# Peekaboo Beans Inc.

**Management's Discussion and Analysis of Financial Condition and Results of Operations as at December 31st, 2017 and 2016.**

The following is management's discussion and analysis ("MD&A") of Peekaboo Beans Inc.'s financial condition and results of operations for three months ended December 31st , 2017 and 2016, and should be read in conjunction with the interim financial statements and related notes for the same reporting periods. The MD&A will also outline the economic operating conditions and how these influence business activities of Peekaboo Beans Inc.

All references herein refer to the audited financial statements and related notes for three months ended December 31st, 2017 and or 2016, except where otherwise indicated. All financial information is expressed in Canadian dollars ("$"). Unless otherwise indicated, a reference to the "Company" or "Peekaboo" means Peekaboo Beans Inc. The Company's fiscal year is the year ended September 30th "("year-end"). Reference to a "fiscal year" means the Company's year commencing on October 1st of that year and ending on September 30th of the following year. For example, fiscal 2018 means the period beginning October 1st, 2017 and ending September 30th, 2018. Reference to "reported quarter" means the three months commencing on October 1, 2017 and ending December 31, 2017. In addition, reference will be made to "Notes", which refers to the Notes to the Financial Statements.

## Organization of the MD&A

# Peekaboo Beans Inc.

## PART 1 – OVERVIEW AND OUTLOOK

### The Company

Peekaboo Beans Inc. is a direct-sales retailer of children's apparel operating in Canada and the United States of America ("US"). Peekaboo is listed on the TSX Venture Exchange in Canada (Symbol: BEAN) and is the first and only Canadian listed company with a majority female board of directors and executive management.

The Company designs and manufactures children's playwear that is stylish, functional and allows free, unstructured play for children. Peekaboo is helping to create a revolutionary lifestyle brand around the growing culture of children's play by focusing on the Company's core customers, "Parents".

Peekaboo's design team in British Columbia, Canada works with child development specialists, educators, and therapists to review, evaluate and create new designs that take into consideration the developmental needs of children by creating value with versatile pieces and longevity through quality construction.

The fabric that Peekaboo designs in-house for its playwear apparel are third-party tested to guarantee that it is aligned with OEKO-TEK® Standard 100, an independent testing and certification system for all stages of production from textile raw materials to end products. The requirement is that all components of an item comply with the required criteria without exception, including the outer material, sewing threads, linings, prints, etc., as well as non-textile accessories such as buttons, zip fasteners, rivets, etc. for harmful substances and sensitivity to skin contact. In addition, Peekaboo conducts its own third-party lab testing to ensure its dying mills are adhering to the Company's standards that its fabric does not contain harmful levels of heavy metals and other harsh additives that are found in most children's clothing fabrics and dyes.

The Company does not own or operate any manufacturing facilities. Peekaboo works closely with its third-party contract manufacturers who adhere to a vendor code of ethics regarding social and environmental sustainability practices. Peekaboo relies on a limited number of suppliers to provide custom designed fabrics and follows the production of its apparel from raw fiber to finished garment.

Peekaboo's apparel is sold exclusively through a direct-sales network of independent sales representatives or "Stylists" in Canada and the US. The Company expanded into the US in September 2017. The Company does not own, lease or operate any retail store locations. Peekaboo's direct-sales business offers Stylists the business opportunity to generate income and not sacrifice time with their families. To date, the Company has paid out approximately $2.8 million in commissions to its Stylists.

The direct-sales channel allows Peekaboo's Stylists to market actual products directly to customers, provide customers with a higher level of service and encourage repeat purchases through building personal relationships. As Stylists purchase the apparel themselves for their children, they can provide the first-hand testimonial of the quality of the apparel, which serves as a powerful sales tool and is strengthened by ongoing personal contact and education between the Stylists and Parents. The Company's network of Stylists encourages friends to host sales parties or "Pop-ups" in their homes to demonstrate and sell the Company's children's playwear apparel. In return for hosting, the hosts receive free products and discounts. Pop-ups also act as business opportunities for Stylists to gain engagement to book more parties, present the direct-sales business opportunity to potential Stylists and market Peekaboo's brand and apparel. Orders are processed through Peekaboo's online system, and payments are made at Pop-ups or directly on the Company's website, usually by credit cards.

