



## **Management's Discussion and Analysis** **For the three months ended February 29, 2012**

### **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, 2011.

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.

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

The disclosures and values in this MD&A were prepared in accordance with International Financial Reporting Standards (IFRS) and with the current issued and adopted interpretations applied to fiscal years beginning on or after January 1, 2011. Comparative figures as at November 30, 2011 and February 28, 2011 have been restated in accordance with IFRS. Some standards expected to be adopted under IFRS may not be adopted or the application of those standards to certain transactions and/or circumstances may be modified. If so, the disclosures and values as at February 28, 2011, November 30, 2011, and December 1, 2010 may be reviewed.

As a result of the adoption of IFRS a number of areas of financial reporting are impacted by the changeover to IFRS; they are highlighted in the MD&A under the heading "Accounting policies adopted in 2012" and in note 35 of the unaudited interim consolidated financial statements.

This MD&A was prepared as at April 26, 2012. 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 2012. Forward-looking statements also include any other statements that do not refer to independently verifiable 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 April 26, 2012 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 April 26, 2012. 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 and renew

our existing leases at sustainable rates; the arrival of foreign concepts, our ability to attract new franchisees; changes in customer tastes, demographic trends and in the attractiveness of our concepts, traffic patterns, occupancy cost and occupancy level of malls and office towers; 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 and 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 April 26, 2012. 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 International Financial Reporting Standards**

Unless otherwise indicated, the financial information presented below, including tabular amounts, is expressed in Canadian dollars and prepared in accordance with International Financial Reporting Standards (“IFRS”). MTY uses income before income taxes, interest on long-term debt, depreciation and amortization (“EBITDA”) because this measure enables management to assess the Company’s operational performance. The Company also discloses same-store sales, which are defined as comparative sales generated by stores that have been open for at least thirteen months or that have been acquired more than 13 months ago.

These measures are widely accepted financial indicators but have no standardized definition as prescribed by GAAP. As a result, they may not be comparable to the EBITDA and same store-sales growth presented by other companies.

### **Highlights of significant events during the quarter ended February 29, 2012**

There were no significant events during the quarter.

## Core business

MTY franchises and operates quick-service restaurants under the following banners: Tiki-Ming, Sukiyaki, La Crémère, Au Vieux Duluth Express, Carrefour Oriental, Panini Pizza Pasta, Chick 'n' Chick, Franx Supreme, Croissant Plus, Villa Madina, Cultures, Thai Express, Vanellis, Kim Chi, "TCBY", Yogen Früz, Sushi Shop, Koya Japan, Vie & Nam, Tandori, O'Burger, Tutti Frutti, Taco Time, Country Style, Buns Master, Valentine, Jugo Juice, Mr. Sub and Koryo Korean Barbeque.

As at February 29, 2012, MTY had 2,232 locations in operation, of which 2,206 were franchised or under operator agreements and the remaining 26 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 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 Crémère, "TCBY", Sushi Shop, Taco Time, Tutti Frutti, Valentine and Mr. Sub banners. La Crémère 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 Santé/Veggirama chain in 1999,
- 74 locations from the La Crémère 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,
- 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. As at the date of acquisition, there were 117 Taco Time restaurants operating in Western Canada,
- On May 1, 2009, the Company acquired the outstanding shares of Country Style Food Services Holdings Inc. with the 480 outlets operated by its subsidiaries,
- On September 16, 2010, the Company acquired the outstanding shares of Groupe Valentine inc. and of its network of 95 stores. The transaction was effective September 1, 2010,
- On August 24, 2011, the Company acquired the assets of Jugo Juice International Inc. with 136 outlets in operation at the date of closing. The transaction was effective August 18, 2011,
- On November 1, 2011, the Company acquired the assets of Mr. Submarine Limited, with 338 stores in operations at the date of closing,
- On November 10, 2011, the Company acquired the assets of Koryo Korean BBQ Franchise Corp. with 20 stores in operations at the effective date of closing. The transaction was effective November 1, 2011.

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, supplier contributions and sales of other goods and services to franchisees. Revenues from corporate owned locations include sales generated from corporate owned locations. Operating expenses related to franchising 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, rent, supplies and equipment sold to franchisees. Corporate owned location expenses include the costs incurred to operate corporate owned locations.

MTY generates revenues from the food processing business discussed herein. The plant produces various products that range from ingredients and ready to eat food sold to restaurants or other food processing plants to microwavable meals sold in retail stores. The plant generates most of its revenues selling its products to distributors and retailers.

The Company also generates revenues from its distribution center located on the south shore of Montreal. The distribution center mainly serves our Valentine and Franx Supreme franchisees with a broad range of products required in the day-to-day operations of the restaurants.

## **Description of recent acquisitions**

On November 10, 2011, the Company acquired the assets of Koryo Korean BBQ Franchise Corp for an estimated total consideration of \$1.8 million. At the effective date of closing, November 1, 2011, the Koryo network was composed of 19 franchised stores and 1 corporate store. Of the purchase price, MTY withheld an amount of \$0.35 million in holdbacks.

On November 1, 2011, the Company acquired substantially all of the assets of Mr. Submarine Limited and Mr. Sub Realty Inc. for an estimated total consideration of \$23.0 million. At the date of closing, there were 338 Mr. Sub stores in operations, all of which were franchised or subject to an operator agreement. MTY withheld an amount of \$2.5 million as holdback, which will become payable in November 2013.

On August 24, 2011, the Company acquired all of the assets of Jugo Juice International Inc., Jugo Juice Canada Inc. and Jugo Juice Western Canada Inc. for an estimated total consideration of \$15.45 million. At the effective date of closing, August 18, 2011, 136 Jugo Juice outlets were in operations, 2 of which we corporately owned and 134 were franchised. Of the total consideration, MTY withheld \$1.735 million as holdbacks on the transaction.

On December 17, 2010, the Company acquired a 51% interest in a food processing plant. The total transaction value was estimated at approximately \$3.5 million including land, building, equipment, inventories, existing workforce and certifications. The newly formed company contracted at \$3.5 million bank loan to finance the acquisition.

As part of the transaction, one of the shareholders in the newly formed company brought in existing activities from another operating plant, in exchange for mandatorily redeemable preferred shares. One third of the preferred shares will be redeemed annually, at a value contingent on the performance of the plant. The value of such shares was estimated at \$300,000 at the inception of the shareholders' agreement and subsequently revalued at \$200,000 following changes in the purchase price allocation.

