

# **Management's Discussion and Analysis**

## **For the second quarter ended May 31, 2010**

### **General**

Management's Discussion and Analysis of the financial position and results of operations ("MD&A") of MTY Food Group Inc. ("MTY") is supplementary information and should be read in conjunction with the Company's consolidated financial statements and accompanying notes and with the most recent annual report, for the fiscal year ended November 30, 2009.

In the MD&A, MTY Food Group Inc., MTY, or the Company, designates, as the case may be, MTY Food Group Inc. and its Subsidiaries, or MTY Food Group Inc., or one of its subsidiaries.

There have been no significant changes with regards to "Corporate Objectives, Core Business and Strategies", "Risk and Uncertainties", and "Critical accounting Policies" to those outlined in the Annual MD&A contained in MTY's 2009 Annual Report. As such, they are not repeated herein.

The consolidated financial statements contained in this interim report have not been reviewed by MTY's external auditors.

This MD&A was prepared as at July 1, 2010. Supplementary information about MTY, including its latest annual and quarterly reports, and press releases, is available on SEDAR's website at [www.sedar.com](http://www.sedar.com).

### **Forward looking statements**

This MD&A and, in particular, but without limitation, the sections of this MD&A entitled Outlook, Same Store Sales and Contingent Liabilities, contain forward-looking statements. These forward-looking statements include, but are not limited to, statements relating to certain aspects of the business outlook of the Company during the course of 2010. Forward-looking statements also include any other statements that do not refer to historical facts. A statement we make is forward-looking when it uses what we know and expect today to make a statement about the future. Forward-looking statements may include words such as aim, anticipate, assumption, believe, could, expect, goal, guidance, intend, may, objective, outlook, plan, project, seek, should, strategy, strive, target and will. All such forward-looking statements are made pursuant to the 'safe harbour' provisions of applicable Canadian securities laws.

Unless otherwise indicated by us, forward-looking statements in this MD&A describe our expectations at July 1, 2010 and, accordingly, are subject to change after such date. Except as may be required by Canadian securities laws, we do not undertake any obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

Forward-looking statements, by their very nature, are subject to inherent risks and uncertainties and are based on several assumptions which give rise to the possibility that actual results or events could differ materially from our expectations expressed in or implied by such forward-looking statements and that our business outlook, objectives, plans and strategic priorities may not be achieved. As a result, we cannot guarantee that any forward-looking statement will materialize and you are cautioned not to place undue reliance on these forward-looking statements. Forward-looking statements are provided in this MD&A for the purpose of giving information about management's current strategic priorities, expectations and plans and allowing investors and others to get a better understanding of our business outlook and operating environment. Readers are cautioned, however, that such information may not be appropriate for other purposes. Forward-looking statements made in this MD&A are based on a number of assumptions that we believed were reasonable on July 1, 2010. Refer, in particular, to the section of this MD&A entitled Risks and Uncertainties for a description of certain key economic, market and operational assumptions we have used in making forward-looking statements contained in this MD&A. If our assumptions turn out to be inaccurate, our actual results could be materially different from what we expect.

Unless otherwise indicated in this MD&A, the strategic priorities, business outlooks and assumptions described in the previous MD&A remain substantially unchanged.

Important risk factors that could cause actual results or events to differ materially from those expressed in or implied by the above-mentioned forward-looking statements and other forward-looking statements included in this MD&A include, but are not limited to: the intensity of competitive activity, and the resulting impact on our ability to attract customers' disposable income; our ability to secure advantageous locations; the arrival of foreign concepts, our ability to attract new franchisees; changes customer tastes and in the attractiveness of our concepts; general economic and financial market conditions, the level of consumer confidence and spending, and the demand for, and prices of, our products; our ability to implement our strategies and plans in order to produce the expected benefits; events affecting the ability of third-party suppliers to provide to us essential products and services; labour availability and cost; stock market volatility; operational constraints the event of the occurrence of epidemics, pandemics and other health risks.

These and other risk factors that could cause actual results or events to differ materially from our expectations expressed in or implied by our forward-looking statements are discussed in this MD&A.

We caution readers that the risks described above are not the only ones that could impact us. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial may also have a material adverse effect on our business, financial condition or results of operations.

Except as otherwise indicated by us, forward-looking statements do not reflect the potential impact of any non-recurring or other special items or of any dispositions, monetizations, mergers, acquisitions, other business combinations or other transactions that may be announced or that may occur after July 1, 2010. The financial impact of these transactions and non-recurring and other special items can be complex and depends on the facts particular to each of them. We therefore cannot describe the expected impact in a meaningful way or in the same way we present known risks affecting our business.

## **Compliance with Generally Accepted Accounting Principles**

Unless otherwise indicated, the financial information presented below, including tabular amounts, is expressed in Canadian dollars and prepared in accordance with Canadian generally accepted accounting principles (“GAAP”). MTY uses income before income taxes, non-controlling interest and amortization (“EBITDA”) because this measure enables management to assess the Company’s operational performance. This measure is a widely accepted financial indicator but is not a measurement determined in accordance with GAAP and may not be comparable to the EBITDA presented by other companies.

## **Highlights of significant events during the quarter**

There was no significant change during the quarter.

## **Core business**

MTY franchises and operates quick-service restaurants under the following banners: Tiki Ming, Sukiyaki, La Cremiere, Caferama, Au Vieux Duluth Express, Carrefour Oriental, Panini Pizza Pasta, Chick ‘N’ Chick, Franx Supreme, Croissant Plus, Villa Madina, Cultures, Thai Express, Mrs. Vanelli's, Kim Chi, “TCBY”, Yogen Früz, Sushi Shop, Koya Japan, Vie & Nam, Tandori, O’Burger, Tutti Frutti, Taco Time, Country Style and Bunsmaster. During the quarter, the Company completed the conversion of the remaining Veggirama outlets into Cultures outlets.

