



K·BRO

Q2, 2017

*CONDENSED
CONSOLIDATED
FINANCIAL
STATEMENTS*

*WE ARE
DEPENDABLE.*

Interim Condensed Consolidated Statements of Financial Position

(unaudited, thousands of Canadian dollars)

	June 30, 2017	December 31, 2016
ASSETS		
Current assets		
Cash and cash equivalents	\$ 5,313	\$ -
Accounts receivable	17,868	18,451
Income tax receivable	472	-
Prepaid expenses and deposits	2,326	1,472
Linen in service	13,236	11,511
	39,215	31,434
Property, plant and equipment (note 4)	133,977	113,258
Intangible assets	2,309	3,141
Goodwill	20,456	20,456
	\$ 195,957	\$ 168,289
LIABILITIES		
Current liabilities		
Accounts payable and accrued liabilities	\$ 14,997	\$ 16,270
Income taxes payable	-	596
Dividends payable to shareholders	958	802
	15,955	17,668
Long-term debt (note 5)	-	25,800
Unamortized lease inducements	2,121	1,863
Deferred income taxes	6,286	6,286
	\$ 24,362	\$ 51,617
SHAREHOLDERS' EQUITY		
Share capital	165,646	109,390
Contributed surplus	2,302	1,944
Retained earnings	3,647	5,338
	\$ 171,595	\$ 116,672
Contingencies and commitments (note 6)	\$ 195,957	\$ 168,289

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

Interim Condensed Consolidated Statements of Earnings & Comprehensive Income

(unaudited, thousands of Canadian dollars, except share and per share amounts)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Revenue	\$ 40,494	\$ 39,469	\$ 79,452	\$ 78,281
Expenses				
Wages and benefits (note 13)	16,571	16,025	32,936	31,784
Linen	4,480	4,407	8,920	8,760
Utilities	2,322	2,319	5,045	4,699
Delivery (note 13)	4,132	3,828	8,308	7,687
Occupancy costs	1,667	1,317	3,124	2,583
Materials and supplies	1,196	937	2,699	2,209
Repairs and maintenance	1,217	1,182	2,591	2,397
Corporate	2,216	1,939	4,372	3,871
	33,801	31,954	67,995	63,990
EBITDA	6,693	7,515	11,457	14,291
Other expenses				
Depreciation of property, plant and equipment (note 4)	2,842	2,246	5,223	4,477
Amortization of intangible assets	404	428	832	934
Finance expense	61	110	246	503
Loss on disposal of property, plant and equipment	36	19	36	19
	3,343	2,803	6,337	5,933
Earnings before income taxes	3,350	4,712	5,120	8,358
Current income tax expense	616	930	824	1,868
Deferred income tax expense	397	398	709	574
Income tax expense	1,013	1,328	1,533	2,442
Net earnings and Comprehensive income	2,337	3,384	3,587	5,916
Net earnings per share:				
Basic	\$ 0.26	\$ 0.43	\$ 0.42	\$ 0.74
Diluted	\$ 0.26	\$ 0.42	\$ 0.42	\$ 0.74
Weighted average number of shares outstanding:				
Basic	9,103,510	7,951,901	8,544,285	7,948,949
Diluted	9,133,276	7,964,583	8,574,839	7,957,525

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

Interim Condensed Consolidated Statements of Changes in Equity

(unaudited, thousands of Canadian dollars)

	Total Share Capital	Contributed surplus	Retained earnings	Total equity
As at January 1, 2017	\$ 109,390	\$ 1,944	\$ 5,338	\$ 116,672
Net earnings	-	-	3,587	3,587
Net proceeds from common shares issued (note 12)	55,006	-	-	55,006
Deferred income tax impact of share issuance	709	-	-	709
Dividends declared (note 7)	-	-	(5,278)	(5,278)
Employee share based compensation expense	-	899	-	899
Shares vested during the period	541	(541)	-	-
As at June 30, 2017	\$ 165,646	\$ 2,302	\$ 3,647	\$ 171,595

