

Peekaboo Beans Inc.



Management’s Discussion and Analysis of Financial Condition and Results of Operations as at June 30, 2018 and 2017

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 June 30, 2018 and 2017, 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 interim financial statements and related notes for three months ended June 30, 2018 and 2017, 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 April 1, 2018 and ending June 30, 2018. In addition, reference will be made to “Notes”, which refers to the Notes to the Financial Statements.

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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 on the OTCQB in the US (Symbol: PBBSF). The company 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 apparel 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 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.

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.

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 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.

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In previous years, Peekaboo produced four seasonal collections each year with the Fall collection being the biggest season for sales. In January 2017, the Company adopted a new rhythm to launch six collections in one calendar year, with the expectations that more frequent launches would 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 source for special product launches to engage with Stylists and customers in between launches. During the second quarter of 2018, the Company has collaborated with other Canadian brands that share similar values with Peekaboo to create special product drops, including underwears and windbreaker jackets. The initiative has proved to be a success as the additional product mix incentivizes our loyal customers to increase their order size.

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. 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, which 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.

As at June 30, 2018, the Company has 1,057 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 while receiving product discounts, 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.

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. 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 weeks before the Company receives payment for goods sold. Up to the public listing of

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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

- Improved gross margin to 22.2%
- Continued on US expansion growth in Q3 by launching a global integrated site
- Expanded US Stylists to 10% of the current Stylist field

Overall Performance

Growth strategies require the Company to fund a permanent source of working capital for increased inventory and apparel production deposits 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 nine months of fiscal 2018, the Company raised \$3.73 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.

The Company has developed an interim compensation plan along with incentive programs to support and facilitate the US Stylists recruitment. In the third quarter of 2018, management introduced an enrollment initiative that came with a two-piece outfit at a price of \$49. The low entry price proved to successfully incentivize Stylists to join since the initial commitment of \$49 is minimal compared to other direct-sales company. Management continued this initiative in the third quarter and is pleased to see the continued growth of US Stylists in our Stylist field. As at August 27, 2018, the Company has recruited 111 US Stylists across 38 states. The Company has also successfully launched a global integration of Canadian and US software systems, which come with an integrated compensation plan that will better motivate the Stylists.

Management is encouraged to see the reported results of the well-executed soft launch plan. The Company has seen strong recruitment of US Stylists in the third quarter of 2018, resulting in 9% of the sales in the third quarter having come from the US market.

With the launch of software integration and compensation plan, which management believes will enhance both Stylists and customer experiences, the Company is well-positioned for strong growth results in North America later this year.

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PART 2 – FINANCIAL PERFORMANCE REVIEW

Summary of Quarterly Results

The following selected financial data as reported by the Company for the three months ended June 30, 2018, which is the third quarter of financial year ending September 30, 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 as a private company prior to fiscal 2016.

	2018 Q3	2018 Q2	2018 Q1	2017 Q4	2017 Q3	2017 Q2	2017 Q1
Revenue	\$ 695,346	\$ 752,227	\$ 760,541	\$ 862,160	\$ 976,381	\$ 658,635	\$ 861,131
Net loss	(439,869)	(935,345)	(677,128)	(1,394,063)	(792,285)	(476,021)	(338,035)
Loss per share, basic and diluted	\$ (0.03)	\$ (0.07)	\$ (0.06)	\$ (0.16)	\$ (0.09)	\$ (0.07)	\$ (0.05)

Summary of Reported Period Results

For the three months ended June 30, 2018

The following analysis of the Company's operating results for the three months ended June 30, 2018, includes a comparison to the corresponding comparative three months ended June 30, 2017. Please refer to the Interim Consolidated Statements of Comprehensive Loss.

	June 30, 2018	% ¹	June 30, 2017	% ¹	YoY% ²
Sales	\$ 695,346	-	\$ 976,381	-	-29%
Cost of sales					
Cost of goods sold	446,302	64%	560,570	57%	-20%
Stylist commission	94,371	14%	203,183	21%	-54%
Gross profit	154,673	22%	212,628	22%	-27%
Operating costs	557,018	80%	975,443	100%	-43%
Number of Stylists	1,057		837		26%

(1) As a percentage (%) of sales.

