



PET VALU HOLDINGS LTD.

Consolidated Financial Statements

For the 52-week periods ended December 30, 2023 and December 31, 2022

INDEPENDENT AUDITOR'S REPORT

To the Shareholders of Pet Valu Holdings Ltd.,

Opinion

We have audited the consolidated financial statements of Pet Valu Holdings Ltd. and its subsidiaries (the Group), which comprise the consolidated statements of financial position as at December 30, 2023 and December 31, 2022, and the consolidated statements of income and comprehensive income, consolidated statements of shareholders' equity and consolidated statements of cash flows for the periods then ended, and notes to the consolidated financial statements, including material accounting policy information.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at December 30, 2023 and December 31, 2022, and its consolidated financial performance and its consolidated cash flows for the years then ended in accordance with International Financial Reporting Standards ["IFRSs"].

Basis for opinion

We conducted our audit in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report. We are independent of the Group in accordance with the ethical requirements that are relevant to our audit of the consolidated financial statements in Canada, and we have fulfilled our ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matter

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our auditor's opinion thereon, and we do not provide a separate opinion on these matters. For each matter below, our description of how our audit addressed the matter is provided in that context.

We have fulfilled the responsibilities described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the consolidated financial statements. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying consolidated financial statements.

Key audit matter	How our audit addressed the key audit matter
Goodwill and indefinite life intangible assets impairment assessment	
<p>As disclosed in Note 8, the Group has goodwill and indefinite life intangible assets of \$97.6M and \$42.5M, respectively.</p> <p>Goodwill and indefinite life intangible assets must be tested for impairment at least annually, at the cash generating unit (CGU) or group of CGUs level. The determination of recoverable amount, being the value-in-use, requires the use of valuation models and significant judgement on the part of management. Recoverable amounts are based on management's view of variables and market conditions such as future cash flows and the most appropriate discount and growth rates. The Group's policy for impairment together with the related significant accounting estimates and assumptions is described in notes 2 and 3 of the consolidated financial statements.</p> <p>This matter has been considered as a key audit matter due to the level of judgment required to estimate the future cash flows, growth rates, and discount rates used in management's impairment assessments.</p>	<p>To test the estimated recoverable amounts, our audit procedures included, among others, assessing the valuation methodology and evaluating significant assumptions and the accuracy of underlying data used by management in its analysis.</p> <p>We evaluated the Group's models, valuation methodology, and significant assumptions, including discount rates. We assessed the selection and application of the discount rate by evaluating the inputs and mathematical accuracy of the calculation. We assessed the historical accuracy of management's estimates on cash flow projections and growth rates by comparing management's past projections to actual and historical performance.</p> <p>We performed sensitivity analyses on the significant assumptions, including growth rates and discount rates, to evaluate changes in the recoverable amount that would result from changes in the assumptions.</p> <p>We assessed the adequacy of disclosures in describing the areas of judgement and estimation uncertainties around this matter.</p>

Other information

Management is responsible for the other information. The other information comprises:

- Management's Discussion & Analysis
- The information, other than the consolidated financial statements and our auditor's report thereon, in the Annual Report.

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

We obtained Management's Discussion & Analysis prior to the date of this auditor's report. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact in this auditor's report. We have nothing to report in this regard.

The Annual Report is expected to be made available to us after the date of the auditor's report. If based on the work we will perform on this other information, we conclude there is a material misstatement of other information, we are required to report that fact to those charged with governance.

Responsibilities of management and those charged with governance for the consolidated financial statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with IFRSs, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, management is responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Group's financial reporting process.

Auditor's responsibilities for the audit of the consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with Canadian generally accepted auditing standards, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure, and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

The engagement partner on the audit resulting in this independent auditor's report is Jeff Glassford.

The logo for Ernst & Young LLP is written in a black, cursive script font.

Chartered Professional Accountants
Licensed Public Accountants

March 4, 2024
Toronto, Canada

PET VALU HOLDINGS LTD.

Consolidated Statements of Financial Position
(Expressed in thousands of Canadian dollars)

	Note	As at December 30, 2023	As at December 31, 2022
Assets			
Current assets:			
Cash		\$ 28,444	\$ 63,034
Accounts and other receivables	9	27,875	22,965
Inventories, net	10	122,069	118,410
Income taxes recoverable	14	6,012	—
Prepaid expenses and other assets		19,403	22,262
Current portion of lease receivables	5	34,332	29,827
Total current assets		238,135	256,498
Non-current assets:			
Long-term lease receivables	5	159,101	141,187
Right-of-use assets, net	5	237,941	82,242
Property and equipment, net	7	120,493	91,774
Intangible assets, net	8	52,205	52,280
Goodwill	8	97,562	97,574
Deferred tax assets	14	7,230	6,652
Investment in associate	20, 21	—	4,708
Other assets		4,240	7,261
Total non-current assets		678,772	483,678
Total assets		\$ 916,907	\$ 740,176
Liabilities and shareholders' equity			
Current liabilities:			
Accounts payable and accrued liabilities	11	\$ 88,416	\$ 103,782
Provisions	24	669	—
Income taxes payable	14	—	15,141
Current portion of deferred franchise fees	4	1,344	1,197
Current portion of lease liabilities	5	64,068	51,335
Current portion of long-term debt	12	17,750	17,750
Total current liabilities		172,247	189,205
Non-current liabilities:			
Long-term deferred franchise fees	4	4,166	4,017
Long-term lease liabilities	5	379,833	215,966
Long-term debt	12	275,474	320,063
Deferred tax liabilities	14	8,864	8,250
Other liabilities	19	3,977	2,299
Provisions	24	2,626	—
Total non-current liabilities		674,940	550,595
Total liabilities		847,187	739,800
Shareholders' equity:			
Common shares	15	321,752	316,208
Contributed surplus		6,877	4,107
Deficit		(258,768)	(319,780)
Currency translation reserve		(141)	(159)
Total shareholders' equity		69,720	376
Total liabilities and shareholders' equity		\$ 916,907	\$ 740,176

Commitments, contingencies and guarantees (Note 25)

Subsequent events (Note 27)

On behalf of the Board of Directors: *Anthony Truesdale (signed)*, Director

The accompanying notes are an integral part of these consolidated financial statements.

PET VALU HOLDINGS LTD.

Consolidated Statements of Income and Comprehensive Income
(Expressed in thousands of Canadian dollars, except per share amounts)

	Note	Periods ended	
		December 30, 2023	December 31, 2022
Revenue:			
Retail sales	4	\$ 421,828	\$ 402,586
Franchise and other revenues	4	634,039	549,111
Total revenue		1,055,867	951,697
Cost of sales	17	690,730	599,400
Gross profit		365,137	352,297
Selling, general and administrative expenses	18	204,411	192,105
Total operating income		160,726	160,192
Interest expenses, net	13	30,646	20,478
Loss on foreign exchange		188	1,111
Other loss (gain)	20	4,718	(68)
Income before income taxes		125,174	138,671
Income tax expense	14	35,626	37,905
Net income		89,548	100,766
Other comprehensive income, net of tax:			
Currency translation adjustments that may be reclassified to net income, net of tax		18	20
Comprehensive income for the period attributable to the shareholders of the Company		\$ 89,566	\$ 100,786
Basic net income per share attributable to the common shareholders	16	\$ 1.26	\$ 1.43
Diluted net income per share attributable to the common shareholders	16	\$ 1.24	\$ 1.40

The accompanying notes are an integral part of these consolidated financial statements.

PET VALU HOLDINGS LTD.

Consolidated Statements of Shareholders' Equity
(Expressed in thousands of Canadian dollars)

	Common shares	Contributed surplus	Deficit	Currency translation reserve	Total
For the period ended December 30, 2023					
Balance, December 31, 2022	\$ 316,208	\$ 4,107	\$ (319,780)	\$ (159)	\$ 376
Net income	—	—	89,548	—	89,548
Exercise of share options (Notes 15, 19)	5,544	(1,195)	—	—	4,349
Share-based compensation on option plans (Note 19)	—	3,965	—	—	3,965
Foreign currency translation	—	—	—	18	18
Dividends on common shares (Note 15)	—	—	(28,536)	—	(28,536)
Balance, December 30, 2023	\$ 321,752	\$ 6,877	\$ (258,768)	\$ (141)	\$ 69,720

	Common shares	Contributed surplus	Deficit	Currency translation reserve	Total
For the period ended December 31, 2022					
Balance, January 1, 2022	\$ 307,497	\$ 1,779	\$ (403,619)	\$ (179)	\$ (94,522)
Net income	—	—	100,766	—	100,766
Exercise of share options (Notes 15, 19)	8,711	(649)	—	—	8,062
Share-based compensation on option plans (Note 19)	—	2,977	—	—	2,977
Foreign currency translation	—	—	—	20	20
Dividends on common shares (Note 15)	—	—	(16,927)	—	(16,927)
Balance, December 31, 2022	\$ 316,208	\$ 4,107	\$ (319,780)	\$ (159)	\$ 376

The accompanying notes are an integral part of these consolidated financial statements.

PET VALU HOLDINGS LTD.

Consolidated Statements of Cash Flows
(Expressed in thousands of Canadian dollars)

	Note	Periods ended	
		December 30, 2023	December 31, 2022
Cash provided by (used in):			
Operating activities:			
Net income for the period		\$ 89,548	\$ 100,766
Adjustments for items not affecting cash:			
Depreciation and amortization	5, 7, 8	50,718	38,073
Impairment of right-of-use assets	5	—	448
Deferred franchise fees		333	420
Gain on disposal of property and equipment		(3,158)	(1,561)
Loss on sale of right-of-use assets	5	1,106	793
Loss on foreign exchange		188	1,111
Loss (gain) on financial instruments	20, 21	1,302	(551)
Share-based compensation expense	19	5,855	6,248
Share of loss from associate	20	3,416	483
Interest expenses, net	13	30,646	20,478
Income tax expense	14	35,626	37,905
Income taxes paid		(56,451)	(36,673)
Security deposits paid		—	(5,073)
Changes in non-cash operating working capital:			
Accounts receivable		(4,949)	(6,834)
Inventories		(3,563)	(26,133)
Prepaid expenses		(2,952)	(8,194)
Accounts payable and accrued liabilities		(12,321)	1,818
Net cash provided by operating activities		135,344	123,524
Financing activities:			
Proceeds from exercise of share options	15	4,349	8,062
Dividends paid on common shares	15	(28,536)	(16,927)
Repayment of 2021 Term Facility	12	(45,750)	(8,875)
Interest paid on long-term debt		(13,526)	(18,626)
Repayment of principal on lease liabilities	5	(52,944)	(43,212)
Interest paid on lease liabilities	5, 13	(16,498)	(11,853)
Standby letter of credit commitment fees	13	(872)	(1,373)
Net cash used in financing activities		(153,777)	(92,804)
Investing activities:			
Business acquisition, net of cash acquired	6	(3,000)	(12,538)
Purchases of property and equipment	7	(57,291)	(38,833)
Purchase of intangible assets	8	(3,257)	(3,424)
Proceeds on disposal of property and equipment		6,579	3,643
Right-of-use asset initial direct costs		(2,627)	(2,157)
Tenant allowances		1,635	1,459
Notes receivable		1,088	950
Lease receivables	5	30,344	27,050
Interest received on lease receivables and other		10,887	8,703
Investment in associate	20	—	(2,178)
Repurchase of franchises	6	(512)	—
Net cash used in investing activities		(16,154)	(17,325)
Effect of exchange rate on cash		(3)	(429)
Net (decrease) increase in cash		(34,590)	12,966
Cash, beginning of period		63,034	50,068
Cash, end of period		\$ 28,444	\$ 63,034

The accompanying notes are an integral part of these consolidated financial statements.

PET VALU HOLDINGS LTD.

Notes to Consolidated Financial Statements
(Expressed in thousands of Canadian dollars, unless otherwise stated)

For the periods ended December 30, 2023 and December 31, 2022

1. Description of business:

Pet Valu Holdings Ltd. and its subsidiaries (collectively referred to as the "Company") is a specialty retailer and wholesaler of pet food and pet-related supplies. As at December 30, 2023, the Company operates 222 corporate-owned stores (December 31, 2022 — 225) and has 561 franchise stores (December 31, 2022 — 519) in 10 provinces in Canada.

The Company is incorporated under the *Business Corporations Act* (British Columbia). The Company's head office is located at 130 Royal Crest Court, Markham, Ontario, Canada.

The Company's common shares are listed on the Toronto Stock Exchange under the symbol "PET".

2. Basis of presentation:

(a) Basis of presentation:

These consolidated financial statements ("financial statements") refer to the financial statements of the Company and include the accounts of the Company and its subsidiaries with intercompany transactions and balances eliminated. The Company has the following wholly owned subsidiaries:

Subsidiaries
Pet Valu Canada Holding Corporation
Pet Holdings ULC
Pet Valu Canada Inc.
Les Franchises Chico Inc.
Pet Retail Brands North America Holdings ULC
Pet Valu Management Services Inc.
Pet Retail Brands US Holdings LLC

These financial statements have been prepared on a historical cost basis, unless otherwise stated.

