

# SWISS WATER DECAFFEINATED COFFEE INC.

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## Management Discussion and Analysis

For the three and six months ended June 30, 2021

### MANAGEMENT DISCUSSION AND ANALYSIS

*This Management's Discussion and Analysis ("MD&A") of Swiss Water Decaffeinated Coffee Inc. ("Swiss Water" or the "Company"), dated as of August 5, 2021, provides a review of the financial results for the three and six months ended June 30, 2021 relative to the comparable period of 2020. The three-month period represents the second quarter ("Q2") of our 2021 fiscal year. This MD&A should be read in conjunction with Swiss Water's condensed consolidated interim financial statements for the three and six months ended June 30, 2021, the audited consolidated financial statements for the year ended December 31, 2020, and in conjunction with the Annual Information Form ("AIF"), which are available on [www.sedar.com](http://www.sedar.com).*

*All financial information is presented in Canadian dollars unless otherwise specified.*

### FORWARD-LOOKING STATEMENTS

This MD&A contains forward-looking statements, including statements regarding the future success of our business and market opportunities. Forward-looking statements typically contain words such as "believes", "expects", "anticipates", "continue", "could", "indicates", "plans", "will", "intends", "may", "projects", "schedule", "would" or similar expressions suggesting future outcomes or events, although not all forward-looking statements contain these identifying words. Examples of such statements include, but are not limited to, statements concerning: (i) expectations regarding Swiss Water's future success in various geographic markets; (ii) future financial results, including anticipated future sales and processing volumes; (iii) future dividends; (iv) the expected actions of the third parties described herein; (v) factors affecting the coffee market including supplies and commodity pricing; (vi) the expected cost to complete the new production line currently under construction; and (vii) the business and financial outlook of Swiss Water. In addition, this MD&A contains financial outlook information that is intended to provide general guidance for readers based on our current estimates, which are based on numerous assumptions and may prove to be incorrect. Therefore, such financial outlook information should not be relied upon by readers. These statements are neither promises nor guarantees but involve known and unknown risks and uncertainties that may cause our actual results, level of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed in or implied by these statements. These risks include, but are not limited to, risks related to processing volumes and sales growth, operating results, supply of coffee, supply of utilities, general industry conditions, commodity price risks, technology, competition, foreign exchange rates, construction timing, costs and financing of capital projects, general economic conditions and those factors described herein under the heading 'Risks & Uncertainties'.

The forward-looking statements contained herein are also based on assumptions that we believe are current and reasonable, including but not limited to, assumptions regarding: (i) trends in certain market segments and the economic climate generally; (ii) the financial strength of our customers; (iii) the value of the Canadian dollar versus the US dollar ("US\$"); (iv) the expected financial and operating performance of Swiss Water going forward; (v) the availability and expected terms and conditions of debt facilities; (vi) the expected level of dividends payable to shareholders; and (vii) the potential impact of the COVID-19 pandemic. We cannot assure readers that actual results will be consistent with the statements contained in this MD&A. The forward-looking statements and financial outlook information contained herein are made as of the date of this MD&A and are expressly qualified in their entirety by this cautionary statement. Except to the extent required by applicable securities law, Swiss Water undertakes no obligation to publicly update or revise any such statements to reflect any change in our expectations or in events, conditions, or circumstances on which any such statements may be based, or that may affect the likelihood that actual results will differ from those described herein.

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### EXECUTIVE SUMMARY

For the three and six months ended June 30, 2021, Swiss Water's revenues increased by 9% and 13% respectively compared to the same periods in the prior year. Volume for the quarter and year-to-date increased by 4% and 8% respectively. EBITDA for the quarter and the year-to-date remained broadly flat compared to the same periods in the prior year. However, gross profit and net income fell, primarily driven by the expected impact of new higher depreciation charges and incremental production expenses following the commissioning of our new production line in the second half of 2020. The first half of the year has demonstrated robust volume resilience with all regions growing, with Europe delivering growth of 74% versus a year ago. Despite the ongoing presence of the COVID-19 pandemic, we continue to see recovery in base business activity as our customers return to business. Ultimately performance is a reflection of our well-diversified customer base and broad international reach.

The primary change in our business, as it adapts to the COVID-19 pandemic environment, continues to be changes in customer mix. At the beginning of the pandemic, we experienced strong volume demands from those customers that supplied the retail grocery trade. Consumer hoarding and pantry loading created a short-term demand peak. Over the course of the second half of 2020 and through the first quarter of 2021, strong grocery demand continued but at a slower pace than when the pandemic started. Many, but not all, shuttered restaurants and out-of-home specialty coffee shops have reopened, and this trend has partially contributed to our volume recovery. This can be seen with a growth of 29% in Q2 2021 compared to Q2 2020 for our specialty customers as they get back on track compared to a decline in commercial customer business of 8% in the quarter.

Gross profit was positively lifted by higher trading volumes, however, this gain was offset by increased depreciation charges and incremental labour and production expenses following our transition to a dual location manufacturing structure during the second half of 2020. These changes were anticipated and in line with expectations.

We are currently well positioned with green coffee inventory and will be able to react to short-term demand increases as trading conditions strengthen. Although we are seeing some divergence from previous patterns in terms of geographic strength in demand. We remain in close contact with our customers, however, it is clear that many of our food service partners remain cautious regarding when their trading activity will fully return to pre-pandemic levels.

In \$000s except per share amounts (unaudited)	3 months ended June 30		6 months ended June 30	
	2021	2020	2021	2020
Sales	\$ 28,759	\$ 26,380	\$ 54,451	\$ 48,197
Gross profit	3,652	5,154	7,204	9,360
Operating income	1,106	2,370	1,844	4,405
Net income	216	1,716	120	3,163
EBITDA <sup>1</sup>	3,163	3,194	5,851	5,834
EBITDA excluding IFRS 16-Leases <sup>2</sup>	2,461	2,536	4,448	4,518
Net income per share – basic <sup>3</sup>	\$ 0.02	\$ 0.19	\$ 0.01	\$ 0.35
Net income per share – diluted <sup>3</sup>	\$ 0.02	\$ 0.19	\$ 0.01	\$ 0.21

<sup>1</sup> EBITDA is defined in the 'Non-IFRS Measures' section of this MD&A and is a "Non-GAAP Financial Measure" as defined by CSA Staff Notice 52-306.

<sup>2</sup> EBITDA excluding the impact of IFRS 16 - Leases is defined as EBITDA, less lease payments made during the year.

<sup>3</sup> Per-share calculations are based on the weighted average number of shares outstanding during the periods. Diluted earnings per share take into account shares that may be issued upon conversion of convertible debt and RSUs as well as the impact on earnings from changes in the fair market value of the embedded option in the convertible debt and conversion of RSUs.

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### Operational highlights

- Total volumes in the second quarter and the first half of the year increased by 4% and 8%, respectively compared to the same periods in 2020. Many of our customers are starting to see strengthening consumer demand and are beginning to plan for trading activity closer to pre-pandemic levels. Encouragingly we recorded 4% and 10% growth in our North America and Asia Pacific regions respectively in the first half of 2021 compared to the same periods in the prior year. In Europe, volumes increased by an impressive 74% during the first half of the year.
- Our largest geographical market by volume in Q2 continued to be the United States, followed by Canada, Europe and other international markets. By dollar value, for the six months ended June 30, 2021, 43% of our sales were to customers in the United States, 35% were to Canada, and the remaining 22% were to other countries. Our international business continues to expand and we anticipate revenues from our European and Asia-Pacific markets will continue to increase in both dollar and percentage terms.

