends to its shareholders. For a more detailed discussion of the risks and uncertainties affecting the Company's liquidity, see the "Risks and uncertainties" section below.

	13 weeks ended		26 weeks ended	
	June 27, 2015	June 28, 2014	June 27, 2015	June 28, 2014
Cash flows provided by operating activities	\$884	\$83	\$118	\$510
Cash flows used in investing activities	(306)	(277)	(782)	(948)
Cash flows used in financing activities	-	(842)	-	(1,684)
Increase (decrease) in cash and cash equivalents during the period	\$578	(\$1,036)	(\$664)	(\$2,122)

Summary of cash flows

Second Quarter

Cash provided by operating activities was \$884 for the Quarter compared to \$83 for the same Quarter in 2014. The difference is primarily attributable to the collection of income taxes receivable, as well as an improvement in net income.

During the Quarter, cash used in investing activities was \$306 compared to cash used of \$277 for the same Quarter in 2014.

We did not have any financing activities for the 13 weeks ended June 27, 2015 (2014 - \$842).

Year to date

Cash provided by operating activities was \$118 for the year to date compared to cash provided of \$510 for the same year to date period in 2014. The difference is attributable to lower royalties, offset by collection of income taxes receivable, as well as an improvement in net income.

Year to date cash used in investing activities was \$782 compared to cash used of \$948 for the same period in 2014. The cash usage was a result of purchases relating to the loyalty program software and hardware, as well as the take-back of additional corporate cafés.

We did not have any financing activities for the 26 weeks ended June 27, 2015 (2014 - \$1,684).

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Working capital as at

	June 27, 2015	December 27, 2014
Current assets	\$ 13,262	\$ 16,430
Current liabilities	<u>10,061</u>	<u>23,684</u>
Working capital (deficiency)	<u>\$ 3,201</u>	<u>\$ (7,254)</u>

The Company has working capital of \$3,201 as of June 27, 2015. The working capital surplus is due to an improvement in trade and other receivables and accounts payables and accrued liabilities. The Company's negative working capital of \$7,254 as of December 27, 2014, was a result of the reclassification of long-term debt to current. Subsequently the debt was classified back to long-term in Q1, 2015.

The Company had cash and cash equivalents of \$9,508 at June 27, 2015 (December 27, 2014 - \$10,918). The Company continues to believe it has sufficient financial resources to pay its operating expenses.

Financial instruments

The following summarizes the nature of certain risks applicable to the Company's financial instruments:

Financial instrument	Risks
<i>Financial assets</i>	
Cash and cash equivalents	Credit and interest rate
Trade and other receivables	Credit
Notes and leases receivable	Credit
<i>Financial liabilities</i>	
Interest rate swap	Credit, liquidity and interest rate
Accounts payable and accrued liabilities	Liquidity, currency, and commodity
Gift card liability	Liquidity
Deposits from franchise partners	Liquidity
Term credit facility	Liquidity and interest rate

(i) Credit risk

Cash and cash equivalents, and interest rate swap

Credit risk associated with cash and cash equivalents, and the interest rate swap is managed by ensuring these assets are placed with institutions of high creditworthiness.

Trade and other receivables, and notes and leases receivable

Trade and other receivables, and notes and leases receivable primarily comprise amounts due from franchisees. Credit risk associated with these receivables is mitigated as a result of the review and evaluation of franchisee account balances beyond a particular age. Prior to accepting a franchisee, the Company undertakes a detailed screening process, which includes the requirement that a franchisee have sufficient capital and financing. The risk is further mitigated due to a broad franchisee base that is spread across the country, which limits the concentration of credit risk.

Other receivables may include amounts owing from large organizations where often those organizations have a simultaneous vendor relationship with the Company's franchisees. Credit risk is mitigated as a result of the Company directing and maintaining certain controls over the vendor relationship with the franchisees.

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(ii) Liquidity risk

Liquidity risk is managed through regular monitoring of forecasts and actual cash flows, monitoring maturity dates of financial assets and liabilities, and also the management of capital structure and debt leverage ratios as outlined above. The main source of income is royalty receipts from franchisees.

(iii) Interest rate risk

Financial instruments exposed to interest rate risk earn and bear interest at floating rates. The Company entered into an interest rate swap agreement to minimize risk on its long-term debt.

(iv) Currency and commodity risk

Transactions occur with a small number of vendors that operate in foreign currencies. The Company believes that due to low volumes of transactions, low number of vendors, and low magnitude of spend, the impact of currency risk is not material.

The Company is directly and indirectly exposed to changes in coffee commodity prices given it is a material input for the Company's product offerings. The direct exposure is mitigated given the ability to adjust its sales price as commodity prices change. Risk is mitigated by entering fixed price forward purchase commitments and by adjusting selling prices.

Contingencies, commitments and guarantees

Second Cup has lease commitments for Company-operated cafés and also acts as the head tenant on most leases, which it in turn subleases to franchisees. To the extent the Company may be required to make rent payments due to headlease commitments, a provision has been recognized.