The accounting policies set out below have been applied consistently in the preparation of the financial statements for the periods presented.

(b) Fiscal period:

The Company operates under a 52- or 53-week fiscal year ending on the Saturday nearest to December 31. The 2023 and 2022 fiscal years are for the 52-week periods from January 1, 2023 to December 30, 2023 and January 2, 2022 to December 31, 2022, respectively.

(c) Statement of compliance:

These financial statements have been prepared by management in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"). The policies set out below have been consistently applied to all periods presented unless otherwise noted.

PET VALU HOLDINGS LTD.

Notes to Consolidated Financial Statements

(Expressed in thousands of Canadian dollars, unless otherwise stated)

For the periods ended December 30, 2023 and December 31, 2022

2. Basis of presentation (continued):

These financial statements were approved and authorized for issuance by the Board of Directors of the Company on March 4, 2024.

(d) Presentation currency:

The financial statements are presented in Canadian dollars, the Company's functional currency, unless otherwise stated. All financial information presented in Canadian dollars has been rounded to the nearest thousand, unless otherwise stated.

(e) Use of estimates and judgments:

The preparation of the financial statements requires management to make various judgments and estimates in applying the Company's accounting policies that affect the reported amounts and disclosures made in the financial statements and accompanying notes.

These judgments and estimates are based on management's historical experience, knowledge of current events and conditions and other factors that are believed to be reasonable under the circumstances. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

Significant judgments and estimates made by management in the process of applying accounting policies and that have the most significant effect on the amounts recognized in the financial statements include the following:

(i) Inventory valuation:

Merchandise inventories are carried at the lower of cost and net realizable value. The estimation of net realizable value is based on the most reliable evidence available of the amount the merchandise inventories are expected to realize. If carrying value exceeds net realizable amount, a write-down is recognized. Additionally, estimation is required for inventory provisions due to shrinkage and obsolescence.

PET VALU HOLDINGS LTD.

Notes to Consolidated Financial Statements

(Expressed in thousands of Canadian dollars, unless otherwise stated)

For the periods ended December 30, 2023 and December 31, 2022

2. Basis of presentation (continued):

(ii) Impairment of non-financial assets:

The Company is required to use judgment in determining the grouping of assets to identify its cash-generating units ("CGUs") for the purpose of testing store related property and equipment, and right-of-use ("ROU") assets. Judgment is further required to determine appropriate groupings of CGUs for the level at which non-store related assets are tested for impairment, including intangible assets and goodwill. Furthermore, on a quarterly basis, judgment has been used in determining whether there has been an indication of impairment, which would require the completion of a quarterly impairment test, in addition to the annual requirement for goodwill and indefinite-life intangible assets.

The Company's estimate of a CGU's or group of CGUs' recoverable amount is based on value in use ("VIU") and involves estimating future cash flows.

VIU is determined based on the Company's assumptions regarding future events, future cash flow projections, growth rates and discount rates.

(iii) Share-based compensation:

The Company measures the value of equity-settled transactions with employees by reference to the fair value of the equity instruments at the date on which they are granted. Estimating fair value for share-based compensation requires determining the most appropriate valuation model for a grant of equity instruments, which is dependent on the terms and conditions of the grant. The Company is also required to determine the most appropriate inputs to the valuation model, including estimates and assumptions with respect to expected life, risk-free interest rate, volatility, distribution yield, forfeiture rate, the Company's share price, expected market conditions and future financial performance of the Company.

The Company makes estimates to determine the fair value of performance based cash-settled awards. These significant estimates include the estimation of the Company's share price, volatility, expected market conditions and future financial performance of the Company.

(iv) Leases:

The Company has applied judgment to determine the lease term for lease contracts that include renewal or termination options. The assessment of whether the Company is reasonably certain to exercise such options impacts the lease term, which significantly affects the amount of lease liabilities and ROU assets recognized (Note 5).

The Company is required to estimate the incremental borrowing rates used to discount lease liabilities if the interest rate implicit in the lease is not readily determined. In determining the incremental borrowing rates, management considers the Company's creditworthiness, the term of the leased asset and Canadian corporate bond yields for companies of a similar credit rating as the Company (Note 5).

PET VALU HOLDINGS LTD.

Notes to Consolidated Financial Statements

(Expressed in thousands of Canadian dollars, unless otherwise stated)

For the periods ended December 30, 2023 and December 31, 2022

2. Basis of presentation (continued):

(v) Provisions:

The Company reviews provisions at each reporting date using judgments to determine the probability that an outflow of economic resources will result from the legal or constructive obligation and an estimate of the associated obligation. Due to the judgmental nature of these items, future settlements may differ from amounts recognized.

(vi) Income taxes:

In calculating current and deferred income and other taxes, the Company uses judgment when interpreting the tax rules in jurisdictions where the Company operates. The Company also uses judgment in classifying transactions and assessing probable outcomes of claimed deductions, which considers expectations of future operating results, the timing and reversal of temporary differences and possible audits of income tax and other tax filings by tax authorities (Note 14).

(vii) Control, joint control, or level of influence:

When determining the appropriate basis of accounting for the Company's interest in affiliates, the Company makes judgments about the degree of influence that it exerts directly or through an arrangement over the investees' relevant activities (Note 20).

(viii) Business combinations:

The Company uses judgment in applying the acquisition method of accounting for business combinations and estimates to value identifiable assets and liabilities at the acquisition date. The Company may engage independent third parties to determine the fair value of inventory, property and equipment and intangible assets. Assumptions and estimates are used to determine cash flow projections, including the period of future benefit, future growth and discount rates, among other factors. The values placed on the acquired assets and liabilities assumed affect the amount of goodwill recorded on an acquisition.

(ix) Fair value measurements:

Certain financial assets are measured at fair value. In estimating fair value, the Company uses market-observable data to the extent it is available. In certain cases where market-observable data is not available, the Company will engage third-party qualified valuation specialists to perform the valuation. Information about the valuation techniques and inputs used in determining the fair value of financial instruments is disclosed in Note 21.

PET VALU HOLDINGS LTD.

Notes to Consolidated Financial Statements

(Expressed in thousands of Canadian dollars, unless otherwise stated)

For the periods ended December 30, 2023 and December 31, 2022

3. Summary of material accounting policies:

(a) Principles of consolidation:

The financial statements incorporate the financial statements of the Company and legal entities controlled by the Company and its subsidiaries. Subsidiaries are fully consolidated from the date on which control is determined, and they are unconsolidated from the date on which control is deemed to have ceased. The financial statements of the subsidiaries are prepared for the same reporting period as the parent company, using consistent accounting policies. All intercompany balances, transactions, unrealized gains and losses resulting from intercompany transactions and dividends are eliminated in full.

(b) Foreign currency:

Each of the Company's operating subsidiaries maintains its accounting records in its functional currency.

(i) Foreign currency transactions:

Transactions carried out in foreign currencies are translated into the functional currency using the exchange rate prevailing at the transaction date. Monetary assets and liabilities denominated in a foreign currency at the reporting date are translated at the exchange rate at that date. Foreign currency denominated non-monetary assets and liabilities are measured at the historical exchange rate prevailing at the transaction date. Realized and unrealized foreign currency gains or losses are recognized as income or expense for the period, specifically as (gain) loss on foreign exchange in the consolidated statements of income and comprehensive income.

(ii) Foreign currency translation:

As at December 30, 2023, the functional currency of each of the Company's operating subsidiaries is Canadian dollars. Prior to September 30, 2023, the Company's U.S. dollar functional currency subsidiary's financial statements were translated into Canadian dollars using the current rate method. Assets and liabilities were translated using the end-of-period exchange rates. Income and expenses were translated at the average exchange rates for each period. Equity accounts were translated at historical foreign exchange rates. Foreign currency differences on translation were reported as a component of shareholders' equity in the financial statements.

PET VALU HOLDINGS LTD.

Notes to Consolidated Financial Statements

(Expressed in thousands of Canadian dollars, unless otherwise stated)

For the periods ended December 30, 2023 and December 31, 2022

3. Summary of material accounting policies (continued):

(c) Business combinations:

Business combinations are accounted for using the acquisition method and all acquisition-related costs are expensed as incurred and included in selling, general and administrative expenses.

Goodwill arising on a business combination represents the excess of the consideration transferred over the fair value of the net assets acquired. Results of operations of a business acquired are included in the Company's financial statements from the date of the business acquisition. Acquisition-related costs are expensed as incurred and included in selling, general and administrative expenses.

The purchase price allocation may be provisional during a measurement period of up to one year to provide reasonable time to obtain the information necessary to identify and measure the assets acquired and liabilities assumed. Measurement period adjustments are recognized in the period in which the adjustment amount is determined and adjustments to fair values and allocations are retrospectively adjusted.

When the consideration transferred by the Company in a business combination includes liabilities resulting from a contingent consideration arrangement, the contingent consideration is measured at its acquisition date fair value and included as part of the consideration transferred in a business combination. Contingent consideration that is classified as a liability is remeasured at subsequent reporting dates at fair value, with the corresponding gain or loss being recognized in the consolidated statements of income and comprehensive income.

When the Company acquires a business, it assesses the financial assets and liabilities assumed for appropriate classification and designation in accordance with the contractual terms, economic circumstances and pertinent conditions as at the acquisition date.

(d) Investment in associates:

Investments in associates are accounted for under the equity method and initially recognized at cost including transaction costs. After initial recognition, the Company's share of the profit or loss and other comprehensive income of the associate is included in other loss (gain) in the consolidated statements of income and comprehensive income, after aligning with the accounting policies of the Company, until the date on which significant influence ceases. An impairment loss is recorded in other loss (gain) in the consolidated statements of income and comprehensive income, when the recoverable amount becomes lower than the carrying amount of the investment.

(e) Inventories and cost of sales:

Inventories are valued at the lower of cost and net realizable value as determined by the first-in, first-out basis and consist of merchandising inventories. As part of the inventory valuations, the Company accrues for inventory shrinkage for lost or stolen items based on historical trends, and obsolescence as applicable.

PET VALU HOLDINGS LTD.

Notes to Consolidated Financial Statements

(Expressed in thousands of Canadian dollars, unless otherwise stated)

For the periods ended December 30, 2023 and December 31, 2022

3. Summary of material accounting policies (continued):

Cost of sales reflects the direct cost of merchandise plus purchasing, warehousing, distribution, depreciation expense for store ROU assets and distribution centre assets and occupancy costs related to store operations, such as variable lease payments and general store maintenance.

(f) Property and equipment:

The Company's property and equipment are measured at cost less accumulated depreciation and impairment losses, with the exception of land, which is held at historical cost.

During their construction, items of property and equipment are classified as construction-in-progress. When the asset is available for use, it is transferred from construction-in-progress to the appropriate category of property and equipment and depreciation on the item commences.

Depreciation is recorded on a straight-line basis over the estimated useful lives as outlined below:

Category	Useful life
Buildings	Up to 25 years
Leasehold improvements	Shorter of remaining lease term or estimated useful life of improvement
Furniture, fixtures and equipment	3 – 15 years

The Company assesses an asset's residual value, useful life and depreciation method on an annual basis and adjusts if appropriate.

Gains and losses on disposal of property and equipment are determined by comparing the proceeds from disposal with the carrying amount of the property and equipment and are recognized in selling, general and administrative expenses in the consolidated statements of income and comprehensive income.

(g) Leases:

At inception of a contract, the Company assesses whether a contract is, or contains, a lease based on whether the contract conveys the right of control for the use of an identified asset for a period of time in exchange for consideration. The Company recognizes an ROU asset and a lease liability at the lease commencement date, which is the date the leased asset is available for use. The ROU asset is primarily composed of leased premises for corporate-owned stores, office space, and distribution centres, as well as leased vehicles and material handling equipment.

ROU assets are measured at cost, comprising the amount of the initial measurement of the lease liability, plus any lease payments made at or before the commencement date less any lease incentives received, plus any initial direct costs and restoration costs.

PET VALU HOLDINGS LTD.

Notes to Consolidated Financial Statements
(Expressed in thousands of Canadian dollars, unless otherwise stated)

For the periods ended December 30, 2023 and December 31, 2022

3. Summary of material accounting policies (continued):

The lease liability is measured at the present value of the lease payments discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, the Company's incremental borrowing rate.

The ROU assets are depreciated to the earlier of the end of the useful life of the ROU asset or the lease term using the straight-line method, as this most closely reflects the expected pattern of the consumption of the future economic benefits. The lease term includes periods covered by an option to extend if the Company is reasonably certain to exercise that option. In addition, the ROU asset can be periodically reduced by impairment losses, if any, and adjusted for certain remeasurements of the lease liability.

