

## HILL STREET BEVERAGE COMPANY INC.

### MANAGEMENT'S DISCUSSION AND ANALYSIS FOR THE THREE MONTH PERIOD ENDING SEPTEMBER 30, 2019

The following management's discussion and analysis ("MD&A") provides a review of the activities, results of operations and financial condition of Hill Street Beverage Company Inc. (the "Company" or "Hill Street") for the three months ended September 30, 2019 in comparison with the three months ended September 30, 2018. These comments should be read in conjunction with the audited financial statements for the years ended June 30, 2019 and June 30, 2018 and accompanying notes included therein, which have been prepared in accordance with International Financial Reporting Standards ("IFRS"). This MD&A has been prepared as of November 28, 2019. Additional information relating to Hill Street is available on SEDAR.

All amounts are stated in Canadian dollars unless otherwise identified.

#### FORWARD-LOOKING STATEMENTS

Except for the historical information contained herein, the discussion in this MD&A contains certain forward-looking statements that involve risks and uncertainties, such as statements of Hill Street's plans, objectives, strategies, expectations and intentions. Forward-looking statements generally can be identified by the use of forward-looking terminology such as "may", "will", "expect", "intend", "anticipate", "seek", "plan", "believe" or "continue" or the negatives of these terms or variations of them or similar terminology. Although Hill Street believes that the expectations and assumptions reflected in these forward-looking statements are reasonable, undue reliance should not be placed on these forward-looking statements. These forward-looking statements are not guarantees and reflect Hill Street's views as of November 28, 2019 with respect to future events. Future events are subject to certain risks, uncertainties and assumptions, which may cause actual performance and financial results to differ materially from such forward-looking statements. The forward-looking statements, including the statements regarding expected volumes, operating efficiencies and costs are based on, among other things, the following material factors and assumptions: sales volumes in the quarter will increase; no material changes in consumer preferences; brewing, blending, and packaging efficiencies will improve; the cost of input materials for brewing and blending will increase; competitive activity from other manufacturers will continue; foreign currency exchange rates will change; no material change to the regulatory environment in which Hill Street operates and no material supply, cost or quality control issues with vendors. Readers are urged to consider the foregoing factors and assumptions when reading the forward-looking statements and for more information regarding the risks, uncertainties and assumptions that could cause Hill Street's actual financial results to differ from the forward-looking statements, to also refer to the remainder of the discussion in this MD&A, Hill Street's various other public filings as and when released by Hill Street. The forward-looking statements included in this MD&A are made only as of November 28, 2019 and, except as required by applicable securities laws, Hill Street does not undertake to publicly update such forward-looking statements to reflect new information, future events or otherwise.

#### DESCRIPTION OF THE BUSINESS

The Company presently has one business segment, the marketing and distribution of non-alcoholic beer and wine in Canada and, to a much lesser extent, the United States. Hill Street sells its products online and in thousands of branded retail chain stores through licensed distributors in Canada. It also provides direct to consumer sales and a monthly subscription service at [www.hillstreetbeverages.com](http://www.hillstreetbeverages.com). In addition, the Company is focusing on expanding its business segments to include Cannabis infused beverages in 2020.

## **INNOVATIVE PRODUCTS AND ADDRESSABLE MARKETS**

### **Alcohol Free Adult Beverages**

Hill Street's account presence continued to grow in the retail market. Loblaws continues to support Hill Street's Brands. In Q1, Fortinos, a Loblaws brand of 23 large format stores in southern Ontario, listed all seven (7) of Hill Street's wines and beer just in time for the holiday quarter. Additionally, in Q1 Hill Street's annual Entertainers multi-pack (3x750mL assorted wines) retailer volume commitment was 3x the volume from last year. Hill Street also partnered with the Loblaws Market banners and have begun a Multi-Save program designed to encourage multiple purchases.

Hill Street's alcohol free beer business had a good summer in the grocery channel. The craft lager business is available in many formats and package sizes depending on the retailer's strategy. Hill Street's license to use Designated Draft as a brand was terminated September 30, 2019. The Company will transition all Designated Draft retail listings to Craft Beer listings.