	Total Share Capital	Contributed surplus	Retained earnings	Total equity
As at January 1, 2016	\$ 108,079	1,737	3,424	\$ 113,240
Net earnings	-	-	5,916	5,916
Net proceeds from common shares issued	-	-	-	-
Dividends declared (note 7)	-	-	(4,799)	(4,799)
Employee share based compensation expense	-	813	-	813
Shares vested during the period	475	(475)	-	-
As at June 30, 2016	\$ 108,554	\$ 2,075	\$ 4,541	\$ 115,170

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

Interim Condensed Consolidated Statements of Cash Flow

(unaudited, thousands of Canadian dollars)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
OPERATING ACTIVITIES				
Net earnings	\$ 2,337	\$ 3,384	\$ 3,587	\$ 5,916
Depreciation of property, plant and equipment (note 4)	2,842	2,246	5,223	4,477
Amortization of intangible assets	404	428	832	934
Lease inducements, net of amortization	(52)	(37)	258	(76)
Fair value loss on derivative instrument	-	-	-	171
Employee share based compensation expense	494	330	899	813
Loss on disposal of property, plant and equipment	36	19	36	19
Deferred income taxes	397	398	709	574
	6,458	6,768	11,544	12,828
Change in non-cash working capital items (note 8)	(4,161)	(2,625)	(2,947)	(1,960)
Cash provided by operating activities	2,297	4,143	8,597	10,868
FINANCING ACTIVITIES				
Net (repayment) proceeds of revolving debt	(32,363)	1,282	(25,800)	4,903
Net proceeds from issuance of common shares	55,006	-	55,006	-
Dividends paid to shareholders	(2,715)	(2,400)	(5,122)	(4,795)
Cash provided (used in) by financing activities	19,928	(1,118)	24,084	108
INVESTING ACTIVITIES				
Purchase of property, plant and equipment	(16,912)	(3,026)	(27,368)	(10,977)
Proceeds from disposal of property, plant and equipment	-	1	-	1
Cash used in investing activities	(16,912)	(3,025)	(27,368)	(10,976)
Change in cash and cash equivalents during the period	5,313	-	5,313	-
Cash and cash equivalents, beginning of period	-	-	-	-
Cash and cash equivalents, end of period	\$ 5,313	\$ -	\$ 5,313	\$ -
Supplementary cash flow information				
Interest paid	\$ 117	\$ 75	\$ 380	\$ 143
Income taxes paid	\$ 946	\$ 1,020	\$ 1,892	\$ 2,043

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

Notes to the Interim Condensed Consolidated Financial Statements

(unaudited, thousands of Canadian dollars except share and per share amounts, three and six months ended June 30, 2017 and 2016)

K-Bro Linen Inc. (the "Corporation" or "K-Bro") is incorporated in Canada under the Business Corporations Act (Alberta). The Corporation and its wholly owned subsidiaries provide a range of linen services to healthcare institutions, hotels and other commercial accounts that include the processing, management and distribution of general linen and operating room linen. The Corporation provides services from nine processing facilities in eight major cities across Canada from Victoria, British Columbia to Québec City, Québec and two distribution centres in Saskatchewan.

The Corporation's common shares are traded on the Toronto Stock Exchange under the symbol "KBL". The address of the Corporation's registered head office is 14903 – 137 Avenue, Edmonton, Alberta, Canada.

These unaudited interim condensed consolidated financial statements were approved and authorized for issuance by the Board of Directors ("the Board") on August 9, 2017.

1 Basis of Presentation

These unaudited interim condensed consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") and Canadian Generally Accepted Accounting Principles ("GAAP"), as applicable to interim financial reports including IAS 34, *Interim Financial Reporting*, and should be read in conjunction with the annual consolidated audited financial statements for the year ended December 31, 2016 which have been prepared in accordance with IFRS, as issued by the International Accounting Standards Board, and GAAP as issued by CPA Canada. The accounting policies followed in these unaudited interim condensed consolidated financial statements are consistent with those of the previous year, except as described below.

2 Significant accounting policies adopted January 1, 2017

On January 1, 2017 the Corporation adopted the amendments to IAS 7, Statement of Cash Flows, and amendments to IAS 12 Recognition of Deferred Tax Assets for Unrealized Losses. IAS 7 was amended to improve information provided to users of financial statements about an entity's financing activities. IAS 12 was amended to provide further clarity and examples in the practice around the recognition of a deferred tax asset that is related to a debt instrument measured at fair value. Adoption of the amendments did not result in any changes to the presentation or disclosures in the financial statements.

