

Second Cup Announces First Quarter Results and accelerated momentum for the company's transformation

MISSISSAUGA, ON, May 7, 2015 /CNW/ - The Second Cup Ltd. (TSX: SCU) reported financial results today for the first quarter ended March 28, 2015.

Highlights:

- Reduced the rate of decline in same store sales from -6.9% in the first quarter of last year to -1.1% this year.
- Grew EBITDA to \$419,000 from \$382,000 last year.
- Net loss of \$76,000 or \$0.01 per share, compared with a net profit of \$56,000 last year or \$0.01 per share.
- Pilot “café of the future” sales increased more than 40% compared to a year ago. Roll-out set to begin across Canada.
- Introduced upgraded baked goods program in Ontario and Quebec to positive response from customers.
- Second Cup Coffee Co. Rewards loyalty program launched on April 27th with very strong early adoption and is currently the number 3 ranking app in the App Store for Food & Drink in Canada.

“The Second Cup Coffee Co. revolution is in full swing and we are clearly headed in the right direction” says Ms. Alix Box, President and CEO, The Second Cup Ltd. “Same store sales are improving and our store of the future is performing very well. We have accelerated our program of taking back underperforming franchised cafes and are replacing underachieving operators to propel our turn-around. In the short term this negatively impacts our net income but will be an important value creation opportunity in the future. As detailed in our strategic plan, our goal is to be asset light. We have already refranchised 4 of the cafés and will continue to attract a new generation of operators who are committed to our new vision.”

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First Quarter 2015

For the first time in many years, the company has seen some positive same store sales weeks, which aim to become the norm. The pilot store of the future is performing very well with roll out set to begin in new and renovated stores across the country. In keeping with its strategy, the company is assuming ownership of more stores in order to modernize them and re-franchise to strong operators. In the short term, this will negatively impact results but will ultimately enhance earnings and the customer experience. By next year, Second Cup will be well on its way to restoring an asset light business model.

Net debt is significantly reduced at \$1,516,000 versus \$5,723,000 a year ago. The quarterly interest expense remains temporarily high at \$176,000 which will be reduced with debt refinancing within the next year.

New developments

The second quarter of 2015 features more innovative introductions from Second Cup:

- The company's loyalty program, Second Cup Coffee Co. Rewards, launched in late April. A simple, smart and fresh approach to loyalty, the program integrates an innovative mobile app which will surprise and delight customers while providing Second Cup with valuable insight and feedback to provide customers with more personalized experiences. Rewards members can even use the app on the Apple® Watch, making Second Cup one of the first companies to debut an app for the new device. The Rewards program launch was met with enthusiasm by both franchisees and customers and is currently the number 3 ranking app in the App Store for Food & Drink in Canada.
- New branding elements were introduced to all cafés in April including updated menu boards and graphics to reflect the modernized premium brand status, the Canadian artist cup series and a stylish new dress code.
- In early May, Second Cup will launch a new cold beverage line of coffee-forward Frappés available in four flavours.

- Dean Michaels joined Second Cup in April as Vice President, Development-Leasing, Franchising and Construction. Mr. Michaels has a proven track record of delivering results in network planning and its execution.
- Barbara J. Mallon, CPA, CMA will be joining the company as Chief Financial Officer, effective June 15th. She will play a pivotal role in the company's transformation strategy applying her financial and operational leadership to create long-term growth and shareholder value. Ms. Mallon brings a history of solid financial and operational leadership including prior roles as Vice President Finance, Operations at Maple Leaf Consumer Foods and The Shopping Channel.

"I am very encouraged by our accomplishments," adds Ms. Box. "While much remains to be done, we are seeing good momentum. We will continue to focus on quality, innovation and in café operational excellence. Our obsession to provide the ultimate coffee experience positions us well as we pursue sustainable long- term growth and value creation for our shareholders."

About Second Cup

Founded in 1975, The Second Cup Ltd. is a Canadian specialty coffee retailer operating over 345 franchised and company owned cafes serving more than 1 million customers each week. All of the approximately 4,000 Second Cup baristas are trained coffee experts who are committed to ensuring excellence in every cup and the very best customer experience possible. For more information, please visit www.secondcup.com or find the company on Facebook and Twitter.

Financial Results

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 weeks ended March 28, 2015.

