K·BRO

Q1, 2016
Condensed
Consolidated
Financial
Statements

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Interim Condensed Consolidated Statements of Financial Position

(unaudited, thousands of Canadian dollars)

	March 31, 2016	December 31, 2015
ASSETS		
Current assets		
Accounts receivable	$ 17,054	$ 17,155
Prepaid expenses and deposits	1,890	1,061
Linen in service	11,562	11,279
	30,506	29,495
Property, plant and equipment (note 4)	91,429	88,141
Intangible assets	4,425	4,931
Goodwill	20,456	20,456
	$ 146,816	$ 143,023
LIABILITIES		
Current liabilities		
Accounts payable and accrued liabilities (note 9)	$ 19,334	$ 19,835
Income taxes payable	107	191
Dividends payable to shareholders	799	799
	20,240	20,825
Long-term debt (note 5)	5,970	2,349
Unamortized lease inducements	658	696
Deferred income taxes	6,089	5,913
	$ 32,957	$ 29,783
SHAREHOLDERS' EQUITY		
Share capital	108,079	108,079
Contributed surplus	2,220	1,737
Retained earnings	3,560	3,424
	$ 113,859	$ 113,240
Contingencies and commitments (note 6)		
	$ 146,816	$ 143,023

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 March 31, 2016	2015
Revenue	**$ 38,812**	$ 33,820
Expenses		
Wages and benefits	**17,537**	15,074
Linen	**4,353**	3,648
Utilities	**2,380**	2,125
Delivery	**2,081**	1,515
Occupancy costs	**1,266**	1,234
Materials and supplies	**1,272**	1,030
Repairs and maintenance	**1,215**	1,098
Corporate	**1,932**	1,792
	32,036	27,516
EBITDA	**6,776**	6,304
Other expenses		
Depreciation of property, plant and equipment (note 4)	**2,231**	1,688
Amortization of intangible assets	**506**	490
Finance expense (recovery) (note 9)	**393**	(98)
	3,130	2,080
Earnings before income taxes	**3,646**	4,224
Current income tax expense	**938**	1,089
Deferred income tax expense	**176**	116
Income tax expense	**1,114**	1,205
Net earnings and Comprehensive income	**2,532**	3,019
Net earnings per share:		
Basic	**$ 0.32**	$0.38
Diluted	**$ 0.32**	$0.38
Weighted average number of shares outstanding:		
Basic	**7,945,997**	7,914,367
Diluted	**7,964,604**	7,942,293

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, 2016	$ 108,079	$ 1,737	$ 3,424	$ 113,240
Net earnings	-	-	2,532	2,532
Dividends declared (note 7)	-	-	(2,396)	(2,396)
Employee share based compensation expense	-	483	-	483
As at March 31, 2016	$ 108,079	$ 2,220	$ 3,560	$ 113,859

	Total Share Capital	Contributed surplus	Retained earnings (deficit)	Total equity
As at January 1, 2015	$ 106,870	1,642	926	$ 109,438
Net earnings	-	-	3,019	3,019
Dividends declared (note 7)	-	-	(2,388)	(2,388)
Employee share based compensation expense	-	379	-	379
As at March 31, 2015	$ 106,870	2,021	1,557	$ 110,448

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 March 31, 2016	2015
OPERATING ACTIVITIES		
Net earnings	$ 2,532	$ 3,019
Depreciation of property, plant and equipment (note 4)	2,231	1,688
Amortization of intangible assets	506	490
Lease inducements, net of amortization	(38)	(39)
Fair value loss on derivative instrument (note 9)	171	-
Employee share based compensation expense	483	379
Deferred income taxes	176	116
	6,061	5,653
Change in non-cash working capital items (note 8)	665	(1,439)
Cash provided by operating activities	6,726	4,214
FINANCING ACTIVITIES		
Net proceeds of revolving credit facility	3,621	-
Dividends paid to shareholders (note 7)	(2,396)	(2,388)
Cash provided (used in) by financing activities	1,225	(2,388)
INVESTING ACTIVITIES		
Purchase of property, plant and equipment (note 4)	(7,951)	(3,808)
Cash used in investing activities	(7,951)	(3,808)
Change in cash and cash equivalents during the period	-	(1,982)
Cash and cash equivalents, beginning of period	-	13,744
Cash and cash equivalents, end of period	$ -	$ 11,762
Supplementary cash flow information		
Interest paid	$ 68	$ -
Income taxes paid	$ 1,022	$ 908

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 months ended March 31, 2016 and 2015)

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 May 11, 2016.