(2) Year-over-year (YoY) change as a percentage (%).

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In this quarter, management's focus was to develop diversified initiatives to recruit potential new Stylists and to support the Stylists to engage new customers. Some key initiatives include:

- Continued the \$49 enrollment opportunity for Stylists that incentivizes recruitment by minimizing the direct-sales entry barrier
- Held four Company-host pop-ups across Canada to support the Stylists in creating excitement in their community and reaching new customers by utilizing past seasons' vintage inventory at a discounted price in exchange of no commission being paid in the four pop-ups

Sales during the third quarter of 2018 was 29% less than the comparative period in 2017 because of the aforementioned launch timing differences. In the third quarter of 2018, the Company only released one Summer collection compared to the third quarter of 2017 when two collections were released, Spring and Summer, which accounted for 54% and 45% of the revenues respectively. Both Summer 2018 and Summer 2017 have similar count of new styles, 41 and 38 respectively. Management is pleased with the results of readopting its four annual launch rhythm. In the meantime, the highlighted initiatives also helped expand 26% of the active Stylists base, to 1,057 active Stylists at June 30, 2018, compared to 837 in the comparative period.

Cost of goods sold fell 20% to \$446,302 compared to \$560,570 in the comparative period while sales had decreased 29%. Management has continued limiting discounts for products sold at regular channels, that is, the Stylists' pop-ups. The Company contracted a new factory partner to source Peekaboo's products starting in 2018, and management is encouraged to see the results of reduction in product sourcing costs, which leads to 5% to 10% lower unit cost, varying among different styles. With the increased margins from regular channel sales, management is comfortable with offering past seasons' vintage inventory at a discount to support the Stylists in engaging new customers and promote Peekaboo's brand. Management's objective is to realize more cash proceeds from older inventory to purchase new seasons' products, to which the Company and Stylists will have a large customer base to sell.

Stylist commission decreased to \$94,371 compared to \$203,183 in the comparative period due to management's initiatives to adjust commission paid on discounted products and the aforementioned sales initiatives were non-commissionable. As such, gross profit as a percentage of sales increased to 22.2% compared to 21.8% in the comparative period.

The Company's main markets in order of sales were Alberta (35%), British Columbia (33%) and the Maritime provinces (11%).

Operating costs totaled \$557,018, which decreased compared to the prior comparative mainly due to the Company had not granted any share-based compensation. The Company has also improved its public company operation costs as groundwork of running a public company had been built in the past year. 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. Operations of a public company 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 and other general growth initiatives, which requires the Company to expand the team and hire

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additional employees and contractors for Stylists and head office support. As of June 30, 2018, the Company has 22 full and part-time employees in Canada.

The Company incurred approximately \$68,995 in distribution and information technology costs, compared to \$35,268 in the comparative period in 2017. The increase was solely due to supporting two software systems in Canada and the US and the preparation costs to launch the global integrated website.

Investor relations expense was \$(94,330) for the quarter compared to \$51,770 in the prior comparative period as the Company reclassified prior investor relation expenses into prepaid expenses and continued several marketing and media services campaigns to further develop its presence and exposure in the capital market which greatly supplemented the Company's effort to successfully close two rounds of private placements in the current period, raising gross proceeds of \$3.73 million on the equity markets.

Other expenses include interest and finance costs, and foreign exchange losses. Loan interest and other finance costs decreased to \$30,468 compared to \$78,450 in the comparative period, due to previous loans being converted into equity or repaid.

The Company reported a net loss of \$439,869 in the third quarter of fiscal 2018 compared to a loss of \$792,285 in the comparative period in 2017. The basic loss per weighted average number of common shares was \$0.03 and a loss of \$0.09 for the respective periods.

The management believes that the Company is positioned to seeing a double-digit growth in the second half of 2018 as the Company further develops new sales initiatives in expanding the Company's product reach and support its quickly-growing Stylists base. The Company also expects to generate great synergy from the US-Canada software integration in terms of customer shopping experience, which allows the Company to better collect and analyze customers' data, leading to more effectively incentivizing current customers and targeting potential customers.