### Financial highlights

- Quarterly revenue increased by 9% over Q2 2020 to \$28.8 million, and six-month revenue increased by 13% to \$54.4 million as a result of increased volume growth and the impact of higher green coffee prices compared to the same period in 2020.
- Gross profit for Q2 of this year was \$3.7 million, a decrease of \$1.5 million from Q2 2020. For the first half of 2021, gross profit decreased by \$2.2 million to \$7.2 million. The reduction in gross profit was driven by increased depreciation charges, incremental labour and production expenses following the commissioning of our new Delta manufacturing facility, and lower differential margin due to foreign exchange variability. These movements were not unexpected and were partially offset by improvements in customer sales mix and supply chain efficiencies within our Seaforth subsidiary. The additional depreciation and amortization expense from the Delta manufacturing facility were \$0.8 million for the second quarter and \$1.7 million for the first half of 2021.
- Net income for the three months and six months ended June 30, 2021 were both lower compared to the same periods in 2020. The quarter-over-quarter and year-over-year difference reflect the combination of changes in gross profit and both operating and non-operating expenses. Operating expenses for the second quarter of 2021 decreased by 9% to \$2.6 million due to reduced salary expenses following the restructuring of various departments during the first quarter of this year. There was also an income tax credit of \$0.1 million for research and development recorded in the second quarter. For the first six months of 2021, operating expenses increased 8% to \$5.4 million compared to the same period in 2020. This increase was largely due to the movement of stock based compensation expenses. In the first half of 2020 there was a significant unplanned cost recovery following a fall in Swiss Waters' share price. Whereas during the equivalent period in 2021 a normal expense was recorded. Non-operating expenses were higher for the quarter and first half of the year due to an increase in finance costs in both our construction loan and credit facility. In 2020, during the construction of Delta Line 1, borrowing costs related to this project were capitalized. Following the commissioning of our first production line in Delta in Q3 2020 related borrowing costs started to be recognized as an expense. Another factor contributing to higher non-operating expenses is due to a large gain realized in Q1 2020 as a result of the revaluation of an embedded derivative due to Swiss Water's lower share price, offset by a slight loss on risk management activities. In the first half of 2021, the revaluation effect was much smaller.

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- EBITDA for the quarter remained flat at \$3.2 million and increased slightly to \$5.9 million for the first half of 2021, compared to the same periods in 2020.

### OUTLOOK

The Company is limiting guidance for the 2021 fiscal year due to the ongoing uncertainty of the effect of the COVID-19 pandemic. During the early stages of the pandemic, we experienced strong short term volume pull from customers that service the retail grocery trade as consumers loaded their pantries in anticipation of quarantines and supply disruptions, or simply consumed their coffee at home. The at-home coffee market has remained strong but has leveled off from the initial spike in demand. We expect this trend to continue for the immediate future; however, we are seeing additional volume from the specialty market indicating that out-of-home is demand strengthening and building some momentum.

Further, we expect customers who serve the out-of-home coffee market through cafes and restaurants to continue to recover from the serious disruption they experienced due to the widespread or targeted food-service shutdowns implemented to combat surges in the number of COVID-19 cases. In the second half of 2020 many countries partially lifted their lockdowns and our sales into the out-of-home channel began to recover. This trend has continued through the first half of 2021.

Some countries and regions have started to see COVID-19 vaccination programs move towards maturity. These include a number of states and major cities in the USA, which is our largest geographical segment. We are cautiously optimistic that high vaccination rates will reduce the scale of subsequent COVID-19 outbreaks and lower the risk of future lockdowns in some of our most important markets. It is particularly encouraging that the Company's sales volumes in Asia Pacific grew by 10% during the first six months of 2021. This region has been acknowledged to have managed the control of the COVID-19 pandemic relatively well, and we are hopeful that the region's growth is a leading indicator of how our volume will continue to rebound in North America and Europe as COVID-19 infection rates fall in these regions.

Despite signs of a recovery uncertainty does persist. The global recovery from the COVID-19 pandemic and the full rollout of the vaccine is unlikely to be without a challenge. Vaccination rates in some countries, and in particular the USA, are starting to slow down and future COVID-19 outbreaks are likely. Given this ambiguity, we cannot reliably predict the ultimate impact that the COVID-19 pandemic will have on our business in 2021, particularly within the out-of-home market. Accordingly, the risk remains that Swiss Water may continue to report sales volumes that under-index recent year trends. However, after a stronger than expected second half of 2020, and a strong first half of 2021, we are cautiously optimistic that our volumes will remain strong and resilient in 2021.

Operationally, Swiss Water continued to run both Burnaby production lines on a 24/7 basis throughout 2020. In September 2020, we announced the completion of our first production run of commercial-grade coffee from our Delta, B.C facility. Following this success, we have transitioned a significant proportion of production volume to Delta and reduced some of the pressure on our Burnaby assets. Currently, Delta is running on a 24/7 basis. As we move through 2021 we expect to gradually increase the processing speed of this asset and move towards optimizing and maximizing production from this line.

On a more cautionary note, the recovery of the global economy has started to place significant stress on international supply chains. This development has started to undermine the efficient movement of coffee from some growing regions, and we are starting to see a delay in the delivery of some coffees to our production facilities. Furthermore, unusually cold weather in Brazil during July has driven a sharp rise in the coffee futures price in recent weeks. High coffee prices can also have a destabilizing impact on the efficient

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movement of coffee inventories. We are paying close attention to these emerging risks and will implement necessary mitigation steps, as required, to ensure that our production schedules are not compromised.

As noted previously, in Q2 of 2020, the landlord of our Burnaby manufacturing site provided formal notice that our lease would not be extended beyond June 2023. Subsequent to the period end of Q2 2021, we were formally issued the building permit to begin construction for our second production line at our Delta location. The targeted completion date of this project is before the 2023 deadline in Burnaby. An additional production line is required to ensure the capacity to process expected volume upon the conclusion of our Burnaby lease and to provide additional capacity for intermediate term growth. Based on engineering reports from a third-party engineering firm, when both are completed, the two lines in Delta are expected to have a targeted endpoint capacity at least 40% greater than the current existing capacity of the two lines at our Burnaby site.

The preliminary cost estimate from our third-party engineering firm for the design and construction of a new production line in Delta is approximately \$45.0 million, plus commissioning costs, which are expected to be approximately \$2.0 million. These estimates are preliminary and like all major design and construction projects are highly dependent on local and global economic factors impacting construction. These include, without limitation, changes in labour, commodity and materials pricing, trade policies, and supply chain issues. In addition, the continuing impact of the worldwide COVID-19 pandemic is unknown and could impact the timing and costs of the proposed project. In Q2, 2021, we concluded a new financing agreement that will contribute \$25.0 million towards this project. These incremental funds, together with existing available credit and projected internally generated cash flow, are anticipated to be sufficient to fund the completion of the new production line.

### BUSINESS OVERVIEW

Swiss Water Decaffeinated Coffee Inc. is a premium green coffee decaffeinator located in Burnaby and in Delta, British Columbia. We employ the proprietary Swiss Water® Process to decaffeinate green coffee without the use of chemical solvents, leveraging science-based systems and controls to produce coffee that is 99.9% caffeine free. Our process is certified organic by the Organic Crop Improvement Association and is the world's only consumer-branded decaffeination process. Decaffeinating premium green coffee without the use of harmful chemical solvents is our primary business.

Our Seaforth subsidiary provides a complete range of green coffee logistics services including devanning coffee received from origin; inspecting, weighing and sampling coffees; and storing, handling and preparing green coffee for outbound shipments. Seaforth provides all of Swiss Water's local green coffee handling and storage services. In addition, Seaforth handles and stores coffees for several other coffee importers and brokers, and is the main green coffee handling and storage company in Metro Vancouver. Seaforth is organically certified by Ecocert Canada.

