



Management's
Discussion
& Analysis
Year Ended
December 31,
2012

dependable.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following Management's Discussion and Analysis ("MD&A") is supplemental to, and should be read in conjunction with, the audited Consolidated Financial Statements of K-Bro Linen Inc. ("the Corporation") for the years ended December 31, 2012 and 2011, as well as the unaudited interim condensed Consolidated Financial Statements for the periods ended March 31, 2012, June 30, 2012 and September 30, 2012. The Corporation and its wholly-owned subsidiaries, including K-Bro Linen Systems Inc., are collectively referred to as "K-Bro" in this MD&A.

Management is responsible for the information contained in this MD&A and its consistency with information presented to the Audit Committee and Board of Directors. All information in this document has been reviewed and approved by the Audit Committee and Board of Directors. This review was performed by management with information available as of March 13, 2013.

In the interest of providing current Shareholders of K-Bro Linen Inc. and potential investors with information regarding current results and future prospects, our public communications often include written or verbal forward-looking statements. Forward-looking statements are disclosures regarding possible events, conditions, or results of operations that are based on assumptions about future economic conditions and courses of action, and include future-oriented financial information.

This MD&A contains forward-looking information that represents internal expectations, estimates or beliefs concerning, among other things, future activities or future operating results and various components thereof. The use of any of the words "anticipate", "continue", "expect", "may", "will", "project", "should", "believe", and similar expressions suggesting future outcomes or events are intended to identify forward-looking information. Statements regarding such forward-looking information reflect management's current beliefs and are based on information currently available to management.

These statements are not guarantees of future performance and are based on management's estimates and assumptions that are subject to risks and uncertainties, which could cause K-Bro's actual performance and financial results in future periods to differ materially from the forward-looking information contained in this MD&A. These risks and uncertainties include, among other things: (i) risks associated with acquisitions, including the possibility of undisclosed material liabilities; (ii) K-Bro's competitive environment; (iii) utility and labour costs; (iv) K-Bro's dependence on long-term contracts with the associated renewal risk; (v) increased capital expenditure requirements; (vi) reliance on key personnel; (vii) changing trends in government outsourcing; and (viii) the availability of future financing. Material factors or assumptions that were applied in drawing a conclusion or making an estimate set out in the forward-looking information include: (i) volumes and pricing assumptions; (ii) expected impact of labour cost initiatives; and (iii) the level of capital expenditures. Although the forward-looking information contained in this MD&A is based upon what management believes are reasonable assumptions, there can be no assurance that actual results will be consistent with these forward-looking statements. Certain statements regarding forward-looking information included in this MD&A may be considered "financial outlook" for purposes of applicable securities laws, and such financial outlook may not be appropriate for purposes other than this MD&A.

All forward-looking information in this MD&A is qualified by these cautionary statements. Forward-looking information in this MD&A is presented only as of the date made. Except as required by law, K-Bro does not undertake any obligation to publicly revise these forward-looking statements to reflect subsequent events or circumstances.

This MD&A also makes reference to certain measures in this document that do not have any standardized meaning as prescribed by IFRS or previous Canadian GAAP and, therefore, are considered additional GAAP measures. These measures may not be comparable to similar measures presented by other issuers. Please see "*Terminology*" for further discussion.

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INTRODUCTION

Core Business

K-Bro is the largest owner and operator of laundry and linen processing facilities in Canada. K-Bro provides a comprehensive range of general linen and operating room linen processing, management and distribution services to healthcare institutions, hotels and other commercial accounts. K-Bro currently has eight processing facilities in seven Canadian cities including Victoria, Vancouver, Calgary, Edmonton, Toronto, Montréal and Québec City.

Industry and Market

K-Bro provides laundry and linen services to Canadian healthcare, hospitality and other commercial customers. Typical services offered by K-Bro include the processing, management and distribution of general and operating room linens, including sheets, blankets, towels, surgical gowns and drapes and other linen. Other types of processors in K-Bro's industry in Canada include independent privately-owned facilities (i.e. typically small, single facility companies), public sector central laundries and public and private sector on-premise laundries (known as "OPLs"). Participants in other sectors of the laundry and linen services industry, such as uniform rental companies (which own and launder uniforms worn by their customers' employees) and facilities management companies (which manage public sector central laundries and OPLs), typically do not offer services that significantly overlap with those offered by K-Bro.

Our partnerships with healthcare institutions and hospitality clients across Canada demonstrate K-Bro's commitment to build relationships that foster continuous improvement, provide flexibility to adjust to changing circumstances as required and which incorporate incentives, penalties and sharing of risks and rewards as circumstances warrant. As a result, clients across the country have entered into long-term relationships with us, with most having renewed their contracts several times.

In this competitive industry, K-Bro is distinctive in Canada in its ability to deliver products and services that provide value to our customers. Management believes that the healthcare and hospitality sectors of the laundry and linen services industry represent a stable base of annual recurring business with opportunities for growth as additional healthcare beds and funds are made available to meet the needs of an aging demographic.

Industry Characteristics and Trends

Management believes that the industry in which K-Bro operates exhibits the following characteristics and trends:

Stable Industry with Moderate Cyclicity – As evidenced by the stability in the number of approved hospital beds in the healthcare system and hotel rooms in the hospitality industry. Service relationships are generally formalized through contracts in the healthcare sector that are typically long term (from seven to ten years), while contracts in the hospitality sector usually range from two to five years.

