



INTERIM CONSOLIDATED FINANCIAL STATEMENTS  
AND MANAGEMENT'S DISCUSSION AND ANALYSIS

FOR THE THREE AND SIX MONTHS ENDED APRIL 30, 2010

INTERIM CONSOLIDATED FINANCIAL STATEMENTS

**COASTAL CONTACTS INC.**

UNAUDITED

FOR THE THREE AND SIX MONTHS ENDED APRIL 30, 2010

(Canadian Dollars)

**COASTAL CONTACTS INC.**  
**CONSOLIDATED BALANCE SHEETS**

(\$000's)

	April 30, 2010	October 31, 2009
	(Unaudited)	
<b>ASSETS</b>		
<b>Current</b>		
Cash and cash equivalents <i>[note 3]</i>	\$ 9,878	\$ 11,532
Accounts receivable	8,338	7,965
Income tax receivable	109	-
Inventory	15,591	15,701
Prepaid expenses	2,203	1,532
Future income tax	93	109
Related party promissory notes <i>[note 7]</i>	199	374
	36,411	37,213
Property, equipment and leasehold improvements	3,762	2,813
Intangible assets	8,287	9,517
Goodwill	7,147	7,757
	\$ 55,607	\$ 57,300
<b>LIABILITIES</b>		
<b>Current</b>		
Accounts payable and accrued liabilities	\$ 17,465	\$ 17,908
Income tax payable	-	615
	17,465	18,523
Future income tax	3,186	3,614
	20,651	22,137
<b>SHAREHOLDERS' EQUITY</b>		
Share capital <i>[note 4]</i>		
Authorized:		
Unlimited common shares without par value		
Unlimited Class A preferred shares without par value		
Issued and outstanding:		
56,993,719 common shares [2009 – 56,901,719]	40,393	40,248
Contributed surplus <i>[note 5]</i>	2,555	2,294
Accumulated other comprehensive loss <i>[note 6]</i>	(5,227)	(3,482)
Deficit	(2,765)	(3,897)
	34,956	35,163
	\$ 55,607	\$ 57,300

See accompanying notes to the unaudited interim consolidated financial statements

Contingencies *[note 9]*

**COASTAL CONTACTS INC.**  
**CONSOLIDATED STATEMENTS OF EARNINGS AND COMPREHENSIVE**  
**EARNINGS (LOSS)**

(Unaudited) (\$000's, except share and per share amounts)

	<b>Three months ended</b>		<b>Six months ended</b>	
	<b>April 30</b>		<b>April 30</b>	
	2010	2009	2010	2009
<b>Sales</b>	<b>\$ 37,318</b>	<b>\$ 33,301</b>	<b>\$ 73,226</b>	<b>\$ 64,643</b>
Cost of sales	27,062	23,423	52,659	44,747
<b>Gross profit</b>	<b>10,256</b>	<b>9,878</b>	<b>20,567</b>	<b>19,896</b>
Advertising	3,920	4,252	7,911	8,378
Selling, general and administration	4,836	4,239	9,478	8,308
Share-based compensation	130	148	350	296
Amortization on property, equipment and leasehold improvements	286	240	568	455
Amortization on intangible assets	391	364	790	763
Foreign exchange (gains) losses	293	(39)	275	(241)
Interest expense (income)	1	(14)	15	(56)
<b>Earnings before income taxes</b>	<b>399</b>	<b>688</b>	<b>1,180</b>	<b>1,993</b>
Income tax	17	160	48	497
<b>Net earnings</b>	<b>382</b>	<b>528</b>	<b>1,132</b>	<b>1,496</b>
Unrealized foreign exchange gains (losses) on translation of financial statements of self-sustaining foreign operations	(630)	202	(1,745)	(1,011)
<b>Comprehensive earnings (loss)</b>	<b>\$ (248)</b>	<b>\$ 730</b>	<b>\$ (613)</b>	<b>\$ 485</b>
Basic earnings per share	\$ 0.01	\$ 0.01	\$ 0.02	\$ 0.03
Diluted earnings per share	\$ 0.01	\$ 0.01	\$ 0.02	\$ 0.03
Weighted average number of common shares outstanding				
Basic	56,961,506	57,974,911	56,931,117	58,149,443
Diluted	58,324,264	57,988,378	58,286,704	58,155,121

*See accompanying notes to the unaudited interim consolidated financial statements*

**COASTAL CONTACTS INC.**  
**CONSOLIDATED STATEMENTS OF DEFICIT**

(Unaudited) (\$000's)

<b>Six months ended April 30</b>	<b>2010</b>	<b>2009</b>
Deficit, beginning of period	\$ (3,897)	\$ (6,476)
Net earnings	1,132	1,496
Premium on purchase of common shares for cancellation	-	(59)
Deficit, end of period	\$ (2,765)	\$ (5,039)

*See accompanying notes to the unaudited interim consolidated financial statements*

**COASTAL CONTACTS INC.**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**

(Unaudited) (\$000's)