In previous years, Peekaboo produced four seasonal collections each year with the Fall collection being the biggest season for sales. Starting in January 2017, the Company has adopted a new rhythm to launch six collections in one calendar year, with the expectations that more frequent launches will generate more consistent sales and keep the Stylists and customers continuously engaged with Peekaboo's products. In evaluation of this product launch strategy, however, management has decided to resume its four seasonal collections rhythm in the calendar year 2018, which is better aligned with seasonal trend of its product. Management plans to work with its new factory partner to source for special product launches to engage with Stylists and customers in between launches.

As at December 31, 2017, the Company has 783 Stylists across Canada and the US. Stylists join Peekaboo's opportunity for a number of reasons. Many become a Stylist to earn part-time money to contribute to their family's income, and some are drawn to Peekaboo because they can be their own boss and earn substantial rewards based on their skills and hard work. Peekaboo has built a community where the Company helps parents across Canada and the US connect with each other, who share the same belief in play as the Company, and together promote a playful lifestyle for children while also supporting their families at home. Peekaboo has ensured that there is an opportunity for everyone of any lifestyle to become a Stylist.

Peekaboo's direct-sales business model allows the business to grow quickly with modest investment capital as most of the Company's costs are fixed once the investment has been made in the independent sales representative network. Peekaboo incurs minimal incremental direct costs to add new Stylists to the Company's existing markets. Stylist compensation varies directly with sales. Unlike other children's apparel manufacturers, direct-sales model does not require significant expenditures for multiple retail store rent, retail sales staff and capital to hold inventory across a retail store network or costs for marketing and returned goods if sold through independent retail store network. The company's direct-sales model also gives it an advantage over traditional E-commerce retailers who also offer convenience and simplicity but operate with thin margins, expensive shipping, extensive online marketing costs and loss of revenue from returned goods. In direct-sales industry, the Stylists bear the majority of the consumer marketing expenses and sponsors coordinate a good proportion of the recruiting and training of new Stylists.

Peekaboo's primary drivers for sales growth are growing the Stylists network, retaining current Stylists and increasing the average sales per Stylist. Other drivers that influence growth include Stylist and sales manager training and the time and costs to market and recruit new Stylists. Investing in brand awareness through campaigns promoting the importance of play to children's development increases the Stylist retention rate.

The Company's recurring cash requirements include executive and employee salary compensation, distribution and information technology costs, administrative and public company costs.

The Company's recurring working capital requirements include financing the lead-time for inventory and apparel production deposits necessary for seasonal collections. The Company places apparel production deposits several months before the final purchase order and pays for goods before shipment to Canada from Vietnam, which happens several months before the Company receives payment for goods sold. Up to the public listing of the Company in late September 2016, the Company has used interest-bearing loans from related parties to fund the working capital required for the production-to-payment cycle.

The Company sells its apparel and holds cash in Canadian and United States Dollars. The fluctuation in the price of the Canadian dollar, United States Dollars and to a lesser degree, the Vietnamese dong may affect financial performance. The economic health of the economies of North America and to a lesser extent Vietnam may affect the financial performance of the Company.

## Highlights during the most recent quarter

- Raised $1.49 million in gross funding through equity financing
- Continued on US expansion growth in Q1
- Improved gross margin by continued management strategies to reduce discounting of products

## Overall Performance

Growth strategies required the Company to fund a permanent source of working capital for increased inventory and apparel production deposits and capital to fund the time when apparel orders are paid for and when the Company receives payment from Stylists and customers. The advantage of the direct-sales business model is that it allows Peekaboo the flexibility on when to expand as the majority of expansion costs are variable in nature and borne on the Stylist. During the first five months of fiscal 2018, the Company raised $3.7 million gross proceeds in private placements at $0.60 and $0.75 to provide working capital for apparel production deposits and US expansion.