Outsourcing and Privatization – Healthcare institutions and regional authorities are facing funding pressures and must continually evaluate the allocation of scarce resources. Consequently there are often advantages to healthcare institutions in outsourcing the processing of healthcare linen to private sector laundry companies such as K-Bro because of the economies of scale and significant management expertise that can be provided on a more comprehensive and cost-effective basis than customers can achieve in operating their own laundry facilities.

Fragmentation – Most Canadian cities have at least one and sometimes several private sector competitors operating in the healthcare and hospitality sectors of the laundry and linen services industry. Management believes that the presence of these operators provides consolidation opportunities for larger industry participants with the financial means to complete acquisitions.

Customers and Product Mix

K-Bro's customers include some of the largest healthcare institutions and hospitality providers in Canada. Healthcare customers include acute care hospitals and long-term care facilities. Most of K-Bro's hospitality customers (typically >250 rooms) generate between 500,000 and 3 million pounds of linen per year. Most healthcare customers generate between 500,000 pounds of linen per year for a hospital and up to 30 million pounds of linen per year for a healthcare region.

STRATEGY

K-Bro maintains the following three-part strategic focus:

Secure and Maintain Long-Term Contracts with Large Healthcare and Hospitality Customers – K-Bro's core service is providing high quality laundry and linen services at competitive prices to large healthcare and hospitality customers under long-term contracts. K-Bro's contracts in the healthcare sector typically range from seven to ten years in length. Contracts in the hospitality sector typically range from two to five years.

Extend Core Services To New Markets – Management has demonstrated its ability to successfully expand K-Bro's business into new markets from its established bases. Since 2005, K-Bro has entered four new geographic markets across Canada. These new markets have contributed significantly to K-Bro's growth. Management believes that new outsourcing opportunities will continue to arise in the near to medium-term and that K-Bro is well-positioned for continued growth, particularly as healthcare and hospitality institutions continue to increase their focus on core services and confront pressures for capital and cost savings.

Management may in the future expand its core services to new markets either through acquisitions or by establishing new facilities. Its choice of areas for expansion will depend on the availability of suitable acquisition candidates, the volume of healthcare and hospitality linen to be processed and the policies of applicable governments.

Introduce Related Services – In addition to focusing on its core services, the Corporation also attempts to capitalize on attractive business opportunities by introducing closely-related services that enable it to provide more complete solutions to K-Bro's healthcare and hospitality customers. These related service offerings include K-Bro Operating Room (“KOR”) services and on-site services. For three major hospitals in Toronto, K-Bro performs the sterilization of operating room linen packs.

FOURTH QUARTER OVERVIEW

In the fourth quarter of 2012, revenue was \$31.6 million which was 8.3% higher than the \$29.2 million generated in the comparative quarter of 2011. This year-over-year increase was due to a combination of the new volumes from the Saskatoon Health Region and organic growth from new volume and price increases at existing customers across the remainder of the plants. EBITDA increased from \$4.6 million in Q4, 2011 to \$5.8 million in Q4, 2012, as the result of the new volume from the Saskatoon Health Region coupled with organic growth and favorable variances in utilities.

SELECTED ANNUAL FINANCIAL INFORMATION

<i>(thousands, except share and per share amounts)</i>	Year Ended December 31,		
	2012	2011	2010
Revenue	\$ 126,290	\$ 116,859	\$ 104,051
Earnings before income taxes	15,324	10,888	7,116
Net earnings	11,149	7,928	6,953
<i>Net earnings per share:</i>			
Basic	\$ 1.60	\$ 1.15	\$ 1.01
Diluted	\$ 1.59	\$ 1.14	\$ 0.99
Total assets	94,800	91,425	90,679
Long-term debt	5,818	6,095	10,763
Dividends declared to Shareholders	7,977	7,706	7,706
Dividends declared to Shareholders per share	\$ 1.13	\$ 1.10	\$ 1.10
<i>Number of shares outstanding:</i>			
Basic	6,981,432	6,918,955	6,905,369
Diluted	6,993,561	6,980,489	6,992,400

SUMMARY OF 2012 RESULTS AND KEY EVENTS

Financial Growth

K-Bro delivered strong financial results in 2012 driven by the operating results from all eight of its processing plants. Net earnings were \$11.1 million or \$1.60 per share (basic). Cash flow from operating activities was \$20.8 million and distributable cash flow was \$19.1 million. Revenue increased in fiscal 2012 to \$126.3 million or by 8.0% compared to 2011. This revenue growth in the year is due to the acquisition of the new plant in Montréal (increases in Q1 and Q2, 2012, acquired on July 1, 2011), increased volumes arising from the Saskatoon Health Region contract and organic volume and price growth in the remainder of the plants. EBITDA (see *Terminology*) increased in the year to \$24.5 million from \$19.9 million in 2011, which is an increase of 21.8%. The EBITDA margin increased to 19.4% in 2012 compared 17.1% in 2011. The increase in margin is driven by the new volume from the Saskatoon Health Region contract coupled with favorable variances in utilities and organic growth of the plants.

Saskatoon Health Region Contract

In January 2012, K-Bro earned the healthcare linen business of Saskatoon Health Region (the "Region") under a one-year contract, while the Region explores its options for longer-term processing arrangements. Under the terms of the original agreement, K-Bro was awarded a portion of the total volume processed with the remainder being processed internally. The agreement was subsequently extended to May 2013 and K-Bro was awarded the remaining volume once processed internally by the Region.