(in thousands of Canadian dollars, except Number of cafés, Same café sales, and per share amounts)	13 weeks ended March 28, 2015	13 weeks ended March 29, 2014
System sales of cafés ¹	\$43,174	\$43,930
Same café sales ¹	(1.1%)	(6.9%)
Number of cafés - end of period	344	357
Total revenue	\$9,014	\$6,623
Gross profit	\$5,248	\$4,745
Operating expenses	\$5,235	\$3,821
Restructuring charges	-	\$559
Provision for café closures	\$(55)	\$139
Operating income	\$68	\$226
Adjusted EBITDA ¹	\$364	\$1,080
Net (loss) income and comprehensive (loss) income	\$(76)	\$56
Basic and diluted (loss) earnings per share as reported	\$(0.01)	\$0.01
Adjusted basic and diluted earnings per share ¹	\$(0.01)	\$0.06
Total Assets - as at end of period	\$51,179	\$76,040
Number of common shares issued and outstanding - end of period	12,830,945	9,903,045

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

BALANCE SHEET DATA

	March 28, 2015	December 27, 2014
Cash and cash equivalents	9,676	10,918
Total assets	51,179	53,449
Total debts	11,192	11,119
Total liabilities	26,248	28,455
Total shareholders' equity	24,931	24,994
<i>Café network</i>		
	13 weeks ended	13 weeks ended
	March 28, 2015	March 29, 2014
Number of cafés - beginning of period	347	356
Cafés opened	2	5
Cafés closed	(5)	(4)
Number of cafés - end of period	<u>344</u>	<u>357</u>

The Company ended the quarter with forty-one (2014 - eleven) Company-operated cafés.

System sales of cafés

System sales of cafés for the 13 weeks ended March 28, 2015 were \$43,174 compared to \$43,930 for the 13 weeks ended March 29, 2014, representing a decrease of \$756 or 1.7%. 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 1.1%, compared to a decline of 6.9% in the comparable quarter of 2014. While negative, the 1.1% sales decline represents a significant improvement in trend and is the best quarterly result since the 13 weeks ended March 31, 2012.

Analysis of revenue

Total revenue for the Quarter was \$9,014 (2014 - \$6,623) and consisted of royalty revenue, revenue from sale of goods, and services and other revenue.

Royalty revenue for the Quarter was \$2,602 (2014 - \$3,195). The reduction in royalty revenue of \$593 is primarily a result of the new royalty incentive introduced in August 2014, lower café sales, and the increase of Company-operated cafés.

Revenue from the sale of goods, which consists of revenue from Company-operated cafés and wholesale revenue was \$5,238 (2014 - \$1,800) for the Quarter. The increase of \$3,438 in revenue from the sale of goods was mainly due to the increased number of Company-operated cafés.

Services and other revenue for the Quarter was \$1,174 (2014 - \$1,628).

Cost of goods sold

Cost of goods sold represents the product cost of goods sold in Company-operated cafés and wholesale channels, plus the cost of direct labour in the Company-operated cafés. Cost of goods sold was \$3,766 (2014 - \$1,878). The \$1,888 increase in cost of goods sold is mainly due to the increase in Company-operated cafés.

Operating expenses

Operating expenses include Coffee Central expenses and the overhead expenses of Company-operated cafés. Total operating expenses for the Quarter were \$5,235 (2014 - \$3,821), an increase of \$1,414.

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Coffee Central

Coffee Central expenses for the Quarter were \$3,712 (2014 - \$3,603), an increase of \$109.

Company-operated cafés

Company-operated café expenses for the Quarter were \$1,523 (2014 - \$218). The \$1,305 increase is attributable to the number of Company-operated cafés.

Interest and financing

The Company incurred interest and financing expenses of \$176 (2014 - \$156). The increase in interest and financing expenses is due to the fair value adjustments of the interest rate swap, which was partially offset by an increase in interest income.

Income taxes

Deferred income tax recoveries of \$32 were recorded in the Quarter (2014 - income tax expense of \$14).

Adjusted EBITDA

Adjusted EBITDA for the Quarter was \$364 (2014 - \$1,080). The decrease of \$716 was primarily due to restructuring and provisions for café closures last year.

Net income

The Company's net loss for the Quarter was \$76 or \$0.01 per share, compared to net income of \$56 or \$0.01 per share in 2014. The decrease in net income of \$132 or \$0.05 per share was mainly due to decreased royalties and increased expenses relating to Company-operated cafés, offset partially by Coffee Central expense savings due to the FY14 restructuring and retail listing fees incurred during the the same period last year. A reconciliation of Net income to Adjusted EBITDA is provided in the section "Definitions and discussion on certain non-GAAP financial measures".