	Three months ended		Six months ended	
	April 30		April 30	
	2010	2009	2010	2009
<b>OPERATING ACTIVITIES</b>				
Net earnings	\$ 382	\$ 528	\$ 1,132	\$ 1,496
Non-cash items affecting earnings:				
Amortization	677	604	1,358	1,218
Amortization of deferred lease inducement	(22)	(20)	(29)	(40)
Share-based compensation	130	148	350	296
Future income taxes	(64)	(25)	(135)	(38)
Changes in non-cash working capital:				
Accounts receivable	186	550	(852)	(504)
Inventory	(1,319)	(3,965)	(712)	(5,523)
Prepaid expenses	(820)	(124)	(482)	298
Accounts payable and accrued liabilities	(918)	6,493	501	4,109
Income tax payable	(416)	(233)	(762)	164
<b>Cash provided by (used in) operating activities</b>	<b>(2,184)</b>	<b>3,956</b>	<b>369</b>	<b>1,476</b>
<b>INVESTING ACTIVITIES</b>				
Repayments from (advances to) related parties	179	(5)	175	(8)
Acquisition of property, equipment and leasehold improvements	(1,550)	(249)	(1,565)	(406)
Acquisition of intangible assets	(159)	(21)	(188)	(21)
Disposition of property and equipment	-	60	-	60
<b>Cash used in investing activities</b>	<b>(1,530)</b>	<b>(215)</b>	<b>(1,578)</b>	<b>(375)</b>
<b>FINANCING ACTIVITIES</b>				
Issuance of common shares on exercise of options	92	-	92	-
Purchase of common shares for cancellation	-	(953)	-	(970)
<b>Cash provided by (used in) financing activities</b>	<b>92</b>	<b>(953)</b>	<b>92</b>	<b>(970)</b>
Effect of exchange rate changes on cash and cash equivalents	(227)	(117)	(537)	(710)
Increase (decrease) in cash and cash equivalents	(3,849)	2,671	(1,654)	(579)
Cash and cash equivalents, beginning of period	13,727	11,956	11,532	15,206
<b>Cash and cash equivalents, end of period</b>	<b>\$ 9,878</b>	<b>\$ 14,627</b>	<b>\$ 9,878</b>	<b>\$ 14,627</b>
Income tax paid in cash	\$ 118	\$ 488	\$ 499	\$ 597

*See accompanying notes to the unaudited interim consolidated financial statements*

# **COASTAL CONTACTS INC.**

## **NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

April 30, 2010  
Unaudited

### **1. NATURE OF OPERATIONS AND BASIS OF PRESENTATION**

Coastal Contacts Inc. ("Coastal") is a global retailer of contact lenses, eyeglasses and related vision care products sold primarily through its internet sites. Coastal has customers in North America, Europe and the Asia Pacific region.

These unaudited interim consolidated financial statements have been prepared by Coastal in accordance with Canadian generally accepted accounting principles ("GAAP") for interim financial statements, and accordingly, do not include all disclosures required for annual financial statements. These unaudited interim consolidated financial statements, which include accounts of Coastal and its wholly owned subsidiaries, reflect the same accounting principles and methods of application as those disclosed in the notes to Coastal's audited consolidated financial statements for the year ended October 31, 2009 and should be read in conjunction with these statements. All intercompany transactions and balances have been eliminated.

The preparation of these unaudited interim consolidated financial statements and the accompanying notes requires management to make estimates and assumptions that affect the amounts reported. In the opinion of management, these unaudited interim consolidated financial statements reflect all adjustments necessary to state fairly the results for the periods presented. Actual results could vary from these estimates and the operating results for the interim periods presented are not necessarily indicative of the results expected for the full year.

### **2. FUTURE ACCOUNTING POLICIES**

#### **Transition to International Financial Reporting Standards**

In accordance with the Canadian Institute of Chartered Accountants Accounting Standards Board (AcSB), Canadian publicly accountable enterprises will be required to prepare financial statements in accordance with International Financial Reporting Standards (IFRS). This changeover to IFRS from Canadian GAAP will apply to Coastal's financial statements for the year beginning on November 1, 2011. Coastal will undertake the appropriate measures to ensure compliance with these new standards by the prescribed adoption date. Coastal is currently assessing the implications of these standards on the consolidated financial statements.

### **3. CASH AND CASH EQUIVALENTS**

Coastal has the Canadian Dollar equivalent of \$1.0 Million of cash on hand which is restricted pursuant to a letter of guarantee issued by a financial institution in favor of the Norwegian Customs and Excise Service to secure the payment of duty and value added tax collected by Coastal.

The Company has access to credit facilities, totaling approximately \$8.5 million. As at October 31, 2009, there was no balance outstanding pursuant to these facilities.

**COASTAL CONTACTS INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

April 30, 2010  
 Unaudited

**4. SHARE CAPITAL**

**(a) Issued and outstanding common shares**

Authorized share capital comprises an unlimited number of common shares without par value and an unlimited amount of Class A preferred shares without par value, of which none are issued. Common shares issued and outstanding are as follows:

	Six Months Ended April 30, 2010		Six Months Ended October 31, 2009	
	#	\$000's	#	\$000's
Balance, beginning of period	56,901,719	40,248	57,699,619	40,812
Issued on exercise of options	92,000	145	-	-
Purchased and cancelled	-	-	(797,900)	(564)
Balance, end of period	56,993,719	40,393	56,901,719	40,248

On December 30, 2009 Coastal renewed a Normal Course Issuer Bid ("NCIB") with the Toronto Stock Exchange ("TSX") for maximum eligible purchases of 3,797,468 of Coastal's common stock. There have been no purchases under this NCIB.