Swiss Water shares trade on the Toronto Stock Exchange under the symbol 'SWP'. As at the date of this report, 9,129,673 shares were issued and outstanding.

### Swiss Water Decaffeinated Coffee's Business

We carry an inventory of premium-grade Arabica coffees that we purchase from the specialty green coffee trade, decaffeinate and then sell to our customers (our "Regular" or "Non-Toll" business). Revenue from our Regular business includes both processing revenue and green coffee cost recovery revenue.

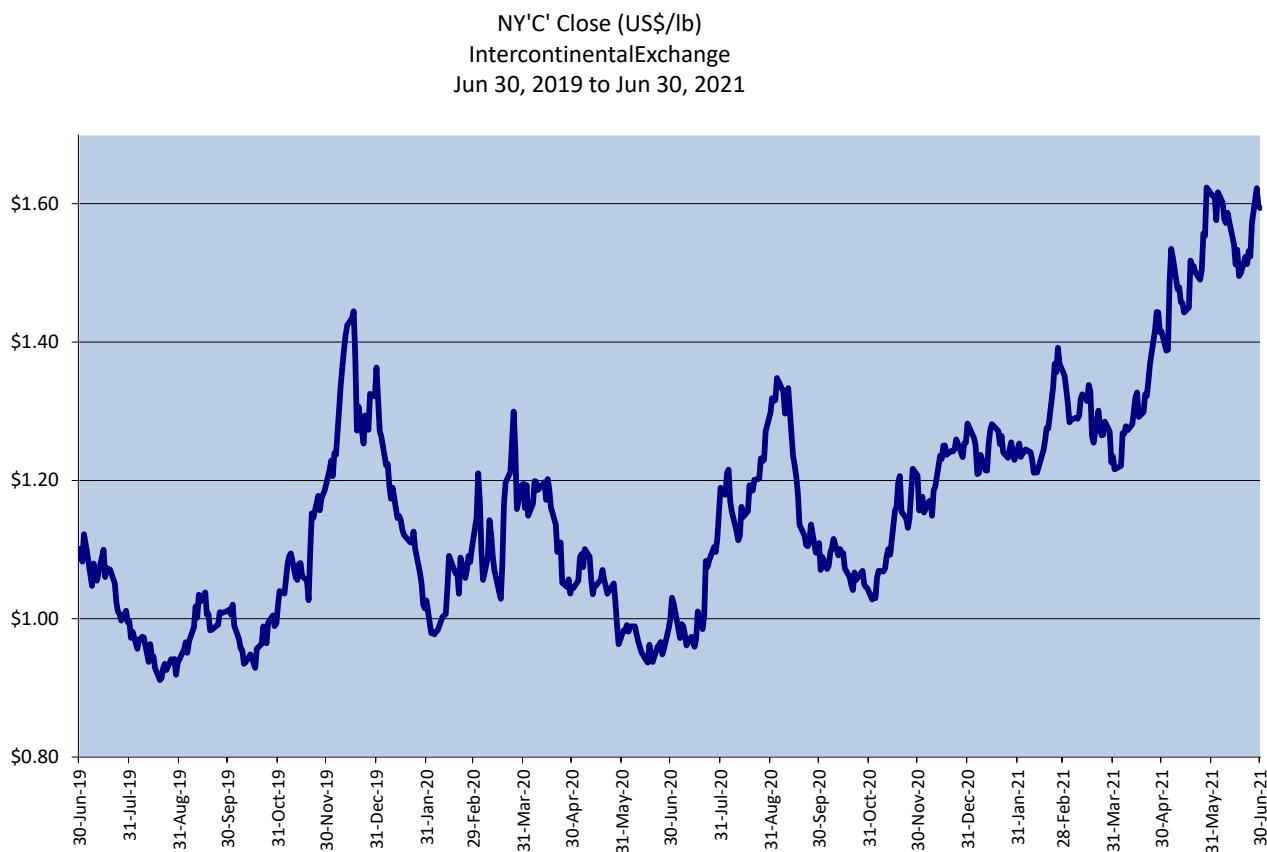
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We also decaffeinate coffee owned by our customers for a processing fee under toll arrangements (our “toll” business). The value of the coffee processed under toll arrangements does not form part of our inventory, our revenue, or our cost of sales. Revenue from toll arrangements consists entirely of processing revenue.

Our cost of sales is comprised primarily of the cost of green coffee purchased for our regular business, plant labour and other processing costs directly associated with our production facility. This incorporates an allocation of fixed overhead costs, which includes depreciation of our production equipment and amortization of our proprietary process technology. For our Regular business, we work with coffee importers to source premium-grade green coffees from coffee-producing countries located in Central and South America, Africa and Asia. The purchase price is based on the NY'C' coffee futures price on the Intercontinental Exchange, plus a quality differential. The NY'C' component typically makes up more than 80% of the total cost of green coffee, while the quality differential typically accounts for less than 20%. Both the NY'C' price and the quality differential fluctuate in response to fundamental commodity factors that affect supply and demand. The chart below shows the movement in the NY'C' for the last eight quarters:



In Q2 2021, the NY'C' averaged US\$1.4614/lb compared to an average of US\$1.0503/lb in Q2 2020. The rise and fall of the NY'C' affects our volume of shipments, our revenues and our cost of sales. In an upward trending market, our customers tend to consume their inventories rather than build them. When the NY'C' declines over a sustained period, our customers tend to add to their inventories.

The majority of our (“C\$”) revenues are generated in US dollars (“US\$”), while a significant portion of our costs is paid in Canadian dollars. We, therefore, have exposure to changes in the US\$/C\$ exchange rates.

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This is managed, in part, through derivative financial instruments. All other factors being equal, our profitability and cash from operations will be higher when the US dollar appreciates relative to the Canadian dollar. A long-term depreciation of the Canadian dollar will improve our long-term profitability and cash generation. The chart below illustrates the US\$ to Canadian dollar (“C\$”) exchange rates for the last eight quarters:



In Q2 2021, the US\$ averaged C\$1.2282, a decrease from C\$1.3853 over the same period in 2020. During Q2 2021 the US\$ ranged between C\$1.2040 and C\$1.2617 (2020: between C\$1.3383 and C\$1.4217). When the US\$ depreciates (appreciates), it decreases (increases) our gross profit on green coffee revenues.

## OPERATING RESULTS

### Revenue

We categorize our customers by the nature of their business: either coffee importers or roasters. Coffee importers act like grocery stores to roasters, sourcing and importing green coffee from various origins and carrying a selection of different origins and quality levels for roasters to choose from. Importers buy from us in order to resell our coffees to roasters when and where they need it. Roasters are in the business of roasting and packaging coffee for sale to consumers in their own coffee shops, or for home or office use. Roasters either buy directly from Swiss Water, or they buy from an importer. Roasters generally carry lower inventories, as they tend to take delivery of green coffee shortly before roasting it. As such, when comparing period to period, shipments to roasters are more stable when compared to shipments to importers.