As at May 31, 2010 MTY had 1605 locations in operation, of which 1586 were franchised and the remaining 19 locations were operated by MTY.

MTY’s locations can be found in: i) food courts and shopping malls; ii) street front; and, iii) non-traditional format within petroleum retailers, convenience stores, cinemas, amusement parks and in other venues or retailers shared sites. The non-traditional locations, which account for approximately 37% of the total location count, are typically smaller in size, require a lower investment and generate lower revenues than the locations found in shopping malls, food courts or street front locations. The street front locations are mostly made up of the Country Style, La Cremiere, “TCBY”, Sushi Shop,

Taco Time and Tutti Frutti banners. La Cremiere and “TCBY” operate primarily from April to September and the others banners operate year round.

MTY has developed several quick service restaurant concepts: Tiki Ming - Chinese cuisine, was its first banner, followed by Sukiyaki - A Japanese delight, Franx Supreme – hot dog/hamburger, Panini Pizza Pasta, Chick’n’Chick, Caferama, Carrefour Oriental, Villa Madina, Kim Chi, Vie & Nam, Tandori and O’Burger. Other banners added through acquisitions include: 18 locations from the Fontaine Sante/Veggirama chain in 1999, 74 locations from the La Cremiere ice cream chain in 2001, 20 locations from the Croissant Plus chain in 2002, 24 locations from the Cultures chain in 2003, 6 locations from the Thai Express chain in May 2004, 103 locations from the Mrs. Vanelli’s chain in June 2004, 91 locations of The Country’s Best Yogurt “TCBY” with the undertaking of the Canadian master franchise right in September 2005. On April 1, 2006, MTY acquired the exclusive master franchise rights to franchise Yogen Früz™ throughout Canada with its network of 152 existing locations. On September 1, 2006, MTY acquired the Sushi Shop banner with its 42 franchise locations and 5 corporate owned locations and on October 19, 2006, the Company acquired the Koya Japan banner with its 24 franchise locations and one corporate owned location. On September 1, 2007 MTY purchased 15 existing Sushi Shop franchise locations from an investor group. On September 15, 2008, MTY acquired the Tutti Frutti banner with its 29 outlets. This banner caters to the breakfast and lunch crowd. On October 31, 2008, MTY acquired the Canadian franchising rights of Taco Time in Canada. As at the date of acquisition, there were 117 Taco Time restaurants operating in Western Canada. This year, the Company acquired the outstanding shares of Country Style Food Services Holdings Inc. with the 480 outlets operated by its subsidiaries. MTY also has an exclusive area development agreement with Restaurant Au Vieux Duluth to develop and sub-franchise Au Vieux Duluth Express quick-service restaurants in the Provinces of Ontario and Quebec.

Revenues from franchise locations are generated from royalty fees, franchise fees, sales of turn key projects, rent, sign rental and sales of other goods and services to franchisees. Revenues from corporate owned locations include sales generated from corporate owned locations. Other operating expenses include salaries, general and administrative costs associated with existing and new franchisees, expenses in the development of new markets, costs of setting up turn key projects, supplies and equipment sold to franchisees. Corporate owned location expenses include the costs to operate corporate owned locations.

### **Description of recent acquisition**

On April 13, 2009, MTY announced that its wholly owned subsidiary MTY Tiki Ming Enterprises Inc. would be acquiring all the issued shares of Country Style Food Services Holdings Inc. The acquisition was completed on May 1, 2009. The Company has paid \$7,936,791 in cash and \$6,750,000 as repayment of long-term debt on closing and retained the amounts of \$997,868 and \$794,576 as holdbacks and withholding taxes respectively. An amount of \$2,697,762 of post-closing adjustments is to be reimbursed

by the sellers to the Company in accordance with the provisions of the purchase agreement. The post-closing adjustments are under litigation.

As at the date of acquisition, there were 117 Country Style traditional restaurants, 348 non-traditional Country Style outlets as well as 15 Bunsmaster retail outlets. All these units were franchised with the exception of 5 corporate owned traditional restaurants.

The purchase price of Country Style has not been finalized as of July 1, 2010.

### Selected annual information

	Year ended November 30,2007	Year ended November 30,2008	Year ended November 30,2009
Total assets	\$52,311,310	\$60,087,474	\$76,535,459
Total long-term liabilities*	\$2,826,714	\$2,217,748	\$2,463,229
Revenue	\$30,526,025	\$34,239,041	\$51,537,788
Income before income taxes and non-controlling interest	\$13,536,341	\$14,327,700	\$17,927,708
Net income and comprehensive income	\$9,167,123	\$9,911,506	\$12,261,503
EPS basic	\$0.48	\$0.52	\$0.64
EPS diluted	\$0.48	\$0.52	\$0.64
Weighted daily average number of common shares	18,932,767	19,120,567	19,120,567
Weighted average number of diluted common shares	19,081,504	19,120,567	19,120,567

\* Total long-term liabilities exclude non-controlling interest

## Summary of quarterly financial information

	Quarter Ended Aug/08	Quarter Ended Nov/08	Quarter Ended Feb/09	Quarter Ended May/09	Quarter Ended Aug/09	Quarter Ended Nov/09	Quarter Ended Feb/10	Quarter Ended May/10
Revenue	\$9,221,730	\$8,827,337	\$9,777,233	\$11,434,753	\$14,838,378	\$15,487,424	\$14,313,553	\$17,287,393
Net income and comprehensive income	\$2,673,826	\$2,836,995	\$2,199,526	\$2,901,760	\$3,384,504	\$3,775,712	\$3,003,595	\$3,809,139
Per share	\$0.14	\$0.15	\$0.12	\$0.15	\$0.18	\$0.20	\$0.16	\$0.20
Per diluted share	\$0.14	\$0.15	\$0.12	\$0.15	\$0.18	\$0.20	\$0.16	\$0.20

## Results of operations for the six-month period ended May 31, 2010

### Revenue

For the first half of 2010, total revenue increased by 49%, to \$31.6 million, from \$21.2 million for the same period last year.