**(b) Share purchase options**

Coastal's shareholder adopted stock option plan (the "Option Plan"), for its directors, officers, employees and service providers, sets out the terms upon which options to purchase common shares may be granted. The maximum number of common shares to be reserved for issuance at any one time under the Option Plan and any other employee incentive plan is 10% of the then issued and outstanding common shares. The exercise price for a share purchase option granted under the Option Plan may not be less than that permitted by applicable regulatory authorities. Options granted may be subject to vesting requirements. Non-assignable options will be granted for a period which may not exceed five years from the date of the grant and will expire within 90 days upon the participant ceasing to be a director, officer, employee, or service provider. The Option Plan is administered by Coastal's Compensation and Corporate Governance Committee.

Share purchase option activity for the six months ended April 30, 2010:

	#	\$
Options outstanding, October 31, 2009	4,403,308	0.69 – 1.14
Granted	325,000	1.46 – 1.49
Exercised	(92,000)	0.87 – 1.09
Cancelled	(98,808)	0.99 – 1.00
Options outstanding, April 30, 2010	4,537,500	0.69 – 1.49

**COASTAL CONTACTS INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

April 30, 2010  
 Unaudited

**4. SHARE CAPITAL (continued)**

Share purchase options outstanding as at April 30, 2010:

Range of exercise price \$	Share purchase options Outstanding			Share purchase options Exercisable	
	Number of common shares issuable	Weighted average remaining contractual life (years)	Weighted average exercise price \$	Number of common shares issuable	Weighted average exercise price \$
\$0.69	50,000	3.48	0.69	25,000	0.69
\$0.80 - \$0.99	2,316,500	2.99	0.85	1,480,665	0.87
\$1.00 - \$1.14	1,846,000	2.71	1.08	1,112,351	1.08
\$1.15 - \$1.49	325,000	4.71	1.48	4,000	1.42
	4,537,500	3.00	0.99	2,622,016	0.96

The fair value of the option grants are estimated on the date of the grant using the Black-Scholes option-pricing model with the following weighted average assumptions:

	2010	2009
Dividend yield	0%	0%
Expected volatility	55.2%	57.3%
Risk free interest rate	2.8%	2.1%
Expected lives	5.0 years	5.0 years

**(c) Employee Share Ownership Plan**

On August 1, 2009, Coastal established an employee share ownership plan ("ESOP") whereby Coastal matches dollar contributions made by eligible employees. The contributions are limited to 8% of gross salary and a maximum of \$7,500 per participant per year. The contributions are used to purchase voting shares of Coastal through the open market. Approximately one half of our employees are eligible to participate in the ESOP.

Coastal's share of contribution made during the six months ended April 30, 2010 totaled \$147,611. There were no such contributions during the six months ended April 30, 2009 as the plan was not in place.

**COASTAL CONTACTS INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

April 30, 2010  
Unaudited

**5. CONTRIBUTED SURPLUS**

	\$000's
Balance – October 31, 2009	2,294
Share-based compensation	350
Impact of options exercised	(53)
Impact of options cancelled and settled in cash	(36)
Balance – April 30, 2010	2,555

**6. ACCUMULATED OTHER COMPREHENSIVE LOSS**

	\$000's
Balance – October 31, 2009	(3,482)
Unrealized foreign exchange losses on translation of financial statements of self-sustaining foreign operations	(1,745)
Balance – April 30, 2010	(5,227)

**7. RELATED PARTY BALANCES AND TRANSACTIONS**

	April 30, 2010 \$000's	October 31, 2009 \$000's
Promissory notes receivable	199	374

As at April 30, 2010, there were four promissory notes outstanding to employees totalling \$0.2 million, of which \$0.04 million was accumulated interest. These loans are payable on demand and bear interest at a rate of 5% per annum. The debtors are employees of Coastal, are personally liable for the amounts owed. Coastal did not have any loans outstanding to its Chief Executive Officer, its Chief Financial Officer or any of its directors at the end of the second quarter of 2010.

**COASTAL CONTACTS INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

April 30, 2010  
 Unaudited

**8. SEGMENTED INFORMATION**

Coastal operates in one business segment, the sale of contact lenses, glasses and related vision care products. Coastal ships product from North America and Europe to customers in North America, Europe and the Asia Pacific region.

Geographical information is based on the location of the customers in which Coastal sells its products. Intercompany sales have been excluded. Certain comparative figures have been adjusted to reflect this reporting.

All figures below are presented in Canadian Dollars.

