



Q2, 2013
Management's
Discussion &
Analysis

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 unaudited interim condensed Consolidated Financial Statements of K-Bro Linen Inc. ("the Corporation") for the three and six months ended June 30, 2013 and the audited Consolidated Financial Statements, as well as the MD&A, for the year ended December 31, 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 August 9, 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.

SELECTED QUARTERLY FINANCIAL INFORMATION

<i>(thousands, except share and per share amounts)</i>	Three Months Ended June 30,		
	2013	2012	2011
Revenue	\$ 32,660	\$ 31,526	\$ 28,871
Earnings before income taxes	4,112	4,084	2,725
Net earnings	2,886	2,963	2,003
<i>Net earnings per share:</i>			
Basic	\$ 0.41	\$ 0.42	\$ 0.29
Diluted	\$ 0.41	\$ 0.42	\$ 0.29
Total assets	104,226	90,505	93,148
Long-term debt	15,338	7,113	13,007
Dividends declared to Shareholders	2,036	1,994	1,927
Dividends declared to Shareholders per share	\$ 0.288	\$ 0.283	\$ 0.275
<i>Number of shares outstanding:</i>			
Basic	7,020,441	6,979,281	6,917,854
Diluted	7,038,100	7,009,458	6,960,674

<i>(thousands, except share and per share amounts)</i>	Six Months Ended June 30,		
	2013	2012	2011
Revenue	\$ 64,307	\$ 61,691	\$ 56,557
Earnings before income taxes	7,919	7,261	4,877
Net earnings	5,648	5,432	3,558
<i>Net earnings per share:</i>			
Basic	\$ 0.81	\$ 0.78	\$ 0.52
Diluted	\$ 0.80	\$ 0.78	\$ 0.51
Total assets	104,226	90,505	93,148
Long-term debt	15,338	7,113	13,007
Dividends declared to Shareholders	4,064	3,921	3,853
Dividends declared to Shareholders per share	\$ 0.575	\$ 0.558	\$ 0.550
<i>Number of shares outstanding:</i>			
Basic	7,013,765	6,955,567	6,904,451
Diluted	7,029,605	6,985,744	6,947,271

SUMMARY OF INTERIM RESULTS AND KEY EVENTS

Edmonton Facility Development

During Q2, K-Bro continued construction of the new leased Edmonton facility. Management estimates that the costs to commission the new facility to be approximately \$26.6 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. Transition into and start-up of the new facility has been postponed due to several construction delays. Transition costs associated with the new facility will be primarily incurred in Q3 and Q4, 2013. As at June 30, 2013, K-Bro has incurred \$16.7 million of the total expected capital cost.

Health Shared Services Saskatchewan (“3sHealth”)

During Q2, K-Bro announced that it had been informed by 3sHealth of its intention to enter into negotiations with K-Bro for a long-term contract to service laundry and linen requirements in Saskatchewan. This is a result of K-Bro being selected pursuant to 3sHealth's Request for Strategic Partner (“RFSP”) process that commenced in 2012.

3sHealth and K-Bro are in negotiations for a long-term services contract and upon the conclusion of successful negotiations and agreement on commercial terms, the Corporation will commence the planning and construction of a processing facility in the province of Saskatchewan.

Effects of Economic Uncertainty

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

- Approximately 67.7% of its revenues in the quarter were from large publicly funded healthcare customers which are geographically diversified across multiple provinces;
- At June 30, 2013, K-Bro had unutilized borrowing capacity of \$24.0 million or 60.0% 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.