Revenue from franchise locations increased by 62% for the first six months of 2010, progressing from \$16.9 million in 2009 to \$27.5 million in 2010. The increase is mainly attributable to the acquisition and subsequent growth of Country Style, which accounted for one month during the first six months of 2009.

In addition, the Company opened 79 new stores during the first six months of 2010 compared to 37 for the same period last year, generating a stronger volume of initial franchise fees and turnkey deliveries.

Revenue from corporate owned locations decreased to \$4.1 million for the first six months of 2010, from \$4.3 million for the same period last year, representing a reduction of 4%. This reduction is mainly due to the decrease in the number of corporate owned locations, which went from 27 a year ago to 19 at the end of the second quarter of 2010.

### Cost of sales and other operating expenses

For the first half of 2010 other operating expenses increased by 100% to \$15.9 million, from \$8.0 million for the same period in 2009. The operations of Country Style, for which only one month of operations was included in our results for the first six months of 2009, account for approximately \$6.8 million of the increase; they are mainly composed of costs incurred to deliver turnkey locations, of rental expenses related to franchised locations, both of which are associated with a stream of revenues, and of labour costs.

Other than Country Style, cost of sales increased by \$0.6 million because of a higher volume of turnkey projects delivered during 2009, royalty payments and commissions, which are related to sales, account for \$0.3M and office and general account for the remainder of the variance, mainly because of a one-time fee resulting from the Company's graduation to the TSX.

Expenses for corporate owned locations decreased to \$3.5 million from \$4.1 million for the six months ended May 31, 2010, as the Company has reduced the number of corporate-owned locations.

## EBITDA

	Six-month period ended			Six-month period ended		
	May 31, 2009			May 31, 2010		
(In millions)	Franchise	Corporate	Total	Franchise	Corporate	Total
Revenues <sup>(1)</sup>	\$16.96	\$4.32	\$21.27	\$27.33	\$4.15	\$31.48
Expenses	\$7.96	\$4.07	\$12.03	\$15.95	\$3.54	\$19.49
EBITDA	\$9.00	\$0.25	\$9.25	\$11.38	\$0.61	\$11.99
EBITDA as a % of Revenue	53.1%	5.7%	43.5%	41.7%	14.7%	38.1%

EBITDA (income before income taxes, non-controlling interest and amortization) is not an earnings measure recognized by GAAP and therefore may not be comparable to similar measures presented by other companies.

<sup>(1)</sup>For purposes of the EBITDA analysis, interest income and gain on disposal of capital assets and on foreign exchange have been included with Franchise revenue. See reconciliation to net income and comprehensive income on page 16.

EBITDA for MTY increased by 30%, from \$9.25 million to \$11.99 million for the first six months of our 2010 fiscal year.

EBITDA from franchise locations for the same period increased from \$9.00 million in 2009 to \$11.38 million in 2010. The main drivers of that growth are the acquisition and subsequent growth of Country Style, which was acquired in April 2009, therefore accounting for only one month in 2009. Generic growth from stores opened in 2009 and 2010 also represents an important portion of the growth.

EBITDA as a percentage of revenue decreased mainly due mainly to larger number of turnkey projects delivered and increased sales of products and services made to franchisees, which typically generate negligible profit margins.

EBITDA from corporate owned locations increased from \$0.25 million in 2009 to \$0.61 million in 2010, mainly because of the stronger general performance of the remaining stores. For the same reason, EBITDA as a percentage of revenue from corporate owned locations increased to 15% for the period, compared to 6% in 2009.

## Net income

For the first six months of 2010, MTY reported a net income of \$6.8 million or \$0.36 per share (\$0.36 per diluted share) compared to a net income of \$5.1 million or \$0.27 per

share (\$0.27 per diluted share) for the same period last year, representing a net income increase of 34%. The increase in net income for the period is mainly attributable to the acquisition Country Style as well as to strong generic growth.

### **Amortization expense**

Amortization of capital assets increased slightly to \$0.4 million for the first half of our 2010 fiscal period. The increase is due to the additional amortization of capital assets resulting from the acquisition of Country Style, which was partly offset by the reduction in amortization related to the disposal of the assets used in corporate stores that were franchised.

Amortization of intangible assets increased to \$1.5 million for the period compared to \$1.4 million in 2009. The increase is mainly attributable to the amortization of franchise rights and distribution rights that resulted from the acquisition of Country Style.

### **Other income**

Interest income decreased from \$0.2 million to \$0.1 million for the six-month period ended May 31, 2010. Interest income is generated from the Company's investments in short-term notes. The decrease is mainly the result of lower interest rates prevailing during 2010.

The loss on disposal of capital assets results from losses on the sale of the assets of corporate stores.

## **Results of operations for the second quarter ended May 31, 2010**

### **Revenue**

For the quarter ended May 31, 2010, total revenue increased by 51%, to \$17.3 million from \$11.4 million in the second quarter of last year.

