

# SWISS WATER DECAFFEINATED COFFEE INC.

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## Management Discussion and Analysis

For the three and nine months ended September 30, 2020

### 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 November 5, 2020, provides a review of the financial results for the three and nine months ended September 30, 2020 relative to the comparable period of 2019. The three month period represents the third quarter ("Q3") of our 2020 fiscal year. This MD&A should be read in conjunction with Swiss Water's condensed consolidated interim financial statements for the three and nine months ended September 30, 2020, the audited consolidated financial statements for the year ended December 31, 2019 and the Annual Information Form, 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 production facility and 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 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; and (vi) the expected level of dividends payable to shareholders; (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 nine months ended September 30, 2020, Swiss Water's revenues increased by 5% and 1% respectively. Despite the ongoing impact of the COVID-19 pandemic, volume is only 1% down versus Q3 2019. Year-to-date volume continues to recover and is now only 6% lower than last year. In the first three months of 2020, our volumes were negatively affected by an increase in commodity futures prices for coffee in late 2019. The negative impact of this persisted through the first quarter. Since then, volumes have recovered more strongly than expected in this COVID environment, and this performance is largely a reflection of our well-diversified customer base.

The primary change in Swiss Water's business following the emergence of the COVID-19 pandemic has been customer mix. Our large commercial roasters and specialty roasters with a grocery presence continue to drive our volume. 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 and third quarter, grocery demand continued but at a slower pace than when the pandemic started. Shuttered restaurants and out-of-home specialty coffee shops started to reopen toward the end of the second quarter, and this trend has partially contributed to our volume recovery in the third quarter.

In Q3 2020, Swiss Water's gross profit, operating income and net income all decreased versus Q3 2019. The main drivers of this change were, higher green coffee prices, the timing of marketing expenditure and increased depreciation charges following the commissioning of our new Delta manufacturing facility. Year-to-date gross profit, operating income and net income have all increased from the comparable period in 2019.

Swiss Water is currently well positioned with green coffee inventory and will be able to support short-term demand increases as trading conditions normalize. 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 return to pre-pandemic levels.

In \$000s except per share amounts (unaudited)	3 months ended September 30		9 months ended September 30	
	2020	2019	2020	2019
Sales	\$ 24,862	\$ 23,645	\$ 73,059	\$ 72,207
Gross profit	3,431	4,737	12,791	12,388
Operating income	606	2,291	5,011	4,623
Net income	106	884	3,269	2,228
EBITDA <sup>1</sup>	2,036	3,485	7,870	8,894
EBITDA excluding IFRS 16-Leases <sup>2</sup>	1,335	2,696	5,853	6,545
Net income per share – basic <sup>3</sup>	\$ 0.01	\$ 0.10	\$ 0.36	\$ 0.25
Net income per share – diluted <sup>3</sup>	\$ 0.01	\$ 0.10	\$ 0.25	\$ 0.25

<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 third quarter and the nine months ended September 30, 2020 declined by 1% and 6%, respectively, compared to the same periods in 2019. Although we have been negatively impacted by the pandemic, our volumes have proven to be more resilient than we originally anticipated.
- Our largest geographical market by volume in Q3 continued to be the United States, followed by Canada, Europe and other international markets. By dollar value, for the nine month period ended September 30, 2020, 50% of our sales were to customers in the United States, 30% were to Canada, and the remaining 20% were to other countries. Our international business continues to expand and we anticipate revenues from our European and Asia-Pacific markets will increase in both dollar and percentage terms.
- Swiss Water's operations have been deemed essential services during the Pandemic, and as such, we have maintained our best efforts to supply decaffeinated coffee to food manufacturers and retailers who are supporting consumers around the world. During these unprecedented times, Swiss Water has remained committed to continuing our decaffeination process and operations, while prioritizing safety for our customers, vendors and employees. To protect our stakeholders, we have implemented best health practices and social distancing in our production facilities, warehouses and offices as recommended by the appropriate health authorities. To date, no positive cases of COVID-19 have been recorded within our workforce.
- In September, we successfully completed the first production run of commercial-grade coffee from our Delta, B.C. facility. This marked the final step in the startup of the initial processing line at our new, technically advanced decaffeination facility and the culmination of a three-year effort to develop additional capacity to service the growing demand for our sustainably sourced, chemical free decaffeinated coffees.

### Financial highlights

- Quarterly revenue increased by 5% over Q3 2019 to \$24.9 million. Revenues have remained strong, despite the decline in volumes. This is due to the positive impact of customer mix that has resulted in higher process revenue, as well as an increase in the coffee futures price and slightly higher distribution revenue. Nine month revenue remained relatively flat, increasing by 1% to \$73.1 million.
- Gross profit for Q3 of this year was \$3.4 million, a decrease of \$1.3 million from the Q3 2019 level. Our Q3 2020 gross profit was negatively affected by a weakening in coffee quality differential gains and by increased depreciation charges following the completion and commissioning of our new manufacturing facility in Delta BC. For the first nine months of 2020, gross profit increased by \$0.4 million to \$12.8 million. The year-to-date improvement was driven by positive customer sales mix, stronger coffee quality differential gains, improved supply chain efficiencies and lower natural gas costs during the first half of this year.
- Third quarter operating expenses were \$2.8 million, an increase of \$0.4 million compared to Q3 2019. Nine month operating expenses of \$7.8 million were comparable to the same period last year. The increase in Q3 expenses was driven by a combination of the difference in timing of marketing expenditure in one period over the next, higher professional fees and the inclusion of engineering salaries. In Q3 2019, during the construction of our Delta manufacturing facility, engineering salaries were capitalized. The higher quarterly expenses this year were partially offset by lower than expected travel and recruitment fees, while nine month expenses were reduced by a recovery of stock-based compensation costs during

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the first half. We continue to pursue margin improvements across our operations and are also focused on seeking variable and fixed cost reduction opportunities without sacrificing the quality of our product.