	Headlease commitments	Sublease to franchisees	Net
June 25, 2016	\$ 19,515	\$ 15,799	\$ 3,716
June 24, 2017	17,391	14,135	3,256
June 30, 2018	15,473	12,507	2,966
June 29, 2019	13,786	10,974	2,812
June 27, 2020	11,432	8,846	2,586
Thereafter	28,361	20,808	7,553
	<u>\$ 105,958</u>	<u>\$ 83,069</u>	<u>\$ 22,889</u>

The Company believes it will have sufficient resources to meet the net commitment of \$22,889.

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

Contracts are in place with third party companies to purchase the coffee that is sold in all cafés. In terms of these supply agreements, there is a guaranteed minimum volume of coffee purchases of \$3,307 USD for the subsequent 12 months. The coffee purchase commitment comprises three components: unapplied futures commitment contracts, fixed price physical contracts and flat price physical contracts.

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The Company has entered into a distribution agreement with a vendor to wholesale its product through grocery and other retail outlets across Canada. As a result of the distribution agreement, there is a requirement to pay a portion of one-time listing fees in the amount of up to \$206 in 2015.

Due to the Company acting as the primary coordinator of café construction costs on behalf its franchisees and for Company-operated cafés, there is \$770 of contractual commitments pertaining to construction costs for new locations and renovations as at the end of the quarter. Construction costs financed for franchise projects are from deposits received from franchisees and for corporate projects from the Company's cash flows.

Related parties

Related parties are identified as key management, members of the Board of Directors, and shareholders that effectively exercise significant influence on the Company. Such related parties include any entities acting with or on behalf of the aforementioned parties.

Certain transactions occurred between a company controlled by a board member, and one of the Company's vendors. For the 13 and 26 weeks ended June 27, 2015, the said vendor purchased \$416 and \$1,010, respectively, of product in the ordinary course of business.

EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES

The Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO") must acknowledge they are responsible for establishing and maintaining disclosure controls and procedures and internal control over financial reporting ("ICFR") for the Company. The control framework used by the CEO and CFO to design the Company's ICFR is Internal Control Over Financial Reporting - Guidance for Smaller Public Companies as issued by COSO. In addition, in respect of:

Disclosure controls and procedures

The CEO and CFO must certify they have designed the disclosure controls and procedures, or caused them to be designed under their supervision, to provide reasonable assurance that material information relating to the Company is made known to them in a timely manner and that information required under securities legislation is recorded, processed, summarized and reported in a timely manner.

As at July 31, 2015, the Company's management, under the supervision of, and with the participation of, the CEO and CFO, evaluated the design of the disclosure controls and procedures. Based on this evaluation, the CEO and CFO have concluded that, as at June 27, 2015, the Company's disclosure controls and procedures were appropriately designed.

Consistent with the concept of reasonable assurance, the Company recognizes that the relative cost of maintaining these controls and procedures should not exceed their expected benefits. As such, the Company's disclosure controls and procedures can only provide reasonable, and not absolute, assurance that the objectives of such controls and procedures are met.

During the 13 weeks ended June 27, 2015 and up to the date of the approval of the Unaudited Condensed Interim Financial Statements and MD&A, there has been no change that has materially affected, or is reasonably likely to materially affect, the Company's disclosure controls and procedures.

Internal controls over financial reporting

The CEO and CFO must certify they have designed such internal controls over financial reporting, or caused them to be designed under their supervision, to provide reasonable assurance regarding the reliability of

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financial reporting and the preparation of the Unaudited Condensed Interim Financial Statements for external purposes in accordance with IFRS.

As at July 31, 2015, the Company's management, under the supervision of, and with the participation of, the CEO and CFO, evaluated the design of the controls over financial reporting. No material weaknesses in the design of these controls over financial reporting were identified. Based on this evaluation, the CEO and CFO have concluded that, as at June 27, 2015 the Company's controls over financial reporting were appropriately designed and were operating effectively.

Consistent with the concept of reasonable assurance, the Company recognizes that the relative cost of maintaining these controls should not exceed their expected benefits. As such, the Company's internal controls over financial reporting can only provide reasonable, and not absolute, assurance that the objectives of such controls are met.

During the 13 weeks ended June 27, 2015 and up to the date of the approval of the Unaudited Condensed Interim Financial Statements and MD&A, there has been no change in the Company's internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

CRITICAL ACCOUNTING ESTIMATES

The preparation of the Unaudited Condensed Interim Financial Statements requires management to make estimates, and assumptions, and use judgement in applying its accounting policies and estimates and assumptions about the future. Estimates and other judgements are continuously evaluated and are based on management's experience and other factors, including expectations about future events that are believed to be reasonable under the circumstances. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected. The accounting estimates will, by definition, seldom equal the related actual results.