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We also monitor and report our revenue in three categories. “Process revenue” represents the amount we charge our customers for decaffeinating green coffee, and it generally increases as our processing volumes increase. “Green coffee cost recovery revenue”, or “green revenue”, is the amount we charge our customers for the green coffee we purchase for decaffeination. “Distribution revenue” consists of shipping, handling, and warehousing charges billed to our customers. It typically rises with our processing volumes and with the growth of Seaforth’s business. Our revenue by category for the indicated period was:

In \$000s (unaudited)	3 months ended June 30		6 months ended June 30	
	2021	2020	2021	2020
Process revenue	\$ 7,121	\$ 6,990	\$ 13,624	\$ 12,740
Green revenue	19,672	17,516	36,998	31,921
Distribution revenue	1,966	1,874	3,829	3,536
Total revenue	\$ 28,759	\$ 26,380	\$ 54,451	\$ 48,197

For the quarter ended June 30, 2021, sales totaled \$28.8 million, an increase of \$2.4 million, or 9%, compared to the same quarter in 2020 driven by the impact of an increase in the New York Arabica Futures market. Sales for the first six months of 2021 totaled \$54.5 million, an increase of \$6.3 million, or 13%, over the same period last year.

Our sales in the second quarter and first half of 2021 compared to the same periods in the prior year by revenue category are as follows:

- Process revenue increased by \$0.1 million, or 2% to \$7.1 million in Q2 and year-to-date revenue increased by \$0.9 million or 7% to \$13.6 million. This increase is reflective of an increase in our processing volumes.
- Green revenue increased by \$2.2 million, or 12% in Q2 2021 to \$19.7 million and by \$5.1 million or 16% to \$37.0 million in the first half of 2021. Movements in green revenue reflect changes in sales processing volumes and fluctuations in coffee futures price, NY'C'.
- Distribution revenue increased by \$0.1 million, or 5% to \$2.0 million in Q2 2021 and increased by \$0.3 million, or 8% in the first six months of 2021. Variability in distribution revenue is driven by shipment volumes.

The sales volume performance in the first quarter of 2021 by geographical segment are as follows:

- Sales volume in North America increased by 4% in both Q2 and first half of 2021.
- Sales volume in Europe increased by 74% in the first half of 2021. There was no growth in Q2.
- Sales volume in Asia Pacific increased by 8% in Q2 and 10% in the first half of 2021.

### Cost of Sales

Cost of sales includes the cost of green coffee purchased for our regular business, the plant labour and other processing costs directly associated with our production facility, customer-specific hedges and commodity hedges. The cost of sales incorporates an allocation of fixed overhead costs, which includes depreciation of our production equipment and amortization of our proprietary process technology. In addition, cost of sales includes the costs of operating Seaforth’s warehouses.

Cost of sales for the second quarter increased by \$3.9 million or 18%, to \$25.1 million compared to the same period in 2020. Cost of sales increased by \$8.4 million, or 22% to \$47.2 million in the first half of 2021. This

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was mainly driven by an increase in the cost of green coffee, depreciation of our Delta manufacturing facility, and incremental labour and production expenses. The additional depreciation and amortization expenses from the Delta manufacturing facility and finance lease were \$0.8 million for the quarter and \$1.7 million for the first half of the year.

### Gross Profit

Gross profit decreased by \$1.5 million or 29% to \$3.7 million for the second quarter of 2021 and by \$2.2 million or 23% to \$7.2 million for the first half of the year mainly due to lower coffee differential margin and depreciation of our Delta manufacturing facility.

### Administration Expenses

Administration includes general management, inbound and outbound logistics, finance and accounting, quality control and assurance, engineering, research and development, and other administrative or support functions. Administration expenses include compensation expenses, travel and other personnel-related expenses for administrative staff, directors' fees, investor relations expenses, professional fees, depreciation of office-related equipment, and amortization of the brand asset.

Administration expenses for the quarter decreased by 18% to \$1.6 million, and for the first six months of the year increased by 13% to \$3.4 million. In Q1 2020, there was a significant cost recovery of share-based compensation costs, which are based on Swiss Water's share price. During the year 2020, our share price dropped. This resulted in an estimated stock-based compensation cost recovery whereas, in 2021, an expense was recorded. If the impact of share-based compensation and recovery of research and development tax credit was excluded, administration expenses for the first half of 2021 would be \$0.2 million lower than the first half of 2020.

### Sales and Marketing Expenses

Sales and marketing expenses include compensation and other personnel-related expenses for sales and marketing staff, consumer initiatives, trade advertising and promotion costs, as well as related travel expenses. We invest in research regarding the behavior of decaffeinated coffee consumers. These insights enable us to create effective consumer advertising programs, and they form a cornerstone of the consultative services we provide to our customers. We also aim to grow brand awareness with both the coffee trade and consumers. We employ a range of marketing activities to achieve this, including digital and print advertising, social media communications, sponsorship and exhibiting at key industry events.

Sales and marketing expenses increased by \$0.1 million to \$0.9 million for the quarter over Q2 2020 and remained relatively flat for the first six months of the year at \$1.9 million. The variability of these expenses throughout the year is mainly driven by timing differences in advertising and marketing campaign activities.

### Finance Expenses and Income

Finance income reflects the charges we bill to customers for financing coffee inventories and interest earned on cash balances and short-term investments. Finance expenses include interest costs on credit facilities and bank debt, other borrowings, the accretion expense on our asset retirement obligation, interest expense on a convertible debenture and interest expense on finance leases.

Net finance expenses for the second quarter of 2021 increased by \$0.4 million to \$0.9 million compared to the same period in 2020. Net finance expenses for the first half of the year increased by \$0.8 million to \$1.8 million. The higher interest relates to higher borrowings from our credit facility. Capitalization of borrowing

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costs and finance lease interest related to Delta Line 1 ended in Q3 of 2020 which also contributed to higher finance expenses during 2021.

Interest on the convertible debenture is expensed at an effective interest rate of 12.15% (a rate determined by management in accordance with IFRS), while the contractual interest paid on this loan is at a rate of 6.85%, causing the amortization of the bond discount to change over time.

Finance lease interest of \$0.3 million and \$0.6 million was recognized during the three and six months ended June 30, 2021 respectively compared to \$0.1 million and \$0.3 million in the same periods in 2020. The increase is a result of the Delta manufacturing facility being operational now as in the prior period the interest was capitalized.

### Gains and Losses on Risk Management Activities

Under hedge accounting, gains or losses on designated hedges are included in either revenue or cost of sales, held on the balance sheet or included in other comprehensive income for future transactions (see 'Hedge Accounting', below). Thus, 'gain (loss) on risk management activities' includes only those gains and losses on derivative financial instruments or portions of such instruments that are not designated as hedging instruments.

For the three and six months ended June 30, 2021, we recorded a gain of \$0.1 million and a loss of \$0.1 million compared to a slight gain of \$0.03 million and a loss of \$0.2 million recorded for the same periods in 2020.

### Fair Value Adjustment on Embedded Option

Swiss Water entered into a convertible debenture in October 2016. Under IFRS, this instrument is deemed to contain an embedded option that must be revalued at each balance sheet date. The fair value of the derivative liability was determined using the Black-Scholes Option Pricing Model. The variables and assumptions used in computing the fair value are based on management's best estimate at each balance sheet date.

The revaluation on this embedded option resulted in a small gain of \$0.04 million in Q2 2021 and is close to zero for first half of 2021, compared to a loss of \$0.1 million and gain of \$1.4 million recorded for the same periods in 2020. The fluctuations are due to Swiss Water's share price and the risk-free interest rate that are used as inputs in the Black Scholes model. In 2020, a large gain was recorded because the share price from December 31, 2019 dropped from \$6.88 to \$3.01 at June 30, 2020. In 2021, the share price increased slightly from a price of \$3.06 on December 31, 2020 to \$3.13 on June 30, 2021.

### Gains and Losses on Foreign Exchange

We realize gains and losses on transactions denominated in foreign currencies when they occur, and on assets and liabilities denominated in foreign currencies when they are translated into Canadian dollars as at the financial statement date.