3 New Standards and interpretations not yet adopted

The following standards have been issued but have not yet been applied in preparing the interim condensed consolidated financial statements.

- IFRS 15, Revenue from Contracts with Customers, was issued in May 2014 by the IASB and supersedes IAS 18, "Revenue", IAS 11 "Construction Contracts" and other interpretive guidance associated with revenue recognition. IFRS 15 provides a single model to determine how and when an entity should recognize revenue, as well as requiring entities to provide more informative, relevant disclosures in respect of its revenue recognition criteria. IFRS 15 is to be applied prospectively and is effective for annual periods beginning on or after January 1, 2018, with earlier application permitted. The new standard introduces expanded disclosure requirements. These are expected to change the nature and extent of the Corporation's disclosures. The Corporation is in the process of evaluating the impact that IFRS 15 may have on the financial statements, and has not yet determined to what extent the new standard will affect EBITDA, net earnings and classification of cash flows.

Notes to the Interim Condensed Consolidated Financial Statements

(unaudited, thousands of Canadian dollars except share and per share amounts, three and six months ended June 30, 2017 and 2016)

- IFRS 9, Financial Instruments, was issued in July 2014 by the IASB and supersedes IAS 39, "Financial Instruments: Recognition and Measurement". IFRS 9 addresses the classification, measurement and recognition of financial assets and financial liabilities. IFRS 9 retains but simplifies the mixed measurement model and establishes three primary measurement categories for financial assets: amortized cost, fair value through OCI and fair value through P&L. IFRS 9 is to be applied prospectively and is effective for annual periods beginning on or after January 1, 2018, with earlier application permitted. The Corporation is in the process of evaluating the impact that IFRS 9 may have on the financial statements.
- IFRS 16, Leases, was issued in January 2016 and applies to annual reporting periods beginning on or after January 1, 2019. IFRS 16 specifies how an IFRS reporter will recognize, measure, present and disclose leases. The standard provides a single lessee accounting model, requiring lessees to recognize assets and liabilities for all leases unless the lease term is 12 months or less or the underlying asset has a low value. Lessors continue to classify leases as operating or finance, with IFRS 16's approach to lessor accounting substantially unchanged from its predecessor, IAS 17. The Corporation is in the process of evaluating the impact that IFRS 16 may have on the financial statements. The standard will affect primarily the accounting for the Corporation's operating leases. The Corporation has not yet determined to what extent these commitments will result in the recognition of assets and liabilities for future payments and how this will affect EBITDA, net earnings and classification of cash flows.
- On June 20, 2016 the IASB issued an amendment to IFRS 2 "Share based Payment" addressing three classification and measurement issues. The amendment clarifies the measurement basis for cash-settled, share based payments and the accounting for modifications that change an award from cash-settled to equity settled. It also introduces an exception to the principles in IFRS 2 that will require an award to be treated as if it was wholly-equity settled, where an employer is obliged to withhold an amount for the employee's tax obligation associated with a share based payment and pay that amount to the tax authority. The Corporation is in the process of evaluating the impact that the amendment may have on the financial statements. The amendments are effective for periods beginning on or after January 1, 2018.

Notes to the Interim Condensed Consolidated Financial Statements

(unaudited, thousands of Canadian dollars except share and per share amounts, three and six months ended June 30, 2017 and 2016)