### **Cannabis Infused Adult Beverages**

Cannabis Edibles (Cannabis v2.0), including beverages, became legal in Canada in October 2019. Hill Street continued to advance its market entry by: (i) developing a consumer driven product portfolio and pricing model, (ii) conducting initial meetings and ongoing dialogue with all provincial regulators, (iii) preparing preliminary channel marketing plans, and (iv) meeting with retail operators across Canada.

Hill Street remains focused on building versatile infrastructure able to address Health Canada regulations pertaining to packaging, licensing, branding and marketing. The Health Canada regulations for edible products were issued in June 2019, with some adjustments in September 2019. Hill Street has been working with these regulations to meet the Company's stated goal of launching these products in 2020. To meet this timeline, the Company remains active in finalizing a partnership(s) with licensed producer(s) who either have facilities where the company can install its owned equipment, or have operational and scalable production equipment in place. Given the size and scope of the product portfolio, the Company expects there to be multiple production facilities. In parallel, the Company will also be looking to secure its own Health Canada licenses and building(s) where some/ all products can be produced. The ability to efficiently ship future product to the global market is a consideration of production and warehousing facilities.

## **Q1 HIGHLIGHTS**

During the first quarter, Hill Street focused on being responsive to retail demands and expanding distribution in the retail sector during the peak summer beverage season. The Company also continued to manage relationships with the capital markets. Hill Street also worked through its planned, and ultimately cancelled acquisition of OneLeaf Cannabis.

Hill Street's alcohol-free business unit's revenue was down 35% or \$280k versus the same year ago period. In June 2019 Hill Street transitioned to a new distributor (CB Powell). This transition resulted in a one-time delay of sales from Q4 FY2018 to Q1 FY2019. This shortfall was also driven by the timing of Shoppers Drug Mart sales expected in FY20Q2. Shipments from distributors to retailers in FY20Q1 were +5% vs same period year ago.

The Company participated in the inaugural Cannabis Drinks Expo in San Francisco, attended by over 1,000 industry participants including manufacturers, suppliers, technology & infusion companies, and cannabis companies. The Company's CEO was asked to present a keynote address on launching cannabis infused beverages into the Canadian and ultimately global markets. A video of the presentation can be seen on the Beverage Daily web site.

The Company also presented at the MicroCap Investor Conference at the Essex House Hotel in New York City, which included participating in a cannabis edibles panel with some of the largest US multi-state operators. This was

followed by a keynote address at the McGill Centre for Cannabis Research, a presentation at the Extraordinary Futures Conference in Vancouver, B.C., and a presentation at the Thinking North Capital Conference in Toronto. These conferences are important activities for the Company to build investor awareness and confidence in its strategy for launching cannabis infused beverages, and to ensure the company has access to capital and provides liquidity for its shareholders.

In July, the Company announced a global license agreement with Lexaria Biosciences to produce cannabis and hemp infused beverages, the first such license ever awarded by Lexaria. This will ensure Hill Street has the ability to use the Lexaria technology in the future as it expands to access global markets for THC and CBD infused beverages. At the same time, the Company announced a Joint Manufacturing Partnership with Lexaria to produce water soluble powder made from hemp and cannabis for use as a manufacturing ingredient, or a drink mix, or as a compressed tablet for consumer use. These new product categories, made possible by Lexaria's patented DehydraTECH process, will give Hill Street new revenue streams not contemplated prior to the signing of this partnership, and are accretive to its existing beverage business. Consumers will enjoy the ability to infuse their own beverages, or to take additional doses of either CBD or THC in addition to what is available in a legally proscribed dosage as determined by Health Canada or other regulatory authorities

On June 10, 2019, the Company closed \$1.7 million of a proposed \$5 million private placement financing of units. The capital markets for small-cap cannabis companies proved extremely difficult through the entire fiscal first quarter, largely due to the industry scandals, including a license suspension of a major player for cultivating cannabis in unlicensed facilities, and health impact posed by vaping illicit cannabis products and nicotine products in the US and Canada. These crises, while not directly linked to Hill Street, had the effect of shaking investor confidence in the sector. During this time Hill Street was attempting to raise money from both retail and institutional investors to support its planned acquisition and build out of OneLeaf Cannabis in Regina. After four months of unsuccessful fundraising, the Company and OneLeaf mutually agreed to terminate the transaction on Sept 30, 2019.