During the second quarter of 2021, we recorded a gain on foreign exchange of \$0.3 million, compared to a gain of \$0.4 million in the same period last year. In the first half of the year, we recorded a gain on foreign exchange of \$0.6 million, compared to a loss of \$0.3 million in the same period last year.

### Income Before Taxes and Net Income

In the second quarter and first half of 2021, we recorded income before taxes of \$0.7 million and \$0.5 million, respectively, compared to \$2.2 million and \$4.3 million in the comparable periods in 2020. Current and deferred income tax recovery decreased our net income by \$0.4 million for the quarter and year-to-date,

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compared to an expense of \$0.5 million and \$1.1 million in Q2 2020 and the first half of 2020 respectively. Deferred income taxes arise mainly from temporary differences between the depreciation and amortization expenses deducted for accounting purposes, and the capital cost allowances deducted for tax purposes, as well as changes in corporate income tax rates as adjusted for substantively enacted higher future tax rates. The latter is offset by the tax benefit of loss carry forwards recognized. Overall, we recorded a net income of \$0.2 million in Q2 2021 and \$0.1 million in the first half of 2021, compared to \$1.7 million and \$3.2 million net income in the same periods last year.

### Other Comprehensive Income

Gains or losses on our designated revenue hedges that will mature in future periods are recorded in other comprehensive income, net of income tax expense. Other comprehensive income, net of tax, for the three months and six months ended June 30, 2021 was a gain of \$0.3 million and \$0.7 million, compared to a gain of \$3.5 million and a loss of \$1.4 million in the same periods of 2020. Increases and decreases are related to fluctuations in the value of the Canadian dollar versus the US dollar.

### Basic and Diluted Earnings per Share

Basic earnings per share are calculated by dividing net income by the basic weighted average number of shares outstanding during the period. Similarly, diluted earnings per share are calculated by dividing net income adjusted for the effects of all dilutive potential common shares, by the diluted weighted average number of shares outstanding. For the purposes of the calculation, under IFRS we are required to assume that the maximum number of shares issuable under the convertible debenture will be issued, even though the debenture contains a net share settlement provision (which, if exercised would result in far fewer shares being issued).

For the three months ended June 30, 2021 and 2020 and for the six months ended June 30, 2021, potential common shares issuable under the RSU Plan and common shares issuable for the convertible debenture were anti-dilutive and excluded from the dilution calculation.

For the six months ended June 30, 2020, all potential common shares issuable under the RSU Plan and common shares issuable for the convertible debenture were dilutive, hence included in the dilution calculation.

The calculations of basic and diluted earnings per share for the current and prior periods are shown in the following table:

In 000s except for shares and per share data (unaudited)	3 months ended June 30		6 months ended June 30	
	2021	2020	2021	2020
<b>Basic earnings per share</b>				
Net income attributable to shareholders	\$ 216	\$ 1,716	\$ 120	\$ 3,163
Weighted average number of shares	9,129,673	9,078,780	9,114,771	9,073,567
Basic earnings per share	\$ 0.02	\$ 0.19	\$ 0.01	\$ 0.35
<b>Diluted earnings per share</b>				
Net income attributable to shareholders	216	1,716	120	3,163
Effect of diluted securities: RSUs	-	-	-	(19)
Interest on convertible debenture	-	-	-	564
Fair value gain loss on the embedded option	-	-	-	(1,350)
Net income after effect of diluted securities	\$ 216	\$ 1,716	\$ 120	\$ 2,358

# SWISS WATER DECAFFEINATED COFFEE INC.

## Management Discussion and Analysis

For the three and six months ended June 30, 2021

In 000s except for shares and per share data (unaudited)	3 months ended June 30		6 months ended June 30	
	2021	2020	2021	2020
Weighted average number of shares – basic	9,129,673	9,078,780	9,114,771	9,073,567
Effect of diluted securities: RSUs	-	-	-	198,672
Effect of diluted securities: convertible	-	-	-	1,818,182
Weighted average number of shares - diluted	9,129,673	9,078,780	9,114,771	11,090,421
Diluted earnings per share	\$ 0.02	\$ 0.19	\$ 0.01	\$ 0.21

### EBITDA and EBITDA which excludes the impact of IFRS 16 - Leases

EBITDA is often used by publicly traded companies as a measure of cash from operations, as it excludes financing costs, taxation and non-cash items. The reporting of EBITDA is intended to assist readers in the performance of their own financial analysis. However, since this measure does not have a standardized meaning prescribed by IFRS, it is unlikely to be comparable to similar measures presented by other entities.

We define EBITDA as net income before interest, depreciation, amortization, impairments, share-based compensation, gains/losses on foreign exchange, gains/losses on disposal of property and capital equipment, fair value adjustments on embedded options, and provision for income taxes. Our definition of EBITDA also excludes unrealized gains and losses on the undesignated portion of foreign exchange forward contracts.

EBITDA for Q2 2021 remained flat at \$3.2 million and increased slightly to \$5.9 million for the six months ended June 30, 2021. Operationally, the change in EBITDA was driven by revenue growth, successful efforts across the Company to enhance cost recovery, and increased financial contribution from Seaforth. These gains were offset by an increase in green coffee costs. The reconciliation of net income to EBITDA is as follows:

In \$000s (unaudited)	3 months ended June 30		6 months ended June 30	
	2021	2020	2021	2020
Income for the period	\$ 216	\$ 1,716	\$ 120	\$ 3,163
Income taxes	440	528	429	1,114
Income before tax	\$ 656	\$ 2,244	\$ 549	\$ 4,277
Finance income	(153)	(127)	(268)	(201)
Finance expenses	1,028	607	2,050	1,175
Depreciation & amortization	1,703	850	3,416	1,699
Unrealized (gain) loss on foreign exchange forward contracts	156	(221)	309	393
Fair value (gain) loss on the embedded option	(41)	124	(8)	(1,350)
(Gain) loss on foreign exchange	(330)	(442)	(571)	258
Share-based compensation (recovery) expense	144	159	374	(417)
EBITDA	\$ 3,163	\$ 3,194	\$ 5,851	\$ 5,834
Impact of IFRS 16, which was adopted in the year 2019	(702)	(658)	(1,403)	(1,316)
EBITDA excluding the impact of IFRS 16	\$ 2,461	\$ 2,536	\$ 4,448	\$ 4,518

To help readers better understand our financial results, the following table shows the reconciliation of operating income to EBITDA:

In \$000s (unaudited)	3 months ended June 30		6 months ended June 30	
	2021	2020	2021	2020
Operating income for the period	\$ 1,106	\$ 2,370	\$ 1,844	\$ 4,405
Depreciation & amortization	1,703	850	3,416	1,699
Share-based compensation	144	159	374	(417)

# SWISS WATER DECAFFEINATED COFFEE INC.

## Management Discussion and Analysis

For the three and six months ended June 30, 2021

In \$000s (unaudited)	3 months ended June 30		6 months ended June 30	
	2021	2020	2021	2020
Gain (loss) on risk management activities	54	36	(92)	(246)
Unrealized (gain) loss on foreign exchange forward contracts	156	(221)	309	393
EBITDA	\$ 3,163	\$ 3,194	\$ 5,851	\$ 5,834
Impact of IFRS 16, which was adopted in the year 2019	(702)	(658)	(1,403)	(1,316)
EBITDA excluding the impact of IFRS 16	\$ 2,461	\$ 2,536	\$ 4,448	\$ 4,518

## QUARTERLY INFORMATION / SEASONALITY

There is an element of seasonality in our business, in that the second half of the year tends to have higher volumes and revenues. The pandemic distorted the typical seasonality pattern during 2020.