Alberta Health Services Contract

In May 2012, K-Bro was awarded a ten-year contract with Alberta Health Services ("AHS") for laundry and linen services for the Edmonton and surrounding areas. The contract encompasses a comprehensive linen supply and service program covering general, operating room and specialty linens as well as on-site services at certain facilities. K-Bro has commenced planning and construction of a new Edmonton processing plant with expected commissioning during Q2 and Q3, 2013. Services under the terms and conditions of this contract will commence on April 1, 2013. The contract is renewable for an additional five years at AHS' option.

The new ten-year contract also includes certain price concessions as compared to the existing services agreement that concludes in fiscal 2013. Management believes that efficiencies arising from a newly designed Edmonton facility will directly offset the price concessions made under the terms of the new AHS contract, as well as additional carrying costs of any associated debt. The Corporation intends to finance the construction through its existing credit facilities. It is anticipated that the new facility will be fully operational by Q3, 2013.

Effects of Economic Uncertainty

A significant degree of uncertainty exists with respect to the development of a new Edmonton facility and the resultant decommissioning of the old plant. Management estimates that the costs to commission a new leased facility are expected to be approximately \$25 million for new efficiency enhancing equipment, leaseholds and conversion costs, with immediate returns anticipated from reduced labour, lower energy consumption and other work-flow improvements. Costs associated with the new facility have been incurred since Q2, 2012, with over half of the total expenditure forecast to be spent in Q1, 2013. As at December 31, 2012, K-Bro has incurred \$5.4 million of the total expected capital cost.

K-Bro feels that it is positioned to withstand market volatility and uncertainty given that:

- Approximately 68.6% of its revenues in the year were from large publicly funded healthcare customers which are geographically diversified across multiple provinces;
- K-Bro routinely enters into natural gas, electricity, and textile supply contracts and typically tries to align terms with existing linen processing contract terms;
- At December 31, 2012, K-Bro had unutilized borrowing capacity of \$33.8 million or 84.5% of the revolving credit line available; and,
- K-Bro's prudent approach to managing capital has added cash flow and liquidity to the Corporation, thereby improving its ability to withstand the turmoil in the national and global capital markets.

KEY PERFORMANCE DRIVERS

K-Bro's key performance drivers focus on growth, profitability, stability and cost containment in order to maintain dividends and maximize Shareholder value. The following outlines our results on a period-to-period comparative basis in each of these areas:

<i>(thousands, except percentages)</i>		Q4, 2012	Q4, 2011	YTD 2012	YTD 2011
Category	Indicator				
Growth	EBITDA ⁽¹⁾	26.8%	13.6%	21.8%	18.2%
	Revenue	8.3%	9.1%	8.0%	12.3%
	Distributable cash flow	14.9%	0.9%	13.8%	12.0%
Profitability	EBITDA ⁽¹⁾	\$ 5,777	\$ 4,556	\$ 24,517	\$ 19,946
	EBITDA margin	18.3%	15.6%	19.4%	17.1%
	Net earnings	\$ 2,758	\$ 1,643	\$ 11,149	\$ 7,928
Stability	Debt to total capitalization	7.9%	8.8%	7.9%	8.8%
	Unutilized line of credit	\$ 33,782	\$ 33,655	\$ 33,782	\$ 33,655
	Payout ratio	45.8%	50.2%	41.8%	45.9%
	Dividends declared per share	\$ 0.287	\$ 0.275	\$ 1.133	\$ 1.100
Cost containment	Wages and benefits	46.1%	46.7%	46.1%	46.4%
	Utilities	6.9%	7.2%	6.6%	7.4%
	Operating expenses	81.7%	84.4%	80.6%	82.9%

⁽¹⁾ EBITDA is defined as revenue less operating expenses (which equates to net earnings before income tax, gain or loss on disposals, financial charges and depreciation and amortization). See *Terminology*.

OUTLOOK

K-Bro's focus is on profitable growth in the years to come as we execute our strategy of expanding geographically and adding new services for our customers. K-Bro is committed to building value for our shareholders, our customers and our employees.

In 2013 K-Bro will commission a new Edmonton facility in a new location and also decommission the former plant site. As a result of the development of the new facility Management expects efficiency and productivity of its Edmonton operations to decline in Q2 and Q3, 2013, and improve once the transition between the two sites is complete. Management believes that EBITDA margin will be negatively impacted during the transition period by up to 3% on a consolidated basis.

K-Bro also has several proposals pending and has entered into discussions with potential new customers. In addition, K-Bro continues to seek potential acquisition candidates. Neither the timing nor the degree of likelihood of success of any of these proposals or acquisitions can be stated with any degree of accuracy.

RESULTS OF OPERATIONS

Overall Performance

For the three month period ended December 31, 2012, K-Bro's revenue was \$31.6 million, compared to \$29.2 million in the comparable prior year period. This growth in the growth is due to the volumes arising from the Saskatoon Health Region contract and organic volume and price growth in the remainder of the plants. EBITDA increased in the current quarter by \$1.2 million (26.8%) over the fourth quarter of 2011 mainly due to increased volumes and the semi-fixed nature of certain costs.