To replace the production capability contemplated in the OneLeaf facility, Hill Street has begun negotiations with a number of copacking partners subsequent to the close of the quarter. On November 12, 2019, the Company announced its first copacking partnership with Peak Processing Solutions of Windsor Ontario, to produce multiple products on behalf of Hill Street. The Company expects this will be the first of multiple cannabis copacking partnerships, as it secures production capacity for its beverages, capsules, drink mixes, cannabis powder, and other new products.

Also, during the period, Hill Street was instrumental in highlighting a problematic issue within the legal cannabis space. As a founding member of the Cannabis Beverage Producers Alliance, Hill Street helped reveal an inadequacy in the banking industry which became the topic of a major media story. As a result of this, an investigation is currently underway to correct the issue.

## **SOCIAL RESPONSIBILITY**

Within the Partnership area, activity with a couple of philanthropic events saw Hill Street featured at some high-profile events.

In June, the annual Plaid for Dad campaign culminated at the "Do it For Dad" day on June 17, 2019; Father's Day. As one of the primary sponsors of Plaid for Dad, Hill Street was also featured as the "matching donor" partner for this campaign. Many celebrities were involved in the campaign including television and screen actor Billy Baldwin. Prostate Cancer Canada was able to maximize the matching donation, generating \$50,000 from constituents due to the promise of a matched gift by Hill Street. In every advertisement, out-of-home buy, social post and direct mail, Hill Street Beverage Company was featured prominently in logo and word format.

In July, Hill street participated as a sponsor in the Muskoka Boat Rally to End Children's Cancer, benefitting SickKids Hospital. This event raised in excess of \$150,000 to fund much needed diagnostic equipment for SickKids Hospital.

At the end of September, Hill Street Beverages was the presenting sponsor of the Prostate Cancer Canada's inaugural Celebrity Battle of the BBQ. Featured in the weeks leading up to the event on Global television, The Food Network, and various print and electronic media which generated 10,087,239 impressions, with a combined media value of \$2,174,704.

## RESULTS OF OPERATIONS

The following table summarizes certain financial information of the Company for the quarter ended September 30, 2019 and the quarter ended September 30, 2018.

Results for the Period Ended	Quarter Ended September 30, 2019	Quarter Ended September 30, 2018
<b>Gross Revenue</b>	\$513,766	\$793,867
<b>Chargebacks, finance fees, and listing fees</b>	\$184,327	\$282,260
<b>Net Revenue</b>	\$329,439	\$511,607
<b>Direct Costs</b>	\$152,036	\$294,613
<b>Gross profit</b>	<b>\$177,403</b>	<b>\$216,994</b>
<b>Operating Expenses</b>	<b>\$1,002,158</b>	<b>\$886,829</b>
<b>Other One-time Expenses</b>	<b>\$545,850</b>	<b>\$304,675</b>
<b>Non Cash Expenses</b>	<b>\$154,982</b>	<b>\$221,286</b>
<b>Loss before other income (Expense)</b>	<b>\$1,525,587</b>	<b>\$1,195,796</b>
<b>Other income (Expenses)</b>		
Charges related to RTO	\$	\$918,345
Foreign exchange gain (loss)	\$12,324	\$(14,888)
Write-off of inventory	\$	\$(8,007)
Write-off of intangibles	\$8,000	\$0
Other Income	\$	\$2,640
<b>Loss and comprehensive loss for the period</b>	<b>\$1,545,911</b>	<b>\$2,134,396</b>
<b>Basic and diluted loss per common share</b>	<b>\$0.02</b>	<b>\$0.03</b>
<b>Weighted average number of common shares outstanding</b>	<b>96,845,070</b>	<b>64,157,068</b>

## REVENUES

During the three months ended September 30, 2019, gross revenues were \$513,766 compared to \$793,867 for the three months ended September 30, 2018; representing a decline of 35% due to a one-time delay of sales from Q4 FY2018 to Q1 FY2019 with a change in distributor which occurred at the end of fiscal 2018.