- Q3 operating income was \$0.6 million, compared to \$2.3 million in the same period last year. For the first nine months of 2020, operating income increased to \$5.0 million from \$4.6 million in the same period last year.
- Third quarter net income was \$0.1 million compared to \$0.9 million in Q3 2019. Nine month net income was \$3.3 million, compared to \$2.2 million last year. The year-over-year difference in net income in both periods reflects the combination of changes in gross profit, and both operating and non-operating expenses. This year non-operating expense was reduced by the revaluation of an embedded derivative as a result of Swiss Water's lower share price, offset by a slight loss on risk management activities.
- EBITDA decreased by \$1.4 million, or 42%, to \$2.0 million in the third quarter, and by \$1.0 million, or 12%, to \$7.9 million for the first nine months, when compared to the same periods in 2019. EBITDA, excluding the impact of IFRS 16, decreased by \$1.4 million, or 50%, to \$1.3 million in Q3, and by \$0.7 million, or 11%, to \$5.9 million for the first nine months of this year, compared to the same periods in 2019. The adverse movement in quarterly EBITDA was expected. It reflects a softening of coffee quality differential gains. Furthermore, the difference in timing of marketing and overhead spend negatively impacted quarterly performance. On a year-to-date basis, the coffee quality differential margin has made a positive contribution to EBITDA, despite pulling back somewhat during Q3. However, this positive contribution has been more than offset with marketing investments and changes in the timing of overhead spend when compared to last year. Marketing and overhead expenditure are tracking in line with budgeted targets for 2020.

## OUTLOOK

The Company is limiting guidance for the 2020 fiscal year due to the 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. Meanwhile, customers who serve the out-of-home coffee market through cafes and restaurants have been much more susceptible to serious disruption as health authorities around the world have declared widespread or targeted food-service shutdowns to combat upsurges in the number of COVID-19 cases. Despite this turbulence, some coffee outlets have stayed open throughout the pandemic to service take-away customers, and others have good drive-through services available. In May and June, many countries lifted their lockdowns and the out-of-home channel began to recover. However, many countries and regions have now started to experience a second wave of COVID-19 and have re-initiated lockdowns. These include a number of states and major cities in the USA, which is our largest geographical segment. Given the uncertainty on the timing of when a vaccine will be developed, we cannot reliably predict the ultimate impact the COVID-19 pandemic will have on our business, particularly our business with the out-of-home coffee market. Accordingly, the risk remains that Swiss Water will report an overall volume decline in 2020. However, we are cautiously optimistic that, after a stronger than expected Q2 and Q3, our volumes have shown good resiliency and may continue to recover faster than we originally anticipated following the sharp drop in Q1 2020.

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Operationally, Swiss Water has continued to run both Burnaby production lines on a 24/7 basis. In September, we announced the completion of our first production run of commercial-grade coffee from our Delta, B.C. facility.

Both Swiss Water and Seaforth have stayed open and fully resourced to supply customers since the beginning of the pandemic. From the outset of the pandemic, we have taken precautions within each of our operating sites to ensure appropriate personal protective equipment has been available to employees and contractors, and that ongoing deep cleaning by internal and third-party suppliers have been performed with increased frequency. During the early stages of the pandemic, we initiated a brief shutdown of one of our operating lines to mitigate the possible risk of a province-wide work stoppage. During this period, we took the opportunity to complete scheduled maintenance on this line, and it was quickly brought back into service when this was completed.

As noted previously, in Q2 of this year, the landlord of our Burnaby manufacturing site provided formal notice that our lease would not be extended beyond June 2023. Accordingly, we are in the process of planning for the construction of an additional production facility, including a second production line, at our Delta location with a targeted completion date 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 facility 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. We are now in the process of formulating financing plans for the project.

## 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's shares trade on the Toronto Stock Exchange under the symbol 'SWP'. As at the date of this report, 9,078,780 shares were issued and outstanding.