Quarterly Financial Information

The following table provides certain selected consolidated financial and operating data prepared by K-Bro management for the preceding eight quarters:

<i>(thousands, except per share amounts and percentages)</i>	2012				2011			
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1
Healthcare revenue	22,222	21,418	21,713	21,257	20,432	19,730	20,042	19,941
Hospitality revenue	9,364	11,595	9,813	8,908	8,726	11,414	8,829	7,745
Total revenue	31,586	33,013	31,526	30,165	29,158	31,144	28,871	27,686
Operating expenses	25,809	26,274	25,122	24,568	24,602	25,098	24,006	23,207
EBITDA ⁽¹⁾	5,777	6,739	6,404	5,597	4,556	6,046	4,865	4,479
EBITDA as a % of revenue	18.3%	20.4%	20.3%	18.6%	15.6%	19.4%	16.9%	16.2%
Depreciation and amortization	1,924	2,283	2,263	2,207	2,082	2,232	2,036	2,216
Financial charges	(66)	272	67	84	93	131	84	104
Loss (gain) on disposal of equipment	39	1	(10)	129	50	4	20	6
Earnings before income taxes	3,880	4,183	4,084	3,177	2,331	3,679	2,725	2,153
Income tax expense	1,122	1,224	1,121	708	688	953	722	597
Net earnings	2,758	2,959	2,963	2,469	1,643	2,726	2,003	1,556
Net earnings as a % of revenue	8.7%	9.0%	9.4%	8.2%	5.6%	8.8%	6.9%	5.6%
Basic earnings per share	0.393	0.422	0.424	0.356	0.237	0.393	0.290	0.226
Diluted earnings per share	0.393	0.420	0.423	0.353	0.235	0.390	0.288	0.223
Total assets	94,800	94,166	90,505	92,529	91,425	90,350	93,148	90,473
Total long-term financial liabilities	11,023	12,830	11,963	8,795	11,203	12,096	17,554	13,079
Funds provided by operations	7,928	6,223	(110)	6,768	3,929	8,217	2,577	4,137
Long-term debt	5,818	7,787	7,113	4,000	6,095	7,224	13,007	8,838
Dividends declared per share	0.287	0.288	0.283	0.275	0.275	0.275	0.275	0.275

⁽¹⁾ EBITDA is defined as revenue less operating expenses (which equates to net earnings before income tax, gain or loss on disposals, financial charges and depreciation amortization). See *Terminology*.

Revenue, Earnings and EBITDA

For the year ended December 31, 2012, K-Bro's revenue was \$126.3 million, compared to \$116.9 million in the prior year. This represents an 8.0% increase in revenue and is attributed to a combination of the new volume from the Saskatoon Health Region contract and organic growth from new volume and price increases at existing customers across the remainder of the plants. In 2012 approximately 68.6% of K-Bro's revenue was generated from healthcare institutions compared to 68.6% in 2011.

Net earnings increased in 2012 to \$11.1 million from \$7.9 million in 2011. Net earnings as a percentage of revenue increased to 8.8% compared to 6.8% in 2011. This net increase in margin resulted from a decline in operating costs of 2.3%. Net earnings before tax increased in 2012 to \$15.3 million from \$10.9 million in 2011. Net earnings before tax as a percentage of revenues increased to 12.1% compared to 9.3% in 2011. This margin increase is due to a flow through effect of the increase in the EBITDA margin discussed below.

EBITDA was \$24.5 million in 2012, compared to \$19.9 million in 2011. This 21.8% improvement is a result of the new volume from the Saskatoon Health Region contract coupled with favorable variances in utilities. The increase is also attributable to the increases in volume and price offsetting the semi-fixed nature of certain operating costs (see *Operating Expenses* for further detail).

Operating Expenses

Wages and benefits increased from \$54.2 million in 2011 to \$58.2 million in 2012 and decreased as a percentage of revenues to 46.1% from 46.4%. Despite the control over labor costs, pressures continue to increase as the economy recovers, employment rates improve and provincially regulated minimum wage increases. Linen expenses increased to \$12.7 million from \$12.0 million but remained constant as a percentage of revenues at approximately 10%.

Utility costs decreased from 7.4% in 2011 to 6.6% as a percentage of revenue in 2012. The decrease is as a result of the maturation of several natural gas forward contracts, thereby permitting K-Bro to purchase a larger percentage at the current lower market rate.

Delivery costs have increased to \$5.6 million or 4.4% of revenues compared to 4.2% in 2011. The rising cost of diesel fuel has contributed to the increase on a year-over-year basis. Additionally the delivery of linens to Saskatoon Health Region has increased delivery expenses as these services are being performed by the Corporation's Calgary facility. Incremental delivery costs for Saskatoon are offset by additional revenues.

Materials and supplies, occupancy costs and repairs and maintenance as a percentage of revenue remained stable in 2012 compared to 2011.

Corporate costs decreased in 2012 by \$0.5 million over the comparative period of 2011 and decreased as a percentage of revenues to 4.1% from 4.9% in 2011. In the prior year comparative period, acquisition costs associated with the acquisition of the Montréal plant ineligible for capitalization were expensed and incurred as corporate costs.

Depreciation of property, plant and equipment and amortization of intangible assets represents the expense related to the appropriate matching of certain of K-Bro's long-term assets to the estimated useful life and period of economic benefit of those assets. Depreciation of property, plant and equipment and amortization of intangibles assets has increased from the comparable period in 2011 primarily due to the purchases of laundry equipment in Montréal, Québec City and Vancouver.

Income tax includes current and future income taxes based on taxable income and the temporary timing differences between the tax and accounting bases of assets and liabilities. The Corporation's effective tax rate remained constant at approximately 27% of net earnings. A decrease in the statutory rate from 26.9% to 25.3% was offset by an increase in non-deductible expenses.