For the three months ended September 30, 2019, chargebacks and listing fees (fees charged by retailers and distributors for program money and discounts) represented 36% of gross revenues for the three months ended September 30, 2019 and for the three months ended September 30, 2018.

Net revenues for the three months ended September 30, 2019 were \$329,439 compared to \$511,607 in the same period a year ago, representing a decline of 36%. Net revenues are calculated by deducting from gross revenues the costs of chargebacks and listing fees paid to retailers to have product available for sale in such retail establishments. The decrease in net revenues is attributable to the decline in gross revenue.

## **COST OF SALES/DIRECT COSTS**

Direct costs were \$152,036 for the three months ended September 30, 2019 compared to \$294,613 for the three months ended September 30, 2018. Direct costs represented 30% of gross revenue in the quarter compared to 37% in the same quarter in 2018. This decrease was primarily driven by better finished wine product costs and associated foreign exchange.

## **OPERATING EXPENSES**

Operating expenses include selling & marketing expenses, employee expenses, donations, dues and licenses professional fees and other general and administrative expenses. For the quarter ended September 30, 2019, operating expenses totaled \$1,002,158 compared to \$886,829 for the quarter ended September 30, 2018.

## **ONE TIME OPERATING EXPENSES**

In addition to ordinary operating expenses, the Company incurred a number of one-time expenses. For the three months ended September 30, 2019, one-time expenses totaled \$545,850 relating to M&A and Cannabis Investment. During the quarter ended September 30, 2018 one-time expenses totaled \$304,675 relating to the RTO and expenses of the Company relating to its cannabis licensing efforts.

## **NON CASH EXPENSES**

For the three months ended September 30, 2019 the Company incurred non-cash expenses totaling \$ 154,982 compared to \$221,296 for the quarter ended September 30, 2019. The non-cash expenses related to stock options and depreciation.

## **NET EARNINGS**

The Company recorded a net loss of \$1,545,911 the three months ended September 30, 2019, compared to a loss of \$2,134,396 for the three months ended September 30, 2018. The improvement is driven by the non-cash cost of listing the Company on the stock exchange of \$918,345 incurred in the three months ended September 30, 2018.

## **SELECTED QUARTERLY INFORMATION**

The following table summarizes certain financial information of the Company for the quarters indicated below:

	<b>Sept. 30, 2019</b>	<b>June 30, 2019</b>	<b>Mar 31, 2019</b>	<b>Dec 31, 2018</b>	<b>Sept 30, 2018</b>	<b>June 30, 2018</b>	<b>Mar 31, 2018</b>	<b>Dec 31, 2017</b>
Gross Revenue	\$513,766	\$506,721	\$603,854	\$527,652	\$793,867	\$174,796	\$364,427	\$599,048
Net Revenue	\$329,439	-\$55,100	\$428,355	\$395,356	\$511,589	\$94,550	\$248,093	\$125,485
Direct Costs	\$152,036	\$164,193	\$219,736	\$169,569	\$294,875	\$199,693	\$19,898	\$244,532
Gross Profit	\$177,403	-\$219,293	\$208,619	\$225,787	\$216,714	-\$105,143	\$228,195	-\$119,047
Net Loss (-gain)	\$1,509,913	-\$6,711,371	\$1,074,283	\$1,443,020	\$2,134,396	\$1,402,174	\$644,880	\$439,405
Total Assets	\$1,908,157	\$3,004,909	\$2,216,288	\$2,997,226	\$4,506,261	\$2,845,751	\$1,650,397	\$598,745
Total Liabilities	\$882,662	\$627,141	\$829,799	\$743,463	\$1,069,283	\$1,387,534	\$674,059	\$1,753,076
Shareholder Equity	\$1,025,495	\$2,377,768	\$1,386,489	\$2,253,763	\$3,436,978	\$1,458,217	\$976,338	-\$1,154,331

## LIQUIDITY AND CAPITAL RESOURCES

### FINANCIAL POSITION

The Corporation's principal capital needs are for operating expenses related to employee and marketing expenses and cannabis investment. Since its formation, the Company has financed its additional cash requirements through revenues generated from operations, issuance of securities and borrowing from shareholders and other lenders.