SELECTED QUARTERLY INFORMATION

(in thousands of Canadian dollars, except Number of cafés, Same café sales, and per share amounts)	Q1 2015²	Q4 2014²	Q3 2014	Q2 2014
System sales of cafés ¹	\$43,174	\$49,427	\$43,596	\$45,829
Same café sales ¹	(1.1%)	(3.9%)	(3.3%)	(5.0%)
Number of cafés - end of period	344	347	349	357
Total revenue	\$9,014	\$8,427	\$6,686	\$6,435
Operating income (loss) ¹	\$68	(\$521)	(\$30,214)	(\$388)
Adjusted EBITDA ¹	\$364	\$1,068	\$1,079	\$1,516
Net income (loss) for the period	(\$76)	(\$469)	(\$26,230)	(\$390)
Basic and diluted earnings (loss) per share	(\$0.01)	(\$0.04)	(\$2.65)	(\$0.04)
Dividends declared per share	-	-	-	-
	Q1 2014	Q4 2013²	Q3 2013	Q2 2013
System sales of cafés ¹	\$43,930	\$51,898	\$44,894	\$47,688
Same café sales ¹	(6.9%)	(4.3%)	(3.7%)	(2.2%)
Number of cafés - end of period	357	356	351	362
Total revenue	\$6,623	\$8,038	\$6,268	\$6,636
Operating (loss) income ¹	\$226	\$1,891	\$1,361	(\$11,401)
Adjusted EBITDA ¹	\$941	\$3,345	\$1,671 ³	\$2,122
Net (loss) income for the period	\$56	\$1,177	\$918	(\$10,152)
Basic and diluted (loss) earnings per share	\$0.01	\$0.12	\$0.09	(\$1.03)
Dividends declared per share	\$0.085	\$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).

³The Company amended its definition of Adjusted EBITDA as discussed in the section "Definitions and discussion on certain non-GAAP financial measures" to include provisions for café closures. Comparative amounts were amended in order to provide adequate comparative figures.

OUTLOOK

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

We believe our renewed dedication to providing the ultimate coffee experience positions us well for creating long-term growth and value creation for our shareholders.

In the second quarter of 2015 we will feature more innovation including; unveiling our new and exciting Cold beverage platform, elements of the new branding in all of our cafes, and the launch of our loyalty program, Second Cup Coffee Co. Rewards.

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, adjusted EBITDA, and adjusted earnings per share.

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.

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 / re-modelling. 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 and Adjusted 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 an indicator 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.

Impairment charges, if incurred, are a reconciling item in the calculation of adjusted EBITDA as its nature is non-cash and management interprets this measure to be similar in substance to depreciation and amortization. This interpretation by management is consistently applied regardless of whether impairment charges are or are expected to be recurring.

Restructuring charges, if incurred, are a reconciling item in the calculation of adjusted EBITDA as management believes such costs are non-recurring and not an indicative performance measure directly linked to the Company's business operations.

Provision for café closures, if incurred, are a reconciling item in the calculation of adjusted EBITDA as management believes that while such costs may be recurring, they could be larger than normal during this period of transformation of the business and are not an indicative performance measure directly linked to the Company's business operations from ongoing cafés.

A reconciliation of Net income to EBITDA and Adjusted EBITDA is provided below:

	13 weeks ended March 28, 2015	13 weeks ended March 29, 2014
Net (loss) income	\$ (76)	\$ 56
Net interest and financing	176	156
Income tax (recovery) expense	(32)	14
Depreciation of property and equipment	273	195
Amortization of intangible assets	78	71
Gain on disposal of property and equipment	-	(110)
EBITDA	<u>419</u>	<u>382</u>
Restructuring charges	-	559
Provision for café closures	<u>(55)</u>	<u>139</u>
Adjusted EBITDA	<u>\$ 364</u>	<u>\$ 1,080</u>

Adjusted basic and diluted earnings per share

Adjusted earnings per share represent earnings per share excluding any impairment charges, provisions for café closures and restructuring charges. Impairment charges are non-cash, but material items that are adjusted as management concluded that this is not a direct measure of the Company's focus on day to day operations, is not indicative of future operating results, and thus better evaluates the underlying business of the Company. Restructuring charges and the provision for café closures are a reconciling item as management believes these costs are non-recurring and not an indicative performance measure directly linked to the focus of the Company's business operations on a per share basis.

A reconciliation of Net income to adjusted basic and diluted earnings per share is provided below:

	13 weeks ended March 28, 2015	13 weeks ended March 29, 2014
Net (loss) income	\$ (76)	\$ 56
Restructuring charges	-	559
Provision for café closures	(55)	139
Tax effect	15	(185)
Adjusted earnings	<u>(116)</u>	<u>569</u>
Weighted average number of shares issued and outstanding (unrounded)	<u>12,830,945</u>	<u>9,903,045</u>
Adjusted basic and diluted earnings per share	<u>\$ (0.01)</u>	<u>\$ 0.06</u>

SOURCE The Second Cup Ltd.
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