The lease liability is classified and accounted for at amortized cost using the effective interest method. It is remeasured when there is a change in future lease payments arising from a change in an index or rate, if there is a change in the Company's estimate of the amount expected to be payable under a residual value guarantee, or if the Company changes its assessment of whether it will exercise a purchase, extension or termination option. When the lease liability is remeasured in this way, a corresponding adjustment is made to the carrying amount of the ROU asset unless it has been reduced to zero. Any further reduction in the lease liability is then recognized in profit or loss.

The Company enters into head lease agreements for most of its franchise store locations and, in turn, enters into a sublease with its franchisees. The Company, as an intermediate lessor, classifies a sublease by reference to the ROU asset arising from the head lease, rather than by reference to the underlying asset.

The Company has assessed its subleases to franchisees as a net investment in finance lease, which are included in lease receivables on the consolidated statements of financial position.

When the Company enters into a sublease, the Company:

- (i) derecognizes the ROU asset relating to the head lease that it transfers to the sublessee and recognizes the lease receivable;
- (ii) recognizes any difference between the ROU asset and the lease receivable in profit or loss; and
- (iii) retains the lease liability relating to the head lease in its consolidated statements of financial position, which represents the lease payments owed to the head lessor.

The Company recognizes finance income on the lease receivables using the effective interest method.

PET VALU HOLDINGS LTD.

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For the periods ended December 30, 2023 and December 31, 2022

3. Summary of material accounting policies (continued):

Lease receivables for the franchise store subleases were measured at the present value of the lease payments from the franchisee discounted using the incremental borrowing rate on the head lease.

(h) Intangible assets and goodwill:

Intangible assets are carried at cost less any accumulated amortization and accumulated impairment losses.

Intangible assets with indefinite useful lives consist of trade names, which are not amortized but are tested for impairment annually at the CGU level. The assessment of indefinite life is reviewed annually to determine whether the indefinite life continues to be supportable. The Company currently plans to continue operating under the Pet Valu and Chico (Note 6) trade names, and therefore these assets are assessed as having an indefinite useful life. If not, the change in useful life from indefinite to finite is made on a prospective basis.

Goodwill is measured at cost less any accumulated impairment and is not amortized.

Intangible assets with finite lives consist of the franchise agreements, software, and other intellectual property including trade names and non-compete agreements. These assets are amortized on a straight-line basis over their useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortization period and the amortization method for an intangible asset with a finite useful life are reviewed on an annual basis. The amortization expense on intangible assets with finite lives is recognized in the consolidated statements of income and comprehensive income in selling, general and administrative expenses.

Estimated useful lives are as follows:

Category	Useful life
Franchise agreements	9 – 10 years
Software	3 – 10 years
Other (trade names and non-compete agreements)	3 – 10 years
Pet Valu and Chico trade name	Indefinite
Goodwill	Indefinite

An intangible asset is derecognized upon disposal (i.e., at the date the recipient obtains control) or when no future economic benefits are expected from its use or disposal. Any gain or loss arising upon derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the consolidated statements of income and comprehensive income.

PET VALU HOLDINGS LTD.

Notes to Consolidated Financial Statements

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For the periods ended December 30, 2023 and December 31, 2022

3. Summary of material accounting policies (continued):

(i) Impairment of non-financial assets:

Non-financial assets with finite lives are tested for impairment at each reporting date whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

Goodwill and indefinite-life intangible assets are tested for impairment at least annually in the fourth quarter of the year, and whenever there is an indication that the asset may be impaired.

The Company considers indicators that include, but are not limited to: a history of operating losses at the individual store level, expected future cash flows from a retail location that are not expected to recover the remaining carrying value of the assets of the location, significant negative industry or economic trends, knowledge of transactions involving the sale of similar assets at amounts below their carrying value, and expectations to dispose of non-financial assets before the end of their estimated useful lives.

An impairment loss is immediately recognized in profit or loss by the amount by which the asset's carrying amount exceeds its recoverable amount.

For purposes of measuring recoverable amounts, store assets that include store property and equipment and ROU assets are grouped at the lowest levels for which there are largely independent cash inflows, which is referred to as a CGU. For the Company, that is at the individual store level.

The Company's non-store related assets, which include goodwill and intangible assets, do not generate separate cash inflows. For the purposes of non-store related assets, CGUs are grouped at the lowest level that the assets can be allocated and/or are monitored for internal management purposes and for which largely independent cash inflows are generated. If there is an indication that a non-store related asset may be impaired, then the recoverable amount is determined for the CGU group.

(j) Income taxes:

Income taxes expense (recovery) comprises current and deferred income taxes. Current income taxes and deferred income taxes are recognized in net income for the period, except for items recognized directly in equity or in other comprehensive income.

Current income tax is the expected tax payable on the taxable income or net income for the period, using tax rates enacted or substantively enacted at the reporting date.

PET VALU HOLDINGS LTD.

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(Expressed in thousands of Canadian dollars, unless otherwise stated)

For the periods ended December 30, 2023 and December 31, 2022

3. Summary of material accounting policies (continued):

Deferred income tax is recognized in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred income tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they relate to income taxes levied by the same tax authority on the same taxable entity.

A deferred tax asset is recognized for unused tax losses, tax credits and deductible temporary differences to the extent that it is probable that future taxable profits will be available against which they can be utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

(k) Financial instruments:

Financial assets and financial liabilities are recognized when the Company becomes a party to the contractual provisions of the instruments. All financial instruments are initially measured at fair value.

(i) Financial assets:

On initial recognition, a financial asset is classified as measured at amortized cost, fair value through other comprehensive income ("FVOCI"), or fair value through profit or loss ("FVTPL"). The classification of financial assets is based on the business model in which a financial asset is managed and its contractual cash flow characteristics.

The following accounting policies apply to the subsequent measurement of financial assets.

Financial assets classified as FVTPL are measured at fair value with any resultant gain or loss recognized in profit or loss. Financial assets classified as FVOCI are measured at fair value with any subsequent remeasurement recognized in other comprehensive income. When FVOCI financial assets that are not considered equity investments are derecognized, the cumulative gain or loss previously recognized directly in equity is recognized in profit or loss. Financial assets that represent solely payments of principal and interest, not designated at FVTPL and held to maturity, are measured at amortized cost using the effective interest method.

(ii) Financial liabilities:

The Company classifies its financial liabilities as either financial liabilities at FVTPL or amortized cost. Subsequent to initial recognition, other liabilities are measured at amortized cost using the effective interest method. Financial liabilities at FVTPL are stated at fair value with changes being recognized in profit or loss.

PET VALU HOLDINGS LTD.

Notes to Consolidated Financial Statements

(Expressed in thousands of Canadian dollars, unless otherwise stated)

For the periods ended December 30, 2023 and December 31, 2022

3. Summary of material accounting policies (continued):

(iii) Classification of financial instruments:

The Company classifies its financial assets and liabilities depending on the purpose for which the financial instruments were acquired, their characteristics and management intent as outlined below:

	Classification
Financial assets:	
Cash	Amortized cost
Accounts and other receivables	Amortized cost
Notes receivable	Amortized cost
Lease receivables	Amortized cost
Call option	FVTPL
Financial liabilities:	
Accounts payable and accrued liabilities	Amortized cost
Lease liabilities	Amortized cost
Long-term debt	Amortized cost

(iv) Impairment of financial assets:

At the end of each reporting period, the Company applies the expected credit loss ("ECL") model to assess for impairment of financial assets measured at amortized cost. The Company's financial assets measured at amortized cost and subject to the ECL model consist primarily of franchise receivables, trade and other receivables, notes receivable, and lease receivables. The Company applies the simplified approach to impairment for franchise receivables, trade and other receivables, and lease receivables by recognizing lifetime expected losses. Lifetime ECL represents the ECL that will result from all probable default events over the expected life of a financial asset. The allowance for ECLs is recorded against the financial assets and the net change in the allowance for ECLs is recorded in net income. For notes receivable, the Company has applied the general ECL model. Under this model, when credit risk is assessed as being low or when there has not been a significant increase in credit risk since initial recognition, the ECL is determined based on the expected losses over the expected life arising from loss events that could occur during the 12 months following the reporting date. If a significant increase in credit risk has occurred throughout a reporting period, impairment is based on lifetime ECL.

PET VALU HOLDINGS LTD.

Notes to Consolidated Financial Statements
(Expressed in thousands of Canadian dollars, unless otherwise stated)

For the periods ended December 30, 2023 and December 31, 2022

3. Summary of material accounting policies (continued):

For franchise receivables, trade and other receivables, notes receivable, and lease receivables, the Company has established a provision matrix that considers the probability of default based on historical credit loss experience, adjusted for forward-looking factors specific to franchisees, vendors, landlords, and macroeconomic conditions. Additionally, the probability of default on franchise receivables, notes receivable, and lease receivables is assessed through regular monitoring of store performance and review of franchisee payment history. In assessing ECL, the Company also considers the expected loss given default including the available collateral such as leasehold improvements, ROU assets, store inventory and personal guarantees, where applicable, that are pledged in the franchise and sub-lease agreements.

Franchise receivables, trade and other receivables, notes receivable, and lease receivables are considered in default when there is no reasonable expectation of recovery. Indicators that there is no reasonable expectation of recovery include, amongst others, the failure of a franchisee, vendor, or landlord to engage in a repayment plan with the Company, a failure to make payments for a period of greater than 180 days past due, and no remaining vendor payments or head lease payments to offset against the trade or other receivables. On this basis, the Company has assessed the risk of default to be minimal.

(v) Derecognition:

A financial asset is derecognized when the contractual rights to the cash flows from the asset expire or when the Company transfers the financial asset to another party without retaining control or substantially all the risks and rewards of ownership of the asset. Any interest in transferred financial assets created or retained by the Company is recognized as a separate asset or liability.

A financial liability is derecognized when its contractual obligations are discharged, cancelled, or expire.

Financial assets and liabilities are offset, and the net amount is reported in the consolidated statements of financial position, where there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis or realize the asset and settle the liability simultaneously.

(l) Revenue recognition:

(i) Retail sales:

The Company's retail sales include corporate-owned store retail and e-commerce merchandise sales as well as in-store grooming services.

Revenue is recognized for corporate-owned store sales when control passes, which occurs at a point in time when the customer completes a transaction in the store and receives the merchandise.

PET VALU HOLDINGS LTD.

Notes to Consolidated Financial Statements
(Expressed in thousands of Canadian dollars, unless otherwise stated)

For the periods ended December 30, 2023 and December 31, 2022

3. Summary of material accounting policies (continued):

The Company's e-commerce operation recognizes revenue when delivery has been completed to the customer.

The Company recognizes revenue for in-store pet grooming services once the service is completed, as this is when the customer has the ability to direct the use of and obtain the benefits of the service.

Retail sales are presented net of indirect tax collected from the customer on behalf of government authorities. Payment terms for all retail sales are at the point of sale.

Retail sales revenue is recognized net of sales discounts and net of an estimated sales return reserve. The Company's sales return policy is generally limited to 30 days. The sales return reserve reflects an estimate of sales returns based on projected merchandise returns determined using historical average return percentages.

The Company administers frequent buyer loyalty programs. These loyalty programs represent a material right to the customer that may be redeemed on future products and services. A portion of revenue from products or services sold that have an associated free-unit loyalty program is deferred based on an estimate of the amount to be earned and the likelihood of the customer reaching the threshold of earning the associated reward (a free product). For certain vendor-supported free-unit loyalty programs, the Company receives reimbursement from the vendor for the cost of the free-unit redeemed by the customer. A portion of the costs from products sold that have an associated vendor-supported free-unit loyalty program is deferred based on an estimate of the amount to be earned and the likelihood of the customer reaching the threshold of earning the associated reward. The expected redemption percentage for all frequent buyer loyalty programs is based on historical redemption patterns and incorporates current information or trends. The revenue previously deferred is recognized when the points or free-unit rewards are redeemed or expire. Depending on the loyalty program type, free-unit rewards expire between 12 and 36 months from the date of issuance.

The Company administers gift card programs. Customer purchases of gift cards are recorded as liabilities and revenue is recognized when the gift card is redeemed through merchandise purchases. If redemption occurs at a franchisee owned store, the gift card funds are remitted to the franchisee. Gift cards do not carry an expiration date; therefore, customers can redeem their gift cards for merchandise indefinitely. Management reviews unredeemed gift cards and recognizes revenue for these amounts when it is determined the likelihood of redemption is remote.

(ii) Franchise revenues:

Franchise revenues include both one-time and ongoing amounts, consisting mostly of initial and renewal franchise fees, royalties, percentage rent and common area maintenance and realty tax revenues from properties subleased to franchisees, wholesale sales, promotion fees, and fees for services.

PET VALU HOLDINGS LTD.

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3. Summary of material accounting policies (continued):

Franchise agreements grant individual franchisees the exclusive right to operate a franchise store within a designated territory. The franchise agreements typically provide for a 10-year initial term, with an opportunity to enter into one or more renewal franchise agreements subject to certain conditions. The franchise agreement requires the Company to perform various activities to support the brand and/or franchisees and these activities represent a single performance obligation.