4 Property, plant and equipment

	Land	Buildings	Laundry Equipment ⁽¹⁾	Office Equipment	Delivery Equipment	Computer Equipment	Leasehold Improvements ⁽²⁾	Spare Parts	Total
Year ended, December 31, 2016									
Opening net book amount	\$ 2,454	\$ 17,964	\$ 54,316	\$ 341	\$ 266	\$ 539	\$ 11,834	\$ 427	\$ 88,141
Additions	-	281	21,464	71	60	208	12,242	136	34,462
Disposals	-	-	(107)	-	(3)	-	-	-	(110)
Transfers	-	-	-	-	-	-	-	-	-
Depreciation charge	-	(980)	(6,056)	(108)	(73)	(370)	(1,648)	-	(9,235)
Closing net book amount	\$ 2,454	\$ 17,265	\$ 69,617	\$ 304	\$ 250	\$ 377	\$ 22,428	\$ 563	\$ 113,258
At December 31, 2016									
Cost	\$ 2,454	\$ 19,012	\$ 110,175	\$ 710	\$ 683	\$ 1,279	\$ 32,065	\$ 563	\$ 166,941
Accumulated depreciation	-	(1,747)	(40,558)	(406)	(433)	(902)	(9,637)	-	(53,683)
Net book amount	\$ 2,454	\$ 17,265	\$ 69,617	\$ 304	\$ 250	\$ 377	\$ 22,428	\$ 563	\$ 113,258
Period ended, June 30, 2017									
Opening net book amount	\$ 2,454	\$ 17,265	\$ 69,617	\$ 304	\$ 250	\$ 377	\$ 22,428	\$ 563	\$ 113,258
Additions	-	1	23,064	48	8	291	2,449	117	25,978
Disposals	-	-	(36)	-	-	-	-	-	(36)
Depreciation charge	-	(484)	(3,345)	(54)	(29)	(223)	(1,088)	-	(5,223)
Closing net book amount	\$ 2,454	\$ 16,782	\$ 89,300	\$ 298	\$ 229	\$ 445	\$ 23,789	\$ 680	\$ 133,977
At June 30, 2017									
Cost	\$ 2,454	\$ 19,013	\$ 132,537	\$ 758	\$ 691	\$ 1,571	\$ 34,470	\$ 680	\$ 192,174
Accumulated depreciation	-	(2,231)	(43,237)	(460)	(462)	(1,126)	(10,681)	-	(58,197)
Net book amount	\$ 2,454	\$ 16,782	\$ 89,300	\$ 298	\$ 229	\$ 445	\$ 23,789	\$ 680	\$ 133,977

(1) Included in laundry equipment are assets under development in the amount of \$15,048 (2016 - \$16,536). These assets are not available for service and accordingly are not presently being depreciated.

(2) Included in leasehold improvements are assets under development in the amount of \$0 (2016 - \$11,547). These assets are not available for service and accordingly are not presently being depreciated.

(3) Total property, plant and equipment additions include amounts in accounts payable of \$331 (2016 - \$1,721).

5 Long-term debt

	Prime Rate Loan ⁽¹⁾
At January 1, 2016	\$ 2,349
Net proceeds from debt	23,451
Closing balance at December 31, 2016	\$ 25,800
At January 1, 2017	\$ 25,800
Net proceeds from debt	-
Net repayment of debt	(25,800)
Closing balance at June 30, 2017	\$ -

- (1) Prime rate loan, collateralized by a general security agreement, bear interest at prime plus an interest margin dependent on certain financial ratios, with a monthly repayment of interest only, maturing on July 31, 2020 (December 31, 2016 – July 31, 2020). The additional interest margin can range between 0.0% to 1.25% dependent upon the calculated Debt/EBITDA financial ratio, with a range between 0 to 3.5x. As at June 30, 2017, the combined interest rate was 2.7% (December 31, 2016 – 2.7%).

The Corporation has a revolving credit facility of up to \$85,000 of which \$1,650 is utilized (including letters of credit totaling \$1,650 as at June 30, 2017). Interest payments only are due during the term of the facility.

Drawings under the revolving credit facility are available by way of Bankers' Acceptances, Canadian prime rate loans, letters of credit or standby letters of guarantee. Drawings under the revolving credit facility bear interest at a floating rate, plus an applicable margin based on certain financial performance ratios.

Notes to the Interim Condensed Consolidated Financial Statements

(unaudited, thousands of Canadian dollars except share and per share amounts, three and six months ended June 30, 2017 and 2016)

A general security agreement over all assets, a mortgage against all leasehold interests and real property, insurance policies and an assignment of material agreements have been pledged as collateral.

The carrying value of borrowings approximate their fair value as the debt is based on a floating rate, the interest rate risk has not changed, and the impact of discounting is not significant.

The Corporation has incurred no events of default under the terms of its credit facility agreement.