K-Bro is a participant in the temporary foreign worker (“TFW”) program in our facilities where genuine labour shortages exist, predominantly within our Alberta plants. During the year, the federal government reviewed the TFW program and proposed various rule changes. These proposed changes include stricter application requirements, the suspension of accelerated labour market opinions and an end to a provision whereby employers could pay wages lower than the labour market opinion to temporary foreign workers. The proposed rule changes have limited applicability to K-Bro and are not expected to have a material effect on the financial results or operations of the Corporation. During the quarter, K-Bro received additional approval to recruit and hire additional temporary foreign workers. However, additional changes or amendments to, or suspension or cancellation of, the TFW program in the future could reduce K-Bro’s ability to recruit employees which could have a negative impact on the Corporation. The impact of the changes to the TFW program as announced on August 8, 2013 have not been evaluated as of the date of filing.

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>		Q2, 2013	Q2 2012	YTD 2013	YTD 2012
Category	Indicator				
Growth	EBITDA ⁽¹⁾	-2.3%	31.6%	1.3%	28.4%
	Revenue	3.6%	9.2%	4.2%	9.1%
	Distributable cash flow	-4.0%	30.3%	0.9%	22.8%
Profitability	EBITDA ⁽¹⁾	\$ 6,257	\$ 6,404	\$ 12,161	\$ 12,001
	EBITDA margin	19.2%	20.3%	18.9%	19.5%
	Net earnings	\$ 2,886	\$ 2,963	\$ 5,648	\$ 5,432
Stability	Debt to total capitalization	18.0%	9.8%	18.0%	9.8%
	Unutilized line of credit	\$ 24,012	\$ 32,637	\$ 24,012	\$ 32,637
	Payout ratio	41.9%	39.2%	43.1%	41.4%
	Dividends declared per share	\$ 0.288	\$ 0.283	\$ 0.575	\$ 0.558
Cost containment	Wages and benefits	45.7%	45.7%	46.0%	45.6%
	Utilities	6.5%	6.1%	6.5%	6.3%
	Operating expenses	80.8%	79.7%	81.1%	80.5%

⁽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. Because most hospitality clients and healthcare institutions are under long-term contract, with pricing mainly dictated by macroeconomic factors including inflation and consumer price indices, Management believes that fiscal 2013 will show a slight increase in revenue compared to 2012.

During Q2, 2013 K-Bro continued the development of a new Edmonton processing facility. Due to construction delays, the commissioning and start-up of the new facility has been delayed to Q3 and Q4, 2013. As a result of the construction delays Management expects efficiency and productivity of its Edmonton operations to be negatively impacted in Q3 and Q4, 2013, and improve once the transition between the two sites is complete. Management continues to believe that the EBITDA margin will be negatively impacted during the transition period by up to 3% on a consolidated basis for fiscal 2013. It remains Management's expectation that efficiencies and improved productivity from the new facility will offset the impact of the price concessions provided to AHS.

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

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>	2013		2012				2011	
	Q2	Q1	Q4	Q3	Q2	Q1	Q4	Q3
Healthcare revenue	22,124	22,288	22,222	21,418	21,713	21,257	20,432	19,730
Hospitality revenue	10,536	9,359	9,364	11,595	9,813	8,908	8,726	11,414
Total revenue	32,660	31,647	31,586	33,013	31,526	30,165	29,158	31,144
Operating expenses	26,403	25,743	25,809	26,274	25,122	24,568	24,602	25,098
EBITDA ⁽¹⁾	6,257	5,904	5,777	6,739	6,404	5,597	4,556	6,046
EBITDA as a % of revenue	19.2%	18.7%	18.3%	20.4%	20.3%	18.6%	15.6%	19.4%
Depreciation and amortization	1,940	1,974	1,924	2,283	2,263	2,207	2,082	2,232
Financial charges	127	123	(66)	272	67	84	93	131
Loss (gain) on disposal of equipment	78	-	39	1	(10)	129	50	4
Earnings before income taxes	4,112	3,807	3,880	4,183	4,084	3,177	2,331	3,679
Income tax expense	1,226	1,045	1,122	1,224	1,121	708	688	953
Net earnings	2,886	2,762	2,758	2,959	2,963	2,469	1,643	2,726
Net earnings as a % of revenue	8.8%	8.7%	8.7%	9.0%	9.4%	8.2%	5.6%	8.8%
Basic earnings per share	0.411	0.393	0.393	0.422	0.424	0.356	0.237	0.393
Diluted earnings per share	0.410	0.391	0.393	0.420	0.423	0.353	0.235	0.390
Total assets	104,226	99,452	94,800	94,166	90,505	92,529	91,425	90,350
Total long-term financial liabilities	20,794	10,442	11,023	12,830	11,963	8,795	11,203	12,096
Funds provided by operations	(1,499)	9,180	7,928	6,223	5	6,658	3,929	8,217
Long-term debt	15,338	5,162	5,818	7,787	7,113	4,000	6,095	7,224
Dividends declared per share	0.288	0.288	0.287	0.288	0.283	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, EBITDA and Earnings