During the same period, revenue from franchise locations increased by 67% to \$15.1 million from \$9.1 million. Among the main drivers of this variance are the increase in initial franchise fees, stronger deliveries of turnkeys and the acquisition and subsequent growth of Country Style are the main drivers of this increase.

Revenue from corporate owned locations decreased by 9% to \$2.2 million for the quarter, from \$2.4 million for the same quarter last year. Revenues decreased because of the lower number of corporate owned locations in operations during the second quarter of 2010 than during the same period a year before.



### Cost of sales and other operating expenses

For the quarter ended May 31, 2010, other operating expenses increased by 120% to \$9.0 million from \$4.1 million for the same quarter in 2009. The aforementioned increase is mainly attributable to the operations of Country Style as well as to the higher number of turnkeys delivered during the second quarter of 2010.

Expenses for corporate owned locations were 20% lower for the second quarter of 2010 than they were for the same period a year before, at \$1.7 million from \$2.1 million. The decrease is attributable to a reduced number of stores compared to 2009 as well as to a stronger general performance of the stores.

### EBITDA

	Second quarter ended			Second quarter ended		
	May 31, 2009			May 31, 2010		
(In millions)	Franchise	Corporate	Total	Franchise	Corporate	Total
Revenues <sup>(1)</sup>	\$9.04	\$2.37	\$11.42	\$15.06	\$2.16	\$17.22
Expenses	\$4.08	\$2.14	\$6.22	\$8.99	\$1.70	\$10.69
EBITDA	\$4.96	\$0.23	\$5.20	\$6.07	\$0.46	\$6.53
EBITDA as a % of revenue	54.8%	9.9%	45.8%	40.3%	21.2%	37.9%

*EBITDA (income before income taxes, non-controlling interest and amortization) is not an earnings measure recognized by GAAP and therefore may not be comparable to similar measures presented by other companies.*

*<sup>(1)</sup>For purposes of the EBITDA analysis, interest income and gain on disposal of capital assets and on foreign exchange have been included with Franchise revenue. See reconciliation to net income and comprehensive income on page 16.*

Total EBITDA for MTY grew by 26%, from \$5.2 million to \$6.5 million for the quarter ended May 31, 2010.

EBITDA from franchise locations for the quarter increased 22%, from \$5.0 million in 2009 to \$6.1 million in 2010. The main drivers of that growth are the acquisition of Country Style, the higher initial franchise fees earned during the quarter and the royalties generated by stores opened in the last twelve months.

EBITDA as a percentage of revenue is lower in the second quarter of 2010 because of higher sales of products and services made to franchisees, which typically generate lower profit margins, as well as to a higher revenues resulting from deliveries of turnkeys.

EBITDA from corporate owned locations increased from \$0.2 million to \$0.5 million, despite a lower number of stores mainly because of stronger overall operations. EBITDA as a % of revenue increased to 21% for the quarter, from 10% for the same period last year due to better performance of some of the remaining corporate stores.

### Net income

For the quarter ended May 31, 2010, net income progressed 31% compared to the second quarter of 2009. MTY reported a net income of \$3.8 million or \$0.20 per share

(\$0.20 per diluted share) compared to a net income of \$2.9 million or \$0.15 per share (\$0.15 per diluted share) for the same quarter last year.

Most of the increase in net income for the quarter is attributable to stronger initial franchise fees and royalties generated by outlets opened during the last twelve months. The impact of the acquisition of Country Style accounts for the remainder of the growth.

### Amortization

Amortization of capital assets decreased slightly to \$0.2 million for the first quarter of 2010, mainly as a result of the disposition of corporate stores in the last 12 months.

Amortization of intangible assets is stable at \$0.8 million for the quarter ended May 31, 2010 compared to the same period last year.

### Other income

For the second quarter of 2010, interest income was stable compared to the second quarter of 2009 despite a higher amount invested, reflecting the lower interest rates that prevail in 2010.

Losses on disposal of assets amounted to \$0.1 million during the quarter, mainly owing to the disposition the capital assets related to an under performing corporate store.

### Contractual obligations and long-term debt

Long-term debt includes non-interest bearing holdbacks on acquisitions with a balance of \$1,710,511 as well as \$204,000 of debt of a partly-owned subsidiary to its non-controlling shareholders. The obligations pertaining to the long-term debt and the minimum rentals for the leases that are not subleased are as follows:

For the period ending	Long term debt	Net lease commitments	Total contractual obligations
12 months ending May 2011	\$1,914,511	\$1,878,799	\$3,793,310
12 months ending May 2012	-	\$2,026,325	\$2,026,325
12 months ending May 2013	-	\$1,943,489	\$1,943,489
12 months ending May 2014	-	\$1,803,911	\$1,803,911
12 months ending May 2015	-	\$1,724,145	\$1,724,145
Balance of commitments	-	\$5,828,100	\$5,828,100
	<b>\$1,914,511</b>	<b>\$15,204,769</b>	<b>\$17,119,280</b>

In addition to the above, the Company has entered into supplier agreements for purchases of coffee beans, wheat, sugar and shortening for delivery between June and December 2010. The total commitment amounts to \$1.2 million.

In relation to the items listed above, the Company has entered into a contract to minimize the impact of variations in foreign currencies. The total commitment on this contract amounts to approximately \$0.3 million.

## **Liquidity and capital resources**

Cash and highly liquid temporary investments amounted to \$24.7 million on May 31, 2010, compared \$15.9 million at the end of the 2009 fiscal period.