## Summary of quarterly financial information

Quarters ended								
in thousands of \$	May 2010 <sup>(1)</sup>	August 2010 <sup>(1)</sup>	November 2010 <sup>(1)</sup>	February 2011	May 2011	August 2011	November 2011	February 2012
Revenue	\$17,287	\$15,942	\$19,344	\$16,761	\$18,629	\$19,852	\$23,116	\$21,945
Net income and comprehensive income attributable to owners	\$3,809	\$4,151	\$4,483	\$3,490	\$3,570	\$4,409	\$4,725	\$4,392
Per share	\$0.20	\$0.22	\$0.23	\$0.18	\$0.19	\$0.23	\$0.25	\$0.23
Per diluted share	\$0.20	\$0.22	\$0.23	\$0.18	\$0.19	\$0.23	\$0.25	\$0.23

(1) — The selected information that is presented for the quarters ended in May, August and November 2010 is reported under previous Canadian GAAP and does not reflect the impact of the adoption of IFRS.

## Results of operations for the first quarter ended February 29, 2012

### Revenue

During the first three months of our 2012 fiscal year, the Company's total revenue increased by 31% to reach \$21.9 million. Revenues for the four segments of business are broken down as follows:

	February 29, 2012 (\$ million)	February 28, 2011 (\$ million)	Variation
Franchise operation	15.5	12.1	28%
Corporate stores	3.3	2.5	34%
Distribution	1.3	1.2	8%
Food processing	2.0	1.0	96%
Intercompany transactions	-0.1	-0.0	N/A
<b>Total operating revenues</b>	<b>21.9</b>	<b>16.8</b>	<b>31%</b>

As is shown in the table above, revenue from franchise locations progressed by 28%. Several factors contributed to the variation, as listed below:

	\$million
Revenues, first quarter of 2011	12.1
Increase in recurring revenue streams	3.5
Decrease in turn-key, sales of material to franchisees and rent revenues	-0.4
Increase in initial franchise fees	0.1
Other non-material variations	0.2
<u>Revenues, first quarter of 2012</u>	<u>15.5</u>

During the first quarter of 2012, the Company benefitted from the results of its most recent acquisitions, Mr. Sub, Jugo Juice and Koryo, which account for \$2.6 million of the increase in recurring streams of revenues. Other factors accounting for the increase in royalties include a favorable same-store-sales growth as well as the good performance of stores opened in the last 12 months.

Revenue from corporate owned locations increased 34%, to \$3.3 million during the first three months of our 2012 fiscal period. The increase is due to the consolidation of certain Special Purpose Entities acquired with Mr. Sub during the fourth quarter of 2011, which generated approximately \$1.3 million during the period. The offset is mainly coming from the reduction caused by the sale of a high-volume restaurant at the end of the first quarter of 2011.

The Company also generated food processing revenues of \$2.0 million during the quarter, nearly doubling the 2011 numbers. The increase is attributable to the timing of the acquisition in the first quarter of 2011 as well as to the transition period which affected the performance of the plant in the early stages following the transaction.

### **Cost of sales and other operating expenses**

During the first quarter of 2012, operating expenses increased by 27% to \$14.6 million, from \$11.5 million for the same period in 2011. Operating expenses for the four business segments were incurred as follows:

	February 29, 2012 (\$ million)	February 28, 2011 (\$ million)	Variation
Franchise operation	8.1	6.8	20%
Corporate stores	3.4	2.5	39%
Distribution	1.2	1.1	14%
Food processing	2.0	1.2	70%
Intercompany transactions	-0.1	-0.0	N/A
<u>Total operating expenses</u>	<u>14.6</u>	<u>11.5</u>	<u>27%</u>



Operating expenses related to the franchising operations increased by \$1.3 million, mainly as a result the additional expenses created by the operations of Jugo Juice and Mr. Sub.

During the period, expenses for corporate owned locations increased by \$0.9 million. The increase is caused by the consolidation of the Special Purposes Entities of Mr Sub.

The expenses of the food processing plant were up by 70%, for the reasons described in the Revenues section above.

### Earnings before interest, taxes, depreciation and amortization (EBITDA)

	Three months ended					
	February 29, 2012					
(In millions)	Franchise	Corporate	Distribution	Processing	Consolidation	Total
Revenues	\$15.46	\$3.35	\$1.27	\$2.01	\$-0.14	\$21.95
Expenses	\$8.08	\$3.44	\$1.21	\$1.97	\$-0.14	\$14.56
EBITDA <sup>(1)</sup>	\$7.38	-\$0.09	\$0.06	\$0.04	\$0.00	\$7.38
EBITDA as a % of Revenue	48%	N/A	5%	2%	N/A	34%

	Three months ended					
	February 28, 2011					
(In millions)	Franchise	Corporate	Distribution	Processing	Consolidation	Total
Revenues	\$12.06	\$2.50	\$1.18	\$1.02	-\$0.0	\$16.76
Expenses	\$6.76	\$2.48	\$1.07	\$1.16	-\$0.0	\$11.47
EBITDA <sup>(1)</sup>	\$5.31	\$0.02	\$0.11	-\$0.14	\$0.0	\$5.29
EBITDA as a % of Revenue	44%	1%	9%	N/A	N/A	32%

EBITDA (income before income taxes, interest on long-term debt, depreciation and amortization) is not an earnings measure recognized by IFRS and therefore may not be comparable to similar measures presented by other companies.

<sup>(1)</sup>EBITDA is defined as operating revenues less operating expenses.

EBITDA increased by 39%, from \$5.3 million to \$7.4 million for the three months ended February 29, 2012.

During the period, the franchising operations generated \$7.4 million in EBITDA, a 39% increase over the results of the first quarter of 2011. The increase is mainly attributable to the contribution of recent acquisitions, the increase in same-store-sales and the performance of stores opened in the last twelve months.

EBITDA from franchise operations as a percentage of revenue increased to 48% because of the lower relative weight of revenues generated by the deliveries of turnkeys and materials to franchisees, which typically generate lower profit margins.

EBITDA from corporate owned locations declined slightly during the first quarter, mainly because of the impact of the sale of a highly profitable store late in the first quarter of 2011.