	Canada \$000's	Sweden \$000's	Norway \$000's	USA \$000's	Other \$000's	Total \$000's
<b>Sales</b>						
<b>Three months ended April 30, 2010</b>	<b>8,049</b>	<b>7,156</b>	<b>4,626</b>	<b>6,424</b>	<b>11,063</b>	<b>37,318</b>
Three months ended April 30, 2009	5,848	7,266	4,676	4,746	10,765	33,301
<b>Six months ended April 30, 2010</b>	<b>15,269</b>	<b>13,924</b>	<b>9,274</b>	<b>12,062</b>	<b>22,697</b>	<b>73,226</b>
Six months ended April 30, 2009	10,656	14,487	9,139	9,162	21,199	64,643
<b>Property, equipment and leasehold improvements</b>						
<b>As at April 30, 2010</b>	<b>2,578</b>	<b>1,184</b>	-	-	-	<b>3,762</b>
As at April 30, 2009	1,496	1,481	-	-	-	2,977
<b>Intangible assets</b>						
<b>As at April 30, 2010</b>	<b>913</b>	<b>2,726</b>	-	-	<b>4,648</b>	<b>8,287</b>
As at April 30, 2009	1,130	3,643	-	-	5,167	9,940
<b>Goodwill</b>						
<b>As at April 30, 2010</b>	-	<b>5,127</b>	-	-	<b>2,020</b>	<b>7,147</b>
As at April 30, 2009	-	5,483	-	-	2,119	7,602

**9. CONTINGENCIES**

Coastal is engaged in certain legal actions in the ordinary course of our business and believes that the ultimate outcome of these actions will not have a material adverse effect on our operating results, liquidity or financial position.

**10. COMPARATIVE FIGURES**

Certain comparative figures have been reclassified to conform to the current period's presentation.

## **Management's Discussion and Analysis of Financial Condition and Results of Operations for the three and six months ended April 30, 2010**

This "Management's Discussion and Analysis of Financial Condition and Results of Operations" (MD&A) is dated as of June 14, 2010 and should be read in conjunction with Coastal Contacts Inc.'s (the "Company", "our", "we", "us", "Coastal" or "Coastal Contacts") unaudited interim consolidated financial statements and notes thereto for the three and six months ended April 30, 2010. We prepare our consolidated financial statements in accordance with Canadian generally accepted accounting principles ("GAAP") and use Canadian dollars as our reporting currency.

### **Forward-looking statements**

All statements made in this management's discussion and analysis, other than statements of historical fact, are forward-looking statements. The words "may", "would", "could", "will", "intend", "plan", "anticipate", "believe", "estimate", "expect", "goal", "target", "should," "likely," "potential," "continue," "project," "forecast," "prospects," and similar expressions typically are used to identify forward-looking statements. Examples of such forward-looking statements within this document include statements relating to: our perception of the contact lens industry or market and anticipated trends in that market in any of the countries in which we do business; our anticipated ability to procure products, or the terms under which we may procure our products; our anticipated business operations, inventory levels, ability to handle specific order and call volumes, ability to fill and timely ship orders, ability to achieve greater marketing efficiency or similar statements; our ability to increase production; our plans for capital expenditure plans; our relationships with suppliers, our anticipated results of operations, including but not limited to anticipated sales, revenues, earnings, tax benefits or similar matters; the effects of seasonality; sufficiency of cash flows; and our perceptions regarding volatility in and impact of foreign currency exchange rates.

Forward-looking statements are based on the then-current expectations, beliefs, assumptions, estimates and forecasts about our business and the industry and markets in which we operate. Forward-looking statements are not guarantees of future performance and involve risks, uncertainties and assumptions which are difficult to predict. Assumptions underlying our expectations regarding forward-looking statements or information contained in this MD&A include, among others: that we will maintain our position in the markets we operate in and expand into other markets in a favourable manner; that we will have sufficient capital to continue making investments in advertising, inventory, equipment and personnel to support our business and new product lines, including our eyeglass business; that we will be able to generate and maintain sufficient cash flows to support our operations; that we will be successful in complying with regulatory requirements in British Columbia and other jurisdictions; that we will be able to establish and/or maintain necessary relationships with suppliers; and that we will retain key personnel. The foregoing list of assumptions is not exhaustive.

Persons reading this MD&A are cautioned that forward-looking statements or information are only predictions, and that our actual future results or performance may be materially different due to a number of factors. These factors include, but are not limited to: changes in the market; potential downturns in economic conditions; consumer credit risk; our ability to implement our business strategies; competition; limited suppliers; inventory risk; disruption in our distribution facilities; mergers and acquisitions; foreign currency exchange rate fluctuations; regulatory requirements; demand for products we sell; competition and dependence on the internet and other risks detailed in our filings with the Canadian and Swedish securities regulatory authorities. Reference should be made to the section entitled "Risk Factors" contained in our most recently filed Annual Information

Form dated January 29, 2010 and our listing prospectus, dated October 14, 2009 and filed with the Swedish Regulatory Agency, both of which are available on SEDAR at [www.sedar.com](http://www.sedar.com)., for a detailed description of the risks and uncertainties relating to our business. These risks, as well as others, could cause actual results and events to vary significantly. Accordingly, readers should not place undue reliance on forward-looking statements and information, which are qualified in their entirety by this cautionary statement. These forward-looking statements are made as of the date of this MD&A and we expressly disclaim any intent or obligation to update these forward-looking statements, unless we specifically state otherwise and except as required by applicable law.

## **Overview**

Coastal Contacts, is the leading worldwide online retailer of contact lenses, eyeglasses, sunglasses and vision care accessories. We service our international customers through our distribution facilities in North America and Europe.