During the second quarter of 2010, cash flows generated by operating activities were \$4.8 million, compared to \$4.6 million during the second quarter of 2009. For the first six months of 2010, operating cash flows reached \$9.1 million, compared to \$6.0 million for the same period last year.

The main drivers of this increase are the strength in net income and the stabilization of the company's working capital requirements since the second quarter of 2009.

MTY anticipates that its positive cash flows will continue and will only borrow for the purpose of financing large acquisitions. In the short-term, Management will continue to open new locations that will be funded by new franchisees. MTY will continue its efforts to sell some of its existing corporate owned locations and will seek new opportunities to acquire other food service operations. MTY has an available line of credit of \$5.0 million that remained unused at May 31, 2010. The facility, when used, bears interest at the bank's annual prime rate plus 1.00%.

## **Balance sheet**

Temporary investments at the end of the second quarter were \$20.0 million, up \$5.4 million compared to the balance at November 30, 2009. Strong cash flows generated by our operations are typically invested until they are needed to fund acquisitions.

These temporary investments are comprised of highly liquid, short-term notes valued at fair value. They have maturity dates between June 2010 and May 2011 and have rates of return between 0.53% and 1.41% (0.35% to 1.01% in November 2009).

Accounts receivable at the end of May 2010 were at \$7.4 million, up from \$6.7 million at the end of November 2009. The increase is mainly due to a small number of proportionally larger receivables related to suppliers and outlets newly opened.

The number of turnkeys delivered during the first and second quarter of this year caused the franchise locations under construction held for resale to decrease to \$0.8 million as at May 31, 2010 from \$1.0 million as at November 30, 2009.

Loans receivable at the end of our second quarter amounted to \$0.9 million, up from \$0.5 million at the end of our 2009 fiscal period. During the first six months of 2010, four new loans were granted in relation to newly franchised restaurants.

Capital assets decreased to \$3.3 million at the end of the second quarter because of the combined impact of the disposal of some of the Company's assets through the sale of corporate-owned locations and amortization recorded during the period, which exceeded the new investments in capital assets.

Intangible assets decreased from \$35.1 million as at November 30, 2009 to \$33.6 million at the end of the second quarter of 2010 due to the amortization charges recorded during the first two quarters of 2010.

Accounts payable increased from \$9.3 million to \$9.9 million between November 30, 2009 and May 31, 2010 mainly because of higher accruals in relation to the construction of turnkey locations to be delivered later in the year.

Deferred revenues consist of distribution rights which are earned on a consumption basis and include initial franchise fees to be earned once substantially all of the initial services have been performed. Deferred revenues were materially unchanged at \$1.6 million as at May 31, 2010 from \$1.7 million as at November 30, 2009.

Long-term debt was stable as no material repayments occurred during the period. The long-term debt is composed of non-interest bearing holdbacks on acquisitions and of debt contracted by one of the company's subsidiary for the set up of its operations. We expect the holdbacks will be repaid over the next year, while the debt from the subsidiary carries no terms of repayment and will be repaid when this subsidiary generates sufficient cash flow to repay its debt without impairing its operations.

Further details on the above balance sheet items can be found in the notes to the May 31, 2010 consolidated financial statements.

## **Capital stock**

No shares were issued during the first quarter of the Company's 2010 fiscal period. As at July 1, 2010 there were 19,120,567 common shares of MTY outstanding.

## Location information

	<b>Number of locations 6 months May 2010</b>	Number of location 6 months May 2009
Franchises, beginning of year	<b>1,550</b>	996
Corporate owned, beginning of year	<b>20</b>	27
Opened during the year	<b>79</b>	37
Closed during the year	<b>(44)</b>	(24)
Additions by acquisition during the period	-	480
<b>Total end of year</b>	<b>1,605</b>	1,516
Franchises, end of year	<b>1,586</b>	1,489
Corporate owned, end of year	<b>19</b>	27
<b>Total end of year</b>	<b>1,605</b>	1,516

For the first six months of 2010, the Company realized a net addition of 35 locations, compared to a net addition of 13 locations for the same period a year earlier. At the end of May, 1,605 locations (1,586 franchises and 19 corporate-owned restaurants) were in operation compared to 1,570 locations (1,550 franchises and 20 corporate-owned restaurants) as at November 30, 2009.

During the first half of 2010, 4 corporate-owned locations were sold, 4 were added and 1 was closed.

Of the 79 stores opened during the first half of 2010, 36 were in shopping malls and food courts, 18 were street front and 25 were non-traditional. There were 7 street front and 10 shopping mall and food court locations closed during the same period, for a net addition of 11 street front locations, 26 mall locations and a loss of 2 non-traditional locations.

Of the 44 locations closed, 19 were the result of a transaction between two petroleum retailers in which non-traditional stores are being replaced by one of the retailers' own outlets. Losses in relation to this transaction are expected to continue into the fourth quarter of 2010, with expected net losses of approximately 60 non-traditional outlets for the year.

As at May 31, 2010, there were 8 test locations in operation, all of which were excluded from the numbers presented above. This is a decrease of 19 since the end of our 2009 fiscal year, resulting from 21 test outlets being closed and 2 opened during the period. Of the 21 outlets closed, 20 result from the loss of a contract to a competitor in a non-traditional environment.