The following table summarizes results for each of the eight most recently completed fiscal quarters. For comparative purposes, we have also provided the averages for the previous 8-quarter period:

In \$000s except for per share amounts (unaudited)	8 Quarter Average	Q2 2021	Q1 2021	Q4 2020	Q3 2020	Q2 2020	Q1 2020	Q4 2019	Q3 2019
Sales	25,086	28,759	25,692	24,512	24,862	26,380	21,817	25,023	23,645
Gross Profit	3,962	3,652	3,552	2,861	3,431	5,154	4,206	4,106	4,737
Operating income	1,226	1,106	738	126	606	2,370	2,035	539	2,291
EBITDA <sup>1</sup>	2,569	3,163	2,689	1,888	2,036	3,194	2,640	1,454	3,485
EBITDA excluding IFRS 16 <sup>2</sup>	1,873	2,461	1,987	1,186	1,335	2,536	1,981	797	2,696
Net income (loss)	584	216	(96)	(320)	106	1,716	1,448	716	884
<b>Per Share<sup>3</sup></b>									
Net income (loss) - basic	0.06	0.02	(0.01)	(0.04)	0.01	0.19	0.16	0.08	0.10
Net income (loss) - diluted	0.05	0.02	(0.01)	(0.04)	0.01	0.19	0.02	0.08	0.10

<sup>1</sup> EBITDA is defined in the 'Non-IFRS Measures' section of this MD&A and is a "Non-GAAP Financial Measure" as defined by CSA Staff Notice 52-306.

<sup>2</sup> EBITDA excluding the impact of IFRS 16 - Leases is defined as EBITDA, less lease payments made during the year.

<sup>3</sup> Per-share calculations are based on the weighted average number of shares outstanding during the periods.

## LIQUIDITY AND CAPITAL RESOURCES

### Operating activities

For the three and six months ended June 30, 2021, we used \$0.7 million and \$0.5 million respectively in net cash from operating activities, compared to generating \$3.2 million and \$1.2 million, respectively, in the same period last year.

### Investing Activities

Cash outflows in investing activities for Q2 2021 were \$2.4 million, compared to cash outflows of \$6.5 million in Q2 2020. Cash outflows in investing activities for the first half of 2021 were \$5.0 million compared to cash outflows of \$10.7 million in the same period of 2020. In both years, the majority of our cash outflows were for capital expenditures related to our plant expansion in Delta, BC. In 2021 the investments relate to the development of a second production line in Delta, BC,

### Financing Activities

During the second quarter and first half of 2021, we received proceeds net of repayment from our credit facility, in the amount of \$0.5 million and \$2.7 million, while in the second quarter and first half of 2020 we obtained proceeds net of repayment of \$1.5 million and \$6.8 million, respectively from our credit facility.

# SWISS WATER DECAFFEINATED COFFEE INC.

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## Management Discussion and Analysis

### For the three and six months ended June 30, 2021

In the second quarter of 2021, we concluded a new financing agreement for the expansion of our plant in Delta, BC. Proceeds received from this credit facility were \$4.3 million during the second quarter.

#### Inventory

Our inventory increased in value and volume by 28% and 12% respectively between December 31, 2020 and June 30, 2021. The increase reflects a higher NY'C', combined with higher coffee inventory on hand in the current year.

Under hedge accounting, gains and losses on derivative instruments for coffee to be sold in future periods are recorded in inventory. The hedge accounting component of inventory as at June 30, 2021 was a gain of \$2.4 million compared to a gain of \$1.1 million in the same period of last year.

#### Accounts Receivable

Our accounts receivable increased by \$1.1 million, or 7%, between December 31, 2020 and June 30, 2021 compared to a decrease of \$1.5 million, or 10%, between December 31, 2019 and June 30, 2020. 95% of Swiss Water accounts receivable are current as at June 30, 2021. The majority of the past due amounts as of June 30, 2021 were collected shortly after the quarter end.

#### Credit Facilities and Liquidity

On October 18, 2019, Swiss Water entered into a revolving credit facility agreement ("Credit Facility"), with a Canadian Bank, for borrowings up to the lower of the Borrowing Base and \$30.0 million. The Credit Facility's Borrowing Base margins eligible inventories and accounts receivable, commodity hedging account equity margin plus its market-to-market gains, which are netted against any losses in the commodity account and foreign exchange contract facility. Amounts can be drawn in either Canadian or in US\$ dollars and can be borrowed, repaid, and re-borrowed to fund operations, capital expansions, letters of credit and for general corporate purposes. The maturity date is October 18, 2022, however, we can repay the Credit Facility at any time on or before the maturity date as long as the outstanding balance is not in excess of the borrowing base. The maturity date can be extended, subject to the lenders' approval.

The Credit Facility has multiple interest rate options that are based on the Canadian Prime Rate, Base Rate, LIBO Rate, Bankers' Acceptance Rate plus an acceptance fee, in addition to an Applicable Margin for each of these rates. Fees apply to outstanding letters of credit and the unused portion of the credit. Swiss Water has pledged substantially all of our assets, except for assets pledged to BDC under the Term Loan (see below, Construction Loan).

In addition, as a part of the Credit Facility, we have a US\$8.0 million foreign exchange and commodity futures contract facility, which allows us to enter into spot, forward and other foreign exchange rate transactions with our bank with a maximum term of 60 months.

Our facilities are collateralized by general security agreements over all of the assets of Swiss Water and a floating hypothecation agreement over cash balances.

We have certain bank and creditor covenants that relate to the maintenance of specified financial ratios and we were in compliance with all covenants in the years 2020 and 2021.

#### Construction Loans with BDC and FCC

In Q4 2018, the Company completed a transaction with the Business Development Bank of Canada ("BDC") for a term loan facility ("Term Loan") of up to \$20.0 million. The purpose of the Term Loan was to assist in the financing of new equipment for the first production line built in Delta, British Columbia. The interest rate

# SWISS WATER DECAFFEINATED COFFEE INC.

## Management Discussion and Analysis

### For the three and six months ended June 30, 2021

for the Term Loan was 4.95% per annum over 12 years. Principal repayment began on July 1, 2021 and matures on June 1, 2033.

On June 3, 2021, the Company completed a financing transaction by increasing the existing term to \$45.0 million from the existing \$20.0 million to fund the planned construction of a second production line in its Delta location. The financing was provided by Business Development Corp (“BDC”), our existing creditor, and Farm Credit Canada (“FCC”) in a Pari Passu structure. Each lender will fund 50% of the \$45 million total loan value. Our existing borrowing with BDC will increase from \$20 million to \$22.5 million (“BDC Amended Term Loan”) and FCC will also fund us \$22.5 million (“FCC Term Loan”). Upon closing of the transaction, the Company’s outstanding debt to each party, FCC and BDC, was \$10 million. FCC paid \$10.0 million to BDC on the Company’s behalf to ensure that existing borrowings were restructured on a Pari Passu basis.

Only interest will be paid on the outstanding balance on a monthly basis prior to July 1, 2024 for both the BDC Amended Term Loan and FCC Term Loan. Principal repayments for both loans commence on July 1, 2024 and will be repaid in monthly installments until both loans mature on June 1, 2034.

The FCC Term Loan consists of a fixed term loan and a variable loan. The fixed term loan bears an interest rate of 4.38% and the variable loan bears an interest rate of variable rate minus 0.75%. The interest rate on the variable loan rate is currently 2.95%.

The BDC Amended Term Loan bears an interest rate of 4.45%. The new terms in the BDC Amended Term Loan supersede the terms on the previous agreement.