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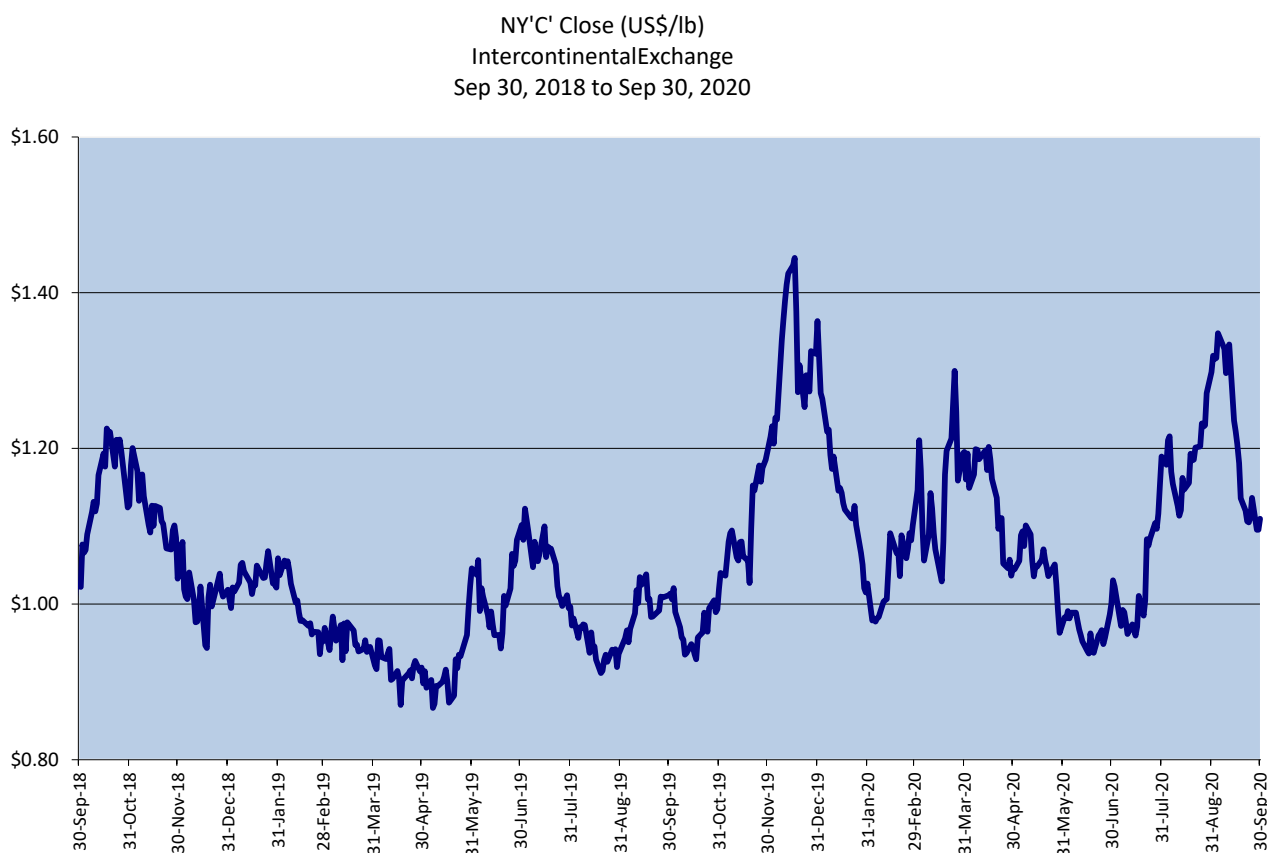
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### Swiss Water Decaffeinated Coffee Company's Business

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.

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:



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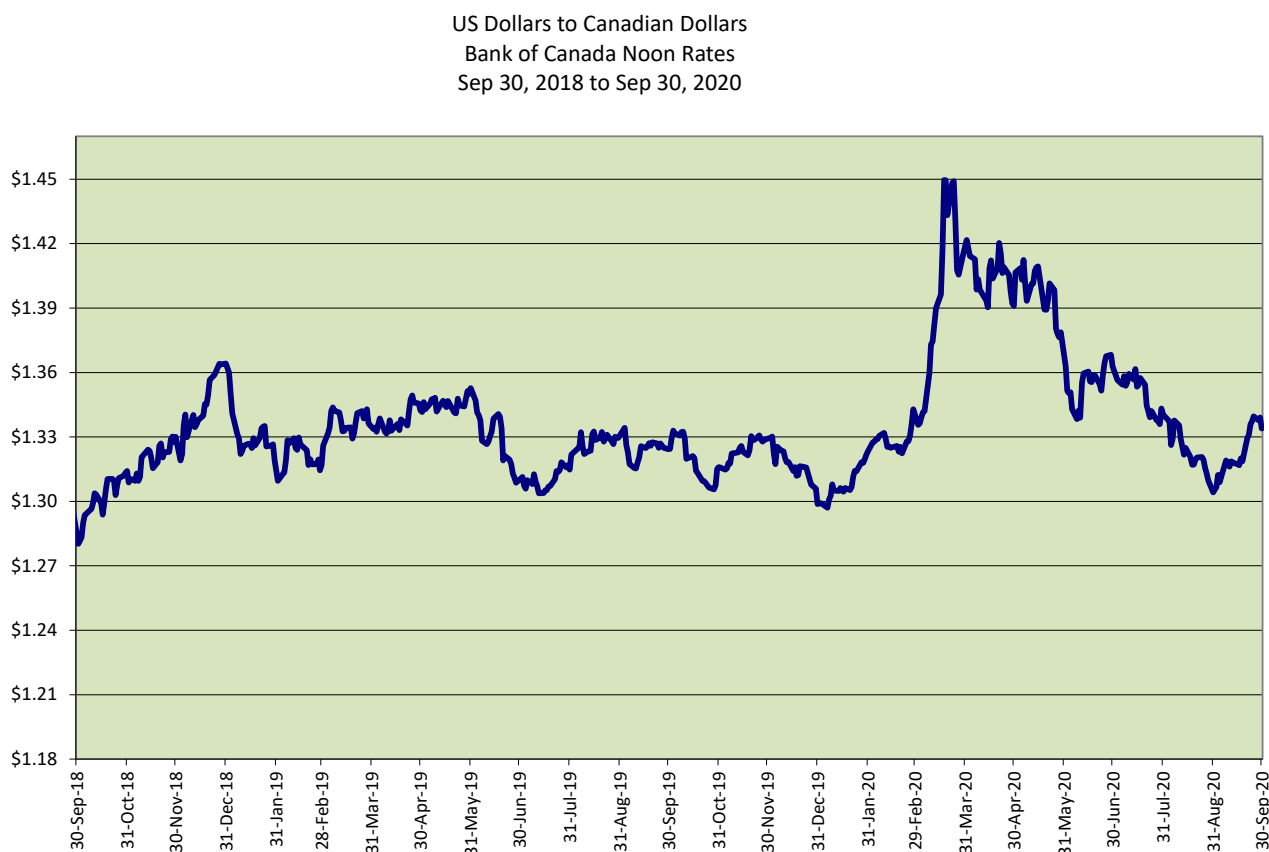
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In Q3 2020, the NY'C' averaged US\$1.14/lbs compared to an average of US\$1.00/lbs in Q3 2019. The rise and fall of the NY'C' affects our volume of shipments, our revenues and our cost of sales. In an upward trending market, our customers tend to consume their inventories rather than build them. When the NY'C' declines over a sustained period, our customers tend to add to their inventories and vice versa.