Initial franchise fees for the licence to operate a franchise store are paid in advance at signing and are deferred as a contract liability and recognized as revenue on a straight-line basis over the applicable franchise agreement term as the Company satisfies its performance obligation per the terms of such franchise agreement.

Franchise royalties are variable consideration based on a percentage of the franchisees' retail sales, which are recognized in the period the franchisees' underlying sales occur and are not included in the initial franchise fee.

Percentage rent is calculated based on a percentage of the franchisees' retail sales that exceeds base rent collected on the lease receivable and is included in royalties and sub-lease revenues (Note 4).

Wholesale sales represent sales of merchandise from the Company's warehouses to franchisees and are recognized at the time of delivery, as title has passed and the Company has transferred possession to the franchisee. Canadian franchisees purchase most of their wholesale inventory from the Company.

Promotion fees represent charges to franchisees to fund system-wide or regional advertising campaigns, under the terms of the franchise agreements. These fees are variable consideration based on a percentage of the franchisees' retail sales and are recognized in the period the franchisees' underlying sales occur and are not included in the initial franchise fee.

Fees for services provided by the Company to a franchisee are recognized when the service has been performed as this is when the franchisee has the ability to direct the use of and obtain the benefits of the service. Fees collected in advance are deferred until earned.

On the sale of an existing corporate-owned store to a franchisee, costs relating to the sale of the store are charged to expense as incurred, and proceeds (excluding fees) in excess of the net book value of store assets sold to the franchisee are recorded as a gain on the date of sale and are included in selling, general and administrative expenses.

The Company does not incur a significant amount of contract acquisition costs in conducting its franchising activities. The Company's franchising arrangements do not contain a significant financing component.

PET VALU HOLDINGS LTD.

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3. Summary of material accounting policies (continued):

(m) Share capital:

Common shares issued by the Company are recorded at the proceeds received in shareholders' equity, less directly attributable issuance costs, net of tax.

(n) Dividends:

Dividends declared and payable to the Company's common shareholders are recognized as a liability in the consolidated statements of financial position in the period in which the dividends are approved by the Company's Board of Directors.

(o) Share-based compensation:

(i) Amended and Restated Share Option Plan and long-term incentive plan:

The Company has an Amended and Restated Share Option Plan (formerly referred to as the Legacy Option Plan or the Legacy Plan) pursuant to which it has granted share options to current and former directors and employees. The Company amended and restated the Amended and Restated Share Option Plan so that no additional awards could be made under this plan, but share options previously granted under the this plan continue to remain outstanding in accordance with their terms and will continue to be governed by the provisions of the Amended and Restated Share Option Plan.

Following the amendment of the Amended and Restated Share Option Plan, the Company adopted a long-term incentive plan (the "LTIP") pursuant to which it can grant awards of share options, restricted share units ("RSUs"), and performance share units ("PSUs") to eligible participants. Share options are accounted for as equity-settled share-based awards at the option of the Company. RSUs and PSUs are accounted for as cash-settled awards.

Equity-settled awards:

The Black-Scholes option pricing model is used to value the share options, taking into account the terms and conditions on which the rights to equity-settled awards are granted. Service and non-market performance conditions are not taken into account when determining the grant date fair value of awards, but the likelihood of the conditions being met is assessed as part of the estimate of the number of equity instruments that will ultimately vest. Market performance conditions are reflected within the grant date fair value. Share-based compensation expense for awards is recognized over the employee's requisite service period on a graded vesting basis and no expense is recognized for awards that do not ultimately vest if the service or non-market performance conditions have not been met. For awards that have market performance conditions, the awards are treated as vested irrespective of whether the market condition is satisfied, provided that the service or non-market performance conditions are satisfied. Share-based compensation expense is recognized in selling, general and administrative expenses with a corresponding increase in contributed surplus. Any consideration paid by plan participants on the exercise of share options is credited to common share capital.

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For the periods ended December 30, 2023 and December 31, 2022

3. Summary of material accounting policies (continued):

Upon the exercise of share options, the corresponding amounts previously credited to contributed surplus are transferred to share capital.

The dilutive effect of outstanding share options is reflected as additional share dilution in the computation of diluted net income per share.

Cash-settled awards:

RSUs and PSUs are grants of notional common shares that are redeemable for cash based on the market value of the Company's common shares and are non-dilutive to common shareholders. RSUs and PSUs are initially measured based on the market value of the Company's common shares at the date of grant and if applicable, consider the expected achievement of performance conditions. The grant-date fair value is recognized as share-based compensation expense with a corresponding increase recorded in other liabilities for the proportion of the service that has been rendered at that date. RSUs and PSUs are remeasured at each reporting date based on the market value of the Company's common shares and if applicable, consider the expected achievement of performance conditions, with changes in fair value recognized as share-based compensation expense for the proportion of the service that has been rendered at that date.

(ii) Deferred share unit plan:

The Company has a deferred share unit plan (the "DSU Plan") for non-employee board members. Each eligible director receives a portion of his or her annual director retainer in deferred share units ("DSUs"). The cash portion of the retainer is paid on a quarterly basis. The DSU portion of the retainer is granted on an annual basis based on the market price of the Company's common shares on the date of such grant and vests in four equal installments on a quarterly basis. DSUs may only be redeemed when a director ceases to be a member of the Board. DSUs issued by the Company under the DSU Plan are settled in cash and are accounted for as cash-settled awards. The cost of the service received as consideration is initially measured based on the market price of the Company's common shares at the date of grant. Deferred share units are remeasured at each reporting date based on the market price of the Company's common shares, with changes in fair value recognized as share-based compensation expense for the proportion of the service that has been rendered at that date.

(p) Provisions:

Provisions are recognized when there is a present legal or constructive obligation as a result of past events, it is more likely than not that an outflow of resources will be required to settle the obligation, and the amount can be reliably estimated. Provisions are measured at the best estimate of the expenditure required to settle the obligation at the end of the reporting period and are discounted to present value where the effect is material. Where discounting is used, the increase in the provision due to the passage of time is recognized as interest expense.

PET VALU HOLDINGS LTD.

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(Expressed in thousands of Canadian dollars, unless otherwise stated)

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3. Summary of material accounting policies (continued):

A restoration provision is a legal obligation associated with the restoration of a leased premise when the Company is contractually obligated to restore the leased premise to the original condition at the end of the lease. The Company recognizes the best estimate of the expenditure required to settle the liability and discounted to present value where the effect is material, with the corresponding increase in the carrying value of the related ROU asset when such obligations are incurred. The liability is classified in current and non-current provisions and is accreted to its projected future value over time. The ROU asset is depreciated over the remaining lease term. Differences between the recorded provision and the actual restoration costs incurred are recognized as a gain or loss in the consolidated statements of income and comprehensive income

(q) Advertising and promotion fund:

Pursuant to the franchise agreements, the Company and its franchisees typically contribute 2.5% of their weekly store merchandise sales to a promotion fund. This fund is used to carry out marketing and advertising activities. Advertising contributions received from franchisees are included in franchise and other revenues, and advertising expenses are included in selling, general and administrative expenses in the consolidated statements of income and comprehensive income.

(r) New standards and interpretations adopted in the period:

In February 2021, the IASB amended IAS 1, *Presentation of Financial Statements* and IAS 8, *Accounting Policies, Changes in Accounting Estimates and Errors*. The narrow-scope amendments require the disclosure of material accounting policy information rather than significant accounting policies and clarify how to distinguish changes in accounting estimates from changes in accounting policies. The Company has adopted these amendments in its consolidated financial statements for the period ended December 30, 2023. The Company assessed the accounting policies disclosed and revised the disclosure to provide material accounting policy information rather than significant accounting policies.

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Notes to Consolidated Financial Statements

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For the periods ended December 30, 2023 and December 31, 2022

3. Summary of material accounting policies (continued):

(s) New standards and interpretations not yet adopted:

In January 2020, the IASB issued *Classification of Liabilities as Current or Non-current*, which amends IAS 1, *Presentation of Financial Statements*. The narrow-scope amendments affect only the presentation of liabilities in the statement of financial position and not the amount or timing of their recognition. The amendments clarify that the classification of liabilities as current or non-current is based on rights that are in existence at the end of the reporting period and specify that classification is unaffected by expectations about whether an entity will exercise its right to defer settlement of a liability. They also introduce a definition of “settlement” to make clear that settlement refers to the transfer to the counterparty of cash, equity instruments, other assets or services. In October 2022, the IASB issued further amendments to IAS 1, *Presentation of Financial Statements*, that aim to improve the information companies provide about long-term debt with covenants. The amendments to IAS 1 specify that covenants to be complied with after the reporting date do not affect the classification of debt as current or non-current at the reporting date. Instead, the amendments require a company to disclose information about these covenants in the notes to the financial statements. The amendments are effective for annual reporting periods beginning on or after January 1, 2024. Earlier application is permitted. These amendments are not expected to have a material impact on the consolidated financial statements.

In September 2022, the IASB issued *Lease Liability in a Sale and Leaseback*, which amends IFRS 16, *Leases*. The narrow scope amendments add to requirements explaining how to account for a sale and leaseback after the date of the transaction. These amendments will not change the accounting for leases other than those arising in a sale and leaseback transaction. The amendments are effective for annual reporting periods beginning on or after January 1, 2024. Earlier application is permitted. These amendments are not expected to have an impact on the consolidated financial statements.

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4. Revenue:

The following table disaggregates the Company's retail sales and franchise revenue by category for the periods ended December 30, 2023 and December 31, 2022:

	December 30, 2023	December 31, 2022
Retail sales:		
Merchandise sales	\$ 416,694	\$ 398,117
In-store services	5,134	4,469
Total retail sales	421,828	402,586
Franchise and other revenues:		
Wholesale merchandise sales	500,009	432,089
Royalties and sub-lease revenues	98,071	88,608
Promotion and other service fees	35,959	28,414
Total franchise and other revenues	634,039	549,111
Total revenue	\$ 1,055,867	\$ 951,697

The changes in the Company's contract liabilities for the period ended December 30, 2023 are as follows:

	Beginning balance	Recognition of revenue included in beginning balance ⁽¹⁾	Contract liability, net of revenue, recognized during the period ⁽²⁾	Ending balance
Franchise fees	\$ 5,214	\$ (1,309)	\$ 1,605	\$ 5,510
Loyalty programs (Note 11)	8,050	(8,050)	7,741	7,741
Gift cards (Note 11)	1,777	(797)	502	1,482

⁽¹⁾ Includes franchise fees recognized in revenue, redemptions of loyalty rewards and gift cards, and estimated gift card breakage.

⁽²⁾ Includes franchise fees on new or renewed franchise agreements, issuances of loyalty rewards, and activation of gift cards.

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4. Revenue (continued):

The balance of franchise fees as at December 30, 2023 that are expected to be recognized in revenue are as follows:

2024	\$	1,344
2025		880
2026		816
2027		617
2028		465
Thereafter		1,388
Total	\$	5,510

5. Leases:

(a) ROU assets:

The following table reconciles the changes in ROU assets for the periods ended December 30, 2023 and December 31, 2022:

	Leased premises		Other	Total
Balance, December 31, 2022	\$	78,532	\$ 3,710	\$ 82,242
Net additions ⁽¹⁾		180,435	1,770	182,205
Depreciation		(25,119)	(1,387)	(26,506)
Balance, December 30, 2023	\$	233,848	\$ 4,093	\$ 237,941

⁽¹⁾ Includes net additions to ROU assets of \$84,310 related to the new Greater Toronto Area ("GTA") distribution centre and \$67,061 related to the new Metro Vancouver Region distribution centre.

	Leased premises		Other	Total
Balance, January 1, 2022	\$	76,637	\$ 4,120	\$ 80,757
Net additions		20,380	891	21,271
Acquired through business acquisition (Note 6)		528	—	528
Depreciation		(18,565)	(1,301)	(19,866)
Impairment		(448)	—	(448)
Balance, December 31, 2022	\$	78,532	\$ 3,710	\$ 82,242

PET VALU HOLDINGS LTD.

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5. Leases (continued):

Depreciation on ROU assets is included in cost of sales and selling, general and administrative expenses in the consolidated statements of income and comprehensive income for the period ended December 30, 2023 in the amounts of \$25,393 and \$1,113, respectively (December 31, 2022 — \$19,157 and \$709, respectively). Loss on sale of ROU assets of \$1,106 and \$793 was recognized on the sale of corporate-owned stores to franchisees for the periods ended December 30, 2023 and December 31, 2022, respectively. Impairment charges against ROU assets of \$448 were incurred as a result of closing or relocating corporate-owned stores during the period ended December 31, 2022.

(b) Lease liabilities:

The following table reconciles the changes in lease liabilities for the periods ended December 30, 2023 and December 31, 2022:

	Leased premises		Other		Total
Balance, December 31, 2022	\$	263,347	\$	3,954	\$ 267,301
Additions ⁽¹⁾		227,739		1,805	229,544
Interest expense on lease liabilities		16,247		251	16,498
Repayment of interest and principal		(67,740)		(1,702)	(69,442)
Balance, December 30, 2023	\$	439,593	\$	4,308	\$ 443,901
Current portion of lease liabilities	\$	62,778	\$	1,290	\$ 64,068
Long-term lease liabilities		376,815		3,018	379,833
Total lease liabilities	\$	439,593	\$	4,308	\$ 443,901

⁽¹⁾ Includes additions to lease liabilities of \$79,684 related to the new GTA distribution centre and \$67,061 related to the new Metro Vancouver Region distribution centre.