Liquidity and Capital Resources

The following analysis of the Company's liquidity and capital resources for the three months ended June 30, 2018, 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 156.7% to \$472,086, during the reported period due to private placements closing in the first two quarters, 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.

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Apparel production deposits increased by 441% to \$343,605 as the Company provided deposits on the increased 2018 Fall and Winter inventory lines.

Inventories increased 18% to \$1,334,323, during the reported period due to the requirement to build up inventory for market expansion into the US and the special product mix initiatives that the Company introduces this year.

Prepaid expense decreased by 28% to \$150,965 compared to \$209,541 the previous year.

Liabilities repayable within the year consisted of trade payables and accrued liabilities of \$333,989, loans that are current totaling \$278,250 and commission payable to Stylists of \$72,365. Commissions owing to Stylists occur when Stylists elect not to have their sales commissions paid to them in cash but instead applied towards future apparel purchases.

Current loans predominately include \$278,250 owing to a Canadian apparel finance company. During the current period, a demand loan from a venture capital company for \$229,643 was repaid.

Trade payables decreased to \$333,989 from \$671,213.

The shareholder equity (deficiency) decreased and reached to a positive figure of \$1,219,899 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 nine months ended June 30, 2018 and 2017. The statement contains cash changes in operating activities, investing activities and financing activities. During the reported period, the Company generated \$3.3 million of cash from private placements to hold \$472,086 at period end. Operating activities used \$2.75 million in cash predominately from operating losses, acquisition of inventory and repayment of liabilities 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 June 30, 2018:

Shares

Peekaboo had 17,646,533 common shares outstanding, of which 2,054,776 common shares are held in escrow.

On December 20, 2017, the Company issued 2,488,500 common shares pursuant to private placement at a price of \$0.60 per share for aggregate gross proceeds of \$1,493,100. A commission of \$101,400 was paid and an aggregate of 169,066 Agents warrants were issued. Each warrant is exercisable for one common share at a price of \$0.60 per common share for a period of 24 months, valued at \$68,643. A corporate finance fee was settled with the issuance of 105,666 common shares, valued at \$63,400 and recorded as share issuance cost.

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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 consisted of one share and one half of one share purchase warrant to purchase another share at \$1.00 for a period of two years. The share purchase warrants were valued at \$417,667 using the residual method. The Company paid share issuance costs of \$267,136 and issued 238,666 share purchase warrants exercisable for two years at \$0.75 for agent's commission. The finders' warrants were valued at \$90,989. The Company also issued the agents 149,166 Units as a corporate finance fee in connection with the private placement. The share purchase warrants on the Units issued as corporate finance fee were valued at \$20,883 using the residual method.

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
- 1,491,666 warrants outstanding exercisable at \$1.00 per share until February 16, 2020
- 313,249 warrants outstanding exercisable at \$0.75 per share until February 16, 2020

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.

During the nine months ended June 30, 2018, 750,000 stock options were issued to consultants and management, exercisable into one common share of the Company at exercise prices of \$0.60 to \$0.80.

Weighted Average Number of Common Shares

The weighted average number of common shares outstanding for the third quarter of fiscal 2018 was 14,432,942 and 8,991,962 for the third 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.

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Part 4 – ADDITIONAL INFORMATION

Transactions Between Related Parties

During the nine months ended June 30, 2018:

- (a) The Company paid its Chief Executive Officer \$105,271 (2017 - \$66,750) and its Chief Financial Officer \$58,875 (2017 - \$58,842) in salary (Note 8).
- (b) The Company paid \$35,254 (2017 - \$270,357) in share-based compensation to officers and directors.
- (c) The Company owes its Chief Financial Officer \$245,202 under a convertible promissory note (Note 15). Total interest accrued during the nine months ending June 30, 2018 is \$22,116 (2017 - \$14,809).
- (d) The Company borrowed \$123,000 from its Chief Executive Officer and \$107,000 from its Chief Financial Officer by way of a bridge shareholder loan, bearing interest at 12% per annum. The shareholder loans were fully repaid along with accrued interest of \$1,352 and \$1,089 respectively.

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.

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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 August 22, 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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