MTY's locations can be found in: i) food courts and shopping malls; ii) street front; and iii) non-traditional format within petroleum retailers, convenience stores, cinemas, amusement parks and in other venues or retailers shared sites. The non-traditional locations are typically smaller in size, require lower investment and generate lower

revenue than the shopping malls, food courts and street front locations. The chart below provides the breakdown of MTY's locations by type as at May 31, 2010:

<b>Location type</b>	<b>% of total location count</b>	<b>% of system sales (year to date)</b>
Shopping mall & food court	<b>39%</b>	<b>54%</b>
Street front	<b>24%</b>	<b>37%</b>
Non-traditional format	<b>37%</b>	<b>9%</b>

The geographical breakdown of MTY's locations at May 31, 2010 consists of:

<b>Geographical location</b>	<b>% of total location count</b>
Ontario	49%
Quebec	29%
Prairies provinces	12%
British Columbia	5%
Maritimes	2%
International	3%

### **System wide sales**

System wide sales reached to \$218.3 million during the six months ended May 31, 2010, compared to \$173.5 million for the same period last year, representing an increase of 26%. System wide sales include sales for corporate and franchise locations, which are for the vast majority of them as reported by franchisees. The increase in system wide sales is mainly attributable to the acquisition of Country Style and to the sales realized by new locations opened since the end of the second quarter of 2009.

For the second quarter of 2010, system sales amounted to \$113.1 million, up 22% compared to the same period last year. The acquisition of Country remains the main driver of this growth, while the increased number of stores opened in the last twelve months accounted for the remainder of the increase.

### **Same store sales**

Same store sales for the first six months of 2010 decreased by 1.14%, while the same measure for the second quarter showed a decline of 1.15%.

Management believes that the decrease is temporary and is due to adverse economic conditions that have affected Canada. Sales are expected to recover once the economy gains momentum.

## **Investors relations**

On January 19, 2004, MTY appointed, for a 12 month-term, Mr. Jean-Francois Dube of Boxe Comm, as its investor relation's specialist. Mr. Dube is responsible for communicating to existing shareholders, potential investors and members of the brokerage community, for and on behalf of MTY. The Company further extended the contract with Boxe Comm to end in April 2011, subject to terms and conditions contained in the Agreement. For the six month period ended May 31, 2010, MTY has paid an amount of \$24,000 to Boxe Comm.

## **Stock options**

During the six-month period, no options were granted or exercised. As at May 31, 2010 there were no options outstanding.

## **Seasonality**

Results of operations for the interim period are not necessarily indicative of the results of operations for the full year. The Company expects that seasonality will not to be a material factor in the quarterly variation of its results. System sales fluctuate seasonally, during January and February sales are historically lower than average due to weather conditions. Sales are historically above average during May to August. This is generally as a result of higher traffic in the street front locations, higher sales from seasonal locations only operating during the summer months and higher sales from shopping centre locations. Sale for shopping malls locations are also higher than average in December during the Christmas shopping period.

## **Use of estimates**

The preparation of financial statements in conformity with Canadian generally accepted accounting principles (GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and revenue and expenses during the period reported. Significant areas requiring the use of management estimates relate to the carrying value of long lived assets, valuation of allowances for accounts receivable and inventories, liabilities for potential claims and settlements, income taxes, the useful life of assets used when calculating amortization, the determination of fair value of assets and liabilities in business acquisitions and impairment testing on goodwill and trademarks. Estimates and assumptions are reviewed periodically and the effects of revisions are reflected in the consolidated financial statements in the period they are determined to be necessary. Actual results could differ from those estimates.

## **Contingent liabilities**

The Company is involved in legal claims associated with its current business activities,

the outcome of which is not determinable. Management believes that these legal claims will have no significant impact on the financial statements of the Company.

## Guarantee

The Company has provided a guarantee in the form of a letter of credit for an amount of \$45,000.

## EBITDA reconciliation to net income and comprehensive income

The following table provides reconciliation of EBITDA to net income and comprehensive income disclosed in this MD&A.

(In millions)	3 months ended May 31, 2010	6 months ended May 31, 2010	3 months ended May 31, 2009	6 months ended May 31, 2009
	\$	\$	\$	\$
<b>EBITDA</b>	6.53	11.99	5.20	9.25
<b>Less:</b>				
Amortization – capital assets	0.16	0.45	0.21	0.38
Amortization – intangible assets	0.74	1.53	0.71	1.40
Total income taxes	1.79	3.16	1.35	2.34
Non-controlling interest	0.03	0.04	0.02	0.03
<b>Net income and comprehensive income</b>	<b>3.81</b>	<b>6.81</b>	<b>2.90</b>	<b>5.10</b>

## Risks and uncertainties

Despite the fact that the Company has a various number of concepts, diversified in type of locations and geographically across Canada, the performance of the Company is also affected by changes in demographic trends, traffic patterns, occupancy level of malls and office towers and the type, number, and location of competing restaurants. In addition, factors such as innovation, increased food, labour and benefits costs, occupancy costs and the availability of experienced management and hourly employees may adversely affect the Company. Changing consumer preferences and discretionary spending patterns could oblige the Company to modify or discontinue concepts and/or menus and could result in a reduction of revenue and operating income. Even if the Company was able to compete successfully with other restaurant companies with similar concepts, it may be forced to make changes in one or more of its concepts in order to respond to changes in consumer tastes or dining patterns. If the Company changes a concept, it may lose additional customers who do not prefer the new concept and menu, and it may not be able to attract a sufficient new customer base to produce the revenue needed to make



the concept profitable. Similarly, the Company may have different or additional competitors for its intended customers as a result of such a concept change and may not be able to successfully compete against such competitors. The Company's success also depends on numerous factors affecting discretionary consumer spending, including economic conditions, disposable consumer income and consumer confidence. Adverse changes in these factors could reduce customer traffic or impose practical

The growth of MTY is dependant on maintaining the current franchise system which is subject to the renewal of existing leases at sustainable rates, MTY's ability to continue to expand by obtaining acceptable store sites and lease terms, obtaining qualified franchisees, increasing comparable store sales and completing acquisitions. The time, energy and resources involved in the integration of the acquired businesses into the MTY system and culture could also have an impact on MTY's results.