The food processing plant generated a \$0.04 million EBITDA in the first quarter of 2012, while it had recorded a loss during the same period last year; 2011 results had been affected by transition costs and various transition-related factors that caused EBITDA to be weak for that period.

### **Net income**

For the three months ended February 29, 2012, MTY reported a net income and comprehensive income attributable to its owners of \$4.4 million or \$0.23 per share (\$0.23 per diluted share) compared to \$3.5 million or \$0.18 per share (\$0.18 per diluted share) for the same period last year, representing a net income increase of 26%.

The increase in net income is mostly attributable to the impact of recent acquisitions as well as to strong generic growth in revenues, which more than offset the decline in the non-recurring other income items.

### **Amortization expense**

The amortization of intangible assets was up by \$0.2 million because of the amortization of the recently acquired franchise rights of Jugo Juice, Mr. Sub and Koryo.

### **Other income**

The gains on disposal of assets, which result from the sale of the assets of corporate stores, decreased to \$0.1 million in 2012 compared to a gain of \$0.7 million during in 2011. The unusual 2011 gain was mainly caused by the sale of one corporate restaurant that generated above-average returns and thus commanded a higher sales price.

### **Income taxes**

The provision for income taxes as a percentage of income before taxes increased by 4.4% during the quarter compared to the same period last year, mainly because of the lower tax burden on certain types of income realized in 2011. The Company also adjusted some reserves and estimates used to calculate the provision as of November 30, 2011, which resulted in additional charges recorded in the first quarter of 2012.

## Contractual obligations and long-term debt

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 (in thousands of \$)	Long term debt	Net lease commitments	Total contractual obligations
12 months ending February 2013	\$2,438	\$2,820	\$5,258
12 months ending February 2014	\$3,897	\$2,715	\$6,612
12 months ending February 2015	\$292	\$2,230	\$2,522
12 months ending February 2016	\$292	\$1,954	\$2,246
12 months ending February 2017	\$2,406	\$1,722	\$4,128
Balance of commitments	\$-	\$4,338	\$4,338
	<b>\$9,325</b>	<b>\$15,829</b>	<b>\$25,154</b>

for total commitments, please refer to February 29, 2012 consolidated condensed interim financial statements

Long-term debt includes non-interest bearing holdbacks on acquisitions, shareholder loans contracted by subsidiaries with the minority shareholders, a bank loan used to finance the acquisition of the food processing plant acquired in December 2010 as well as mandatorily redeemable preferred shares issued to a minority shareholder of a subsidiary.

In addition to the above, the Company has entered into supplier agreements for purchases of coffee beans, wheat, sugar and shortening for delivery between March 2012 and December 2012. The total commitment amounts to \$1.5 million.

In relation to the items listed above, the Company has entered into contracts to minimize the impact of variations in foreign currencies. The total commitment on these contracts amounts to approximately \$1.6 million.

## Liquidity and capital resources

Cash and highly liquid temporary investments totalled \$16.1 million on February 29, 2012, an increase of \$5.5 million since the end of our 2011 fiscal period. The increase is attributable to the strong cash flows generated during the first quarter of 2012.

Cash flows generated by operating activities were \$6.4 million. Excluding the variation in non-cash working capital items, our operations generated \$8.7 million in cash flows, compared to \$5.2 million in 2011.

The main drivers of the \$3.5 million increase are 39% increase in EBITDA discussed above as well as the receipt of material amounts of deferred revenues that will be recognized into income in the coming quarters.

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 February 29, 2012. The facility, when used, bears interest at the bank's annual prime rate plus 1.00%.

Cash flows generated by our operations are typically invested until they are needed to fund acquisitions.

### **Statement of financial position**

The temporary investments are comprised of highly liquid, short-term notes and guaranteed investment certificates valued at fair value. They have maturity dates between March 2012 and June 2012 and have rates of return between 1.02% and 1.62% (1.02% to 1.62% in November 2011).

Accounts receivable at the end of the first quarter were at \$9.6 million, a decrease of \$0.9 million compared to the balance at the end of our 2011 fiscal period. The decrease is due to the typically lower amounts receivable for sales to franchisees (including turnkeys) at the end of the first quarter of every year.

Property, plant and equipment and intangible assets both decreased during the first quarter, mainly as a result of the depreciation and amortization recorded during the period.

Accounts payable decreased to \$12.0 million from \$13.5 million between November 30, 2011 and February 29, 2012. This decrease is in part caused by the settlement of certain obligations resulting from the acquisitions of Jugo Juice and Mr. Sub; it is also related to the seasonal nature of certain activities, and as such varies somewhat in line with the amount of accounts receivable.

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. The balance as at February 29, 2012 was \$2.8 million, an increase of \$1.2 million compared to the balance at year end. The variation is due to increases in both franchise fee deposits and distribution rights; franchise fee deposits are dependent on the level of activity and deliveries during a certain period; distribution rights were impacted by material receipts during the first quarter. These amounts will be recognized into revenues as they are earned.

The long-term debt is composed of non-interest bearing holdbacks on acquisitions, of bank loans contracted by a subsidiary to finance an acquisition, of loans payable by subsidiaries to their minority shareholders and of mandatorily redeemable preferred shares payable to a minority shareholder of a subsidiary. There were no material issuances or reimbursement during the quarter.

The loans payable by a subsidiary to non-controlling shareholders carry no terms of repayment and will be repaid when this subsidiary generates sufficient cash flow to repay its debt without impairing its operations. One third of the preferred shares will be redeemed annually at a value that is contingent on the performance of a subsidiary. Management expects that the value of the preferred shares at redemption will be approximately \$200,000.

Further details on the above statement of financial position items can be found in the notes to the February 29, 2012 condensed interim consolidated financial statements.

## Capital stock

No shares were issued during the first quarter ended February 29, 2012. As at April 26, 2012 there were 19,120,567 common shares of MTY outstanding.

## Location information

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.

	<b>Number of locations three months ended February 2012</b>	Number of locations three months ended February 2011
Franchises, beginning of period	2,233	1,701
Corporate owned, beginning of period	30	26
Opened during the period		
Mall	10	7
Street	8	11
Non-traditional	12	10
Closed during the period		
Mall	(9)	(3)
Street	(8)	(7)
Non-traditional	(44)	(4)
<b>Total end of period</b>	<b>2,232</b>	<b>1,741</b>
Franchises, end of period	2,206	1,714
Corporate owned, end of period	26	27
<b>Total end of period</b>	<b>2,232</b>	<b>1,741</b>

The net reduction in the number of stores during the first quarter of 2012 is 31 stores, compared to a net addition of 14 stores for the same period a year ago. The main driver

of the net reduction is the termination of a contract that resulted in the loss of 28 low-volume non-traditional stores.