The majority of our 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. 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 Q3 2020, the US\$ averaged C\$1.3321, an increase of 0.9% over the same period in 2019. 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

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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 compared one period to period, shipments to roasters are more stable when compared to shipments to importers.

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 September 30		9 months ended September 30	
	2020	2019	2020	2019
Process revenue	\$ 6,613	\$ 6,558	\$ 19,353	\$ 19,905
Green revenue	16,427	15,290	48,348	46,769
Distribution revenue	1,822	1,797	5,358	5,533
Total revenue	\$ 24,862	\$ 23,645	\$ 73,059	\$ 72,207

For the quarter ended September 30, 2020, sales totaled \$24.9 million, an increase of \$1.2 million, or 5%, compared to the same quarter in 2019 driven by the impact of an increase in the New York Arabica Futures market and increase in process revenue rates. Sales for the first nine months of 2020 totaled \$73.1 million, an increase of \$0.9 million, or 1%, over the same period last year.

Our sales in the third quarter and first nine months of 2020 by revenue category are as follows:

- Process revenue remained flat at \$6.6 million even though our processing volumes declined by 1%. Year-to-date process revenue declined by \$0.6 million or 3% to \$19.4 million which is represented by a decrease in year-to-date volumes of 6%.
- Green revenue increased by \$1.1 million, or 7% in Q3 2020 to \$16.4 million in Q3 2020 and by \$1.6 million of 3% to \$48.3 million in the first nine months of 2020. The increase was driven by a sustained increase in coffee quality differentials in relationship to our existing inventory generating a positive short-term gain.
- Distribution revenue remained flat at \$1.8 million in Q3 2020 and was slightly lower by \$0.2 million, or 3% in the first nine months of 2020. Decreased distribution revenue has been driven by lower shipment volumes and disruption in the coffee supply chain following the emergence of COVID-19. However, volumes appeared to be returning to normal levels by the end of Q3.

Sales volumes by geographical segments have been negatively impacted by the appreciation of coffee futures prices through Q1 2020, and later by the uncertainty generated by the COVID-19 pandemic for Q2 and Q3 2020. Sales volumes in the third quarter of 2020 by geographical segment are as follows:

- Sales volume in North America decreased by 1% in Q3 2020 and by 7% in the nine months of the year.
- Sales volume in Europe increased by 12% in Q3 2020 and decreased by 14% in the nine months of the year.



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- Sales volume in the Asia Pacific decreased by 4% in Q3 2020 and increased by 3% in the nine months of the year.

### Cost of Sales

Cost of sales includes the cost of green coffee purchased for our regular business, 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.

Our third quarter cost of sales increased by \$2.5 million, or 13%, to \$21.4 million compared to the same period in 2019, driven by an increase in the cost of green coffee. In addition, we started depreciating our Delta manufacturing facility. As a result the depreciation expense increased by \$0.4 million in the quarter. Cost of sales increased by \$0.4 million, or 1% to \$60.3 million in the first nine months of 2020. The slight increase during the first nine months of 2020 is reflective of operating activities during this period.

### Gross Profit

Gross profit decreased by \$1.3 million or 28% to \$3.4 million for the third quarter of 2020 and by \$0.4 million or 3% to \$12.8 million for the first nine months of the year. These results were impacted by revenue growth, short-term differential margin losses, higher depreciation expense, improved supply chain efficiencies including consolidating our Seaforth warehouses, and lower natural gas costs.