### **Off-balance sheet arrangement**

MTY has no off-balance sheet arrangements

### **Future accounting policies**

#### **International Financial Reporting Standards**

In February 2008, Canada's Accounting Standards Board (AcSB) confirmed that Canadian GAAP, as used by publicly accountable enterprises, will be superseded by International Financial Reporting Standards (IFRS) for fiscal years beginning on or after January 1, 2011. For the Company, the conversion to IFRS will be required for interim and annual financial statements for the year ending November 30, 2012. IFRS uses a conceptual framework similar to Canadian GAAP, but there are significant differences on recognition, measurement and disclosures. The Company is currently preparing its IFRS conversion plan. The plan will be aimed in particular at identifying the differences between IFRS and the Company's accounting policies, assessing their impact and, where necessary, analyzing the various policies that the Company could elect to adopt.

#### **Business Combinations**

In January 2009, the CICA issued the following new Handbook sections: Section 1582, Business Combinations, Section 1601, Consolidated Financial Statements and Section 1602, Non-Controlling Interests which replace Section 1581, Business Combinations and Section 1600, Consolidated Financial Statements. These new Sections will be applicable to financial statements relating to fiscal years beginning on or after January 1, 2011. Early adoption is permitted to the extent the three new Sections are adopted simultaneously. Together, the new Sections establish standards for the accounting for a business combination, the preparation of consolidated financial statements and the accounting for a non-controlling interest in subsidiary in consolidated financial statements subsequent to a business combination. The Company is currently evaluating the impact of the adoption of these new Sections on its consolidated financial statements. The

Company does not expect that the adoption of these new Sections will have a material impact on its consolidated financial statements.

## **Critical accounting policies**

MTY's significant accounting policies are those which are set forth in the notes to the consolidated financial statements as at May 31, 2010. There are no critical accounting estimates that, if changed, would materially affect MTY's overall financial condition or results of operations.

## **Capital assets**

Capital assets are recorded at cost. Amortization is based on their estimated useful life using the following methods and rates or terms:

Equipment diminishing balance		20%
Computer hardware	diminishing balance	30%
Computer software	diminishing balance	50%
Leasehold improvements	straight-line	term of leases
Rolling stock	diminishing balance	30%

## **Goodwill**

Goodwill represents the excess of the purchase price over the fair values assigned to identifiable net assets acquired. Goodwill, which is not amortized, is tested for impairment annually or more frequently if impairment indicators arise to determine whether the fair value of each reporting unit to which goodwill has been attributed is less than the carrying value of the reporting unit's net assets including goodwill, thus indicating impairment. The fair value of a reporting unit is calculated based on future cash flows. Any impairment is then recorded as a separate charge against income and a reduction of the carrying value of goodwill.

## **Intangible assets**

### *Franchise rights*

Franchise rights include franchise rights and master franchise rights. The franchise rights and master franchise rights represent the fair value of the future revenue stream related to the acquisition of franchises. The franchise rights and master franchise rights are generally amortized on a straight-line basis over the term of the agreements which range between 10 to 20 years. Master franchise rights with an indefinite life are not amortized. They are tested for impairment annually or more frequently when events or circumstances indicate that the master franchise rights might be impaired.

### *Trademarks*

Trademarks represent the cost incurred to operate under a trade name and are not amortized as they have an indefinite life. They are tested annually for impairment or more

frequently when events or circumstances indicate that the trademarks might be impaired. The impairment test compares the carrying amount of the trademarks with their fair market value.

### *Leases*

Leases, which represent the value associated to preferential terms or locations, are amortized on a straight-line basis over the term of the leases.

### *Other*

Included in other intangible assets are a sponsorship fee and a licensing agreement acquired in the 2004 acquisition of Mrs. Vanelli's Restaurants Ltd., which are both fully amortized, and distributions rights obtained from the acquisition of Country Style Food Services Inc., which are being amortized over the remaining life of the contracts (three years).

### **Revenue recognition**

Revenue is generally recognized on the sale of products or services when the products are delivered or the services performed, all significant contractual obligations have been satisfied and the collection is reasonably assured.

#### *Revenue from franchise locations*

Royalties are based either on a percentage of gross sales as reported by the franchisees or on a fixed monthly fee and are recognized as revenue in the period earned.

Initial franchise fees are recognized when substantially all of the initial services as required by the franchise agreement have been performed. This occurs when the location commences operations.

Revenue from the sale of franchise locations is recognized at the time the franchisee assumes control of the franchise location.

Master license fees are recognized when the Company has performed substantially all material initial obligations under the agreement, which usually occurs when the agreement is signed.

Renewal and transfer fees are recognized when substantially all applicable services required by the Company under the franchise agreement have been performed. This generally occurs when the agreement is signed.

The Company earns rent revenues on certain leases it holds and sign rental revenues; both are recognized in the month they are earned.

The Company receives considerations from certain suppliers. Supplier contributions are recognized as revenues as they are earned.

### *Revenue from corporate-owned locations*

Revenue from corporate-owned locations is recorded when services are rendered.

### **Financial instruments**

Financial assets and financial liabilities are initially recognized at fair value and their subsequent measurement is dependent on their classification as described below. Their classification depends on the purpose for which the financial instruments were acquired or issued, their characteristics and the Company's designation of such instruments.