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, 2015 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, 2016

On January 1, 2016, the Corporation adopted the Amendments to IAS 1, Presentation of Financial Statements. IAS 1 was amended to clarify guidance on materiality and aggregation, the presentation of subtotals, the structure of financial statements and the disclosure of accounting policies. 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 Corporation is in the process of evaluating the impact that IFRS 15 may have on the financial statements.

- 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.

(unaudited, thousands of Canadian dollars except share and per share amounts, three months ended March 31, 2016 and 2015)

- 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.

There are no other IFRSs or IFRIC interpretations that are not yet effective that would be expected to have a material impact on the Corporation.

4 Property, plant and equipment

	Land	Buildings	Laundry Equipment[1]	Office Equipment	Delivery Equipment	Computer Equipment	Leasehold Improvements	Spare Parts	Total
Year ended, December 31, 2015									
Opening net book amount	$ 2,425	$ 6,676	$ 44,257	$ 274	$ 417	$ 324	$ 11,188	$ 758	$ 66,319
Additions	29	11,638	17,161	164	15	509	74	17	29,607
Disposals	-	-	(138)	-	(74)	-	-	-	(212)
Transfers	-	-	(1,857)	-	-	-	2,205	(348)	-
Depreciation charge	-	(350)	(5,107)	(97)	(92)	(294)	(1,633)	-	(7,573)
Closing net book amount	$ 2,454	$ 17,964	$ 54,316	$ 341	$ 266	$ 539	$ 11,834	$ 427	$ 88,141
At December 31, 2015									
Cost	$ 2,454	$ 18,730	$ 88,858	$ 640	$ 641	$ 1,071	$ 19,823	$ 427	$ 132,644
Accumulated depreciation	-	(766)	(34,542)	(299)	(375)	(532)	(7,989)	-	(44,503)
Net book amount	$ 2,454	$ 17,964	$ 54,316	$ 341	$ 266	$ 539	$ 11,834	$ 427	$ 88,141
Period ended, March 31, 2016									
Opening net book amount	$ 2,454	$ 17,964	$ 54,316	$ 341	$ 266	$ 539	$ 11,834	$ 427	$ 88,141
Additions	-	110	5,241	55	-	94	-	19	5,519
Disposals	-	-	-	-	-	-	-	-	-
Transfers	-	-	-	-	-	-	-	-	-
Depreciation charge	-	(242)	(1,447)	(24)	(20)	(89)	(409)	-	(2,231)
Closing net book amount	$ 2,454	$ 17,832	$ 58,110	$ 372	$ 246	$ 544	$ 11,425	$ 446	$ 91,429
At March 31, 2016									
Cost	$ 2,454	$ 18,840	$ 94,099	$ 696	$ 641	$ 1,165	$ 19,823	$ 446	$ 138,164
Accumulated depreciation	-	(1,008)	(35,989)	(324)	(395)	(621)	(8,398)	-	(46,735)
Net book amount	$ 2,454	$ 17,832	$ 58,110	$ 372	$ 246	$ 544	$ 11,425	$ 446	$ 91,429

[1] Included in laundry equipment are assets under development in the amount of $4,946 (2015 - $65). These assets are not available for service and accordingly are not presently being depreciated.

(unaudited, thousands of Canadian dollars except share and per share amounts,
three months ended March 31, 2016 and 2015)

5 Long-term debt

	Prime Rate Loan[(1)]
At January 1, 2015	$ -
Net proceeds from debt	2,349
Closing balance at December 31, 2015	$ 2,349
At January 1, 2016	**$ 2,349**
Net proceeds from debt	**3,621**
Repayment of debt	**-**
Closing balance at March 31, 2016	**$ 5,970**

(1) Prime rate loan, collateralized by a general security agreement, bear interest at prime plus 0.0% to 1.0% depending on certain financial ratios, monthly repayment of interest only, maturing on July 31, 2018. As at March 31, 2016, the combined interest rate was 2.7%.