	Leased premises		Other		Total
Balance, January 1, 2022	\$	234,683	\$	4,231	\$ 238,914
Additions		70,104		904	71,008
Acquired through business acquisition (Note 6)		528		—	528
Interest expense on lease liabilities		11,577		276	11,853
Deferred lease payments		63		—	63
Repayment of interest and principal		(53,608)		(1,457)	(55,065)
Balance, December 31, 2022	\$	263,347	\$	3,954	\$ 267,301
Current portion of lease liabilities	\$	50,060	\$	1,275	\$ 51,335
Lease liabilities		213,287		2,679	215,966
Total lease liabilities	\$	263,347	\$	3,954	\$ 267,301

PET VALU HOLDINGS LTD.

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5. Leases (continued):

The Company makes variable lease payments for common area maintenance, property tax, security, and utilities on leased premises. The Company also has certain retail store leases where portions of the lease payments are contingent on a percentage of sales earned in the retail store. Expenses for variable lease components are included in cost of sales and selling, general and administrative expenses in the consolidated statements of income and comprehensive income. Expenses for variable lease components included in cost of sales and selling, general, and administrative expenses for the period ended December 30, 2023 were \$31,488 and \$157, respectively (December 31, 2022 — \$26,553 and \$169, respectively).

The following is a summary of the Company's future undiscounted contractual lease payments:

2024	\$	85,529
2025		87,506
2026		71,088
2027		61,474
2028		48,021
Thereafter		189,564
Total	\$	543,182

(c) Lease receivables:

The Company is considered an intermediate lessor related to head leases the Company has for franchise store locations. As at December 30, 2023 and December 31, 2022, the Company had lease receivables as follows:

	December 30,		December 31,	
	2023		2022	
Current portion of lease receivables	\$	34,332	\$	29,827
Long-term lease receivables		159,101		141,187
Total lease receivables	\$	193,433	\$	171,014

Finance income on lease receivables for the period ended December 30, 2023 was \$8,844 (December 31, 2022 — \$7,418). Franchisees make variable lease payments primarily for common area maintenance, property tax, and a percentage of sales earned in their retail store. Revenue from variable lease components included in franchise and other revenues in the consolidated statements of income and comprehensive income for the period ended December 30, 2023 was \$45,093 (December 31, 2022 — \$41,159).

The Company assesses the collectability of all lease receivables on an ongoing basis by considering its historical credit loss experience, current and forward-looking macroeconomic conditions, and other relevant factors (Note 3(k)(iv)). Based on this analysis, the expected credit loss is less than 1.0% of the lease receivables as at December 30, 2023 and December 31, 2022, respectively.

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5. Leases (continued):

The following table presents the contractual undiscounted cash inflows for lease receivables:

2024	\$	43,152
2025		41,860
2026		36,102
2027		29,590
2028		22,063
Thereafter		54,656
Total undiscounted lease receivables		227,423
Unearned interest income		(33,990)
Total lease receivables	\$	193,433

6. Business acquisitions:

On February 25, 2022, the Company acquired all of the issued and outstanding shares of Les Franchises Chico Inc. and 9353-0145 Quebec Inc. (collectively referred to as "Chico"), a franchisor of pet specialty stores in Quebec, Canada. The purpose of the acquisition was to expand the Company's presence into the Quebec market.

The following table summarizes the final purchase consideration that was paid during the period ended December 31, 2022:

Cash paid	\$	14,016
Contingent consideration		3,000
Net purchase price		17,016
Less: cash acquired and contingent consideration		(4,478)
Net consideration paid/cash outflow⁽¹⁾	\$	12,538

⁽¹⁾ Includes \$2,100 in holdbacks paid to escrow, with a term of 18 months from the acquisition date, for indemnity purposes.

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6. Business acquisitions (continued):

The final purchase price allocation is as follows as at December 31, 2022:

	Final allocation
Cash	\$ 1,478
Accounts and other receivables, net	1,493
Inventories, net	578
Prepaid expenses and other assets	35
Current assets acquired	3,584
Right-of-use assets	528
Property and equipment	220
Intangible assets	13,597
Goodwill	4,735
Total assets acquired	22,664
Accounts payable and accrued liabilities	1,609
Income taxes payable	658
Current portion of deferred franchise fees	45
Current portion of lease liabilities	158
Current liabilities assumed	2,470
Long-term deferred franchise fees	373
Long-term lease liabilities	370
Deferred tax liabilities	2,435
Total liabilities assumed	5,648
Net assets acquired	\$ 17,016

Intangible assets consist of trade names, franchise agreements and non-compete agreements. Recognized goodwill reflects how the acquisition will impact the Company's ability to generate future profits in excess of existing profits. The consideration paid mostly relates to expected future synergies and revenue growth. The goodwill is not deductible for tax purposes.

Acquisition related costs of \$462, incurred during the period ended December 31, 2022, are included in selling, general and administrative expenses in the consolidated statements of income and comprehensive income and in operating activities in the consolidated statements of cash flows.

The sellers of the shares were entitled to receive contingent consideration of \$3,000 based on the achievement of certain performance milestones. The contingent consideration was paid to sellers during the period ended December 30, 2023.

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For the periods ended December 30, 2023 and December 31, 2022

6. Business acquisitions (continued):

Franchise repurchases:

The following table discloses franchise repurchases for the period ended December 30, 2023. There were no repurchases of franchise stores for the period ended December 31, 2022. The franchise repurchases have been accounted for through the acquisition method.

	December 30, 2023
Number of stores repurchased	1
Inventories	\$ 96
Property and equipment	309
Goodwill	107
Cash consideration	\$ 512

7. Property and equipment:

The Company's property and equipment include the following:

	Land	Buildings	Furniture and fixtures	Equipment	Leasehold improvements	Construction- in-progress	Total
Cost							
December 31, 2022	\$ 120	\$ 497	\$ 67,258	\$ 2,639	\$ 97,240	\$ 17,387	\$185,141
Additions	—	—	9,682	1,468	20,844	20,770	52,764
Transfers	—	—	11,527	—	12,216	(23,743)	—
Disposal/retirement	—	—	(11,742)	—	(9,235)	—	(20,977)
December 30, 2023	120	497	76,725	4,107	121,065	14,414	216,928
Accumulated depreciation							
December 31, 2022	—	(281)	(37,407)	(695)	(54,984)	—	(93,367)
Depreciation	—	(20)	(9,698)	(391)	(10,771)	—	(20,880)
Disposal/retirement	—	—	10,599	—	7,213	—	17,812
December 30, 2023	—	(301)	(36,506)	(1,086)	(58,542)	—	(96,435)
Net book value, December 30, 2023	\$ 120	\$ 196	\$ 40,219	\$ 3,021	\$ 62,523	\$ 14,414	\$120,493

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For the periods ended December 30, 2023 and December 31, 2022

7. Property and equipment (continued):

	Land	Buildings	Furniture and fixtures	Equipment	Leasehold improvements	Construction- in-progress	Total
Cost							
January 1, 2022	\$ 120	\$ 497	\$ 56,614	\$ 2,414	\$ 83,712	\$ —	\$ 143,357
Additions	—	—	12,821	236	17,000	17,387	47,444
Acquired through business acquisition (Note 6)	—	—	79	86	55	—	220
Disposal/retirement	—	—	(2,256)	(97)	(3,527)	—	(5,880)
December 31, 2022	120	497	67,258	2,639	97,240	17,387	185,141
Accumulated depreciation							
January 1, 2022	—	(245)	(31,811)	(482)	(48,752)	—	(81,290)
Depreciation	—	(36)	(7,298)	(296)	(8,477)	—	(16,107)
Disposal/retirement	—	—	1,702	83	2,245	—	4,030
December 31, 2022	—	(281)	(37,407)	(695)	(54,984)	—	(93,367)
Net book value, December 31, 2022	\$ 120	\$ 216	\$ 29,851	\$ 1,944	\$ 42,256	\$ 17,387	\$ 91,774

For the periods ended December 30, 2023 and December 31, 2022, construction-in-progress includes costs for the new distribution centres in the GTA and Metro Vancouver Region.

8. Intangible assets and goodwill:

The Company's intangible assets include the following:

	Franchise agreements	Software	Definite-life trade name	Non-compete agreements	Indefinite-life trade name	Total
Cost						
December 31, 2022	\$ 33,901	\$ 25,773	\$ 2,815	\$ 853	\$ 42,469	\$ 105,811
Additions	—	3,257	—	—	—	3,257
Disposal/retirement	—	(4,790)	—	—	—	(4,790)
December 30, 2023	33,901	24,240	2,815	853	42,469	104,278
Accumulated amortization						
December 31, 2022	(32,525)	(17,743)	(2,489)	(774)	—	(53,531)
Amortization	(168)	(3,037)	(108)	(19)	—	(3,332)
Disposal/retirement	—	4,790	—	—	—	4,790
December 30, 2023	(32,693)	(15,990)	(2,597)	(793)	—	(52,073)
Net book value, December 30, 2023	\$ 1,208	\$ 8,250	\$ 218	\$ 60	\$ 42,469	\$ 52,205

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Notes to Consolidated Financial Statements
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For the periods ended December 30, 2023 and December 31, 2022

8. Intangible assets and goodwill (continued):

	Franchise agreements	Software	Definite-life trade name	Non-compete agreements	Indefinite-life trade name	Total
Cost						
January 1, 2022	\$ 32,400	\$ 22,322	\$ 2,815	\$ 760	\$ 30,500	\$ 88,797
Additions	—	3,424	—	—	—	3,424
Acquired through business acquisition (Note 6)	1,501	34	—	93	11,969	13,597
Disposal/retirement	—	(7)	—	—	—	(7)
December 31, 2022	33,901	25,773	2,815	853	42,469	105,811
Accumulated amortization						
January 1, 2022	(32,400)	(15,897)	(2,381)	(760)	—	(51,438)
Amortization	(125)	(1,853)	(108)	(14)	—	(2,100)
Disposal/retirement	—	7	—	—	—	7
December 31, 2022	(32,525)	(17,743)	(2,489)	(774)	—	(53,531)
Net book value, December 31, 2022	\$ 1,376	\$ 8,030	\$ 326	\$ 79	\$ 42,469	\$ 52,280

Goodwill changed during the periods as follows:

	Periods ended	
	December 30, 2023	December 31, 2022
Beginning balance	\$ 97,574	\$ 92,938
Net change in goodwill during the period	(12)	4,636
Ending balance	\$ 97,562	\$ 97,574

For the period ended December 30, 2023, included in the net change in goodwill during the period are \$107 of additions (December 31, 2022 — \$4,735) to the goodwill balance due to the franchise repurchase described in Note 6, which are net of reductions to goodwill balances of \$119 (December 31, 2022 — \$99) due to the sale of corporate-owned stores to franchisees. The addition to goodwill in the comparative period is due to the acquisition described in Note 6.

For impairment testing, the Company allocated the goodwill acquired from business combinations to the consolidated CGU group, which is also the Company's one operating segment, based on the expected future benefits to be derived. The Company allocated the carrying value of the Pet Valu tradenames of \$30,500 to the consolidated CGU group and the carrying value of the Chico tradename of \$11,969 to the Chico CGU group based on the lowest level that generates largely independent cash inflows (December 31, 2022 — \$30,500 and \$11,969, respectively).

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For the periods ended December 30, 2023 and December 31, 2022

8. Intangible assets and goodwill (continued):

During the fourth quarter of the periods ended December 30, 2023 and December 31, 2022, the Company performed an impairment test. The recoverable amount of the CGU groups for goodwill and indefinite-life tradenames for each year was determined to be higher than their carrying value, and as such, no impairment was recorded.

The VIU for the CGU groups for goodwill and the indefinite-life trade name was calculated using key assumptions including discounted cash flows over five years based on management's budget projections. Other assumptions used in the Company's annual impairment assessment as at December 30, 2023 include:

- Terminal growth rate of 2.0% (December 31, 2022 — 2.0%)
- After-tax discount rate of 6.7% (December 31, 2022 — 6.4%)

A reasonable change in these assumptions would not have resulted in an impairment.

9. Accounts and other receivables:

The Company's accounts and other receivables include the following:

	December 30, 2023	December 31, 2022
Franchise receivables	\$ 15,033	\$ 12,221
Trade accounts receivable	8,937	6,724
Other	3,905	4,020
	\$ 27,875	\$ 22,965

The Company's accounts and other receivables are aged no more than 90 days and 70% are aged less than 30 days. The Company's franchise receivables consist primarily of franchise billings from the last few days of the fiscal year, which are settled within the first days of the next fiscal year. The Company's trade accounts receivable primarily consist of balances due from vendors related to volume and co-operative advertising rebates. The other receivables primarily consist of tenant allowances from landlords.