#### *Classification*

Cash	Held for trading
Temporary investments	Held for trading
Accounts receivable	Loans and receivables
Deposits	Loans and receivables
Loans receivable	Loans and receivables
Other receivable	Loans and receivables
Accounts payable and accrued liabilities	Other liabilities
Long-term debt	Other liabilities

#### *Held for trading*

Held-for-trading financial assets are financial assets typically acquired for resale prior to maturity or that are designated as held for trading. They are measured at fair value at the balance sheet date. Fair value fluctuations including interest earned, interest accrued, gains and losses realized on disposal and unrealized gains and losses are included in other income.

#### *Loans and receivables*

Loans and receivables are accounted for at amortized cost using the effective interest method.

#### *Other liabilities*

Other liabilities are recorded at amortized cost using the effective interest method and include all financial liabilities other than derivative instruments.

#### *Effective interest method*

The Company uses the effective interest method to recognize interest income or expense which includes transaction costs or fees, premiums or discounts earned or incurred for financial instruments.

## Credit risk

The Company's credit risk is primarily attributable to its trade receivables. The amounts disclosed in the balance sheet are net of allowances for bad debts, estimated by the Company's management based on prior experience and their assessment of the current economic environment. The Company believes that the credit risk of accounts receivable is limited for the following reasons:

- The Company's broad client base is spread mostly across Canada.
- The Company accounts for a specific bad debt provision when management considers that the expected recovery is less than the actual account receivable.

The following table sets forth details of the age receivables that are not overdue as well as an analysis of overdue amounts and related allowance for the doubtful accounts:

	<u>May 31, 2010</u>	<u>November 30, 2009</u>
	\$	\$
Total accounts receivable	8,354,573	7,429,147
Less: Allowance for doubtful accounts	919,573	754,110
<u>Total accounts receivable, net</u>	<u>7,435,000</u>	<u>6,675,037</u>

Of which:

Not past due	4,120,036	5,003,899
Past due for more than one day but for no more than 30 days	1,490,733	147,782
Past due for more than 31 days but for no more than 60 days	197,550	616,139
Past due for more than 61 days	1,626,681	907,217
<u>Total accounts receivable, net</u>	<u>7,435,000</u>	<u>6,675,037</u>
Allowance for doubtful accounts beginning of year	754,110	648,934
Additions	334,960	443,939
Acquisition	-	115,107
Write-off	(169,497)	(453,870)
<u>Allowance for doubtful accounts end of period</u>	<u>919,573</u>	<u>754,110</u>

The credit risk on cash and temporary investments is limited because the Company invests its excess liquidity in high quality financial instruments.

## **Economic environment risk**

The business of the Company is dependent upon numerous aspects of a healthy general economic environment, from strong consumer spending to provide sales revenue, to available credit to finance the franchisees and the Company. In light of recent upheaval in economic, credit and capital markets, the Company's performance and market price may be adversely affected. The Company's current planning assumptions forecast that the quick service restaurant industry will be impacted by the current economic recession in the provinces in which it operates. However, management is of the opinion that the current economic situation will not have a major impact on the Company due to the following reasons: 1) the Company has strong cash flows; 2) quick service restaurants represent an affordable dining out option for consumers in an economic slowdown.

## **Outlook**

It is Management's opinion that the trend in the quick service restaurants industry will continue to grow in response to the demand from busy and on-the-go customers.

Management will maintain its focus on producing innovative menus and revamping the store designs of its banners which should result in positive same store sales growth when renovations are completed.

For 2010, MTY has already realized its objective of opening 75 new locations and will continue to pursue the growth of its existing concepts. Management also remains committed in seeking potential acquisitions to further strengthen its market position.

## **Controls and Procedures**

Disclosure controls and procedures

Disclosure controls and procedures are designed to provide reasonable assurance that information required to be disclosed in reports filed with the securities regulatory authorities are recorded, processed, summarized and reported in a timely fashion. The disclosure controls and procedures are designed to ensure that information required to be disclosed by the Company in such reports is then accumulated and communicated to the Company's management to ensure timely decisions regarding required disclosure.

The Company's management, including the CEO and the CFO, does not expect that the Company's disclosure controls and procedures will prevent or detect all errors and all fraud. Because of the inherent limitations in all control systems, an evaluation of controls can provide only reasonable, not absolute, assurance that all control issues and instances of fraud or error, if any, within the Company have been detected.

Based upon the evaluation of the disclosure controls and procedures, subject to the inherent limitations noted above, the Chief Executive Officer and Chief Financial Officer have concluded that the Company's disclosure controls and procedures were effective as

at May 31, 2010, in providing reasonable assurance that the material information relating to the Company is made known to the Company's management.

#### Internal controls over financial reporting

The Chief Executive Officer and the Chief Financial Officer are responsible for establishing and maintaining internal control over financial reporting. The Company's internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Canadian GAAP.

The Chief Executive Officer and the Chief Financial Officer, together with Management, after evaluating the effectiveness of the Company's internal control over financial reporting as at May 31, 2010, have concluded that the Company's internal control over financial reporting was effective.

The Chief Executive Officer and the Chief Financial Officer, together with Management, have concluded after having conducted an evaluation and to the best of their knowledge that, as at May 31, 2010, no change in the Company's internal control over financial reporting occurred that could have materially affected or is reasonably likely to materially affect the Company's internal control over financial reporting.

*"Stanley Ma"*

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Stanley Ma, Chief Executive Officer

*"Claude St-Pierre"*

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Claude St-Pierre, Chief Financial Officer

*"Eric Lefebvre"*

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Eric Lefebvre, CA, Vice President Finance