LIQUIDITY AND CAPITAL RESOURCES

In 2012 cash generated by operating activities was \$20.8 million, compared to cash generated by operating activities of \$18.9 million in 2011. The change in cash from operations is due to the increases in earnings offset by smaller changes in other operating accounts.

During 2012, cash used in financing activities amounted to \$8.2 million compared to \$11.7 million in 2011 mainly attributable to repayment of revolving debt. Financing activities in 2012 included \$2.1 million in net proceeds of long term debt and \$7.9 million in dividends paid to Shareholders.

The Corporation used cash of \$12.6 million for investing activities during 2012 compared to \$7.1 million in 2011. The increase in cash used in investing activities is driven by the purchase of property, plant and equipment for existing operations and the new Edmonton facility.

Contractual Obligations

At December 31, 2012, payments due under contractual obligations for the next five years and thereafter are as follows:

<i>(thousands)</i>	Payments due by Period				
	Total	< 1 Year	1 - 3 Years	4 - 5 Years	> 5 Years
Long-term debt	\$ 5,818	-	5,818	-	-
Operating leases and utility commitments	\$ 31,101	4,160	7,927	3,323	15,691
Linen purchase obligations	\$ 2,551	2,551	-	-	-
Property, plant and equipment commitments	\$ 20,332	20,332	-	-	-

Scheduled lease and forward utility contract payments for 2013 are expected to be \$1.5 million. The operating lease obligations are secured by automotive equipment and are more fully described in the audited annual consolidated financial statements. The source of funds for these commitments will be from operating cash flow and, if necessary, the undrawn portion of the revolving credit facility.

Financial Position

<i>(thousands, except percentages)</i>	December 31, 2012	2011
Long term debt	\$ 5,818	\$ 6,095
Shareholders' equity	67,685	62,933
Total capitalization	\$ 73,503	\$ 69,028
Debt to total capitalization	7.9%	8.8%

For the year ended December 31, 2012, the Corporation had a payout ratio (see *Terminology*) of 41.8%, a debt to total capitalization of 7.9%, an unused revolving credit facility of \$33.8 million and has not incurred any events of default under the terms of its credit facility agreement.

As at December 31, 2012, the Corporation had net working capital of \$8.1 million compared to its working capital position of \$7.2 million at December 31, 2011. The increase in working capital is attributable to the increased earnings during the year offset by capital expenditures.

Management believes that K-Bro has the capital resources and liquidity necessary to meet its commitments, support its operations and finance its growth strategies. In addition to K-Bro's ability to generate cash from operations and its revolving credit facility, K-Bro may also be able to access equity financing, depending upon pricing and availability, for capital spending to sustain its property, plant and equipment.

DIVIDENDS

Fiscal Period	Payment Date	# of Shares outstanding	2012		2011	
			Amount per Share	Total Amount ⁽¹⁾	Amount per Share	Total Amount ⁽¹⁾
January	February 15	7,006,365	\$ 0.09167	\$ 642	\$ 0.09167	\$ 642
February	March 15	7,006,365	0.09167	642	0.09167	642
March	April 13	7,006,365	0.09167	642	0.09167	642
Q1			\$ 0.27501	\$ 1,927	\$ 0.27501	\$ 1,927
April	May 15	7,006,365	\$ 0.09167	\$ 642	\$ 0.09167	\$ 642
May	June 15	7,055,207	0.09580	676	0.09167	642
June	July 13	7,055,207	0.09580	676	0.09167	642
Q2			\$ 0.28328	\$ 1,994	\$ 0.27501	\$ 1,927
July	August 15	7,055,207	\$ 0.09580	\$ 676	\$ 0.09167	\$ 642
August	September 15	7,055,207	0.09580	676	0.09167	642
September	October 15	7,055,207	0.09580	676	0.09167	642
Q3			\$ 0.28741	\$ 2,028	\$ 0.27501	\$ 1,927
October	November 15	7,055,207	\$ 0.09580	\$ 676	\$ 0.09167	\$ 642
November	December 14	7,055,207	0.09580	676	0.09167	642
December	January 15	7,055,207	0.09580	676	0.09167	642
Q4			\$ 0.28741	\$ 2,028	\$ 0.27501	\$ 1,927
YTD			\$ 1.13	\$ 7,977	\$ 1.10	\$ 7,706

⁽¹⁾ - The total amount of dividends paid was \$0.09167 per share for a total of \$642,273 per month for Jan - Apr 2012 and \$642,146 per month in 2011; when rounded in thousands \$1,927 of dividends were paid for each of the quarterly periods, respectively.

For the year ended December 31, 2012, the Corporation distributed \$1.13 per share compared with \$2.73 per diluted share of Distributable Cash (see *Terminology*). The actual payout ratio was 41.8%.

The Corporation's policy is to pay dividends to Shareholders from its available distributable cash flow while considering requirements for capital expenditures, working capital, growth capital and other reserves considered advisable by the Directors of the Corporation. All such dividends are discretionary. Dividends are declared payable each month in equal amounts to Shareholders on the last business day of each month and are paid by the 15th of the following month.

The Corporation designates all dividends paid or deemed to be paid as Eligible Dividends for purposes of subsection 89(14) of the Income Tax Act (Canada), and similar provincial and territorial legislation, unless indicated otherwise.