## US Expansion Update

The Company executed a soft launch in the US in September 2017 to begin building the US Stylist network and promoting Peekaboo's brand while the Company further prepares for a global launch with integrated software for both countries. As at March 1, 2018, the Company has recruited 114 US Stylists across 34 states. This equates to 192% growth since the Company's fiscal year end.

In light of the growing Stylist network in both Canada and the expanding US network, the Company hired a new Director of Sales and Field Development, Ms. Cindy Tokoly, in October 2017. Ms. Tokoly previously held the same position with Matilda Jane Clothing, a US children direct sales company, since its inception. The Company also engages Ms. Sandy Spielmaker to act as interim General Manager to oversee the integration of operations in Canada and the US. Ms. Spielmaker has over two decades of expertise in the direct selling world and previously held Chief Sales Officer positions at Scentsy and Origami Owl, and served as VP, Global Sales in Amway. Ms. Tokoly and Ms Spielmaker's primary focus in the Quarter was to grow the US stylist base while preparing for an integration of the Canadian and US software and compensation systems.

The Company has developed an interim compensation plan along with incentive programs to support and facilitate the US Stylists recruitment. Management continues to plan and prepare to launch a global compensation plan in the third quarter of fiscal 2018 that will motivate Stylists to expand and build up strong selling teams. The launch of the global compensation plan will be in conjunction with a global integration of Canadian and US software systems.

The Company has completed most of its ground work for entering the US market in the fourth quarter of fiscal 2017, including engaging with consulting expertise to introduce Peekaboo's unique brand, designing a motivational US compensation plan and customizing US software for Stylist support. Management is encouraged to see the initial results of the well-executed soft launch plan. The Company has seen strong recruitment of US Stylists in January 2018, resulting in 12% of the sales in the second quarter having come from the US market.

With initiatives of software integration to deliver enhanced customer experiences, the launch of first-class global compensation plan and refining the brand's message, management is confident that the Company is well-positioned for strong growth results in North America later this year.

## PART 2 – FINANCIAL PERFORMACE REVIEW

### Summary of Quarterly Results

The following selected financial data as reported by the Company for the three months ended December 31, 2017, which is the first quarter of financial year ending September 2018, has been summarized from the Company's unaudited interim consolidated financial statements and are qualified in their entirety by reference to, and should be read in conjunction with, such financial statements.

The Company has not presented quarterly information for its past eight quarters, as it has not prepared quarterly financial statements for such quarters as a private company prior to fiscal 2016.

| | 2018 Q1 | 2017 Q4 | 2017 Q3 | 2017 Q2 | 2017 Q1 |
|---|---|---|---|---|---|
| Revenue | $ 760,541 | $ 862,160 | $ 976,381 | $ 658,635 | $ 861,131 |
| Net loss | (677,128) | (1,394,063) | (792,285) | (476,021) | (338,035) |
| Loss per share, basic and diluted | $ (0.06) | $ (0.16) | $ (0.08) | $ (0.07) | $ (0.05) |

### Summary of Reported Period Results

*For the three months ended December 31, 2017*

The following analysis of the Company's operating results for the three months ended December 31st, 2017, includes a comparison to the corresponding comparative three months ended December 31st, 2016. Please refer to the Interim Consolidated Statements of Comprehensive Loss.

| | December 31, 2017 | %[1] | December 31, 2016 | %[1] | YoY%[2] |
|---|---|---|---|---|---|
| **Sales** | **$ 760,541** | **-** | $ 861,131 | - | -12% |
| **Cost of sales** | | | | | |
| **Cost of goods sold** | **463,721** | **61%** | 501,931 | 58% | -8% |
| **Stylist commission** | **155,426** | **20%** | 209,180 | 24% | -26% |
| **Gross profit** | **141,394** | **19%** | 150,020 | 17% | -6% |
| **Operating costs** | **626,296** | **82%** | 387,569 | 45% | 62% |
| **Number of Stylists** | **783** | **-** | 704 | - | 11% |

(1) As a percentage (%) of sales.
(2) Year-over-year (YoY) change as a percentage (%).