We launched our business in the year 2000 selling contact lenses online. In 2004, after a successful start up phase, we completed an initial public offering of our common shares in Canada. From 2004 to 2008 we targeted a significant portion of our investments in various international markets and acquired several businesses in Europe and Asia as part of our strategy to establish a globally diversified business platform.

We have built a diversified international base of more than 2 million vision corrected customers and have the largest market share of any online optical retailer in many of our markets.

During the second quarter of fiscal 2010 we experienced a 12% increase in sales (19% excluding the effects of foreign exchange), when compared to the same period in 2009. We shipped a total of 384,258 orders, approximately 27% of which were to new customers with the remaining amount representing reorders. Eyeglasses sales in the quarter totaled \$4.7 million, a 136% increase over the same period last year. In our North American market, sales of eyeglasses grew 195% year over year for the periods referenced. Shipped orders and reorders are non-GAAP measures that do not have a standardized meaning prescribed by Canadian GAAP and are therefore unlikely to be comparable to similar measures presented by other companies. Refer to *Supplemental Non-GAAP Measures* below for further information.

We expanded our glasses team, mostly in our manufacturing and customer service functions in both North America and Europe, and we made significant capital investments in equipment and leasehold improvements in our eyeglasses production facilities, along with improvements to our information technology infrastructure. We continued to broaden our selection of eyeglasses, update our websites, and expand the capacity for assembly facilities to meet customer demand.

During the second quarter of fiscal 2010, new health care regulations were introduced in British Columbia, certain of which positively impact our business as they permit individuals to order glasses or contact lenses online without having to provide the seller a copy of their prescription, sight-test assessment or contact lens specifications. Furthermore it provides for the mandatory release of information held by the British Columbia opticians and optometrists to the clients; namely a copy of their prescription, sight-test assessment or contact lens specifications, including to a third-party eyewear seller if requested by the client.

Volatility in the foreign currency exchange markets impacted our financial performance in our second quarter more than in recent quarters. We experienced a negative 7% impact on our reported sales, largely as a result of weakness in the value of the US dollar relative to Canadian dollar and the Euro relative to the Swedish Krona. Additionally, we incurred an unrealized foreign exchange loss of \$0.3 million, which included a \$0.4 million unrealized loss on Euro denominated monetary assets such as cash and receivables relative to the Swedish Krona and this negatively affected our earnings. Excluding the foreign exchange impact on monetary assets and liabilities, our earnings before income taxes increased by 6% during the three months ended April 30, 2010 compared to the same period in 2009.

### Recent Developments

On March 30, 2010, we announced the termination of the Managing Director of our European operations. Subsequently, we appointed Mr. Bo Wänghammar, an experienced executive in the IT industry, as the Managing Director of our European operations.

On May 18, 2010, Coastal filed a statement of claim in the British Columbia Supreme Court against the former European Managing Director, who is also one of our current directors, in respect of breaches of fiduciary duties and a failure to act honestly and in good faith with a view to the best interests of Coastal. The remedies being sought include injunctive relief, and general, special and punitive damages.

### Results of Operations – for the three and six months ended April 30, 2010 compared to the three and six months ended April 30, 2009

(\$000's)	For the three months ended April 30,		For the six months ended April 30,	
	2010	2009	2010	2009
<b>Sales</b>	37,318	33,301	73,226	64,643
<b>Gross profit</b>	10,256	9,878	20,567	19,896
<b>Foreign exchange (gains) losses</b>	293	(39)	275	(241)
<b>Earnings before income taxes</b>	399	688	1,180	1,993
<b>Net earnings</b>	382	528	1,132	1,496
<b>Adjusted EBITDA<sup>1</sup></b>	1,500	1,387	3,178	3,210

Sales increased by \$4.0 million or 12% (19% excluding the effects of foreign exchange) in the second quarter of fiscal 2010 to \$37.3 million (384,258 orders shipped) from \$33.3 million (324,577 orders

<sup>1</sup> Adjusted EBITDA is a non-GAAP measure that does not have a standardized meaning prescribed by Canadian GAAP and is therefore unlikely to be comparable to similar measures presented by other companies. Refer to *Supplemental Non-GAAP Measures* for further information and a reconciliation of net earnings to adjusted EBITDA.

shipped) in the second fiscal quarter of 2009. During the three months ended April 30, 2010 our sales grew 18% due to an increase in shipped orders and 1% due to an increase in our average revenue per order and declined 7% due to foreign currency exchange rate fluctuations, as compared to the same period in 2009

Comparing the second fiscal quarter of 2010 to the same period in 2009, sales in our North American business grew 29%, representing 51% of our total sales, largely as a result of the success of our eyeglasses business in Canada and the United States, while sales from our European business remained flat year over year. Eyeglasses sales in the quarter totaled \$4.7 million, a 136% increase over the same period last year. These sales were primarily shipped out of our North American facilities.