Subsequent to the end of the quarter, another non-traditional contract was terminated. It is expected that approximately 21 locations will be closed during the second and third quarter as a result of this event.

At the end of the period, the Company had 26 corporate stores, a net decrease of four. During the quarter, four corporate-owned locations were sold, one was added and one was closed.

As at February 29, 2012, there were two test locations in operation, all of which were excluded from the numbers presented above.

The chart below provides the breakdown of MTY's locations and system sales by type:

Location type	% of location count		% of system sales 3 months ended	
	<b>February 29, 2012</b>	February 28, 2011	<b>February 29, 2012</b>	February 28, 2011
Shopping mall & food court	<b>37%</b>	39%	<b>49%</b>	54%
Street front	<b>37%</b>	27%	<b>41%</b>	38%
Non-traditional format	<b>26%</b>	34%	<b>10%</b>	8%

The geographical breakdown of MTY's locations and system sales consists of:

Geographical location	% of location count		% of system sales 3 months ended	
	<b>February 29, 2012</b>	February 28, 2011	<b>February 29, 2012</b>	February 28, 2011
Ontario	<b>47%</b>	45%	<b>37%</b>	33%
Quebec	<b>27%</b>	33%	<b>32%</b>	39%
Western Canada	<b>20%</b>	16%	<b>25%</b>	21%
Maritimes	<b>2%</b>	2%	<b>1%</b>	1%
International	<b>4%</b>	4%	<b>5%</b>	6%

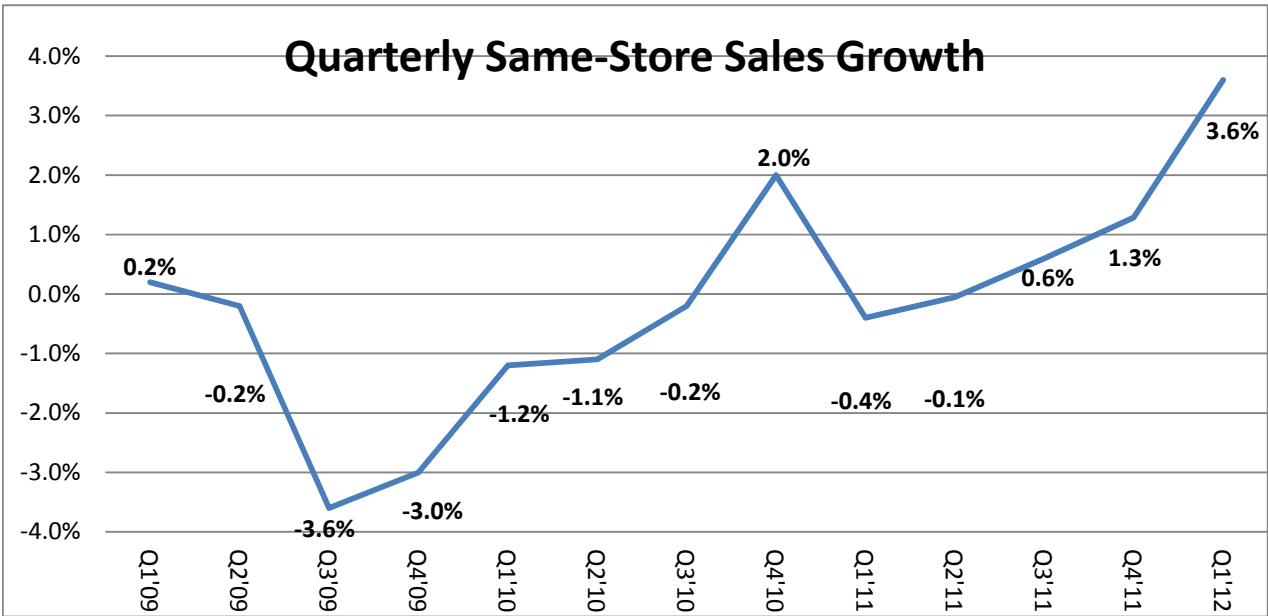
### Same-store sales

During the quarter, same-stores sales have improved by 3.64% over the same period last year, our strongest performance since the third quarter of 2007.

Most of our concepts experienced growth in same-store sales during the quarter, with a few achieving double-digit growth. The growth was consistent from one type of restaurants to another. The restaurants located in western provinces experienced the strongest growth, while those located in Ontario were stable over last year's number.

A portion of the growth in same-store sales is also attributable to the additional day of sales realized on February 29 of this year; this accounts for approximately one third of the growth realized.

The following table shows quarterly information on same-stores sales growth for the last 13 quarters:



## **System wide sales**

System wide sales for the first three months of our 2012 fiscal year grew 39%, reaching \$163.2 million during period, compared to \$117.7 million for the same period last year.

Approximately 80% of the increase in system wide sales for the year is attributable to the acquisitions of Mr. Sub, Jugo Juice and Koryo. Approximately 10% of the increase comes from the growth in the same-store sales, and the rest is due to new restaurants opened in the last 12 months.

System wide sales include sales for corporate and franchise locations and exclude sales realized by the distribution center or by the food processing plant.

## **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 extends the contract with Boxe Comm on a monthly basis since May 2011, subject to terms and conditions contained in the Agreement. For the three-month period ended February 29, 2012, MTY has paid an amount of \$12,000 to Boxe Comm.

## **Stock options**

During the period, no options were granted or exercised. As at February 29, 2012 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 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. Sales for shopping malls locations are also higher than average in December during the Christmas shopping period.

## **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.

## **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 influenced 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 limits on pricing, either of which could reduce revenue and operating income.

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

## Related party transactions

Balances and transactions between the Company and its subsidiaries, which are related parties of the Company, have been eliminated on consolidation. Details of transactions between the Company and other related parties are disclosed below.