Sales during the first quarter of 2018 was 12% less than the comparative 2017 period, due to the two seasonal collections launched in this period were smaller compared to the collection launched in the comparative 2017 period. Cost of goods sold increased to $463,721 compared to $501,931 in the comparative period, due to the increased cross-border shipping charges in US expansion. Stylist commission decreased to $155,426 compared to $209,180 in the comparative period due to management's initiatives to adjust commission paid on discounted products. As such, gross profit as a percentage of sales increased to 19% compared to 17% in the comparative period.

Sales are driven by the number of Stylists and the average sales per Stylist per year. The retention rate of Stylists is an equally important driver of sales and is largely influenced by Peekaboo's unique mission, culture and quality apparel. To be an active Stylist, a sales representative must achieve $900 in personal sales in a twelve-month period on a rolling basis.

The Stylists base expanded 11% through organic growth requiring little or no additional costs over the year to 783 Stylists at December 31, 2017, compared to 704 in the comparative period. The Company also had success in digital marketing and social media campaigns initiatives, which proved to be more effective in supporting the Stylists and more cost efficient than previously contracted PR efforts.

The Company's main markets in order of sales were Alberta (35%), British Columbia (34%) and the Maritime provinces (12%).

Operating costs totaled $626,296 increased 62% compared to the prior comparative period due to the addition of support staff, technology infrastructure and consulting services relating to the US expansion launch. Operating expenses related to the operation of a direct-sales company include investment in Stylists training, recruitment and marketing, administrative, distribution and information technology, salary compensation for executives and employees, and operations of public company, which further include professional fees, public company costs, investor relations and share-based compensation.

Executive and employee salaries and administrative expenses increased due to the Company's US expansion initiative, which requires the Company to expand the team and hire additional employees and contractors for Stylists and head office support. As of December 31, 2017, the Company has 19 full and part-time employees in Canada.

The Company incurred approximately $134,749 in distribution and information technology costs in of which approximately $81,000 is for development of the Company's US software and preparation of the global integration of software for both Canada and the US operations in fiscal 2018.

The Company reported an operating loss of $598,478 in the first quarter of fiscal 2018 compared to $294,585 in the comparative period of fiscal 2017.

Investor relations expense was $42,408 for the quarter compared to nil in fiscal 2016 as the Company continued to develop its presence and exposure in the capital market by engagement with marketing and media services to enhance the Company's exposure in the capital markets, which greatly supplemented the Company's effort to successfully closed two rounds of private placements in fiscal 2017 and upcoming fiscal 2018.

Other expenses include interest and finance costs, and foreign exchange losses. Loan interest and other finance costs increased to $65,979 compared to $28,528.

The Company reported a net loss of $677,128 in the first quarter of fiscal 2018 compared to a loss of $338,035 in fiscal 2017. The basic loss per weighted average number of common shares was $0.06 and a loss of $0.05 for the respective periods.

The management is confident that the Company is positioned to see a double-digit growth in the second half of 2018 as the Company's equity financing in 2017 has allowed the management to launch the US expansion initiative to grow its Stylist base across North America. The risk of product launches disruption has been reduced with a new factory term, which will be further explained below in the Liquidity and Capital Resources.

## Liquidity and Capital Resources

The following analysis of the Company's liquidity and capital resources for the three months ended December 31, 2017, includes a comparison to the corresponding, comparative year ended September 30th 2017. Please refer to the Statement of Financial Position and Statement of Cash Flows.

The Company's principal source of funds available are equity financing and to a lesser degree, debt financing.