The Corporation has a revolving credit facility of up to $50,000 of which $7,620 is utilized (including letters of credit totaling $1,650 as at March 31, 2016). The agreement is a committed facility maturing on July 31, 2018. 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.

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, 2015 – $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:

(unaudited, thousands of Canadian dollars except share and per share amounts,
three months ended March 31, 2016 and 2015)

Operating lease commitments [1.]

Remainder of 2016	$	3,656
2017		4,541
2018		3,658
2019		2,940
2020		2,705
Subsequent		18,140
	$	35,640

1. The commitments reflected above include the commitments for the new Toronto facility lease that was signed on April 25, 2016.

Utility commitments

Remainder of 2016	$	1,393
2017		1,230
2018		828
2019		-
2020		-
Subsequent		-
	$	3,451

(ii) Linen purchase commitments

At March 31, 2016, the Corporation was committed to linen expenditure obligations in the amount of $7,345 (December 31, 2015 – $5,254) to be incurred within the next year.

(iii) Property, plant and equipment commitments

At March 31, 2016, the Corporation was committed to capital expenditure obligations in the amount of $20,086 (December 31, 2015 – $3,675) to be incurred within the next year.

7 Dividends to shareholders

During the three months ended March 31, 2016, the Corporation declared total dividends to shareholders of $2,396 or $0.300 per share (March 31, 2015 - $2,388 or $0.300 per share).

(unaudited, thousands of Canadian dollars except share and per share amounts,
three months ended March 31, 2016 and 2015)

8 Net change in non-cash working capital items

	Three months ended March 31, 2016	2015
Accounts receivable	$ 101	$ (527)
Linen in service	(283)	(284)
Prepaid expenses and deposits	(829)	(132)
Accounts payable and accrued liabilities	1,760	(677)
Income taxes payable	(84)	181
	$ 665	$ (1,439)

9 Fair value of financial instruments

The Corporation's financial instruments at March 31, 2016 consist of cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities, dividends payable to shareholders, long term debt, and derivatives. 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. Derivatives are initially recognized at fair value on the date a derivative contract is entered into and are subsequently remeasured to their fair value at the end of each reporting period and included as part of the profit and loss.

During the most recent quarter, the Corporation entered into a derivative contract used to mitigate the overall risk and exposure for future cash settlements related to the current commitments to purchase plant equipment denominated in foreign currency. The derivative financial instrument has been included as part of, accounts payable and accrued liabilities, and is expected to settle by year end. The fair value loss on the derivative instrument during the most recent quarter was $171 and has been presented in the statement of earnings within "finance expense (recovery)".

The derivative contract is included in Level 2 of the fair value hierarchy as it is valued using an option valuation model. The main inputs to this model are USD and CAD discount curves, USD and CAD volatility and USD and CAD spot rates. These inputs are all obtained from observable market data.

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 March 31, 2016, the Corporation incurred such fees totaling $35 (2015 – $35).

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.

(unaudited, thousands of Canadian dollars except share and per share amounts,
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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 three months ended March 31, 2016, the Corporation has recorded revenue of $22,158 (2015 – $17,903) from these four major customers, representing 57.1% (2015 – 52.9%) of total revenue.

	Three Months Ended March 31, 2016			Three Months Ended March 31, 2015		
Healthcare	**$**	**28,124**	**72.5%**	$	23,857	70.5%
Hospitality		**10,688**	**27.5%**		9,963	29.5%
	$	**38,812**	**100.0%**	$	33,820	100%

12 Subsequent events

a) Dividends

On April 15, 2016, the Board declared an eligible dividend of $0.1000 per common share of the Corporation payable on May 13, 2016 to shareholders of record April 30, 2016.

On May 11, 2016, the Board declared an eligible dividend of $0.1000 per common share of the Corporation payable on June 15, 2016 to shareholders of record May 31, 2016.

b) Approval of Long-term Incentive Compensation

On April 18, 2016, the Board of Directors approved the recommendations of the Compensation, Nominating and Governance Committee with respect to long-term incentive compensation for the senior management of the Corporation. Total compensation to be awarded to employees is $1,575 which will be satisfied through the issuance of treasury shares based on the five-day volume weighted average price for the period ending May 13, 2016.