Both loans are secured by a general security agreement and a first security interest on all existing equipment and machinery plus new equipment and machinery financed with the BDC and FCC construction loans. Seaforth has provided a guarantee for the construction loans to FCC and BDC. As of June 30, 2021, the construction loans amount outstanding was \$24.4 million including interest accrued of \$0.08 million.

### Contractual Obligations

The following table sets forth our contractual obligations and commitments as at June 30, 2021:

(In \$000s) (unaudited)	Total	Less than 1 year	2-3 years	4-5 years	Over 5 years
Long-term debt <sup>1</sup>	\$ 39,388	\$ 81	\$ 15,000	\$ 6,488	\$ 17,819
Financing leases <sup>2</sup>	10,738	2,806	4,131	2,513	1,288
Credit facility <sup>3</sup>	12,895	-	12,895	-	-
Purchase obligations <sup>4</sup>	74,210	72,990	1,220	-	-
Total contractual obligations	\$ 137,231	\$ 75,877	\$ 33,246	\$ 9,001	\$ 19,107

<sup>1</sup> Long-term debt represents the principal amounts of the convertible debenture and construction loan.

<sup>2</sup> Minimum obligations for our finance leases.

<sup>3</sup> Credit facility matures in 2022.

<sup>4</sup> Purchase obligations represent outstanding capital, coffee and natural gas purchase commitments.

Swiss Water leases the following offices, warehouses and equipment:

On August 26, 2016, we signed a lease agreement for a build-to-suit production facility. The lease has an initial term of five years and can be renewed at our option in five-year increments up to a total of 30 years. The lease commenced in July 2018. Under the lease, Swiss Water has multiple options to buy out the lease starting at the end of the second five-year term. The buy-out value will be equal to the fair market value of the property as determined by an appraisal process, subject to specified maximum and minimum values.

# SWISS WATER DECAFFEINATED COFFEE INC.

## Management Discussion and Analysis

### For the three and six months ended June 30, 2021

Seaforth leases a warehouse in Delta and the lease expires in June 2027. The Company has two options to renew the lease for an additional term of five years each.

Swiss Water leases a sales office in France which expires in October 2027.

Swiss Water leases a facility in Burnaby that houses its decaffeination plant and offices. The lease expires in June 2023.

Swiss Water Decaffeinated Coffee Company USA, Inc. leases a sales office in Seattle, Washington, which expires in October 2022.

Seaforth leases a truck. The lease expires in April 2023.

Swiss Water leases various office equipment with expiring dates of October 2024 and January 2025.

### OFF-BALANCE SHEET ARRANGEMENTS

Swiss Water has no off-balance sheet arrangements.

### RELATED PARTY TRANSACTIONS

We provide toll decaffeination services and/or sell finished goods to, and purchase raw material inventory from a company that is related to Swiss Water Director, Roland Veit.

The following table summarizes related party sales and purchases during the periods:

In \$000s (unaudited)	3 months ended June 30		6 months ended June 30	
	2021	2020	2021	2020
Sales	\$ 145	\$ 121	\$ 341	\$ 190
Purchases of raw materials	\$ 1,908	\$ 955	\$ 2,102	\$ 2,215

All transactions were in the normal course of operations and were measured at the fair value of the consideration received or receivable, which was established and agreed to by the related parties. As at June 30, 2021, our accounts receivable balance with this company was six thousand dollars (December 31, 2020: \$0.04 million) while our accounts payable balance with this company was \$1.4 million (December 31, 2020: \$0.3 million).

### RISKS AND UNCERTAINTIES

Cash from operations may fluctuate with the performance of the business, which can be susceptible to a number of risks. These risks may include, but are not limited to, foreign exchange fluctuations, labour relations, coffee prices (notwithstanding hedging programs, as exact hedging correlation is not attainable), the availability of coffee, competition from existing chemical and other natural or chemical free coffee decaffeinator, competition from new entrants with alternate processing methods or agricultural technologies, environmental and regulatory risks, terms of credit agreements, commodity futures losses, ability to maintain organic certification, adequacy of insurance, risks related to information technology, dependence on key personnel, product liability, uncollectable debts, liquidity risk and timing and costs of capital projects including the construction of the second line at the Delta facility and general economic downturns. These risks and how Swiss Water manages them are described in the AIF. The future effect of these risks and uncertainties cannot be quantified or predicted.

Swiss Water's operations may be negatively impacted in the event of a local or global outbreak of disease, such as the novel coronavirus, COVID-19 outbreak pandemic declared in March 2020. A pandemic may impact demand for our products and services and the capability of our supply chains. It may also impact expected

# SWISS WATER DECAFFEINATED COFFEE INC.

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## Management Discussion and Analysis

For the three and six months ended June 30, 2021

credit losses on our amounts due from customers and whether the entity continues to meet the criteria for hedge accounting. For example, if a hedged forecast transaction is no longer highly probable to occur, hedge accounting would be discontinued.

### CHANGES IN ACCOUNTING STANDARDS

The following standard became effective for annual periods beginning on or after January 1, 2021. The adoption of these revised standards by the Company did not have a material impact on its condensed consolidated interim financial statements.

- IFRS 9/ IAS 39 and IFRS 7 relate to interest benchmark reform and has amendments that provide temporary relief from applying specific hedge accounting requirement to hedging relationships directly affected by IBOR reform and that required certain disclosures; IAS 1 and IAS 8 redefined materiality.

There are a number of changes in accounting standards not yet effective. The Company does not anticipate a material impact on its financial statements:

- IFRS 9 Amended to address which fees should be included in the 10% test for derecognition of financial liability.
- IAS 37 Amended to clarify (i) the meaning of “costs to fulfil a contract”, and (ii) that, before a separate provision for an onerous contract is established, an entity recognizes any impairment loss that has occurred on assets used in fulfilling the contract, rather than on assets dedicated to that contract.
- IAS 16 Amended to (i) prohibit an entity from deducting from the cost of an item of PP&E any proceeds received from selling items produced while the entity is preparing the asset for its intended use (for example, the proceeds from selling samples produced when testing a machine to see if it is functioning properly), (ii) clarify that an entity is “testing whether the asset is functioning properly” when it assesses the technical and physical performance of the asset and (iii) require certain related disclosures.
- IAS 12 Amended to require companies to recognize deferred tax on transactions that, on initial recognition, give rise to equal amounts of taxable and deductible temporary differences. Consequential amendment to IFRS 1 to add an exception to retrospective application.

### HEDGE ACCOUNTING

There are risks related to unpredictability over coffee commodity prices and foreign exchange rates. To minimize these risks, we follow our risk management program, which is carried out under two policies approved by the Board of Directors: the Foreign Exchange Risk Management Policy and the Commodity Price Risk Management Policy. With the use of derivative financial instruments, we hedge potential adverse effects on our financial performance and cash flows. Under the risk management program we enter into three types of hedges and each type is discussed below:

- 1) Commodity price risk hedges on coffee purchase commitments and coffee inventory (“commodity hedges”);
- 2) Currency risk hedges related to US\$ denominated future process revenues (“revenue hedges”); and
- 3) Currency risk hedges related to US\$ denominated purchases of green coffee (“purchase hedges”).

# SWISS WATER DECAFFEINATED COFFEE INC.

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## Management Discussion and Analysis

For the three and six months ended June 30, 2021

### Commodity Hedges

When we enter into a purchase commitment to buy green coffee, the contract specifies that the purchase price will be based, in part, on the future (to-be-determined) coffee futures price, or NY'C'. We agree on or 'fix' the NY'C' price with the vendor on or before receiving the coffee into inventory. When we bear the economic risk of a change in the commodity price, we offset this risk by selling short a futures contract on the Intercontinental Exchange. When we later sell such coffee at a fixed price to a customer, we cover our short by going long on a futures contract on the Intercontinental Exchange.