Sales increased by \$8.6 million or 13% in the first six months of fiscal 2010 to \$73.2 million from \$64.6 million in the first six months of fiscal 2009. Sales grew 17% due to an increase in shipped orders, primarily of eyeglasses in North America, 2% due to an increase in our average revenue per order and decreased 5% as a result of foreign currency exchange rates. Our four largest national markets are Canada, Sweden, Norway and the United States. In Canada and the United States, sales grew by 43% and 32%, respectively, during the six months ended April 30, 2010. In Sweden and Norway our sales remained relatively flat during the same comparative period.

Our gross profit as a percentage of sales, or gross margin, in the three months ended April 30, 2010 was 27.5%, compared to 29.7% in the same period in 2009. For the six months ended April 30, 2010, our gross margin decreased to 28.1% from 30.8% when compared to the same period in 2009. Gross margin decreased in both comparison periods as a result of increased cost of promotions to encourage sales and market adoption of our products, an increase in the proportion of sales coming from lower gross margin markets, retail price declines in some of our markets, particularly in Europe, and the cost of hiring additional production staff to support higher sales volumes of eyeglasses and contact lenses. Finally when comparing the three and six months ended April 30, 2010 to the same periods in 2009, foreign currency exchange rates, in particular European currencies relative to the Swedish Krona, had a negative effect on our gross margins as short term declines in those currencies were not correspondingly offset by improvements in input costs.

Advertising expenses decreased to \$3.9 million (11% of sales) in the second quarter of fiscal 2010, compared to \$4.3 million (13% of sales) during the same period in 2009. During the six months ended April 30, 2010, advertising expenses decreased to \$7.9 million (11% of sales), compared to \$8.4 million (13% of sales) during the same period in 2009. This decrease is attributable to a reduction in advertising expenditures in our European operation and our use of alternative promotional methods to gain customers and encourage the online adoption of the eyeglasses model.

Selling, general and administrative expenses ("SG&A") increased to \$4.8 million in the second quarter of fiscal 2010, as compared with \$4.2 million in the second quarter of 2009, and increased to \$9.5 million in the six months ended April 30, 2010, from \$8.3 million in 2009. Approximately \$0.3 million of this increase related to travel, professional, and severance costs relating to management changes in Europe in the second quarter of 2010, with the remainder relating to increased personnel costs to support our growing business.

During both the three and six months ended April 30, 2010 we recognized foreign currency exchange losses on the translation of our monetary assets of \$0.3 million, compared to a loss of \$0.04 million and a gain of \$0.2 million during the respective three and six month periods in the previous year.

Our unrealized foreign exchange loss included a \$0.4 million unrealized translation loss on Euro denominated monetary assets, such as cash and receivables, which was partially offset by translation gains in other geographies.

Amortization for the three months ended April 30, 2010 increased by \$0.1 million to \$0.7 million when compared to the three months ended April 30, 2009. Amortization for the six months ended April 30, 2010 increased by \$0.2 million to \$1.4 million. Increases in amortization are directly attributable to the increased investment in capital spending compared to previous periods.

Adjusted EBITDA was \$1.5 million in the second quarter of fiscal 2010, an 8% improvement over the same period in 2009.

Our income tax expense decreased overall to \$0.02 million in the second quarter of 2010 from \$0.16 million for the quarter ended April 30 2009. Our income tax rates, as a percentage of taxable earnings in the countries in which we generate taxable earnings, remained unchanged in the second quarter of fiscal 2010 compared to the same period of fiscal 2009. Certain operations generate taxable earnings, while in certain other jurisdictions we have incurred losses historically that can be applied against current and future taxable earnings to reduce our tax liability on those earnings. We have taken a valuation allowance against these future tax assets. Consequently, our consolidated tax expense, as a percentage of earnings before income taxes, will vary from quarter to quarter in line with the mix of net earnings within each taxable jurisdiction.

### **Liquidity and Capital Resources**

At April 30, 2010 we had cash and cash equivalents of \$9.9 million, as compared to cash and cash equivalents of \$11.5 million at October 31, 2009.

Cash used in operations was \$2.2 million during the second quarter of fiscal 2010 compared to cash provided by operating activities of \$4.0 million during the same period in fiscal 2009. Our earnings after adjustments for non cash items was \$1.1 million and \$3.3 million was used for changes in non-cash working capital items such as inventory, prepaid expenses and accounts payable. We expect cash flows from changes in working capital to vary from quarter to quarter due to the timing of ordinary course receipts and payments.

Cash used for investing activities was \$1.5 million for the second quarter of fiscal 2010, compared to cash used of \$0.2 million during the same period in fiscal 2009. During the three months ended April 30, 2010, we expanded our investments in our eyeglasses production facilities as well as our information technology infrastructure.

We believe that existing available cash, operating facilities, and operational cash flow will be sufficient to support our capital expansion plans, stock purchases and operations through to the end of fiscal 2011. We are actively expanding our product offerings, assessing capital financing alternatives, assessing strategic opportunities, and considering strategic acquisitions. We may seek additional sources of funds to support our capital expansion or for accelerated growth, acquisitions of companies or assets or other activities, and there can be no assurance that such funds will be available on satisfactory terms or at all. Failure to obtain such financing could delay or prevent our planned growth, which could adversely affect our business, financial condition and results of operations.

As at April 30, 2010, we had access to two separate credit facilities totaling approximately \$8.5 million. Neither of these credit facilities had been drawn on as of that date.