The maximum exposure to credit risk at the reporting date is the carrying value of the accounts and other receivables. The Company assesses the collectability of all receivables on an ongoing basis by considering its historical credit loss experience, current and forward-looking macroeconomic conditions, and other relevant factors (Note 3(k)(iv)). Historically, the Company has not experienced defaults on receivables from franchisees, vendors and landlords. Based on this analysis, the expected credit loss is less than 1.0% of the accounts and other receivables as at December 30, 2023 and December 31, 2022, respectively.

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10. Inventories:

The Company's inventories comprise the following:

	December 30, 2023	December 31, 2022
Merchandise	\$ 124,925	\$ 120,503
Provision for obsolescence and shrinkage	(2,856)	(2,093)
	\$ 122,069	\$ 118,410

Included in cost of sales are write-downs due to obsolescence, shrinkage and damage of \$5,460 and \$4,806, for the periods ended December 30, 2023 and December 31, 2022, respectively.

11. Accounts payable and accrued liabilities:

The Company's accounts payable and accrued liabilities include the following:

	December 30, 2023	December 31, 2022
Trade payables	\$ 34,014	\$ 33,787
Accrued liabilities	23,404	37,317
Accrued interest	3,689	—
Accrued salaries, wages, benefits and incentives	13,334	19,061
Loyalty program liabilities (Note 4)	7,741	8,050
Gift card liabilities (Note 4)	1,482	1,777
Sales taxes payable	4,752	3,790
	\$ 88,416	\$ 103,782

12. Long-term debt:

Total long-term debt, net of deferred financing costs, as at December 30, 2023 and December 31, 2022 consists of the following:

	December 30, 2023	December 31, 2022
2021 Term Facility (a)	\$ 295,937	\$ 341,687
Deferred financing (b)	(2,713)	(3,874)
	293,224	337,813
Less current portion of long-term debt	(17,750)	(17,750)
Total long-term debt	\$ 275,474	\$ 320,063

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12. Long-term debt (continued):

(a) 2021 Credit Agreement:

The Company has a credit agreement with a syndicate of lenders (the "2021 Credit Agreement"), which provides for (i) a \$355,000 term facility (the "2021 Term Facility") and (ii) a \$130,000 revolving credit facility (the "2021 Revolving Facility"), a portion of which not in excess of \$20,000 shall be available for the issuance of letters of credit in Canadian or U.S. dollars (collectively referred to as the "2021 Credit Facilities").

The 2021 Credit Facilities mature on June 30, 2026. The 2021 Term Facility is repayable in quarterly instalments and contains mandatory prepayment provisions with respect to non-ordinary course asset sales, excess cash flow and issuances of debt obligations (excluding debt permitted to be incurred under the 2021 Credit Agreement) by the Company and its subsidiaries (in each case, subject to customary thresholds, qualifications and exceptions set forth in the 2021 Credit Agreement).

Borrowings under the 2021 Credit Facilities will bear interest, according to the type of borrowing advanced, at short-term floating rates, plus a margin per annum depending on the Company's net total leverage ratio.

During the period ended December 30, 2023, the Company amended the 2021 Credit Agreement to update the type of borrowing advanced at short-term floating rates. Specifically, the reference rates were modified from the LIBOR rate and the bankers' acceptance rate to the SOFR rate and Canadian reference rate, respectively. As at December 30, 2023, the effective interest rate on the 2021 Credit Facilities was 7.58% (December 31, 2022 — 6.87%).

The obligations under the 2021 Credit Agreement are unconditionally guaranteed by the Company and are secured by a charge over substantially all of the property and assets of the Company.

The 2021 Credit Agreement contains affirmative and negative covenants customary for credit facilities of this nature, subject to certain exceptions set forth in the 2021 Credit Agreement. The 2021 Credit Agreement also contains certain financial covenants over the term of the 2021 Credit Facilities, which include a net leverage ratio and an interest coverage ratio. As at December 30, 2023 and December 31, 2022, the Company was in compliance with all of its covenants.

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12. Long-term debt (continued):

As at December 30, 2023, mandatory long-term debt repayments are as follows:

2024	\$	17,750
2025		17,750
2026		260,437
		295,937
Less current portion of long-term debt		(17,750)
Total long-term debt	\$	278,187

Voluntary prepayments of the 2021 Term Facility are permitted at any time (subject to minimum repayment amounts and customary notice periods set forth in the 2021 Credit Agreement) without premium or penalty (other than customary “breakage” costs, if applicable) and will reduce the scheduled principal repayments. The 2021 Credit Agreement provides that amounts under the 2021 Revolving Facility may be borrowed, repaid and re-borrowed.

The Company had unused borrowing capacity available under the 2021 Revolving Facility of \$130,000 as at December 30, 2023 and December 31, 2022, respectively.

(b) Deferred financing costs:

In connection with the 2021 Credit Agreement, deferred financing costs of \$5,668 were incurred. The total unamortized deferred financing costs were \$2,713 as at December 30, 2023 (December 31, 2022 — \$3,874) and are being amortized using the effective interest method.

13. Interest expenses:

Interest expenses, net consist of the following:

	Periods ended	
	December 30, 2023	December 31, 2022
2021 Credit Agreement	\$ 23,024	\$ 15,025
Amortization of deferred financing costs	1,161	1,192
Interest on lease liabilities	16,498	11,853
Interest income on lease receivables	(8,844)	(7,418)
Standby letter of credit commitment fees	868	1,377
Other interest income, net	(2,061)	(1,551)
Interest expenses, net	\$ 30,646	\$ 20,478

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For the periods ended December 30, 2023 and December 31, 2022

14. Income taxes:

Significant components of income tax expense consist of the following for the periods ended:

	December 30, 2023	December 31, 2022
Current tax expense:		
Current periods	\$ 35,423	\$ 37,633
Adjustments with respect to prior periods	158	49
	35,581	37,682
Deferred tax expense (recovery):		
Origination and reversal of temporary differences	217	166
Adjustments with respect to prior periods	(172)	57
	45	223
Income tax expense	\$ 35,626	\$ 37,905

The Company's income tax expense differs from that calculated by applying the combined substantively enacted Canadian federal and provincial statutory income tax rates for the periods ended December 30, 2023 and December 31, 2022 of 26.5% as follows:

	December 30, 2023	December 31, 2022
Income before income taxes	\$ 125,174	\$ 138,671
Expected income tax expense	\$ 33,171	\$ 36,748
Increase (decrease) in income taxes resulting from:		
Change in deferred tax asset recognition	959	(182)
Non-deductible expenditures	1,125	900
Other	371	439
Income tax expense	\$ 35,626	\$ 37,905

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For the periods ended December 30, 2023 and December 31, 2022

14. Income taxes (continued):

The tax effects of the significant temporary differences that comprise deferred tax assets and liabilities as at December 30, 2023 and December 31, 2022 are as follows:

	December 30, 2023	December 31, 2022
Deferred tax assets:		
Ordinary loss carryforwards	\$ 12,701	\$ 8,958
Capital loss carryforwards	9,207	9,191
IFRS 16, Leases	117,508	69,647
Financing fees	2,200	3,352
Reserves and accruals	3,059	2,824
Deferred franchise fees	1,318	1,228
Capital lease obligation	1,143	1,048
Other	1,149	944
	\$ 148,285	\$ 97,192
Deferred tax liabilities:		
Intangible assets and property fair value increments on business acquisition	\$ 10,308	\$ 10,854
IFRS 16, Leases	112,855	65,994
Property and equipment	7,311	5,855
Other	—	148
	\$ 130,474	\$ 82,851
Value of deferred tax assets not recognized in the current period	(19,445)	(15,939)
Net deferred tax liabilities	\$ (1,634)	\$ (1,598)

As at December 30, 2023, the Company had approximately \$12,701 of tax effected ordinary loss carryforwards available (December 31, 2022 — \$8,958). The total U.S. federal losses as at December 30, 2023 were \$9,216 (December 31, 2022 — \$6,696) and have no expiry date. No deferred tax asset has been recognized with respect to these losses. The Canadian losses that expire between 2039 and 2043 as at December 30, 2023 were \$3,485 (December 31, 2022 — \$2,262). A deferred tax asset has been recognized on these Canadian losses as the Company expects to have taxable income available to utilize these losses. As at December 30, 2023, the Company had approximately \$9,207 of tax effected capital loss carryforwards available, which have no expiry date (December 31, 2022 — \$9,191). No income tax benefit has been recognized in respect of those losses.

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14. Income taxes (continued):

The net change in deferred income tax assets and liabilities is recorded as follows:

	December 30, 2023	December 31, 2022
Deferred tax expense recorded in net income	\$ (45)	\$ (223)
Deferred tax expense recorded through current tax payable	9	(1)
Deferred tax recorded from business acquisition (Note 6)	—	(2,435)
	\$ (36)	\$ (2,659)

The Company is subject to routine audits of its tax filing positions by the Canada Revenue Agency (“CRA”). In September 2023, the CRA reassessed the Company an additional approximately \$6,000 of income tax plus interest in respect of the Company’s 2018 taxation year on the basis that certain interest expenses incurred in that year were not deductible. It is possible that the CRA will reassess certain subsequent taxation years on a similar basis. The Company has filed an objection to, and intends to vigorously contest, the reassessment. The Company and its tax advisors believe that the tax filing positions are appropriate. Accordingly, no amount or provision has been recorded in the consolidated financial statements in respect of the 2018 reassessment.

The CRA is also currently examining the Company’s tax filing positions for the 2016 year and subsequent taxation years with respect to certain cross-border matters. To date, the CRA has not proposed any reassessment of the Company’s tax liability as a consequence of such audit. The Company and its tax advisors continue to believe that the Company’s tax filing positions are appropriate, and accordingly no amounts have been recorded in the consolidated financial statements in respect of any potential reassessment which may result from such audit. If the CRA were to reassess the Company, the Company would vigorously oppose any such reassessment. The Company has tax insurance against the risk of the Company ultimately being unsuccessful in opposing certain potential reassessments that may arise in connection with its acquisition of its former interest in Pet Supermarket, Inc., although there can be no assurance that such insurance will fully cover the amount of tax which may ultimately be imposed.

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15. Share capital:

(a) Authorized share capital:

The Company's authorized share capital consists of an unlimited number of common shares and an unlimited number of preferred shares, issuable in series.

The holders of common shares are entitled to receive dividends as declared from time to time by the Board of Directors. Shareholders are entitled to one vote per common share at shareholder meetings of the Company.

Preferred shares of each series, if and when issued, will, with respect to the payment of dividends, be entitled to preference over common shares. Except as provided in any special rights or restrictions attaching to any series of preferred shares issued from time to time, the holders of preferred shares will not be entitled to vote at any shareholder meetings of the Company.

As at December 30, 2023, there were 71,463,986 common shares and no preferred shares issued and outstanding.

The following table provides a summary of changes to the Company's share capital:

	Common shares outstanding	Amount
Balance, January 1, 2022	70,083,989 \$	307,497
Exercise of share options	892,482	8,711
Balance, December 31, 2022	70,976,471 \$	316,208
Exercise of share options	487,515	5,544
Balance, December 30, 2023	71,463,986 \$	321,752

(b) Dividends:

The Company's dividend policy is at the discretion of the Board of Directors. For the period ended December 30, 2023, the Company paid \$28,536 in dividends to holders of common shares (December 31, 2022 — \$16,927) or \$0.40 per common share (December 31, 2022 — \$0.24).

(c) Secondary offering:

On June 1, 2023, a secondary offering (the "2023 Secondary Offering") of the Company's common shares was completed by its principal shareholders on a bought deal basis. The 2023 Secondary Offering of 4,690,000 common shares at an offering price of \$32.05 per common share raised gross proceeds of \$150,315 for the principal shareholders. The Company did not issue additional common shares or receive any of the proceeds from the 2023 Secondary Offering. Underwriting fees were paid by the principal shareholders, and other expenses related to the 2023 Secondary Offering of approximately \$322 were paid by the Company and included in selling, general and administrative expenses for the period ended December 30, 2023.

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15. Share capital (continued):

(d) Normal course issuer bid:

On November 28, 2023, the Company announced that the Toronto Stock Exchange ("TSX") had accepted its notice of intention to launch a normal course issuer bid ("NCIB"). Pursuant to the NCIB, the Company may purchase for cancellation up to an aggregate of 1,786,599 common shares, representing approximately 2.5% of the Company's issued and outstanding common shares as at November 16, 2023, over the 12-month period commencing November 30, 2023 and ending November 29, 2024.