### 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 increased by 17% to \$1.7 million and for the first nine months of the year, decreased to \$4.7 million or by 8%. The increase during the quarter was driven by a combination of higher professional fees, general inflation and the inclusion of engineering salaries that were capitalized in Q3 2019 during the construction of our Delta manufacturing facility. The year-to-date decrease is largely due to cost recovery of share-based compensation, which is based on Swiss Water's share price. During the first nine months of 2020, our share price dropped. This resulted in an estimated stock-based compensation cost recovery whereas, in 2019, an expense was recorded. Administration expenses were also lower due to reduced travel costs and less recruiting activities.

### Sales and Marketing Expenses

Sales and marketing expenses include compensation and other personnel-related expenses for sales and marketing staff, consumer and trade advertising and promotion costs, as well as related travel expenses.

Sales and marketing expenses increased by \$0.1 million or 14% to \$1.1 million for the quarter and increased by \$0.4 million or 16% to \$3.0 million year-to-date. The increase was driven by timing differences in advertising and marketing campaign activities.

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### Occupancy Expenses

Occupancy expenses include the cost of renting offices for sales, marketing and administrative use. Occupancy costs for the first quarter were largely unchanged from the prior year.

### 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 bank debts, other borrowings, the accretion expense on our asset retirement obligation, interest expense on the convertible debenture and interest expense on finance leases.

Net finance expenses for the third quarter of 2020 increased by \$0.1 million or 16% to \$0.7 million compared to the same period in 2019. Net finance expenses increased by \$0.04 million or by 2% to \$1.7 million for the first nine months of 2020. The interest expenses on a convertible debenture, credit facility and on finance leases, due to the adoption of IFRS 16 in 2019, accounted for the majority of the change.

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.

The adoption of IFRS 16 Leases in 2019 resulted in interest expenses of \$0.3 million in Q3 2020, and \$0.9 million for the nine months ended September 30, 2020. Interest expense was the same in 2019 for both comparative periods.

During the construction phase of our Delta facility, interest expense related to the construction loan and related lease liability was capitalized in property plant and equipment.

### 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', above). Thus, 'Gain 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 third quarter of 2020 we recorded a slight gain of \$0.1 million compared to a loss of \$0.1 million for the same period in 2019, For the nine months ended September 30, 2020 we recorded a loss of \$0.2 million compared to gains of \$1.1 million for the same period in 2019, these gains and losses correspond with fluctuations in the foreign exchange rates and the coffee prices on NY'C'.

### 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 slight gain of \$0.1 million and a gain of \$1.4 million in the third quarter and first nine months of 2020, respectively, compared to a loss of \$0.2 million and a loss of \$0.8 million, respectively, in the same periods of last year. The fluctuations are due to Swiss Water's share

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price and risk-free interest rate that are used as inputs in the Black Scholes model. During the year, our share price and risk-free interest rate dropped.

### 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 third quarter of 2020, we recorded a gain on foreign exchange of \$0.3 million, compared to a loss of \$0.1 million in the same period last year. In the first nine months of the year, we recorded a gain on foreign exchange of \$0.1 million, compared to a loss of \$0.2 million in the same period last year.

### Income before Taxes and Net Income

In the third quarter and first nine months of 2020, we recorded income before taxes of \$0.4 million and \$4.7 million, respectively, compared to \$1.3 million and \$3.1 million in the comparable periods in 2019. Current and deferred income tax expenses decreased our net income by \$0.3 million for the quarter, compared to a net income tax expense of \$0.4 million in Q3 2019. For the first nine months ended September 30, 2020 and 2019, income taxes reduced our net income by \$1.4 million and \$0.9 million 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 are offset by the tax benefit of loss carry forwards recognized. Overall, we recorded a net income of \$0.1 million in Q3 2020 and \$3.3 million for the first nine months of 2020, compared to a net income of \$0.9 million and \$2.2 million respectively in the same periods last year.

### Other Comprehensive Income

Gains or losses on our designated revenue hedges that will mature in a future period are recorded in other comprehensive income, net of income tax expense. Other comprehensive income, net of tax, for the three months and nine months ended September 30, 2020 was a gain of \$1.0 million and a loss of \$0.5 million, compared to a loss of \$0.5 million and a gain of \$1.2 million in the same periods of 2019. The 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 September 30, 2020 and 2019, potential common shares issuable under the RSU Plan and common shares issuable for the convertible debenture are anti-dilutive and excluded from the dilution calculation.

# SWISS WATER DECAFFEINATED COFFEE INC.

## Management Discussion and Analysis

### For the three and nine months ended September 30, 2020

For the nine months period ended September 30, 2020, all potential common shares issuable were dilutive, hence included in the dilution calculation. For the same period in 2019, all potential common shares issuable were anti-dilutive, therefore excluded from the calculation.