### **Critical Accounting Estimates**

Coastal prepares its consolidated financial statements in accordance with Canadian GAAP. The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements as well as the reported amounts of sales and expenses during the reporting period. Estimates are based upon historical experience and other assumptions that are believed to be reasonable under the circumstances. These estimates are evaluated on an on-going basis and form the basis for making decisions regarding the carrying value of assets and liabilities and the reported amount of sales and expenses. Actual results may differ from these estimates under different assumptions.

We have identified the following as critical accounting estimates, which are defined as those that are reflective of significant judgments and uncertainties, are the most pervasive and important to the presentation of our financial condition and results of operations and could potentially result in materially different results under different assumptions and conditions.

#### *Revenue Recognition*

Revenue from product sales is recognized when the product has been shipped to the customer. At this point, the amount of sales revenue is determinable, no significant vendor obligations remain and the collection of the revenue is reasonably assured.

Deferred revenue includes revenue collected in advance of the product being shipped to the customer.

#### *Accounting for Long-lived Assets*

The ability to realize long-lived assets which are primarily comprised of customer lists and website creation costs are evaluated periodically as events or circumstances indicate a possible inability to recover their carrying amount. Such evaluation is based on assessment of reorder rates and various analyses, including undiscounted cash flow and profitability projections that incorporate, as applicable, the impact on the existing business. The analyses necessarily involve significant management judgment. Any impairment loss, if indicated, is measured as the amount by which the carrying amount of the asset exceeds the estimated fair value of the asset.

#### *Accounting for Goodwill and Intangible Assets with Indefinite Lives*

Goodwill represents the excess of the purchase price over the fair value of the net assets acquired. Goodwill is not amortized and we perform an annual impairment test of our recorded goodwill. In addition, we test our other indefinite-lived intangible assets for impairment. These impairment tests can be significantly altered by estimates of future performance, long-term discount rates used or market price valuation multiples. The analyses necessarily involve management judgment. These estimates will likely change over time. Goodwill and intangible assets with indefinite lives totaled \$15.4 million and \$17.3 million at April 30, 2010 and October 31, 2009, respectively.

### *Allowance for Doubtful Accounts*

We offer credit to most of our customers. These customers do not have to pay for the order until the goods are received – generally estimated to be less than 15 days. The majority of the individual receivable balances are small amounts of less than \$150 and there are a large number of records. Given the composition of the receivable portfolio, using a specific balance approach to determine an allowance for doubtful accounts for the bulk of the receivables is not feasible. Consequently, management estimates an allowance for doubtful accounts based on the aging of the receivable portfolio. The analyses necessarily involve significant judgment. These analyses can be significantly altered by estimates of the probability of future collection or changes in payment patterns of customers. The allowance for doubtful accounts at April 30, 2010 was \$0.8 million.

### *Income Taxes*

We account for income taxes using the liability method of accounting. Under the liability method, future income tax assets and liabilities are determined based on differences between the carrying amounts of balance sheet items and their corresponding tax values. The determination of the income tax provision requires management to interpret regulatory requirements and to make certain judgements. While income tax filings are subject to audits and assessments, management believes that adequate provision has been made for all income tax obligations. However, changes in the interpretations or judgements may result in an increase or decrease in our income tax provision in the future. The amount of any such increase or decrease cannot be reasonably estimated.

### **Future Accounting Policies**

#### *Transition to International Financial Reporting Standards*

In accordance with the Canadian Institute of Chartered Accountants Accounting Standards Board (AcSB), Canadian publicly accountable enterprises will be required to prepare financial statements in accordance with International Financial Reporting Standards (IFRS). This changeover to IFRS from Canadian GAAP will apply to the Coastal's financial statements for the year beginning on November 1, 2011. Coastal will undertake the appropriate measures to ensure compliance with these new standards by the prescribed adoption date. Coastal is currently assessing the implications of these standards on the consolidated financial statements.

IFRS consists of a conceptual framework similar to Canadian GAAP and therefore differences in accounting policies will have to be addressed. In order to meet the requirement to transition to IFRS, the Company is currently undertaking a project to ensure compliance with the new standards by the adoption date. The Company's IFRS project plan is comprised of four stages: awareness, assessment, design and implementation. The company is currently in the assessment stage which includes an analysis of the difference between IFRS and Canadian GAAP and an evaluation of the potential impact on financial reporting, accounting policies, systems and internal controls over financial reporting.

### **Common Shares**

As at June 14, 2010, Coastal had 56,993,719 common shares and 4,537,500 share purchase options outstanding.