At each period-end, commodity hedges are re-measured to their fair value. Under hedge accounting, gains/losses for hedged coffee purchase commitments and inventory are recorded in the statement of financial position until such coffee is sold, at which time the gains/losses on our commodity hedges are recognized in cost of sales. In this way, gains/losses on our commodity hedges are matched to our sales in the period.

### Revenue Hedges

We enter into forward contracts to sell US\$ at future dates to hedge the foreign exchange cash flow variability of expected US\$ processing fee revenue up to 60 months in advance. The hedged process revenue includes both process revenue from tolling arrangements (processing of customer-owned coffee) as well as the US\$ processing fee layer of inventory sales agreements. This enables us to more reliably predict how much Canadian currency we will receive for our US\$ process revenue. Cash flows in the immediate 12-month period are hedged at a higher percentage of expected future revenues than those farther out, reflecting greater uncertainty in the 13-to 60-month period.

At each period end, revenue hedges are re-measured to their fair value. Under hedge accounting, unrealized gains/losses for open revenue hedges are recorded in other comprehensive income. When a revenue hedge matures, the realized gain/loss on that contract is reclassified from accumulated other comprehensive income to process revenue.

### Purchase Hedges

We enter into forward contracts to buy US\$ for green coffee inventory which, once decaffeinated, will be sold at a fixed C\$ price pursuant to a customer-specific contract. To mitigate the exposure to margin changes on these transactions arising from fluctuations in the US\$/C\$ exchange rate, we enter into US\$ forward purchase contracts which economically lock in the US\$/C\$ exchange rate, and effectively locks in the C\$ cost of inventory to be sold at the fixed C\$ amount.

The hedge accounting allows for matching of US\$ purchases with the associated gains/losses on the forward contracts used to economically hedge these items. At each period-end, customer-specific hedges are re-measured to their fair value. Under hedge accounting, the gains/losses on these hedges are deferred on the statement of financial position until the inventory is sold, at which time the gains/losses are recorded in the cost of sales on the income statement.

## FINANCIAL INSTRUMENTS

We use financial instruments to mitigate economic risks associated with our business. The three types of hedges we enter into, and the hedging instruments used, are discussed in more detail under 'Hedge Accounting' above.

We classify our financial assets and financial liabilities in the following measurement categories (i) those to be measured subsequently at fair value (either through other comprehensive income or through profit or

# SWISS WATER DECAFFEINATED COFFEE INC.

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## Management Discussion and Analysis

For the three and six months ended June 30, 2021

loss); and (ii) those to be measured at amortized cost. We have implemented the following classifications for financial instruments other than derivatives:

- Cash and cash equivalents and short-term investments are classified as assets at fair value and any period change in fair value is recorded through interest income in the consolidated statement of income, as applicable.
- Accounts receivable and other receivables are classified as assets at amortized cost using the effective interest rate method. Interest income is recorded in the consolidated statement of income, as applicable.
- Accounts payable, credit facilities, the debt portion of the convertible debenture and other liabilities are classified as other financial liabilities and are measured at amortized cost using the effective interest rate method. Interest expense is recorded in the consolidated statement of income, as applicable.

### Commodity Price Risk

Commodity price risk is the risk that the fair value of inventory or future cash flows will fluctuate as a result of changes in commodity prices. The Company utilizes futures contracts to manage its commodity price exposure. The Company buys and sells futures contracts for coffee on the Intercontinental Exchange in order to offset its inventory position and fix the input cost of green coffee. As at June 30, 2021, the Company had futures contracts to buy 12.5 million lbs of green coffee with a notional value of US \$19.3 million, and contracts to sell 18.5 million lbs of green coffee with a notional value of US\$28.5 million. The furthest contract matures in December 2021. (December 31, 2020: buy 2.5 million lbs of green coffee with a notional value of US\$3.0 million, and contracts to sell 6.6 million lbs of green coffee with a notional value of US\$7.9 million).

### Foreign Currency Risk

We realize a significant portion of our revenues in US\$ and we purchase green coffee in US\$ which is, in some cases, sold to customers in Canadian dollars. The Company enters into forward foreign currency contracts to manage its exposure to currency rate fluctuations and to minimize the effect of exchange rate fluctuations on business decisions.

As at June 30, 2021, the Company had forward currency contracts to buy US\$9.6 million and sell US\$46.5 million (December 31, 2020: buy US\$5.6 million and sell US\$51.0 million) from July 2021 through to February 2025 at various Canadian exchange rates ranging from \$1.2090 to \$1.3626.

### SUBSEQUENT EVENT

On July 20, 2021, we amended our convertible debenture agreement with Mill Road. Under the new terms of the agreement, the maturity date was extended by one year from October 31, 2023 to October 31, 2024. Other amended terms were: (i) increase the maximum current interest rate from 7.85% to 9%, (ii) provide an additional 1.5% “payment in kind” interest, (iii) amend the conversion feature by (A) cancelling the existing conversion feature and (B) replacing the existing conversion feature with warrants to allow Mill Road to purchase up to 2.25 million common shares at a price of \$3.33 per share. The warrants expire on October 31, 2024.

Under IFRS 9, the accounting for the transaction depends on whether the debt restructuring is considered an extinguishment or an adjustment to the existing liability (“extinguishment accounting” vs “modification accounting”).

# SWISS WATER DECAFFEINATED COFFEE INC.

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## Management Discussion and Analysis

For the three and six months ended June 30, 2021

We have determined that this modification should be considered an extinguishment as the terms of the agreement are substantially different given as there is a 2.15% change in the interest rate and a replacement of the conversion shares with warrants.

In Q3 2021, the warrants will be recorded as a component of equity as it will be settled by the exchange of a fixed amount of cash for a fixed number of the Company's equity and will not be subsequently remeasured. The warrants will be valued using the Black Scholes model.

Subsequent to the end of Q2 2021, we received final building permits and in July 2021 we formally initiated the construction of our second production line at our Delta, BC production facility.

## INTERNAL CONTROLS OVER FINANCIAL REPORTING & DISCLOSURE CONTROLS AND PROCEDURES

The Chief Executive Officer ("CEO") and the Chief Financial Officer ("CFO") of Swiss Water are responsible for establishing and maintaining adequate internal control over financial reporting ("ICFR") to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS. Under the supervision and with the participation of management, we conducted an evaluation of the design and effectiveness of our ICFR as of June 30, 2021, based on the updated framework issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO 2013"). Based on this assessment, the CEO and CFO concluded that, as of June 30, 2021, Swiss Water's ICFR was effective.

The CEO and CFO are also responsible for establishing and maintaining adequate disclosure controls and procedures. Disclosure controls and procedures are controls and other procedures designed to provide reasonable assurance that information required to be disclosed in documents filed or submitted under securities legislation is recorded, processed, summarized and reported within the time periods specified in securities legislation and includes controls and procedures designed to ensure that information required to be disclosed in documents filed or submitted under securities legislation is accumulated and communicated to Swiss Water's management, including the CEO and CFO, as appropriate to allow timely decisions regarding required disclosure.

The CEO and CFO evaluated or caused to be evaluated under supervision, the effectiveness of our disclosure controls and procedures and based on this evaluation, the CEO and CFO concluded that, as of June 30, 2021, Swiss Water's disclosure controls and procedures were effective. There were no changes in our ICFR that occurred during the period beginning on January 1, 2021 and ended on June 30, 2021 that have materially affected or are reasonably likely to materially affect, Swiss Water's ICFR.