The Company's tangible assets include cash, inventories, and apparel production deposits. Other assets required for the operation of the Company include trade receivables and software and equipment. Direct sales companies do not account for the value for their independent sales network that sells and distributes its apparel or its brand.

Cash increased 311% to $768,342, during the reported period due to private placements closing in Q1, while trade receivables were immaterial as the Company receives payment in full when a customer places a purchase order with an independent sales representative on the Company's website using their credit cards. The difference is due to the credit card companies' processing time.

Apparel production deposits increased by 581% to $432,351 as the Company provided deposits on the increased 2018 Spring and Summer inventory lines.

Inventories decreased by 21% to $871,258, during the reported period.

Prepaid expense increased by 2% to $213,905 compared to $209,541 the previous year.

Debt repayable within the year consisted of trade payables and accrued liabilities of $683,022, loans that are current totaling $725,655 and commission payable to Stylists of $103,783. Commissions owing to Stylists occur when Stylists elect not to have their sales commissions paid to them but instead applied towards future apparel purchases.

Current loans predominately include $278,250 owing to a Canadian apparel finance company and a demand loan from a venture capital company for $229,643. The venture capital company has lent over $1.2-million of which $1-million has been converted into 974,714 shares of unit financings throughout the year. The Company is currently in negotiation with another current loan holder to extend the lending term.

Trade payables increased slightly to $683,022 from $671,213.

The shareholder equity deficiency decreased and reached to a positive figure of $542,596 during the reported period compared to a deficit of $136,062 a year earlier due to the issuance of shares in private placements.

The statement of cash flows shows the structure of and changes in cash for the three months ended December 31st, 2017 and 2016. The statement contains cash changes in operating activities, investing activities and financing activities. During the reported period, the Company generated $1,318,700 of cash from private placements to hold $768,342 at period end. Operating activities used $734,238 in cash predominately from operating losses during the period. Other than the aforementioned, other uses and generation of cash flows did not materially affect cash flows during the reported period.

## PART 3 – CAPITALIZATION

As of December 31, 2017:

### Shares

Peekaboo had 14,488,701 common shares outstanding, of which 2,054,777 common shares are held in escrow.

On December 20, 2017, the Company issued 2,488,500 common shares at a price of $0.60 per share for gross proceeds of approximately $1.5-million. The brokered portion of the Private Placement consisted of the issuance of 2,113,334 Common Shares and the non-brokered portion of the Private Placement consisted of the issuance of 375,166 Common Shares. The Agents were paid a commission comprised of a cash fee in the amount of $101,440 and issued an aggregate of 169,066 Agents' warrants. Each Agents' warrant is exercisable for one Common Share at a price of $0.60 per Common Share for a period of 24 months from the date of issue. In addition, the Company also issued the Agents 105,666 Common Shares as a corporate finance fee in connection with the Private Placement.

On January 23, 2018, the Company completed a brokered private placement and issued an aggregate of 2,983,333 units of the Company at a price of $0.75 per Unit for gross proceeds of approximately $2.2-million. Each Unit consists of one common share and one half of one common share purchase warrant, exercisable into one common share at $1.00 until February 16, 2020. The Agents were paid a commission of $179,000 in cash and 238,666 Agents' warrants, exercisable at $0.75 per Unit for 24 months. The Company also issued the Agents 149,166 Units as a corporate finance fee in connection with the private placement.

### Warrants

The Company has the following warrants outstanding:

- 300,000 warrants outstanding exercisable at $0.80 per share until March 30, 2019
- 1,428,429 warrants outstanding exercisable at $0.80 per share until May 12, 2019
- 476,385 warrants outstanding exercisable at $0.80 per share until June 29, 2019
- 439,055 warrants outstanding exercisable at $0.80 per share until September 28, 2019
- 169,066 warrants outstanding exercisable at $0.60 per share until December 20, 2019

### Stock Options

During fiscal 2017, 855,000 and 20,000 stock options were issued to management, staff and consultants, respectively on May 12th, 2017 and September 26th, 2017. The options are exercisable into one common share at $0.60 until May 12th, 2019 and September 26th, 2019, respectively.