## Quarterly Financial Information

(in \$000's, except per share amounts)

Quarter ended	Apr. 30, 2010	Jan. 31, 2010	Oct. 31, 2009	July 31, 2009	Apr. 30, 2009	Jan. 31, 2009	Oct. 31, 2008	July 31, 2008
<b>Sales</b>	37,318	35,908	37,716	37,511	33,301	31,342	32,027	32,725
<b>Adjusted EBITDA<sup>1</sup></b>	1,500	1,678	2,828	1,967	1,387	1,823	1,664	1,276
<b>Foreign exchange (gain) loss</b>	293	(18)	(121)	252	(39)	(202)	361	(64)
<b>Net Earnings</b>	382	750	648	603	528	968	397	211
<b>Weighted average # of shares - basic</b>	56,962	56,902	56,902	57,057	57,975	58,318	58,451	63,430
<b>Weighted average # of shares - diluted</b>	58,324	58,502	57,705	57,374	57,988	58,320	58,605	63,535
<b>Basic earnings per share</b>	0.01	0.01	0.01	0.01	0.01	0.02	0.01	0.00
<b>Diluted earnings per share</b>	0.01	0.01	0.01	0.01	0.01	0.02	0.01	0.00

Seasonality may impact our sales distribution throughout the year. Our sales are generally stronger during the spring, summer and fall months. Our industry generally experiences lower sales and profits during the holiday season as we believe that customers choose to divert discretionary funds towards holiday purchases.

<sup>1</sup> Adjusted EBITDA is a non-GAAP measure that does not have a standardized meaning prescribed by Canadian GAAP and is therefore unlikely to be comparable to similar measures presented by other companies. Refer to *Supplemental Non-GAAP Measures* for further information and a reconciliation of net earnings to Adjusted EBITDA.

## **Related Party Transactions**

As at April 30, 2010, there were four promissory notes outstanding, owing from employees, totaling \$200,000, of which \$40,000 represented accumulated interest. These loans are payable on demand and bear interest at a rate of 5% per annum. The debtors are personally liable for the amounts owed. Coastal did not have any loans outstanding to its Chief Executive Officer, its Chief Financial Officer or any of its directors at the end of the second quarter of 2010.

## **Contingent Liabilities**

Coastal is engaged in certain legal actions in the ordinary course of our business and believes that the ultimate outcome of these actions will not have a material adverse effect on our operating results, liquidity or financial position.

## **Off-Balance Sheet Arrangements**

Coastal does not have any off-balance sheet arrangements as defined by applicable securities regulations in Canada at April 30, 2010 that have, or are reasonably likely to have, a current or future material effect on our results of operations or financial condition.

## **Critical Suppliers**

We currently purchase significant amounts of inventory from a limited number of major suppliers. We believe that alternative suppliers are available should those suppliers refuse or be unable to provide us with products.

## **Disclosure Controls and Procedures**

Disclosure controls and procedures are designed to provide reasonable assurance that all relevant information is gathered and reported to senior management, including the Chief Executive Officer (“CEO”) and Chief Financial Officer (“CFO”), on a timely basis so that appropriate decisions can be made regarding public disclosure.

As of January 31, 2010, an evaluation of the design of Coastal’s disclosure controls and procedures as defined in National Instrument 52-109 was carried out. Based on that evaluation, the CEO and CFO concluded that the design and operation of those disclosure controls and procedures were effective.

## **Internal Controls over Financial Reporting**

Management is responsible for certifying the design of Coastal’s internal control over financial reporting as required by National Instrument 52-109.

Our internal control over financial reporting is intended to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with applicable generally accepted accounting principles. A company’s internal control over financial reporting includes those policies and procedures that pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting

principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management, including the CEO and CFO, carried out an evaluation of the design of our internal controls over financial reporting as at April 30, 2010. Management believes the design, based upon the Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission, to be effective for the nature and size of Coastal's business, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Canadian generally accepted accounting principles.

During the second quarter of 2010, management did not make changes to its system of internal controls that materially affect internal controls over financial reporting.

#### **Supplemental Non-GAAP Measures and Definitions**

Our reorder rate is defined as the percentage of orders in the quarter shipped to customers that we estimate have ordered from us in the past.

We report our results in accordance with Canadian GAAP, however, we present adjusted EBITDA as we believe that our investors may use these figures to make more informed investment decisions about us.

Adjusted EBITDA is a non-GAAP measure that does not have any standardized meaning prescribed by Canadian GAAP and is therefore unlikely to be comparable to similar measures presented by other companies. Adjusted EBITDA should be considered in addition to, and not as a substitute for, net income, cash flows and other measures of financial performance and liquidity reported in accordance with Canadian GAAP.

Adjusted EBITDA is a measure we believe is useful in assessing performance and highlighting trends on an overall basis. Adjusted EBITDA differs from the most comparable GAAP measure, net earnings, primarily because it does not include interest, income taxes, depreciation and amortization, share-based compensation expense and foreign exchange gains and losses.

The following table provides a reconciliation of net earnings to adjusted EBITDA:

(\$000's)	For the three months ended April 30,		For the six months ended April 30,	
	2010	2009	2010	2009
<b>Net earnings</b>	<b>382</b>	<b>528</b>	<b>1,132</b>	<b>1,496</b>
Depreciation and amortization	677	604	1,358	1,218
Interest (income) expense, net	1	(14)	15	(56)
Income tax expense	17	160	48	497
Share-based compensation	130	148	350	296
Foreign exchange (gain) loss	293	(39)	275	(241)
<b>Adjusted EBITDA</b>	<b>1,500</b>	<b>1,387</b>	<b>3,178</b>	<b>3,210</b>

**Additional Information**

Additional information relating to Coastal, including Coastal's most recently filed annual information form, dated January 29, 2010, can be found on SEDAR at [www.sedar.com](http://www.sedar.com).