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

In 000s except for shares and per share data (unaudited)	3 months ended September 30		9 months ended September 30	
	2020	2019	2020	2019
<b>Basic earnings per share</b>				
Net income attributable to shareholders	\$ 106	\$ 884	\$ 3,269	\$ 2,228
Weighted average number of shares	9,078,780	9,061,210	9,075,317	9,061,210
Basic earnings per share	\$ 0.01	\$ 0.10	\$ 0.36	\$ 0.25
<b>Diluted earnings per share</b>				
Net income attributable to shareholders	106	884	3,269	2,228
Effect of diluted securities: RSUs	-	-	52	-
Interest on convertible debenture	-	-	853	-
Gain on fair value adjustment of the embedded	-	-	(1,400)	-
Net income after effect of diluted securities	\$ 106	\$ 884	\$ 2,774	\$ 2,228
Weighted average number of shares – basic	9,078,780	9,061,210	9,075,317	9,061,210
Effect of diluted securities: RSUs	-	-	234,994	-
Effect of diluted securities: convertible	-	-	1,818,182	-
Weighted average number of shares - diluted	9,078,780	9,061,210	11,128,493	9,061,210
Diluted earnings per share	\$ 0.01	\$ 0.10	\$ 0.25	\$ 0.25

### 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 Q3 2020 was \$2.0 million, down by 42% compared to Q3 2019. EBITDA excluding the effect of IFRS 16 for the three months ended September 30, 2020 was \$1.3 million, down by 50% compared to Q3 2019. EBITDA for the first nine months of 2020 was \$7.9 million, down by 12% compared to the same period in 2019. EBITDA excluding the effect of IFRS 16 for the nine months ended September 30, 2020 was \$5.9 million, down by 11% compared to the same period in 2019. Operationally, the change in EBITDA was driven by revenue growth, successful efforts across the Company to enhance cost recovery, an increased financial contribution from Seaforth and lower costs for natural gas. These gains were offset by lower sales volumes, increase in green coffee costs and annual increases in labour costs.

# SWISS WATER DECAFFEINATED COFFEE INC.

## Management Discussion and Analysis

For the three and nine months ended September 30, 2020

The reconciliation of net income to EBITDA is as follows:

In \$000s (unaudited)	3 months ended September 30		9 months ended September 30	
	2020	2019	2020	2019
Income for the period	\$ 106	\$ 884	\$ 3,269	\$ 2,228
Income taxes	267	440	1,381	866
Income before tax	\$ 373	\$ 1,324	\$ 4,650	\$ 3,094
Finance income	(169)	(108)	(370)	(377)
Finance expenses	851	698	2,026	1,996
Depreciation & amortization	1,325	914	3,024	2,893
Unrealized (gain) loss on foreign exchange forward contracts	(70)	195	323	(343)
Fair value (gain) loss on the embedded option	(50)	186	(1,400)	758
(Gain) loss on foreign exchange	(320)	59	(62)	235
Share-based compensation (recovery) expense	96	217	(321)	638
EBITDA	\$ 2,036	\$ 3,485	\$ 7,870	\$ 8,894
Impact of IFRS 16, which was adopted in the year 2019	(701)	(789)	(2,017)	(2,349)
EBITDA excluding the impact of IFRS 16	\$ 1,335	\$ 2,696	\$ 5,853	\$ 6,545

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 September 30		9 months ended September 30	
	2020	2019	2020	2019
Operating income for the period	\$ 606	\$ 2,291	\$ 5,011	\$ 4,623
Depreciation & amortization	1,325	914	3,024	2,893
Share-based compensation	96	217	(321)	638
Gain (loss) on risk management activities	79	(132)	(167)	1,083
Unrealized (loss) gain on foreign exchange forward contracts	(70)	195	323	(343)
EBITDA	\$ 2,036	\$ 3,485	\$ 7,870	\$ 8,894
Impact of IFRS 16, which was adopted in the year 2019	(701)	(789)	(2,017)	(2,349)
EBITDA excluding the impact of IFRS 16	\$ 1,335	\$ 2,696	\$ 5,853	\$ 6,545

## QUARTERLY INFORMATION / SEASONALITY

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-quarters:

In \$000s except for per share amounts (unaudited)	8 Quarter Average	Q3 2020	Q2 2020	Q1 2020	Q4 2019	Q3 2019	Q2 2019	Q1 2019	Q4 2018
Sales	24,159	24,862	26,380	21,817	25,023	23,645	24,392	24,170	22,979
Gross profit	4,121	3,431	5,154	4,206	4,106	4,737	4,106	3,544	3,686
Operating income	1,474	606	2,370	2,035	539	2,291	1,356	976	1,618
EBITDA <sup>1</sup>	2,534	2,036	3,194	2,640	1,454	3,485	3,097	2,312	2,050
EBITDA excluding IFRS 16 <sup>2</sup>	1,906	1,335	2,536	1,981	797	2,696	2,278	1,573	2,050
Net income (loss)	892	106	1,716	1,448	716	884	1,353	(9)	919
<b>Per Share<sup>3</sup></b>									
Net income - basic	0.10	0.01	0.19	0.16	0.08	0.10	0.15	-	0.10
Net income- diluted	0.07	0.01	0.19	0.02	0.08	0.10	0.14	-	0.03

<sup>1</sup> EBITDA is defined in the section on 'Non-IFRS Financial Measures' along with details of its calculation.

# SWISS WATER DECAFFEINATED COFFEE INC.

## Management Discussion and Analysis

### For the three and nine months ended September 30, 2020

<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 period.

There is an element of seasonality in our business, in that the second half of the year tends to have higher volumes and revenues.