Estimates

The following are examples of estimates and assumptions the Company makes:

- the allowance for doubtful accounts;
- the allowance for inventory obsolescence;
- the estimated useful lives of assets;
- the recoverability of tangible and intangible assets subject to depreciation, amortization, or with indefinite lives;
- the derivation of income tax assets and liabilities;
- café lease provisions; and
- gift card breakage.

Use of judgement

The following discusses the most significant accounting judgements and estimates that the Company has made in the preparation of the Unaudited Condensed Interim Financial Statements:

(i) Deferred income taxes

The timing of reversal of temporary differences and the expected income allocation to various tax jurisdictions within Canada affect the effective income tax rate used to compute the deferred income taxes. Management estimates the reversals and income allocation based on historical and budgeted operating results and income tax laws existing at the Statements of Financial Position dates. In addition, management occasionally estimates the current or future deductibility of certain expenditures, affecting current or deferred income tax balances and expenses.

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(ii) Estimated useful lives

Management estimates the useful lives of property and equipment based on the period during which the assets are expected to be available-for-use. The amounts and timing of recorded expenses for depreciation of property and equipment for any period are affected by these estimated useful lives. It is possible that changes in these factors may cause significant changes in the estimated useful lives of the Company's property and equipment in the future.

(iii) Café lease provisions

Café lease provisions require judgement to evaluate the likelihood and measurement of settlements, temporary payouts, or sub-leasing. Management works with landlords and franchisees to obtain adequate information needed to make applicable judgements.

RISKS AND UNCERTAINTIES

This section is qualified by the section "Caution Regarding Forward-Looking Statements" at the beginning of this MD&A.

The performance of Second Cup is primarily dependent on its ability to maintain and increase the sales of existing cafés, add new profitable cafés to the network and redevelop and modernize cafés as their leases come due. System sales of the café network are affected by various external factors that can affect the specialty coffee industry as a whole.

A more detailed discussion of the risks and uncertainties affecting Second Cup is set out in the Company's MD&A for the year ended December 27, 2014 and Second Cup's Annual Information Form, which is available at www.sedar.com.

OUTLOOK

This section is qualified by the section "Caution Regarding Forward-Looking Statements" at the beginning of this MD&A.

The Company is in the early stages of executing its three year strategic plan to restore long-term growth and value creation for its shareholders. This plan is both bold and achievable. The necessary steps and decisions relating to the take back of sub-standard cafes corporately will have an impact on short-term profitability. The Company expects significantly improved income as it returns to an asset light business model in the long-term.

DEFINITIONS AND DISCUSSION ON CERTAIN NON-GAAP FINANCIAL MEASURES

In this MD&A, the Company reports certain non-IFRS measures such as System sales of cafés, same café sales, operating income (loss), EBITDA.

System sales of cafés

System sales of cafés comprise the net revenue reported to Second Cup by franchisees of Second Cup cafés and by Company-operated cafés. This measure is useful in assessing the operating performance of the entire Company network, such as capturing the net change of the overall café network.

Changes in System sales of cafés result from the number of cafés and same café sales (as described below). The primary factors influencing the number of cafés within the network include the availability of quality locations and the availability of qualified franchisees.

The Second Cup Ltd.

Management's Discussion and Analysis

Same café sales

Same café sales represents the percentage change, on average, in sales at cafés operating system-wide that have been open for more than 12 months, including cafés closed temporarily for renovations/remodelling. The inclusion of cafés temporarily closed is a change in methodology. Since the impact of this revision is inconsequential, the Company will not restate same café sales results for previously reported years. It is one of the key metrics the Company uses to assess its performance as an indicator of appeal to customers. Same café sales provide a useful comparison between periods while also encompassing other matters such as seasonality. The two principal factors that affect same café sales are changes in customer traffic and changes in average transaction size.

Operating income (loss)

Operating income (loss) represents revenue, less cost of goods sold, less operating expenses, and less impairment charges. This measure is not defined under IFRS, although the measure is derived from input figures in accordance with IFRS. Management views this as an indicator of financial performance that excludes costs pertaining to interest and financing, and income taxes.

EBITDA

EBITDA represents earnings before interest, taxes, depreciation, and amortization. As there is no generally accepted method of calculating EBITDA, this measure is not necessarily comparable to similarly titled measures reported by other issuers. EBITDA is presented as management believes it is a useful indicator of the Company's ability to meet debt service and capital expenditure requirements, and evaluate liquidity. Management interprets trends in EBITDA as indicators of relative financial performance. EBITDA should not be considered by an investor as an alternative to net income or cash flows as determined in accordance with IFRS.

A reconciliation of net income to EBITDA is provided below:

	13 weeks ended		26 weeks ended	
	June 27, 2015	June 28, 2014	June 27, 2015	June 28, 2014
Net income (loss)	\$ (72)	\$ (390)	\$ (148)	\$ (334)
Interest and financing	71	99	248	256
Recovery for income taxes	(6)	(98)	(38)	(84)
Depreciation of property and equipment	267	197	540	392
Amortization of intangible assets	74	79	151	150
EBITDA	\$ 334	\$ (113)	\$ 753	\$ 380