6 Contingencies and commitments

a) Contingencies – Letters of credit

The Corporation has standby letters of credit issued as part of normal business operations in the amount of \$1,650 (December 31, 2016 – \$1,650) which will remain outstanding for an indefinite period of time.

b) Commitments

(i) Operating leases and utility commitments

Minimum lease payments for operating leases on buildings and equipment and estimated natural gas and electricity commitments for the next five calendar years and thereafter are as follows:

Operating lease commitments

Remainder of 2017	\$	2,643
2018		6,009
2019		5,414
2020		5,087
2021		4,444
Subsequent		32,135
	\$	55,732

Utility commitments

Remainder of 2017	\$	1,563
2018		1,797
2019		1,287
2020		1,288
2021		1,274
Subsequent		-
	\$	7,209

Notes to the Interim Condensed Consolidated Financial Statements

(unaudited, thousands of Canadian dollars except share and per share amounts, three and six months ended June 30, 2017 and 2016)

(ii) Linen purchase commitments

At June 30, 2017, the Corporation was committed to linen expenditure obligations in the amount of \$7,471 (December 31, 2016 – \$6,926) to be incurred within the next year.

(iii) Property, plant and equipment commitments

At June 30, 2017, the Corporation was committed to capital expenditure obligations in the amount of \$13,606 (December 31, 2016 – \$28,897) to be incurred within the next year and \$2,465 (December 31, 2016 – \$8,628) to be incurred in the next two years.

7 Dividends to shareholders

During the three months ended June 30, 2017, the Corporation declared total dividends to shareholders of \$2,871 or \$0.300 per share (June 30, 2016 - \$2,403 or \$0.300 per share). During the Six months ended June 30, 2017, the Corporation declared total dividends to shareholders of \$5,278 or \$0.600 per share (2016 - \$4,799 or \$0.600 per share).

8 Change in non-cash working capital items

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Accounts receivable	\$ 76	\$ (216)	\$ 583	\$ (115)
Linen in service	(762)	(430)	(1,725)	(713)
Prepaid expenses and deposits	(786)	(735)	(854)	(1,564)
Accounts payable and accrued liabilities	(2,358)	(1,153)	117	607
Income taxes payable / Receivable	(331)	(91)	(1,068)	(175)
	\$ (4,161)	\$ (2,625)	\$ (2,947)	\$ (1,960)

9 Fair value of financial instruments

The Corporation's financial instruments at June 30, 2017 consist of cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities, dividends payable to shareholders, and long term debt. The carrying value of accounts receivable, accounts payable and accrued liabilities, and dividends payable to shareholders approximate fair value due to the immediate or short-term maturity of these financial instruments. The fair value of the Corporation's interest-bearing debt approximates the respective carrying amount due to the floating rate nature of the debt, at June 30, 2017 the balance is nil.

10 Related party transactions

The Corporation incurred expenses in the normal course of business for advisory consulting services provided by a Director. The amounts charged are recorded at their exchange amounts and are subject to normal trade terms. For the three months ended June 30, 2017, the Corporation incurred such fees totaling \$35 (2016– \$35). For the six months ended June 30, 2017, the Corporation incurred such fees totaling \$69 (2016– \$69).

Notes to the Interim Condensed Consolidated Financial Statements

(unaudited, thousands of Canadian dollars except share and per share amounts, three and six months ended June 30, 2017 and 2016)

11 Segmented information

The Corporation provides laundry and linen services to the healthcare and hospitality sectors through nine operating divisions located in Vancouver, Victoria, Calgary, Edmonton, Regina, Toronto, Montréal, and Québec City. Management has assessed that the services offered and the economic characteristics associated with these divisions are similar, and therefore they have been aggregated into one reportable segment which operates exclusively in Canada.

The aggregation assessment requires significant judgment by management. Economic indicators used by management to assess the economic characteristics are the gross margin and the growth rate of each division.

In Edmonton, the Corporation is the significant supplier of laundry and linen services to the entity which manages all major healthcare facilities in the region and this contract expires on March 31, 2023. In Calgary, the major customer is contractually committed to February 28, 2018, in Vancouver the major customer is contractually committed to March 1, 2027, and in Saskatchewan the major customer is contractually committed to June 1, 2025. For the six months ended June 30, 2017, from these four major customers the Corporation has recorded revenue of \$45,223 (2016 – \$44,498), representing 56.9% (2016 – 56.8%) of total revenue.