DISTRIBUTABLE CASH FLOW *(see Terminology)*

(all amounts in this section in \$000's except per share amounts and percentages)

The Corporation's source of cash for dividends is distributable cash flow provided by operating activities. Distributable cash flow, reconciled to cash provided by operating activities as calculated under IFRS, is presented as follows:

<i>(thousands, except per share amounts and percentages)</i>	2012				2011			
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1
Cash provided by operating activities	\$ 7,928	\$ 6,223	\$ (110)	\$ 6,768	\$ 3,929	\$ 8,217	\$ 2,577	\$ 4,137
<i>Deduct (add):</i>								
Net changes in non-cash working capital items ⁽¹⁾	2,866	598	(5,659)	1,774	(583)	2,567	(2,143)	(260)
Share-based compensation expense ⁽²⁾	176	177	250	502	503	361	407	390
Maintenance capital expenditures	486	168	232	134	179	9	423	224
Distributable cash flow	\$ 4,400	\$ 5,280	\$ 5,067	\$ 4,358	\$ 3,830	\$ 5,280	\$ 3,890	\$ 3,783
Distributable cash flow per weighted average diluted shares outstanding	\$ 0.627	\$ 0.750	\$ 0.723	\$ 0.622	\$ 0.548	\$ 0.756	\$ 0.559	\$ 0.541
Dividends declared	2,028	2,028	1,994	1,927	1,927	1,927	1,927	1,927
Dividends declared per share	0.287	0.288	0.283	0.275	0.275	0.275	0.275	0.275
Payout ratio ⁽³⁾	45.8%	38.3%	39.2%	44.2%	50.2%	36.4%	49.2%	50.8%
Weighted average shares outstanding during the period, basic	7,007	7,007	6,979	6,932	6,932	6,930	6,918	6,891
Weighted average shares outstanding during the period, diluted	7,019	7,040	7,009	7,003	6,993	6,983	6,961	6,993
Trailing-twelve months ("TTM")								
Distributable cash flow	19,105	18,535	18,535	17,358	16,783	16,748	16,043	15,763
Dividends	7,977	7,876	7,774	7,706	7,706	7,706	7,706	7,706
Payout ratio ⁽²⁾	41.8%	42.5%	41.9%	44.4%	45.9%	46.0%	48.0%	48.9%

⁽¹⁾ Net changes in non-cash working capital is excluded from the calculation as management believes it would introduce significant cash flow variability and affect underlying cash flow from operating activities. Significant variability can be caused by such things as the timing of receipts (which individually are large because of the nature of K-Bro's customer base and timing may vary due to the timing of customer approval, vacations of customer personnel, etc.) and the timing of disbursements (such as the payment of large volume rebates done once annually). As well, large increases in working capital are generally required when contracts with new customers are signed as linen is purchased and accounts receivable increase. Management feels that this amount should be excluded from the distributable cash flow calculation.

⁽²⁾ Share-based compensation expenses have historically been excluded from the calculation of distributable cash flow. Previously the share-based compensation was recorded as part of the net changes in non-cash working capital items, however the amount has been disclosed separately commencing in Q4, 2012. The comparative figures for the quarterly periods as presented have been restated to reflect this revised presentation.

⁽³⁾ The ratio of dividends paid compared to distributable cash flow is periodically reviewed by the Board of Directors to take into account the current and prospective performance of the business and other items considered to be prudent. Payout ratio is calculated on the dividends declared per share divided by the distributable cash flow per weighted average diluted shares outstanding.

OUTSTANDING SHARES

At December 31, 2012, the Corporation had 7,055,207 common shares outstanding. Basic and diluted weighted average number of common shares outstanding for 2012 were 6,981,432 and 6,993,561 respectively, (6,918,955 and 6,980,489, respectively for the comparative 2011 periods).

In accordance with the LTI plan and in conjunction with the performance of the Corporation in the 2011 fiscal year, on May 2, 2012 the Compensation, Nominating and Corporate Governance Committee of the Board of Directors approved LTI compensation of \$1.2 million (2011 – \$1.8 million under the previous LTI plan) to be paid as shares issued from treasury under the terms of the revised plan approved by Shareholders. As at December 31, 2012, the value of the shares held in trust by the LTI trustee was \$1.4 million (2011 – \$1.3 million) which was comprised of 48,191 in unvested common shares (December 31, 2011 – 74,511) with an aggregate cost of \$0.3 million (2011 – \$1.9 million). The basic net earnings per share calculation excludes the unvested common shares held by the LTI Trust.

As at March 13, 2013, there were 7,055,207 common shares issued and outstanding.

RELATED PARTY TRANSACTIONS

The Corporation incurred expenses in the normal course of business for advisory consulting services provided by Mr. Matthew Hills, a director of the Corporation, primarily relating to acquisitions. The amounts charged are recorded at their exchange amounts and are subject to normal trade terms. For the year ended December 31, 2012, the Corporation incurred fees totaling \$137,500 (2011 – \$137,500).

OFF-BALANCE SHEET ARRANGEMENTS

The Corporation had a foreign exchange forward contract for the purchase of US dollars in place as at December 31, 2012. This forward contract was marked-to-market and was settled on January 31, 2013.

CRITICAL ACCOUNTING ESTIMATES

The Corporation's summary of significant accounting policies are contained in note 2 to the audited consolidated financial statements.

The Corporation's financial statements include estimates and assumptions made by management in respect of operating results, financial conditions, contingencies, commitments, and related disclosures. Actual results may vary from these estimates. The following are, in the opinion of management, the Corporation's most critical accounting estimates, being those that involve the most difficult, subjective and complex judgments, and/or requiring estimates that are inherently uncertain and which may change in subsequent reporting periods.