Effective November 24, 2023, the Company established an automatic share purchase plan ("ASPP") in connection with the NCIB to facilitate the purchase of common shares during certain periods when the Company would not be permitted to purchase shares due to regulatory restrictions or a self-imposed blackout period. Before entering a blackout period, the Company may, but is not required to, instruct its designated broker to make purchases at the broker's sole discretion and based on parameters set by the Company in accordance with the ASPP, NCIB, TSX rules, and applicable securities laws. The Company records a liability for the share purchase commitment during blackout periods based on the parameters of the ASPP. There was no obligation outstanding under the ASPP as at December 30, 2023.

16. Net income per share:

(a) Basic net income per share:

Basic net income per share is calculated by dividing the net income for the period attributable to shareholders of the Company by the weighted average number of common shares outstanding during the period.

	December 30, 2023		December 31, 2022	
Net income attributable to shareholders of the Company	\$	89,548	\$	100,766
Weighted average number of common shares outstanding during the period (<i>thousands</i>)		71,285		70,450
Basic net income per share attributable to the common shareholders	\$	1.26	\$	1.43

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16. Net income per share (continued):

(b) Diluted net income per share:

Diluted net income per share is calculated by dividing the net income attributable to shareholders, adjusted for the effects of dilutive options and share units, if applicable, for the period attributable to the shareholders of the Company by the weighted average number of common shares outstanding during the period, plus the weighted average number of common shares that would be issued on exercise of dilutive options and share units granted, as calculated under the treasury stock method.

	December 30, 2023	December 31, 2022
Net income attributable to shareholders of the Company	\$ 89,548	\$ 100,766
Weighted average number of common shares outstanding during the period (<i>thousands</i>)	72,385	72,130
Diluted net income per share attributable to the common shareholders	\$ 1.24	\$ 1.40

The following table provides a reconciliation from the basic weighted average number of common shares outstanding to the diluted weighted average number of common shares outstanding (number of shares in thousands):

	December 30, 2023	December 31, 2022
Basic weighted average number of common shares	71,285	70,450
Dilutive effect of share options in the Amended and Restated Share Option Plan	992	1,566
Dilutive effect of share options in the LTIP	108	114
Diluted weighted average number of common shares	72,385	72,130

For the period ended December 30, 2023, 81,664 performance-based share options granted pursuant to the Amended and Restated Share Option Plan were not included in the calculation of diluted net income per share, as the vesting conditions required to convert these options to common shares were not met (December 31, 2022 — 319,557).

For the period ended December 30, 2023, 363,797 service-based LTIP share options were not included in the calculation of diluted net income per share as they were not in the money (December 31, 2022 — nil).

For the period ended December 30, 2023, 564,374 performance-based LTIP share options were not included in the calculation of diluted net income per share, as the vesting conditions required to convert these options to common shares were not met (December 31, 2022 — nil).

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17. Cost of sales:

	Periods ended	
	December 30, 2023	December 31, 2022
Merchandise costs	\$ 542,795	\$ 479,015
Store occupancy costs	51,485	46,481
Distribution costs	96,450	73,904
	\$ 690,730	\$ 599,400

18. Selling, general and administrative expenses:

	Periods ended	
	December 30, 2023	December 31, 2022
Salaries, wages and benefits	\$ 112,711	\$ 105,298
Depreciation and amortization	20,364	16,263
Advertising	28,105	25,243
Technology and telecommunication	20,877	19,939
Professional fees	7,786	11,052
Other store expenses	7,113	6,161
Other selling, general and administrative expenses	7,455	8,149
	\$ 204,411	\$ 192,105

19. Share-based compensation:

(a) Amended and Restated Share Option Plan:

The Company has an Amended and Restated Share Option Plan (formerly referred to as the Legacy Option Plan or the Legacy Plan) pursuant to which it has granted share options to current and former directors and employees.

The Company amended and restated the Amended and Restated Share Option Plan so that no additional awards could be made under this plan, but share options previously granted under this plan continue to remain outstanding in accordance with their terms and will continue to be governed by the provisions of the Amended and Restated Share Option Plan.

Amended and Restated Share Option Plan option awards were granted at an exercise price determined by the Company's Board of Directors, which was not less than the fair market value of the underlying share on the date the option was granted. The Amended and Restated Share Option Plan option awards generally vest equally from the date of grant over five years and generally contain an equal number of service-based and performance-based awards. The share options can generally be exercised up to five years after the five-year vesting period and, therefore, the contractual term of each option granted is typically ten years. The Company accounts for the Amended and Restated Share Option Plan as an equity-settled plan.

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19. Share-based compensation (continued):

The fair value of each option award was calculated on the date of grant using the Black-Scholes option pricing model. Expected volatilities were based on the historical volatility of comparable publicly traded companies operating in the Company's industry. The expected life of options granted was based on management's best estimate using the mid-point between the vesting date and the maturity date for each tranche. The risk-free rate for periods within the expected life of the option was based on the U.S. Treasury yield curve in effect at the time of grant.

The tables below summarize the option activity under the Amended and Restated Share Option Plan:

	Options	Weighted average exercise price
Outstanding, January 1, 2022	2,703,397	\$ 9.31
Exercised	(892,482)	\$ 9.03
Forfeited	(43,616)	\$ 9.73
Outstanding, December 31, 2022	1,767,299	\$ 9.44
Exercised	(478,176)	\$ 8.66
Forfeited	(30,160)	\$ 9.73
Outstanding, December 30, 2023	1,258,963	\$ 9.72

The table below provides information relating to the share options outstanding and exercisable under the Amended and Restated Share Option Plan as at December 30, 2023:

	Share options outstanding			Share options exercisable		
	Number of share options	Weighted average remaining contractual term (years)	Weighted average exercise price	Number of share options	Weighted average remaining contractual term (years)	Weighted average exercise price
Exercise price range						
\$0.01 — \$9.73	1,258,963	\$ 5.53	9.72	871,662	5.27	\$ 9.72

During the period ended December 30, 2023, the Company recorded share-based compensation expense in relation to the Amended and Restated Share Option Plan of \$1,217 (December 31, 2022 — \$1,862), which was included in selling, general and administrative expenses.

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19. Share-based compensation (continued):

(b) LTIP:

The Company's LTIP allows for the grant of share options, stock appreciation rights, tandem stock appreciation rights, RSUs, PSUs and restricted stock awards to eligible participants. Any individual employed by the Company, including a service provider, who in the opinion of the Board of Directors is in a position to contribute to the success of the Company shall be eligible to receive awards under the LTIP. The number of common shares that can be issued under the LTIP, combined with all other security-based compensation arrangements of the Company, shall not exceed 10% of the aggregate number of issued and outstanding common shares, from time to time.

The number and the timing of the awards granted to eligible participants are determined by the Board of Directors. The exercise price per share with respect to each share option is also determined by the Board of Directors but cannot be less than the Market Price (as defined in the LTIP) of the common shares on the day on which the share option is granted. Share options typically vest over a period of three or four years and may contain service-based and performance-based vesting conditions. Share options granted under the plan may be exercised during a period not exceeding ten years from the grant date subject to earlier termination due to employment termination, death or disability. The performance-based options issued under the LTIP are based on the relative total shareholder return compared to the return of the following indices: S&P/TSX Completion Index, S&P/TSX Capped Composite Consumer Discretionary, and S&P/TSX Capped Composite Consumer Staples. The fair values of the service-based options and performance-based options are calculated at the date of the grant using the Black-Scholes option pricing model and the Monte Carlo simulation method, respectively.

RSUs and PSUs issued by the Company under the LTIP are settled in cash and are accounted for as cash-settled awards. The Company is required to record a liability for the potential future settlement of the vested RSUs and PSUs at each reporting date by reference to the fair value of the liability. The RSUs and PSUs cliff vest in three years following the grant date. The performance based component of PSUs is based 50% on operating income growth before share-based compensation expense and 50% on total return to the Company's shareholders relative to the total return of companies comprising a blend of the S&P/TSX Completion Index, S&P/TSX Capped Composite Consumer Discretionary, and the S&P/TSX Capped Composite Consumer Staples. The number of PSUs that vest is determined by multiplying the number of units granted to the participant by the adjustment factor, which ranges from 0 to 2.0, depending on the achievement of such targets. Additional RSUs and PSUs issued in lieu of cash dividends vest at the same time and are subject to the same conditions as the RSUs and PSUs to which they are attributable.

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19. Share-based compensation (continued):

(i) Share options:

The tables below summarize the share option activity under the LTIP:

	Options	Weighted average exercise price
Outstanding, January 1, 2022	276,490	\$ 20.00
Granted	304,764	\$ 30.92
Forfeited	(49,111)	\$ 25.10
Outstanding, December 31, 2022	532,143	\$ 25.78
Granted	1,259,961	\$ 26.88
Exercised	(9,339)	\$ 22.06
Forfeited	(111,486)	\$ 27.26
Outstanding, December 30, 2023	1,671,279	\$ 26.53

The table below provides information relating to the share options outstanding and exercisable under the LTIP as at December 30, 2023:

Exercise price range	Share options outstanding			Share options exercisable		
	Number of share options	Weighted average remaining contractual term (years)	Weighted average exercise price	Number of share options	Weighted average remaining contractual term (years)	Weighted average exercise price
\$20.00 — \$28.14	1,288,258	6.95	\$ 23.56	80,757	7.65	\$ 21.72
\$30.26 — \$40.24	383,021	8.84	\$ 36.53	42,316	8.38	\$ 32.06
\$20.00 — \$40.24	1,671,279	7.38	\$ 26.53	123,073	7.90	\$ 25.28

The Company uses the Black-Scholes option pricing model to calculate the fair value of the service-based options at the date of grant. The weighted average assumptions used in the model for options granted during the periods ended December 30, 2023 and December 31, 2022 are as follows:

	December 30, 2023	December 31, 2022
Weighted average risk-free interest rate	3.96 %	2.50 %
Expected life (years)	5.50 — 7.00	5.50 — 7.00
Expected dividend yield	1.45 %	0.79 %
Expected volatility	25.68 %	26.16 %
Forfeiture rate	3.32 %	10.00 %
Weighted average fair value per option granted	\$ 8.38	\$ 8.77

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19. Share-based compensation (continued):

The Company uses the Monte Carlo simulation method to calculate the fair value of the performance-based options at the date of the grant. The weighted average assumptions used in the model for options granted during the period ended December 30, 2023 are as follows:

Weighted average risk-free interest rate		4.76 %
Share price as at grant date	\$	23.87
Share price as at valuation date	\$	24.10
Expected life (years)		5.00
Expected dividend yield		1.66 %
Expected volatility		33.03 %
Weighted average fair value per option granted	\$	6.42

During the period ended December 30, 2023, the Company recorded share-based compensation expense in relation to the LTIP share options of \$2,748 (December 31, 2022 — \$1,115), which was included in selling, general and administrative expenses.

(ii) RSUs:

The table below summarizes the RSU activity under the LTIP:

	Number of RSUs
Outstanding, January 1, 2022	—
Granted ⁽¹⁾	102,397
Forfeited	(8,138)
Outstanding, December 31, 2022	94,259
Granted ⁽¹⁾	114,517
Forfeited	(20,957)
Outstanding, December 30, 2023	187,819

⁽¹⁾ Includes additional units issued in lieu of cash dividends.

The fair market value of future RSU cash-settlement obligations was \$2,206 at December 30, 2023 (December 31, 2022 — \$943). During the period ended December 30, 2023, the Company recorded share-based compensation expense for RSU cash-settlement obligations of \$1,262 (December 31, 2022 — \$943).

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19. Share-based compensation (continued):

(iii) PSUs:

The table below summarizes the PSU activity under the LTIP:

	Number of PSUs
Outstanding, January 1, 2022	—
Granted ⁽¹⁾	87,438
Forfeited	(8,351)
Outstanding, December 31, 2022	79,087
Granted ⁽¹⁾	70,229
Forfeited	(12,342)
Outstanding, December 30, 2023	136,974

⁽¹⁾ Includes additional units issued in lieu of cash dividends.

The expectation of the adjustment factor for the performance target linked to the total return to the Company's shareholders relative to the total return of companies comprising a blend of the S&P/TSX Completion Index, S&P/TSX Capped Composite Consumer Discretionary, and the S&P/TSX Capped Composite Consumer Staples is measured based on the Monte Carlo simulation method.

The key inputs used in the measurement of the fair value of the PSUs for the period ended December 30, 2023 are as follows:

	December 30, 2023	December 31, 2022
Average share price as at grant date	\$ 33.92	\$ 28.04
Share price as at valuation date	\$ 28.78	\$ 39.13
Average risk-free interest rate	4.05 %	4.49 %
Average expected remaining life (years)	1.50	2.00
Average expected volatility	26.55 %	36.88 %

The fair market value of future PSU cash-settlement obligations was \$1,517 at December 30, 2023 (December 31, 2022 — \$1,103). During the period ended December 30, 2023, the Company recorded share-based compensation expense for PSU cash-settlement obligations of \$414 (December 31, 2022 — \$1,103).

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19. Share-based compensation (continued):

(c) DSU Plan:

The Company has a DSU plan for non-employee board members. Each eligible director receives a portion of his or her annual director retainer in DSUs. The DSU portion of the retainer is granted on an annual basis based on the market price of the Company's common shares on the date of such grant. DSUs may only be redeemed when a director ceases to be a member of the Board. DSUs issued by the Company under the DSU Plan are settled in cash and are accounted for as cash-settled awards.