### Compensation of key management personnel

The remuneration of key management personnel and directors during the period was as follows:

<i>(in thousands)</i>	Period ended February 29, 2012	Period ended February 28, 2011
	\$	\$
Short-term benefits	139	138
Post-employment benefits, share-based payments and other long-term benefits	Nil	Nil
<b>Total remuneration of key management personnel</b>	<b>139</b>	<b>138</b>

Key management personnel is composed of the Company's CEO and CFO. The remuneration of directors and key executives is determined by the Board of directors having regard to the performance of individuals and market trends.

Given its widely held share base, the Company does not have an ultimate controlling party; its most important shareholder is its CEO, who controls 26% of the outstanding shares.

The Company also pays employment benefits to individuals related to members of the key management personnel described above. Their total remuneration was as follows

<i>(in thousands)</i>	Period ended February 29, 2012	Period ended February 28, 2011
	\$	\$
Short-term benefits	98	89
Post-employment benefits, share-based payments and other long-term benefits	nil	nil
<b>Total remuneration of employees related to key management personnel</b>	<b>98</b>	<b>89</b>

A corporation owned by individuals related to key management personal has participation in two of the Company's subsidiaries. During the period, dividends of nil (2011-nil) were

paid by those subsidiaries to the above-mentioned company, and advances of nil (2011-nil) were repaid.

### **Critical accounting estimates**

In the application of the Company's accounting policies, which are described in note 3 of the consolidated condensed interim financial statements, the directors are required to make judgements, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

### **Critical judgements in applying accounting policies**

The following are the critical judgements, apart from those involving estimations, that management has made in the process of applying the Company's accounting policies and that have the most significant effect on the amounts recognized in the condensed interim consolidated financial statements.

#### Identification of cash-generating units

The Company assesses whether there are any indicators of impairment for all non-financial assets at each reporting period date. Doing so first requires the identification of cash-generating units; the determination is done based on management's best estimation of what constitutes the lowest level at which an asset or group of asset has the possibility of generating cash inflows.

#### Revenue recognition

In making their judgement, management considered the detailed criteria for the recognition of revenue from the sale of goods and for construction contracts set out in IAS 18 Revenue and, in particular, whether the Company had transferred to the buyer the significant risks and rewards of ownership of the goods.

#### Consolidation of special purpose entities

In determining which entities are required to be consolidated in the fashion described below, the Company must exercise judgment to determine who has *de facto* control of the entities being considered. Such judgment is reassessed yearly to take into account the most recent facts relevant to each entity's situation.

## **Key sources of estimation uncertainty**

The following are the key assumptions concerning the future, and other key sources of estimation uncertainty at the end of the reporting period, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

### **Business combinations**

For business combinations, the Company must make assumptions and estimates to determine the purchase price allocation of the business being acquired. To do so, the Company must determine the acquisition-date fair value of the identifiable assets acquired, including such intangible assets as franchise rights and trademarks, and liabilities assumed. Goodwill is measured as the excess of the fair value of the consideration transferred including the recognized amount of any non-controlling interest in the acquiree over the net recognized amount of the identifiable assets acquired and liabilities assumed, all measured at the acquisition date. These assumptions and estimates have an impact on the asset and liability amounts recorded in the condensed interim consolidated statement of financial position on the acquisition date. In addition, the estimated useful lives of the acquired amortizable assets, the identification of intangible assets and the determination of the indefinite or finite useful lives of intangible assets acquired will have an impact on the Company's future profit or loss.

### **Impairment of non-financial assets**

The recoverable amounts of the Company's assets is generally estimated based on value-in-use calculations as this was determined to be higher than fair value less cost to sell, except for certain corporate store assets for which fair value less cost to sell was higher than their value in use. The fair value less cost to sell of corporate stores is generally determined by estimating the liquidation value of the restaurant equipment.

Other than the value of the assets of certain corporate stores and of one of the company's trademarks, the value in use of cash generating units ("CGUs") tested was higher or equal to the carrying value of the assets. An impairment charge of \$229,000 was recognized to reduce the value of the impaired assets at the date of transition. The impairment assessments were established using a 17% discount rate on the corporate store assets and 15% on the trademarks and franchise rights. No further impairment charges were required as at November 30, 2011 and February 29, 2012.

These calculations use our best estimate of future cash flows, using previous year's cash flows for each CGU to extrapolate a CGU's future performance to the earlier of the termination of the lease (if applicable) or 5 years and a terminal value is calculated beyond this period, assuming no growth to the cash flows of previous periods.

A decrease in annual cash flows of 1% would result in no additional impairment. Similarly, increasing the discount rate by 1% would result in an additional impairment of \$4,000.

## Impairment of goodwill

Determining whether goodwill is impaired requires an estimation of the value in use of the CGUs to which goodwill has been allocated. The value in use calculation requires management to estimate the future cash flows expected to arise from the cash-generating unit and a suitable discount rate in order to calculate present value. It was determined that goodwill is not impaired as at February 29, 2012, November 30, 2011 and December 1, 2010.

The Company used a 13% discount rate for its assessment of goodwill. No growth was applied to the cash flows used to estimate the terminal value.

A decrease of 1% in cash flows or an increase of 1% of the discount rate would have resulted in no impairment of the Company's goodwill.

## Useful lives of property, plant and equipment

As described at Note 3 of the condensed interim consolidated financial statements, the Company reviews the estimated useful lives of property, plant and equipment at the end of each reporting period. During the current year, management determines that the useful lives of certain items of equipment should be shortened or extended, due to various factors including technology, competition and revised service offerings. During Q1, the Company was not required to adjust the useful lives of any assets based on the factors described above.

## Provisions

The Company makes assumptions and estimations based on its current knowledge of future disbursements it will have to make in connection with various events that have occurred in the past and for which the amount to be disbursed and the timing of such disbursement are uncertain at the date of producing its financial statements.

## Valuation of financial instruments

As described in note 21 of the condensed interim consolidated financial statements, the Company uses valuation techniques that include inputs that are not based on observable market data to estimate the fair value of certain types of financial instruments. Note 21 provides detailed information about the key assumptions used in the determination of the fair value of financial instruments.

Management believe that the chosen valuation techniques and assumptions used are appropriate in determining the fair value of financial instruments.

### Consolidation of special purpose entities

The Company is required to consolidate a small number of special purpose entities. In doing so, the Company must make assumptions with respect to some information that is either not readily available or that is not available within reporting time frames. As a result, assumptions and estimates are made to establish a value for the current assets, short-term and long-term liabilities and results of operations in general.