	Three Months Ended June 30, 2017		Three Months Ended June 30, 2016	
Healthcare	\$ 28,499	70.4%	\$ 27,553	69.8%
Hospitality	11,995	29.6%	11,916	30.2%
	\$ 40,494	100.0%	\$ 39,469	100.0%

	Six Months Ended June 30, 2017		Six Months Ended June 30, 2016	
Healthcare	\$ 56,552	71.2%	\$ 55,677	71.1%
Hospitality	22,900	28.8%	22,604	28.9%
	\$ 79,452	100.0%	\$ 78,281	100.0%

Notes to the Interim Condensed Consolidated Financial Statements

(unaudited, thousands of Canadian dollars except share and per share amounts, three and six months ended June 30, 2017 and 2016)

12 Share Capital

a) Authorized

The Corporation is authorized to issue an unlimited number of common shares and such number of shares of one class designated as preferred shares which number shall not exceed 1/3 of the common shares issued and outstanding from time to time.

b) Issued

	2017	2016
Balance, beginning of year	8,023,480	7,985,713
Common shares issued under LTI	42,422	37,767
Common share issuance under equity offering	1,518,000	-
As at June 30, 2017	9,583,902	8,023,480
Unvested common shares held in trust for LTI	73,178	66,052

	2017
Proceeds from share issuance	\$ 57,684
Underwriter fee	(2,307)
Costs associated with share issuance	(371)
Net proceeds from share issuance	55,006
Deferred income tax impact of share issuance	709
Total impact to share capital	\$ 55,715

On April 25, 2017 the Corporation closed a bought deal offering of 1,518,000 common shares at \$38.00/share. The net proceeds of the offering after deducting expenses of the offering and the underwriter's fee were \$55.0 million. The net proceeds of the offering were used to reduce the revolving debt to nil, and to fund the build out of the Corporation's state-of-the-art facilities in Toronto and Vancouver, and for general corporate purposes.

13 Statements of Earnings & Comprehensive Income - reclassification

The Corporation has made a reclassification that affects some of the costs related to wages and benefits, and delivery costs. The reason is to give a true and fair view based off the intended function of the delivery costs, which have been emphasized with the strategic growth of the Corporation. In order to maintain comparability, the financial statements for 2016 and 2017 have been adjusted. The reclassification does not affect EBITDA or net earnings.

Notes to the Interim Condensed Consolidated Financial Statements

(unaudited, thousands of Canadian dollars except share and per share amounts, three and six months ended June 30, 2017 and 2016)

	Three Months Ended June 30, 2017			Three Months Ended June 30, 2016		
	Before Reclassification	Reclassification	After Reclassification	Before Reclassification	Reclassification	After Reclassification
Wages and benefits	\$ 18,107	\$ (1,536)	\$ 16,571	\$ 17,777	\$ (1,752)	\$ 16,025
Delivery	2,596	1,536	4,132	2,076	1,752	3,828
Total	\$ 20,703	\$ -	\$ 20,703	\$ 19,853	\$ -	\$ 19,853

	Six Months Ended June 30, 2017			Six Months Ended June 30, 2016		
	Before Reclassification	Reclassification	After Reclassification	Before Reclassification	Reclassification	After Reclassification
Wages and benefits	\$ 36,069	\$ (3,133)	\$ 32,936	\$ 35,314	\$ (3,530)	\$ 31,784
Delivery	5,175	3,133	8,308	4,157	3,530	7,687
Total	\$ 41,244	\$ -	\$ 41,244	\$ 39,471	\$ -	\$ 39,471

14 Subsequent events

a) Dividends

On July 14, 2017, the Board declared an eligible dividend of \$0.1000 per common share of the Corporation payable on August 15, 2017 to shareholders of record July 31, 2017.

On August 9, 2017, the Board declared an eligible dividend of \$0.1000 per common share of the Corporation payable on September 15, 2017 to shareholders of record August 31, 2017.