K-Bro has continuously refined and documented its management and internal reporting systems to ensure that accurate, timely, internal and external information is gathered and disseminated. Management also regularly evaluates these estimates and assumptions which are based on past experience and other factors that are deemed reasonable under the circumstances.

K-Bro has hired individuals and consultants who have the skills required to make such estimates and ensures that individuals or departments with the most knowledge of the activity are responsible for the estimates. Furthermore, past estimates are reviewed and compared to actual results, and actual results are compared to budgets in order to make more informed decisions on future estimates.

K-Bro's leadership team's mandate includes ongoing development of procedures, standards and systems to allow K-Bro staff to make the best decisions possible and ensuring those decisions are in compliance with the Corporation's policies.

Preparation of the Corporation's consolidated financial statements requires management to make estimates and assumptions that affect:

- volume rebates;
- linen in service;
- intangible assets;
- goodwill;
- income taxes; and,
- allowance for doubtful accounts.

Volume Rebates

The Corporation earns revenue from linen management and laundry services based on written service agreements whereby K-Bro has agreed to collect, launder, deliver and replenish linens. K-Bro recognizes revenue in the period in which the services are provided. Volume rebates, where applicable, are recorded based on annualized expected volumes when it is reasonable that the criteria are likely to be met. Based on past experience, management believes that volumes utilized for any estimates are reasonable and would not expect a material deviation to the balance of accrued liabilities or revenue.

Linen in Service

Linen in service is recorded at cost. Operating room linen is amortized on a straight-line method over an estimated service life of 24 months. General linen is amortized based on usage which results in an estimated service life of the linen equal to 24 months. Based on past experience, management believes that a service life of 24 months is representative of the average service life of linen and would not expect a material deviation to the balance of linen in service or linen expense.

Intangible Assets

The Corporation accounts for intangible assets and goodwill in accordance with IFRS 3, *Business Combinations* and IAS 38, *Intangible Assets*. In a business combination, K-Bro may acquire the assets and assume certain liabilities of an acquired entity. The allocation of the purchase price for these transactions involves judgment in determining the fair values assigned to the tangible and intangible assets acquired and the liabilities assumed on the acquisition. The determination of these fair values involves a variety of assumptions, including revenue growth rates, expected operating income, discount rates, and earnings multiples. If K-Bro's estimates or assumptions change prior to finalizing the purchase price allocation for a transaction, a revision to the purchase price allocation or the carrying value of the related assets and liabilities acquired may impact our net income in future periods.

At the date of the acquisition, K-Bro must estimate the value of acquired intangible assets that do not have a well defined market value, such as the value of customer lists and relationships and non-competition agreements.

Valuing these assets involves estimates of the future net benefit to K-Bro and the useful life of such benefits and is based upon various internal and external factors. A change in those estimates could cause a material change to the value of the intangible assets.

Although intangible assets are amortized over their useful life, if the estimated value of an intangible asset has declined below its amortized book value, a write-down would be recorded in the period in which the event causing the decline in value occurred, which would increase amortization expense and decrease the intangible assets balance. At this time, K-Bro does not believe any intangible assets have a book value in excess of their fair market value.

TERMINOLOGY

EBITDA

We report on our EBITDA (Earnings before interest, taxes, depreciation and amortization) because it is a key measure used by management to evaluate performance. EBITDA is utilized in measuring compliance with debt covenants and in making decisions relating to dividends to Shareholders. We believe EBITDA assists investors in assessing our performance on a consistent basis as it is an indication of our capacity to generate income from operations before taking into account management's financing decisions and costs of consuming tangible and intangible capital assets, which vary according to their vintage, technological currency and management's estimate of their useful life. Accordingly, EBITDA comprises revenues less operating costs before: financing costs, capital asset and intangible asset amortization, loss on disposal and impairment charges, and income taxes.

EBITDA is not a calculation based on IFRS and is not considered an alternative to net earnings in measuring K-Bro's performance. EBITDA does not have a standardized meaning and is therefore not likely to be comparable with similar measures used by other issuers. EBITDA should not be used as an exclusive measure of cash flow since it does not account for the impact of working capital changes, capital expenditures, debt changes and other sources and uses of cash, which are disclosed in the consolidated statements of cash flows.

<i>(thousands)</i>	Three Months Ended December 31,		Year Ended December 31,	
	2012	2011	2012	2011
Net earnings	\$ 2,758	\$ 1,643	\$ 11,149	\$ 7,928
<i>Add:</i>				
Income tax expense	1,122	688	4,175	2,960
Interest expense and financial charges, net	(66)	93	357	412
Depreciation of property, plant and equipment	1,617	1,409	6,350	5,938
Amortization of intangible assets	307	673	2,327	2,628
Loss on disposal of property, plant and equipment	39	50	159	80
EBITDA	\$ 5,777	\$ 4,556	\$ 24,517	\$ 19,946

Distributable Cash Flow

Distributable cash flow is a measure used by management to evaluate its performance. While the closest IFRS measure is cash provided by operating activities, distributable cash flow is considered relevant because it provides an indication of how much cash generated by operations is available after capital expenditures. It shall be noted that although we consider this measure to be distributable cash flow, financial and non-financial covenants in our credit facilities and dealer agreements may restrict cash from being available for dividends, re-investment in the Corporation, potential acquisitions, or other purposes. Investors should be cautioned that distributable cash flow may not actually be available for growth or distribution from the Corporation. References to "Distributable cash flow" are to cash provided by (used in) operating activities (including the net change in non-cash working capital balances) less capital expenditures.