### Onerous contracts

A provision for onerous contracts is recognized when the unavoidable costs of meeting our obligations under the contract exceed the expected benefits to be received from the contract. The provision is measured at the present value of the lower of the expected cost of terminating the contract and the expected net cost of completing the contract.

### Contingencies

The Company is involved in various litigation and disputes as a part of our business that could affect some of our operating segments. Pending litigations represent potential loss to our business.

We accrue potential losses if we believe the loss is probable and can be reasonably estimated, based on information that is available at the time. Any accrual would be charged to earnings and included in accounts payable and accrued liabilities. Any cash settlement would be deducted from cash from operating activities. We estimate the amount of the loss by analyzing

### **Accounting policies adopted in 2012**

On December 1, 2010, MTY adopted International Financial Reporting Standards for its financial reporting, using December 1, 2010 as its transition date. Accordingly, the consolidated condensed interim financial statements for the first quarter of 2012 and comparative figures have been prepared in accordance with IFRS 1 “First-Time Adoption of International Financial Reporting Standards” and IAS 34 “Interim Financial Reporting” issued by the International Accounting Standards Board (“IASB”).

The accounting policies used to prepare these financial statements and the comparative figures are presented in Note 3 of the consolidated condensed interim financial statements for the first quarter ended February 29, 2012. These accounting policies have been applied retrospectively to December 1, 2010. Reconciliations for the Company’s income and financial position are presented in Note 35 of the condensed interim consolidated financial statements.

The following standards had an impact on the financial information that had previously been presented in accordance with Canadian GAAP:

### IFRS 3 “Business Combinations”

IFRS 3 eliminated the concept of negative goodwill and instead introduces “gain on bargain purchase”. Under Canadian GAAP, when the consideration paid for an acquisition was lower than the fair value of the identifiable assets received, the difference was pro-rated over the non-financial assets acquired. Under IFRS 3, a gain needs to be recognized on the statement of comprehensive income. This resulted in the restatement of one of the acquisitions realized during our 2011 fiscal year; as a result, the historical cost of the non-financial assets acquired was increased by \$0.1 million, deferred income taxes were restated to reflect the variation in the temporary differences and the depreciation charge on the increased cost of the property, plant and equipment was also restated. The net impact on the net income and comprehensive income was \$0.1 million.

### IAS 12 “Income Taxes”

Under IFRS, deferred taxes related to intangible assets and goodwill are accounted for differently than they were under Canadian GAAP when intangible assets are acquired through a business combination. Upon initial recognition of the business combination, a long-term deferred tax asset or liability must be recognized when a difference, temporary or permanent, exists between the fair value of an asset and its tax base according to the applicable corporate tax laws. Specifically, the Company had to restate the deferred taxes on its trademarks. Because the Company had elected not to apply IFRS 3 to acquisitions made prior to the transition date, the adjustment to deferred taxes related to this period was applied against retained earnings. For acquisitions subsequent to that date, the adjustment impacted the amount of goodwill recognized on each business combination.

In addition, IAS 12 eliminates the short-term portion of deferred income taxes. Consequently, short-term deferred tax assets are now reported with long term assets. As at December 1, 2010, the Company reclassified an amount of \$3.6 million in such fashion.

### IAS 16 “Property, Plant and Equipment”

The Company has elected to use the cost method of accounting for its property, plant and equipment (“PP&E”) and will continue to use this method to recognize such assets.

Other than the impact on property, plant and equipment (“PP&E”) of IFRS 3 discussed above, the Company has identified a conversion adjustment resulting from a difference in the consumption patterns of components of PP&E. Under IFRS, components of capitalized assets are required to be isolated and depreciated separately. Previously, components of one given asset were depreciated as a whole. The effect of this change has been to reduce the carrying value of PP&E by \$0.04 million at the date of transition, December 1, 2010, reduce the deferred tax liability by \$0.01 million and reduce retained earnings by the net of the two previously mentioned amounts. Subsequent depreciation and gains or losses on disposition were also impacted by the change in the depreciation policy.

## IAS 18 “Revenue”

Under Canadian GAAP, the Company accounted for its turnkey projects using the completed contract method and as a result recognized revenues, expenses and profits from projects once they were delivered to the franchisees. Under IFRS, the Company is required to use the percentage of completion method, which accelerates the recognition of revenues and expenses on individual projects. Accordingly, accounts receivable, accounts payable and inventories of projects under construction held for resale had to be restated.

As of December 1, 2010, the Company had to increase its retained earnings by \$0.10 million for amounts that should have been recognized in the previous fiscal period; as a result, the net income of the subsequent period, in which such profits had been recognized under Canadian GAAP, were reduced by the same amount. The reversal of revenues and expenses recognized in previous fiscal periods on transition date creates a reduction of revenues in the first quarter of 2011 of \$1.08 million, a reduction of expenses of \$0.94 million and a reduction of the income tax expense of \$0.04 million. This change is partly offset by additional revenues and expenses recognized in the first quarter of 2011. The net impact is presented in Note 35 to the condensed interim consolidated financial statements.

## IAS 39 “Financial instruments: recognition and measurement”

Under Canadian GAAP, the Company did not discount the non-interest bearing holdbacks on its acquisitions because a specific exemption existed. Under IFRS, such exemption is no longer available; as a result, the Company discounted its non-interest bearing holdbacks and adjusted the consideration paid for its acquisitions accordingly, with the impact of the reduction in the fair value of the holdbacks being allocated to goodwill.

Because of the exemption available under IFRS 1, the Company did not, however, restate the purchase price of the Valentine acquisition; the differences between the carrying values of the holdbacks per Canadian GAAP and IFRS were offset into retained earnings. The impact on retained earnings was \$0.1 million.



## **Future accounting policies**

### **IFRS 9 “Financial Instruments”**

IFRS 9 “Financial Instruments” was issued in November 2009 and contains requirements for financial assets. It addresses classification and measurement of financial assets and replaces the multiple category and measurement models in IAS 39 “Financial Instruments: Recognition and Measurement” for debt instruments with a new mixed measurement model having only two categories: amortized cost and fair value through profit or loss. IFRS 9 also replaces the models for measuring equity instruments, and such instruments are either recognized at fair value through profit or loss or at fair value through other comprehensive income. Where such equity instruments are measured at fair value through other comprehensive income, dividends are recognized in profit or loss to the extent they do not clearly represent a return on investment; however, other gains and losses (including impairments) associated with such instruments remain in accumulated other comprehensive income indefinitely.