### Weighted Average Number of Common Shares

The weighted average number of common shares outstanding for the first quarter of fiscal 2018 was 11,972,715 and 6,890,108 for the first quarter of fiscal 2017. The weighted average of outstanding shares incorporates any changes of shares outstanding over a reported period and is used to calculate key financial measures such as earnings per share for the period.

Other than the aforementioned, no other dilutive securities were outstanding at year-end.

## Part 4 – ADDITIONAL INFORMATION

### Transactions Between Related Parties

During the year ended September 30th, 2017, the Company entered into the following related party transactions:

(a) The Company paid its Chief Executive Officer $22,250 (2016 - $22,250) and its Chief Financial Officer $19,625 (2016 - $16,650) in salary (Note 8).
(b) The Company paid $3,840 in share-based compensation to directors.
(c) The Company owes its Chief Financial Officer $252,694 under a convertible promissory note (Note 15). Total interest accrued during the three months ending December 31, 2017 is $5,873 (2016 - $2,768).

## Forward-Looking Statements

This document contains forward-looking statements. The Company's representatives may also make forward-looking statements orally from time to time.

Statements in this document that are not historical facts, including statements about the Company's beliefs and expectations, recent business and economic trends constitute forward-looking statements. Forward-looking statements include, without limitation, statements regarding the outlook for future operations, forecasts of future revenue and expenditures, market conditions or other business plans. Forward-looking statements include statements regarding the intent, belief or current expectations of the Company, primarily on the results of operations, financial position or cash flows of the Company.

The statements are based on current plans, estimates, and projections and are subject to change. A number of factors could cause actual results to differ materially from those contained in any forward-looking statement, and the Company undertakes no obligation to update publicly any changes in light of new information or future events.

Shareholders and potential investors are cautioned that any such forward-looking statements are not guarantees and involve risks and uncertainties. Actual results may differ from those in the forward-looking statements as a result of various factors, such as general economic and business conditions particularly in Canada and North America, including changes in interest rates, actions by government authorities in Canada, including changes in government regulation in the direct-sales industry; political conditions and future decisions by the Company's directors or executive officers in response to changing conditions; the ability to execute prospective business plans; and misjudgments in the course of preparing forward-looking statements.

Material factors and assumptions underlying the Company's expectations regarding forward-looking statements include, among others: the ability of the Company to obtain financing on acceptable terms; that the Company will be able to maintain appropriate levels of liquidity and working capital; stability in the global economic environment particularly in Canada and Vietnam and broadly in regard to North America and Canadian interest rates; and that interest rates and foreign exchange rates, particularly with regard to the Canadian dollar, the United States of America ("United States") dollar ("US$") and to a lesser degree the Vietnamese dong, the currency of Vietnam, will not vary materially from current levels.

Shareholders and potential investors are advised that these cautionary remarks expressly qualify in their entirety all forward-looking statements attributable to the Company or persons acting on its behalf contained in this MD&A.

This forward-looking statement dated March 1, 2018, references CSA Staff Notice 51-330 Guidance regarding the Application of Forward-Looking Information Requirements under National Instrument 51-102 Continuous Disclosure Obligations dated November 20, 2009.

## Accounting Policy

Financial information for fiscal 2018 and 2017 presented and discussed in this MD&A is prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB").

Significant accounting policies and outline the measurement and other accounting policies that are relevant to understanding Peekaboo's financial statements, business operations, and the direct-selling industry.

Changes in accounting policies distinguish how the Company should present and disclose different types of accounting changes in its financial statements. Changes in accounting policies need to be applied retroactively while changes in accounting estimates are accounted for prospectively.

Critical accounting estimates and judgments outline the estimates and assumptions that management made that can significantly affect Peekaboo's financial statements and include inventory valuation, income taxes, and stock-based compensation during fiscal 2018.

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