CHANGES IN ACCOUNTING POLICIES

The Corporation has prepared its December 31, 2012 audited Consolidated Financial Statements in accordance with IFRS. See note 2 of the Corporation's audited Consolidated Financial Statements for more information regarding the significant accounting principles used to prepare the audited Consolidated Financial Statements. There have been no changes in accounting policies during the year ended December 31, 2012.

RECENT ACCOUNTING PRONOUNCEMENTS

There are no changes in accounting standards applicable to future periods that are relevant and significant to the Corporation other than as disclosed in the most recent audited Consolidated Financial Statements as at and for the year ended December 31, 2012.

FINANCIAL INSTRUMENTS

K-Bro's financial instruments at December 31, 2012 consist of accounts receivable, accounts payable and accrued liabilities and long-term debt. The Corporation does not enter into financial instruments for trading or speculative purposes. Financial assets are either classified as available for sale, held to maturity, trading or loans and receivables. Financial liabilities are recorded at amortized cost. Initially, all financial assets and financial liabilities must be recorded on the balance sheet at fair value. Subsequent measurement is determined by the classification of each financial asset and liability. Unrealized gains and losses on financial assets that are held as available for sale are recorded in other comprehensive income until realized, at which time they are recorded in the consolidated statement of earnings. All derivatives, including embedded derivatives that must be separately accounted for, are recorded at fair value in the consolidated balance sheet. Transaction costs related to financial instruments are capitalized and then amortized over the expected life of the financial instrument using the effective interest method.

Derivative financial instruments are utilized by K-Bro to manage cashflow risk against the volatility in interest rates on its long-term debt and foreign exchange rates on its equipment purchase commitments. K-Bro typically does not utilize derivative financial instruments for trading or speculative purposes. K-Bro has floating interest rate debt that gives rise to risks that its earnings and cash flows may be adversely impacted by fluctuations in interest rates. In order to manage these risks, K-Bro may enter into interest rate swaps, forward contracts on foreign currency, utilities and textiles or option contracts.

CRITICAL RISKS AND UNCERTAINTIES

As at December 31, 2012, there are no material changes in the Corporation's risks or risk management activities since December 31, 2011. The Corporation's results of operations, business prospects, financial condition, cash dividends to Shareholders and the trading price of the Corporation's Shares are subject to a number of risks. These risk factors include: dependence on long-term contracts and the associated renewal risk thereof; the effects of market volatility and uncertainty; potential future tax changes; the competitive environment; our ability to acquire and successfully integrate and operate additional businesses; utility costs; the labour markets; the fact that our credit facility imposes numerous covenants and encumbers assets; and, environmental matters.

For a discussion of these risks and other risks associated with an investment in Corporation Shares, see *Risk Factors – Risks Related to K-Bro and the Laundry and Linen Industry* detailed in the Corporation's Annual Information Form that is available at www.sedar.com.

CONTROLS AND PROCEDURES

In order to ensure that information with regard to reports filed or submitted under securities legislation present fairly in all material respects the financial information of K-Bro, management, including the President and Chief Executive Officer (“CEO”) and the Vice-President and Chief Financial Officer (“CFO”), are responsible for establishing and maintaining disclosure controls and procedures, as well as internal control over financial reporting.

Disclosure Controls and Procedures

The Corporation has established disclosure controls and procedures to ensure that information disclosed in this MD&A and the related financial statements of K-Bro was properly recorded, processed, summarized and reported to the Board of Directors and the Audit Committee. The Corporation’s CEO and CFO have evaluated the effectiveness of these disclosure controls and procedures for the year ended December 31, 2012, and the CEO and CFO have concluded that these controls were operating effectively.

Internal Controls over Financial Reporting

The CEO and CFO acknowledge responsibility for the design of internal controls over financial reporting (“ICFR”). Consequently the CEO and CFO confirm that the additions to these controls that occurred during the year ended December 31, 2012 did not materially affect, or are reasonably likely to materially affect, the Corporation’s ICFR. Based upon their evaluation of these controls for the year ended December 31, 2012, the CEO and CFO have concluded that these controls were operating effectively.

A control system, no matter how well conceived and operated, can provide only reasonable, and not absolute, assurance that the objectives of the control system are met. As a result of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues, including instance of fraud, if any, have been detected. These inherent limitations include, amongst other items: (i) that managements’ assumptions and judgments could ultimately prove to be incorrect under varying conditions and circumstances; or, (ii) the impact of isolated errors.

Additionally, controls may be circumvented by the unauthorized acts of individuals, by collusion of two or more people, or by management override. The design of any system of controls is also based, in part, upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential (future) conditions.

Additional information regarding K-Bro including required securities filings are available on our website at www.k-brolinen.com and on the Canadian Securities Administrators’ website at www.sedar.com; the System for Electronic Document Analysis and Retrieval (“SEDAR”).

Vous pouvez obtenir des renseignements supplémentaires sur la Société, y compris les documents déposés auprès des autorités de réglementation, sur notre site Web, au www.k-brolinen.com et sur le site Web des autorités canadiennes en valeurs mobilières au www.sedar.com, le site Web du Système électronique de données, d’analyse et de recherche (« SEDAR »).