In October 2010, the IASB amended IFRS 9 “Financial Instruments,” which replaced IFRS 9 “Financial Instruments” and IFRIC 9 “Reassessment of Embedded Derivatives.” This change provides guidance on classification, reclassification and measurement of financial liabilities and on the presentation of gains and losses, through profit or loss, of financial liabilities designated as measured at fair value. The requirements for financial liabilities, added in October 2010, largely replicate the requirements of IAS 39 “Financial Instruments: Recognition and Measurement,” except with respect to changes in fair value attributable to credit risk for liabilities designated as measured at fair value through profit or loss, which would generally be recognized in other comprehensive income.

This new standard applies to fiscal years beginning on or after January 1, 2015. Early application is permitted.

### **IFRS 10 “Consolidated Financial Statements”**

In May 2011, the IASB issued IFRS 10 “Consolidated Financial Statements,” which establishes principles for the preparation and presentation of consolidated financial statements when an entity controls one or more other entities. IFRS 10 provides a single consolidation model that identifies control as being the basis for consolidation. The new standard describes how to apply the principle of control to identify situations when a company controls another company and must therefore present consolidated financial statements. IFRS 10 also provides disclosure requirements for the presentation of consolidated financial statements. IFRS 10 cancels and replaces IAS 27 “Consolidated and Separate Financial Statements” and SIC-12 “Consolidation – Special Purpose Entities.”

This new standard applies to fiscal years beginning on or after January 1, 2013. Early application is permitted.

## IFRS 12 “Disclosure of Interests in Other Entities”

In May 2011, the IASB issued IFRS 12 “Disclosure of Interests in Other Entities.” IFRS 12 incorporates, in a single standard, guidance on disclosing interests in subsidiaries, joint arrangements, associates and structured entities. The objective of IFRS 12 is to require the disclosure of information that enables users of financial statements to evaluate the basis of control, any restrictions on consolidated assets and liabilities, exposures to risks arising from interests in non-consolidated structured entities and the share of minority interests in the activities of consolidated entities.

This new standard applies to fiscal years beginning on or after January 1, 2013. Early application is permitted.

## IFRS 13 “Fair Value Measurement”

In May 2011, the IASB issued a guide to fair value measurement providing note disclosure requirements. The guide is set out in IFRS 13 “Fair Value Measurement,” and its objective is to provide a single framework for measuring fair value under IFRS. It does not provide additional opportunities to use fair value.

This new standard applies to fiscal years beginning on or after January 1, 2013. Early application is permitted.

## IAS 1 “Presentation of Financial Statements”

In June 2011, the IASB amended IAS 1 “Presentation of Financial Statements” requiring entities preparing financial statements in accordance with IFRS to group together items of other comprehensive income (OCI) that potentially may be reclassified to the profit or loss section of the income statement and to separately group items that will not be reclassified to the profit or loss section of the income statement. The amendments also reaffirm existing requirements that profit or loss and OCI be presented as either a single statement or two consecutive statements.

This amended version of this standard applies to fiscal years beginning on or after July 1, 2012. Early application is permitted.

## IAS 19 “Employee Benefits”

In June 2011, the IASB amended IAS 19 “Employee Benefits” to improve the accounting for pensions and other post-employment benefits. The amendments make important improvements by:

- Eliminating the option to defer the recognition of gains and losses, known as the “corridor method” or the “deferral and amortization approach”;
- Simplifying the presentation of changes in assets and liabilities arising from defined benefit plans, including requiring re-measurements to be presented in other comprehensive income, thereby separating those changes from changes frequently perceived to be the result of day-to-day operations; and

- Enhancing the disclosure requirements for defined benefit plans, providing better information about the characteristics of defined benefit plans and the risks to which entities are exposed through their participation in those plans.

This amended version of this standard applies to fiscal years beginning on or after January 1, 2013. Early application is permitted.

IFRS 7 “Financial Instruments: Disclosures” and IAS 32 “Financial Instruments: Presentation”

In December 2011, the IASB amended IFRS 7 “Financial Instruments: Disclosures” and IAS 32 “Financial Instruments: Presentation” as part of its offsetting financial assets and financial liabilities project. IFRS 7 was amended to harmonize the disclosure requirements with those of the Financial Accounting Standards Board (FASB), while IAS 32 was amended to clarify certain items and address inconsistencies encountered upon practical application of the standard.

The amended versions of IFRS 7 and IAS 32 apply retrospectively to annual periods beginning on or after January 1, 2013 and on or after January 1, 2014, respectively. Early application is permitted.

The Company is assessing the impact of adopting these new standards on its consolidated financial statements and will determine whether it will opt for early application.

## 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.

## Financial instruments and financial risk exposure

In the normal course of business, the Company uses various financial instruments which by their nature involve risk, including market risk and the credit risk of non-performance by counterparties. These financial instruments are subject to normal credit standards, financial controls, risk management as well as monitoring procedures.

### *Fair value of recognized financial instruments*

Following is a table which sets out the fair values of recognized financial instruments using the valuation methods and assumptions described below:

*In thousands of \$*

	<u>At February 29, 2012</u>		<u>At November 30, 2011</u>		<u>At December 1, 2010</u>	
	<u>Carrying amount</u>	<u>Fair value</u>	<u>Carrying amount</u>	<u>Fair value</u>	<u>Carrying amount</u>	<u>Fair value</u>
	\$	\$	\$	\$	\$	\$
Financial assets						
Cash	6,935	6,935	5,995	5,995	5,637	5,637
Temporary investments	9,154	9,154	4,632	4,632	23,383	23,383
Accounts receivable	9,598	9,598	10,496	10,496	8,156	8,156
Loans receivable	1,079	1,079	1,119	1,119	1,245	1,245
Other receivable	-	-	-	-	2,698	N/A
Prepaid and deposits	414	414	312	312	186	186
Financial liabilities						
Accounts payable and accrued liabilities	12,022	12,022	13,540	13,540	10,992	10,992
Long-term debt	9,047	9,047	9,008	9,008	2,726	2,726

### *Determination of fair value*

The following methods and assumptions were used to estimate the fair values of each class of financial instruments:

**Accounts receivable, deposits, accounts payable and accrued liabilities** - The carrying amounts approximate fair values due to the short maturity of these financial instruments.