### 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 one of Swiss Water's Directors, Roland Veit.

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

In \$000s (unaudited)	3 months ended September 30		9 months ended September 30	
	2020	2019	2020	2019
Sales	\$ 90	\$ 320	\$ 280	\$ 587
Purchases of raw materials	\$ 688	\$ 1,235	\$ 2,903	\$ 2,910

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 September 30, 2020, our accounts receivable balance with this company was \$0.01 million (December 31, 2019: \$0.01 million) while our accounts payable balance with this company was \$0.4 million (December 31, 2019: \$0.5 million).

On March 16, 2017, a subsidiary of Swiss Water and a member of Key Management (the borrower) entered into a promissory note in the amount of US\$0.1 million. For as long as the borrower remains an employee, the obligation to repay the principal is forgiven against current and future awards under the RSU Plan, by forfeiture of awards. The loan is interest-free other than in the event of default, in which case the promissory note shall bear simple interest at a rate of 10% per annum.

### LIQUIDITY AND CAPITAL RESOURCES

#### Operating activities

For the three and nine months ended September 30, 2020, we generated net cash of zero and \$1.1 million respectively in net cash from operating activities, compared to generating \$6.1 million and \$6.3 million, respectively, in the same period last year.

#### Inventory

Our inventory increased in value by 3% and in volume by 3% between December 31, 2019 and September 30, 2020. The increase reflects additions to raw materials inventory and finished goods.

Under hedge accounting, gains/losses on derivative instruments for coffee to be sold in future periods are recorded in inventory. The hedge accounting component of inventory, as at September 30, 2020 and 2019 was a gain of \$0.1 million.

#### Accounts Receivable

Our accounts receivable increased by \$2.2 million, or 15%, between December 31, 2019 and September 30, 2020 compared to a decrease of \$0.2 million, or 1%, between December 31, 2018 and September 30, 2019. 93% of Swiss Water accounts receivable are current as at September 30, 2020.

# SWISS WATER DECAFFEINATED COFFEE INC.

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## Management Discussion and Analysis

For the three and nine months ended September 30, 2020

### Investing Activities

Cash outflows in investing activities for Q3 2020 were \$1.5 million, compared to cash outflows of \$5.4 million in Q3 2019. Cash outflows in investing activities for the first nine months of 2020 were \$12.1 million compared to cash outflows of \$14.1 million in the same period of 2019. In both years, the majority of our cash outflows were for capital expenditures related to our plant expansion in Delta, BC.

### Financing Activities

No dividends were paid for the nine months ended September 30, 2020. In the comparable period of 2019, Swiss Water paid \$1.7 million in dividends to the shareholders. During the third quarter and first nine months of 2020, we received proceeds from our credit facility, in the amount of \$1.3 million and \$11.4 million, while in the same periods of 2019 we obtained \$1.4 million and \$8.6 million, respectively from our construction loan. During the first nine months of 2020, we repaid funds of \$3.3 million to our credit facility. The funds drawn during the first nine months of 2020 were mainly used to settle costs relating to our new plant in Delta, and support working capital management following the emergence of the COVID-19 pandemic.

### 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 covenants that relate to the maintenance of specified financial ratios and we were in compliance with all covenants as at September 30, 2020.

### Foreign exchange facility guarantee

On June 1, 2020, Swiss Water entered into a foreign exchange facility guarantee to cover margin requirements in relation to our foreign exchange facility. On August 4, 2020, Swiss Water’s Credit Facility Lender amended the credit agreement to recognize the foreign exchange facility guarantee provided by the third party. The

# SWISS WATER DECAFFEINATED COFFEE INC.

## Management Discussion and Analysis

For the three and nine months ended September 30, 2020

facility guarantees a maximum aggregate liability of up to \$6.0 million and it is valid until May 31, 2021. This guarantee provides additional borrowing capacity within the referenced credit facility.

### Contractual Obligations

The following table outlines our contractual obligations and commitments as at September 30, 2020:

In \$000s (unaudited)	Total	Less than 1 year	2-3 years	4-5 years	Over 5 years
Long-term debt <sup>1</sup>	\$ 35,081	\$ 499	\$ 3,333	\$ 18,333	\$ 12,916
Lease liabilities <sup>2</sup>	12,971	2,807	5,303	2,483	2,378
Credit facility <sup>3</sup>	11,782	-	11,782	-	-
Purchase obligations <sup>4</sup>	31,374	31,319	55	-	-
Total contractual obligations	\$ 91,208	\$ 34,625	\$ 20,473	\$ 20,816	\$ 15,294

<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> The 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 leases a facility that houses our Burnaby decaffeination plant and offices. The lease expires in June 2023.

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

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

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

### Construction Loan

In Q4 2018, Swiss Water 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 facility in Delta, British Columbia. The Term Loan bears interest at 4.95% per annum over 12 years with principal repayment commencing on July 1, 2021.

The Term Loan matures on June 1, 2033. Only interest will be paid on the outstanding balance, monthly, prior to July 1, 2021. The Term Loan was 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 Term Loan. Seaforth has provided a guarantee for the Term Loan. As of September 30, 2020, the loan amount outstanding was \$20.0 million with interest accrued of \$0.1 million.



# SWISS WATER DECAFFEINATED COFFEE INC.

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## Management Discussion and Analysis

For the three and nine months ended September 30, 2020

### OFF-BALANCE SHEET ARRANGEMENTS

Swiss Water has no off-balance sheet arrangements.