The Company is required to record a liability for the potential future settlement of the vested DSUs at each reporting date by reference to the fair value of the liability. The DSUs vest in four equal installments on the last day of each fiscal quarter during the one-year period following the grant date. Additional DSUs issued in lieu of cash dividends vest at the same time and are subject to the same conditions as the DSUs to which they are attributable.

The following is a summary of the Company's DSU Plan activity:

	Number of DSUs
Outstanding, January 1, 2022	25,501
Granted ⁽¹⁾	26,392
Outstanding, December 31, 2022	51,893
Granted ⁽¹⁾	19,480
Settled	(15,814)
Forfeited	(2,010)
Outstanding, December 30, 2023	53,549

⁽¹⁾ Includes additional units issued in lieu of cash dividends.

The fair market value of future DSU cash-settlement obligations was \$1,447 at December 30, 2023 (December 31, 2022 — \$1,645). During the period ended December 30, 2023, the Company recorded share-based compensation expense for DSU cash-settled obligations of \$214 (December 31, 2022 — \$1,225).

20. Investment in associate:

During the period ended January 1, 2022, the Company acquired a 19.9% ownership interest in HAFTAL LLC ("HAFTAL"). This ownership interest and other rights gave the Company significant influence over HAFTAL, and the Company accounted for its investment using the equity method. HAFTAL is a Delaware-based company formed for the purposes of developing an elevated experience for tracking pet health and lifestyle statistics.

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20. Investment in associate (continued):

In connection with the investment, the Company had a call option to purchase the remaining interest in HAFTAL (the "Call Option"). The Call Option had a term of five years following the date of the initial investment and was exercisable after April 1, 2023. The Call Option was accounted for at FVTPL and is included in the investment in associate in the Company's consolidated statements of financial position.

During the period ended December 30, 2023, the agreement in connection with the investment in HAFTAL was amended to eliminate the Call Option and the Company terminated its membership interest in HAFTAL. As a result, the Company derecognized the Call Option from the investment in associate in the consolidated statements of financial position and recorded an impairment loss of \$3,160, which is included in share of loss from associate. The Company's share of loss from associate and the loss on the derecognition of the Call Option are included in other loss (gain) in the consolidated statements of income and comprehensive income.

The following table reconciles the change in the investment in associate:

	Investment		Call Option		Total
Balance, January 1, 2022	\$	1,505	\$	674	\$ 2,179
Additional investment		2,178		—	2,178
Share of loss from associate		(483)		—	(483)
Unrealized gain on fair value		—		551	551
Currency translation adjustments		217		66	283
Balance, December 31, 2022	\$	3,417	\$	1,291	\$ 4,708
Share of loss from associate ⁽¹⁾		(3,416)		—	(3,416)
Loss on derecognition		—		(1,302)	(1,302)
Currency translation adjustments		(1)		11	10
Balance, December 30, 2023	\$	—	\$	—	\$ —

⁽¹⁾ Includes impairment of investment in associate.

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21. Financial instruments and risk management:

(a) Credit risk:

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Company's cash and cash equivalents, accounts and other receivables and lease receivables. The risk on cash and cash equivalents is mitigated by the fact that its deposits are with various high-quality financial institutions. The Company has receivables from the Company's suppliers and from the Company's franchise operators. The credit risk on its receivables from suppliers is managed by the ability to offset any monies owed by the supplier against amounts owed to the suppliers. The management of credit risk on the Company's franchisee accounts receivable and lease receivable is maintained by having short settlement terms on these receivables, and prior to accepting a franchisee, the Company undertakes a detailed screening process that includes the requirement that a franchisee has sufficient financing.

(b) Liquidity risk:

Liquidity risk is the risk the Company will not be able to meet its financial obligations as they come due. The Company mitigates liquidity risk by management of working capital, cash flows, and by maintaining various financing sources, including bank debt and finance leases. Adequate availability is maintained on the operating loan component of its credit facility to minimize this risk. The Company's trade and other payables are all due within 12 months from the date of these consolidated financial statements.

(c) Market risk:

Market risk is the risk the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises two types of risk: foreign currency risk and interest rate risk.

(i) Foreign currency risk:

The Company is exposed to foreign currency risk related to some of its purchases. Specifically, the Company sources some of its merchandise in U.S. dollars.

The Company is also exposed to foreign currency risk on financial assets and liabilities denominated in foreign currencies. These assets and liabilities are of a short-term nature, and management does not believe they represent a significant risk to the Company. A five percentage point change in the Canadian dollar against the U.S. dollar, assuming that all other variables are constant, would have changed income before income taxes for the period ended December 30, 2023 by \$421 (December 31, 2022 — \$354), as a result of the revaluation on these financial assets and liabilities.

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21. Financial instruments and risk management (continued):

(ii) Interest rate risk:

Interest rate risk is the risk the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The 2021 Credit Facilities (Note 12) are at variable interest rates. Changes in the short-term floating rates can cause fluctuations in interest payments and cash flows.

A one percentage point change in the applicable interest rate on the 2021 Credit Agreement based on the debt outstanding as at December 30, 2023 would have changed income before income taxes for the period ended December 30, 2023 by \$2,959 (December 31, 2022 — \$3,417).

(d) Fair values:

Financial instruments that are measured subsequent to initial recognition at fair value are to be categorized in Levels 1 to 3 of the fair value hierarchy, based on the degree to which the fair value is observable. The three levels of the fair value hierarchy are:

- Level 1 – inputs that are quoted market prices (unadjusted) in active markets for identical instruments;
- Level 2 – inputs other than quoted market prices included within Level 1 that are observable either directly (i.e., as prices) or indirectly (i.e., derived from prices). This category includes instruments valued using: quoted market prices in active markets for similar instruments, quoted prices for identical or similar instruments in markets that are considered less than active, or other valuation techniques in which all significant inputs are directly or indirectly observable from market data, and
- Level 3 – inputs that are unobservable. This category includes all instruments for which the valuation technique includes inputs that are not observable, and the unobservable inputs have a significant effect on the instrument's valuation. This category includes instruments that are valued based on quoted prices for similar instruments for which significant unobservable adjustments or assumptions are required to reflect the difference between the instruments.

There were no transfers between levels of the fair value hierarchy for the periods ended December 30, 2023 and December 31, 2022.

The carrying values of cash, accounts and other receivables, and accounts payable and accrued liabilities approximate fair values due to the short-term maturity of these financial instruments.

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21. Financial instruments and risk management (continued):

The carrying amounts and fair values of the Call Option, contingent consideration, and long-term debt are as follows:

	December 30, 2023		December 31, 2022	
	Carrying value	Fair value	Carrying value	Fair value
Assets:				
Call Option (Note 20) (Level 3)	\$ —	\$ —	\$ 1,291	\$ 1,291
Liabilities:				
Contingent consideration related to the acquisition of Chico (Note 6) (Level 3)	\$ —	\$ —	\$ 3,000	\$ 3,000
Long-term debt, including current portion ⁽¹⁾ (Level 2)	\$ 293,224	\$ 295,937	\$ 337,813	\$ 341,687

⁽¹⁾ Carrying value is net of deferred financing fees.

The Company used the Black-Scholes option pricing model to determine the fair value of the Call Option as at December 31, 2022.

22. Capital management:

The Company's capital management objectives are to maintain prudent financial flexibility and strength in order to pursue its strategy of growth and to provide stakeholder value creation. The Company defines capital as the aggregate of its shareholders' equity and long-term debt.

In order to maintain or adjust its capital structure, the Company may elect to issue or repay financial liabilities, issue shares, repurchase shares, pay dividends or undertake any other activities as deemed appropriate under the specific circumstances.

The Company is subject to financial and customary affirmative and negative covenants pursuant to the 2021 Credit Agreement presented in Note 12.

23. Operating segments:

The Company defines an operating segment on the same basis that it uses to evaluate performance internally and to allocate resources by the Chief Operating Decision Maker (the "CODM"). The Company has determined that the Chief Executive Officer is its CODM and there is one operating segment. Operating revenues are primarily composed of retail sales and franchise revenues (Note 4).

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24. Provisions:

For the period ended December 30, 2023, the Company recognized a restoration provision of \$3,252 associated with its distribution centres as the Company is contractually obligated to restore the leased premises to the original condition at the end of the lease. The Company recognized a corresponding increase in the cost of the associated ROU asset.

The following table reconciles the changes in restoration provisions for the period ended December 30, 2023.

Balance, December 31, 2022	\$	—
Restoration provisions recognized		3,252
Accretion from passage of time		43
Balance, December 30, 2023	\$	3,295
Current provisions		669
Non-current provisions		2,626
Total provisions	\$	3,295

25. Commitments, contingencies and guarantees:

(a) Distribution centre commitments:

The Company has provided the following commitments as at December 30, 2023:

(i) GTA:

The Company entered into agreements to procure certain material handling systems and equipment with commitments totaling approximately \$8,495 to be paid in fiscal year 2024.

(ii) Metro Vancouver Region:

The Company entered into an agreement to procure certain equipment with commitments totaling approximately \$1,570 to be paid in fiscal year 2024.

(b) Guarantees of indebtedness:

The Company had a guarantee related to certain lease obligations of a former subsidiary. As at December 31, 2023, these lease obligations were repaid in full by the former subsidiary and as such the guarantee was terminated. As at December 31, 2022, the future lease commitment related to the lease obligations under the guarantee was \$82 (US\$60).

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25. Commitments, contingencies and guarantees (continued):

(c) Bank comfort letters:

The Company has provided comfort letters to certain financial institutions at their request when these financial institutions provide financing to new franchisees. In the comfort letters, the Company has agreed that for three years from the date of the letter, if the bank is forced to realize on its security, including inventory held by the franchisee, the Company will repurchase the inventory previously sold to the franchisee at a stated discount of 15%, provided that such inventory can be sold by the bank to the Company free and clear of any and all liens, charges and encumbrances or rights of others.

Standard practice is for the Company to realize its rights under the franchise agreement prior to the franchisee reaching default under their finance arrangement; therefore, the risk associated with being required to repurchase inventory under these comfort letters is considered remote. Accordingly, no amount has been provided for in the accompanying consolidated financial statements.

(d) Other:

The Company may, from time to time, be named as a defendant in legal proceedings that arise from its normal course of business. Although the amount of any liability that could arise with respect to any pending claims cannot be estimated, the Company believes that any such liability is not reasonably likely to have a material adverse effect on its consolidated financial position, operating results or liquidity.

26. Related party transactions:

(a) Transactions with related parties:

On May 1, 2021, the Company entered into a transition services agreement with its former subsidiaries, pursuant to which the parties provide to each other certain information technology, real estate and human resources and benefits services on a no cost or at cost basis. The transition services agreement expired on August 23, 2023. The Company charged the former subsidiaries \$nil under the transition services agreement for the the period ended December 30, 2023 (December 31, 2022 — \$114).

During the period ended January 1, 2022, the Company entered into a product sourcing and brand license agreement with a former subsidiary, pursuant to which the Company sources certain pet food and pet supply products licensed under the Company's proprietary brands in consideration of a sourcing fee. The original product sourcing and brand license agreement had an initial term of 18 months that was automatically renewable for successive 18-month terms unless earlier terminated upon notice. This agreement was amended and restated on August 10, 2022, and includes an initial term of five years, terminating on August 9, 2027, which automatically renews for successive 18-month periods unless earlier terminated. The Company earned sourcing fees of \$996 under the product sourcing and brand license agreement for the period ended December 30, 2023 (December 31, 2022 — \$899).

PET VALU HOLDINGS LTD.

Notes to Consolidated Financial Statements

(Expressed in thousands of Canadian dollars, unless otherwise stated)

For the periods ended December 30, 2023 and December 31, 2022

26. Related party transactions (continued):

During the period ended December 28, 2019, the Company received a promissory note related to the exercise of options by an employee. During the period ended December 30, 2023, the outstanding balance of \$499 (US\$372) was repaid by the employee. This promissory note had a balance outstanding of \$504 (US\$372) as at December 31, 2022.

All of the related party transactions noted above were measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

(b) Compensation of key management personnel:

Key management personnel include the Board of Directors as well as senior executives and officers of the Company that are responsible for planning, directing and controlling the Company's business activities.

Key management personnel remuneration includes the following:

	Periods ended	
	December 30, 2023	December 31, 2022
Salaries and benefits	\$ 5,430	\$ 9,091
Share-based compensation	4,532	4,898
Termination benefits	—	704
Directors' fees	459	401
	\$ 10,421	\$ 15,094

The compensation amounts noted in the above table are recognized in selling, general and administrative expenses during the reporting periods.

27. Subsequent events:

On March 4, 2024, the Board of Directors of the Company declared a dividend of \$0.11 per common share payable on April 15, 2024 to holders of common shares of record as at the close of business on March 28, 2024.