The Company has positive working capital and will continue to focus on cost management and revenue growth. However, it is very likely the Company will need to raise capital through debt or equity financings in the near future.

### WORKING CAPITAL

Working capital represents current assets less current liabilities. As of September 30, 2019, the Company had a positive working capital of \$558,195 compared to a working capital of \$3,430,236 as at September 30, 2018.

### CASH FLOWS

During the quarter ended September 30, 2019, Hill Street generated negative cash flows from operations of \$933,381 compared to negative cash flow of \$1,728,808 during the quarter ended September 30, 2018. The amount of cash (used) in investing activities in the quarter ended September 30, 2019 was (\$2,240) compared to \$214,955 cash acquired from the RTO in the quarter ended September 30, 2018. The amount of cash provided by financing activities in during the quarter ended September 30, 2019 was \$71,200 compared to \$2,524,335 in the quarter ended September 30, 2018.

### CONTRACTUAL OBLIGATIONS

A summary of the Company's contractual obligations for future periods is as follows:

Contractual Obligations	Payments due by Period					Total
	FY2020	FY2021	FY2022	FY2023	FY2024	
Contractual Royalty Obligations	\$0	\$0	\$0	\$0	\$0	\$0
Operating Leases	\$0	\$0	\$0	\$0	\$0	\$0
Purchase Obligations	\$93,750	\$114,000	\$77,167	\$0	\$0	\$284,917
Other Debt Obligations	\$0	\$0	\$0	\$0	\$0	\$0
<i>Total</i>	\$93,750	\$114,000	\$77,167	\$0	\$0	\$284,917

### SHARE CAPITAL

The Company is authorized to issue an unlimited number of Common Shares of which 97,150,581 Common Shares are issued and outstanding as of the date hereof.

### CAPITAL RESOURCES

As of September 30, 2019, the Company did not have commitments for capital expenditures.

### OFF BALANCE SHEET ARRANGEMENTS

Hill Street does not have any off-balance sheet arrangements that have, or are reasonably likely to have, a current or future effect on the financial performance or financial condition of the Company.

## TRANSACTIONS WITH RELATED PARTIES

The Company considers its executive officers and directors to be key management personnel. The Company incurred the following amounts to related parties during the respective periods for key management personnel compensation.

<b>During three month period ended September 30,</b>	<b>2019</b>	<b>2018</b>
Management Salaries & Stock Option Compensation	246,763	382,542

Included in accounts payable as at September 30, 2019 is \$8,246 payable to Directors and Officers of the Company for management compensation. The amount is non-interest bearing, unsecured and due on demand.

## LEGAL PROCEEDINGS

There are no legal proceedings material to Hill Street to which Hill Street is a party to or of which any of its property is the subject matter, and there are no such proceedings known to Hill Street to be contemplated.

## CRITICAL ACCOUNTING ESTIMATES

The determination of income tax is inherently complex and requires making certain estimates and assumptions about future events. While income tax filings are subject to audits and reassessments, the Company has adequately provided for all income tax obligations. However, changes in facts and circumstances as a result of income tax audits, reassessments, jurisprudence and any new legislation may result in an increase or decrease in the provision for income taxes.

Calculation of the net book value of machinery and equipment requires Management to make estimates of the useful economic life of the assets, residual value at the end of the asset's useful economic life, method of depreciation and whether impairment in value has occurred. Residual values of the assets, estimated useful lives and depreciation methodology are reviewed annually with prospective application of any changes, if deemed appropriate. Changes to estimates could be caused by a variety of factors, including changes to the physical life of the assets. A change in any of the estimates would result in a change in the amount of depreciation and, as a result, a charge to net income recorded in the period in which the change occurs, with a similar change in the carrying value of the asset on the balance sheet.

## CRITICAL FUTURE ACCOUNTING POLICIES

The following new standards, and amendments to standards and interpretations, are effective for the current year and have been applied in preparing these consolidated financial statements.

- i) IFRS 16, "Leases", In January 2016, the IASB issued IFRS 16, Leases, effective for annual periods beginning on or after January 1, 2019, with earlier adoption permitted. IFRS 16 will replace IAS 17, Leases. The Company adopted this standard on July 1, 2019 with no material impact on its consolidated statement of financial position or results of operations.