### RISKS AND UNCERTAINTIES

During March 2020, the World Health Organization declared a global pandemic known as COVID-19. The impacts on global commerce are expected to be far reaching. This may impact the demand for our products and services in the near term and possibly impact the efficiency of our supply chain. It may also impact expected 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 is discontinued. Swiss Water may experience disruptions to our business operations if any of our employees, or those of our customers or suppliers, are quarantined and unable to work. There may be significant disruptions and delays in our ongoing business or in the start-up procedures at our new facility, in Delta, BC.

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, and general economic downturns. The future effect of these risks and uncertainties cannot be quantified or predicted.

In addition, Swiss Water leases the building in Burnaby, BC, that houses two decaffeination lines. The lease on this facility expires in 2023 and the landlord has formally notified Swiss Water that it will not grant the five-year renewal term (to 2028) outlined, at the landlord's discretion, in the lease. Relocating the existing production equipment would result in significant capital expenditures and payment of the asset retirement obligation (currently recorded as a long-term liability on our financial statements).

### CRITICAL ACCOUNTING JUDGMENTS AND ESTIMATES

Critical accounting judgments and estimates used in preparing our unaudited condensed consolidated interim financial statements are described in the Swiss Water's annual MD&A and annual consolidated financial statements for the year ended December 31, 2019. The preparation of consolidated financial statements in accordance with IFRS requires us to make both estimates and assumptions that could materially affect the amounts recognized in the financial statement. By their nature, judgments and estimates may change in light of new facts and circumstances in the internal and external environment.

Effective January 1, 2019, we adopted IFRS 16 Leases in accounting for leases of our offices, warehouses, and equipment. Estimates and assumptions were made and applied, including the useful lives of right-of-use assets and the implicit borrowing rates. The useful lives of right-of-use assets are estimated to be the length of the related lease terms, ranging from 2 to 20 years. The weighted average implicit borrowing rate is 4.92% per annum which was based on borrowing rates available to Swiss Water.

An accounting estimate is deemed critical only if it requires us to make assumptions about matters that are highly uncertain at the time the accounting estimate is made, and different estimates that we could have used in the current period would have a material impact on our financial condition or results of operations.

# SWISS WATER DECAFFEINATED COFFEE INC.

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## Management Discussion and Analysis

For the three and nine months ended September 30, 2020

### CHANGES IN ACCOUNTING STANDARDS

The following amendments to accounting standards became effective for annual periods beginning on or after January 1, 2020. The adoption of these revised standards by Swiss Water 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; IFRS 3 was amended to revise the definition of a business; Conceptual Framework replaces the conceptual framework for financial reporting issued by IASB in September 2010.

These standards will become effective for periods beginning after January 1, 2022 and Swiss Water does not anticipate a material impact on our financial statements:

- IAS 1 amendments address the classification of liabilities between current and non-current.

### HEDGE ACCOUNTING

We account for hedges using IFRS 9, as we enter into three types of hedges:

- 1) Commodity price risk hedges on our coffee purchase commitments and inventory (“commodity hedges”);
- 2) Foreign currency risk hedges on future US\$ process revenues (“revenue hedges”); and
- 3) Customer-specific foreign currency risk hedges on US\$ purchases of green coffee (“customer-specific hedges”).

Each type of hedge is discussed below.

#### 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

# SWISS WATER DECAFFEINATED COFFEE INC.

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## Management Discussion and Analysis

For the three and nine months ended September 30, 2020

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.

### Customer-Specific 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.

Hedge accounting allows for better 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 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 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. Swiss Water utilizes futures contracts to manage our commodity price

# SWISS WATER DECAFFEINATED COFFEE INC.

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## Management Discussion and Analysis

For the three and nine months ended September 30, 2020

exposure. We buy and sell futures contracts for coffee on the Intercontinental Exchange in order to offset our inventory position and fix the input cost of green coffee.

As at September 30, 2020, we had futures contracts to buy 4.6 million lbs of green coffee with a notional value of US \$5.0 million, and contracts to sell 7.6 million lbs of green coffee with a notional value of US\$8.4 million. The furthest contract matures in September 2021. (December 31, 2019: buy 3.6 million lbs of green coffee with a notional value of US\$4.7 million, and contracts to sell 6.6 million lbs of green coffee with a notional value of US\$8.3 million).

### Foreign Currency Risk

We realize a significant portion of our sales in US dollars and we purchase green coffee in US\$ which is, in some cases, sold to customers in C\$ dollars. We enter into forward exchange contracts to manage our exposure to currency rate fluctuations and to minimize the effect of exchange rate fluctuations on business decisions. These contracts relate to our future net cash flows in US\$ from sales. In addition, we enter into forward contracts to purchase US\$ for coffee that we resell in C\$ dollars.

As at September 30, 2020, Swiss Water had forward currency contracts to buy US\$6.7 million and sell US\$55.2 million (December 31, 2019: buy US\$3.8 million and sell US\$53.0 million) from October 2020 through to February 2025 at various Canadian exchange rates ranging from \$1.2147 to \$1.3974.

### 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 September 30, 2020, 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 September 30, 2020, 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 September 30, 2020, 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, 2020 and ended on September 30, 2020 that have materially affected or are reasonably likely to materially affect, Swiss Water’s ICFR.