**Cash and temporary investments** - The carrying amounts are reflected at fair values, which are determined by quoted prices in active markets for identical securities.

**Loans receivable** - The loans receivable bear interest at market rates and therefore it is management's opinion that the carrying value approximates the fair value.

**Other receivable** - The other receivable was the result of post-closing adjustments claimed by the Company from the sellers of Country Style Food Services Holdings Inc. in accordance with the provisions of the purchase agreement. The litigation has been settled during the second quarter of our 2011 fiscal period.

**Long-term debt** - The fair value of long-term debt is determined using the present value of future cash flows under current financing agreements based on the Company's current estimated borrowing rate for a similar debt.

All financial instruments recognized at fair value on the consolidated condensed interim statement of financial position must be measured based on the three fair value hierarchy levels, which are as follows:

Level 1: quote prices (unadjusted) in active markets for identical assets or liabilities;

Level 2: inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e., as prices) or indirectly (i.e., derived from prices); and

Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The Company considers that its temporary investments are classified as Level 1 under the fair value hierarchy.

#### *Risk management policies*

The Company, through its financial assets and liabilities, is exposed to various risks. The following analysis provides a measurement of risks as at February 29, 2012.

#### **Credit risk**

The Company's credit risk is primarily attributable to its trade receivables. The amounts disclosed in the statement of financial position 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:

- Other than receivables from international locations, the Company's broad client base is spread mostly across Canada limits the concentration of credit risk.
- The Company accounts for a specific bad debt provision when management considers that the expected recovery is less than the actual account receivable.

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

The credit risk on the loans receivable is similar to that of accounts receivable. There is currently no allowance for doubtful accounts applicable to the loans receivable.

### **Foreign exchange risk**

The Company has entered into a contract to minimize its exposure to fluctuations in foreign currencies, mainly on purchases of coffee. As of February 29, 2012, the total value of such contracts was approximately \$1,593,000. Immediate liquidation of the contracts at February 29, 2012 would have resulted in a loss of \$26,000.

Other than the above-mentioned contracts, the Company has minimal exposure to the US\$ and is subject to fluctuations as a result of exchange rate variations to the extent that transactions are made in the currency. The Company considers this risk to be relatively limited.

As of February 29, 2012, the Company carried US\$ cash of US\$856,000 and had net accounts receivable of US\$557,000. As a result, a 1% change in foreign exchange rates would result in a change net comprehensive income of \$14,000 Canadian dollars.

### **Interest rate risk**

The Company is exposed to interest rate risk with regards temporary investments. Given the very short term nature of the temporary investments, the risk that changes in interest rates will cause material fluctuations in the fair value is considered limited.

The Company's is also exposed to interest rate risk with its operating line of credit and a bank loan contracted by a subsidiary. Both facilities bear interest at a variable rate and as such the interest burden could potentially become more important. The line of credit is not currently used by the Company; as a result, the exposure to interest rate risk is minimal.

A 100 basis points increase in the bank's prime rate would result in additional interest of \$35,000 per annum on the outstanding bank loan.

## Liquidity risk

The Company actively maintains credit facilities to ensure it has sufficient available funds to meet current and foreseeable financial requirements at a reasonable cost.

The following are the contractual maturities of financial liabilities as at February 29, 2012:

*In thousands of \$*

	Carrying Amount	Contractual Cash Flows	0 to 6 Months	6 to 12 Months	12 to 24 Months
	\$	\$	\$	\$	\$
Accounts payable and accrued liabilities	12,022	12,022	11,765	257	-
Long-term debt	9,047	9,324	1,809	629	3,897
Interest on long-term debt	N/A	N/A	78	75	140
	21,069	21,347	13,652	961	4,037

## 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 consumers.

Management will maintain its focus on completing the integration of the latest acquisitions and maximizing the value of those new locations and concepts to our network.

Management also remains committed on offering its customers a wide range of innovative menus and modern store designs. The quick service restaurant environment will remain challenging in the future, and management believes that the focus on the food offering, consistency and store design will give MTY's restaurants a strong position to face challenges.

For 2012, the Company expects to open 85 new locations. We will continue to emphasize the growth of our network while 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.

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 February 29, 2012, 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 February 29, 2012, 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 February 29, 2012, 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.

#### Limitations of Controls and Procedures

The Company's management, including the President and Chief Executive Officer and Chief Financial Officer, believes that any disclosure controls and procedures or internal control over financial reporting, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, they cannot provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been prevented or detected. These inherent limitations include the realities judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by unauthorized override of the control. The design of any control system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions.



Accordingly, because of the inherent limitations in a cost effective control system, misstatements due to error or fraud may occur and not be detected.

#### Limitation on scope of design

The Company's management, with the participation of its President and Chief Executive Officer and Chief Financial Officer, has limited the scope of the design of the Company's disclosure controls and procedures and internal control over financial reporting to exclude controls, policies and procedures and internal control over financial reporting of the recently acquired operations of Jugo Juice (acquired August 24, 2011) and Mr. Sub (acquired November 1, 2011). Excluding the goodwill created on the acquisitions, these operations respectively represent 9% and 15% of the Company's assets (1% and 6% of current assets, 11% and 18% of non-current assets); they also represent 9% and 10% of current liabilities (0% and 0% of long-term liabilities), 4% and 14% of the Company's revenues and 4% and 21% of the Company's net income and comprehensive income.

The Company's management, with the participation of its President and Chief Executive Officer and Chief Financial Officer, has also limited the scope of the design of the Company's disclosure controls and procedures and internal control over financial reporting to exclude controls, policies and procedures and internal control over financial reporting of certain special purpose entities ("SPEs") on which the Company has the ability to exercise *de facto* control and which have as a result been consolidated in the Company's consolidated financial statements. For the quarter ended February 29, 2012, these SPEs represent 1% of the Company's current assets, 0% of its non-current assets, 1% of the Company's current liabilities, 0% of long-term liabilities, 1% of the Company's revenues and 0% of the Company's net earnings.

*"Stanley Ma"*

\_\_\_\_\_  
Stanley Ma, Chief Executive Officer

*"Claude St-Pierre"*

\_\_\_\_\_  
Claude St-Pierre, Chief Financial Officer

*"Eric Lefebvre"*

\_\_\_\_\_  
Eric Lefebvre, CA, MBA Vice President Finance