For the three months ended June 30, 2013, K-Bro's revenue increased by 3.6% to \$32.7 million from \$31.5 million in the comparative period. This increase was due to a combination of additional volume from the Saskatoon Health Region and organic growth and price increases at existing customers across the plants, offset by price concessions as the result of the new contract with AHS in Edmonton. In Q2, 2013 approximately 67.7% of K-Bro's revenue was generated from healthcare institutions which has decreased slightly from 68.9% in Q2, 2012.

EBITDA was \$6.3 million for the three months ended June 30, 2013, compared to \$6.4 million in the comparative period of 2012. This 2.3% decrease was predominantly a result of price concessions as the result of the new contract with AHS in Edmonton, while partially offset by organic growth and price increases from existing customers. The quarter-over-quarter decline in EBITDA is consistent with the Company's expectation and was anticipated as the result of price concessions provided to Alberta Health Services as part of the new long-term Edmonton contract. We expect the impact of these price concessions to be offset by cost savings from efficiencies in our new Edmonton facility. The transition to the new facility will commence in Q3, 2013.

Net earnings decreased by \$0.1 million or 2.6% from \$3.0 million in Q2, 2012 to \$2.9 million in Q2, 2013. Net earnings as a percentage of revenue decreased to 8.8% compared to 9.4% in 2012. This margin decrease is due to a flow through effect of the decrease in the EBITDA.

Operating Expenses

Wages and benefits increased to \$14.9 million from \$14.4 million and increased as a percentage of revenue to 45.7% compared to 45.6% in the same period of 2012. This increase was a result of increments in the wage rate provided earlier in the year during Q1, 2013.

Linen expenses increased to \$3.5 million from \$3.2 million and increased as a percentage of revenue to 10.6% compared to 10.2% in the same period of 2012.

Utility costs slightly increased to 6.5% as a percentage of revenue in Q2, 2013, compared to 6.3% in 2012.

Delivery costs remained constant at \$1.4 million or 4.3% of revenues compared to 4.4% in Q2, 2012.

Corporate costs increased in Q2, 2013 by \$0.1 million over the comparative period of 2012 and decreased as a percentage of revenues to 4.5% in Q2, 2013 from 4.7% in Q2, 2012 due to an increase in the long term incentive compensation plan.

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.

Financial charges for Q2, 2013 increased slightly compared to Q2, 2012. The increase is attributable to interest on additional debt relating to the development and construction of the new Edmonton production facility, as well as fees associated with renewal of K-Bro's credit agreement.

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. Income tax reflects the quarterly provision on the earnings of the Corporation.

LIQUIDITY AND CAPITAL RESOURCES

In Q2, 2013 cash used by operating activities was \$1.5 million, compared to cash used by operating activities of \$0.1 million during Q2, 2012. The change in cash from operations is due to the payment of corporate income tax, as well as the payment of a number of volume rebates and discounts.

During Q2, 2013, cash generated from financing activities amounted to \$8.1 million compared to \$1.1 million in Q2, 2012. Financing activities in Q2, 2013 included \$10.1 million in net proceeds of long term debt and \$2.0 million in dividends paid to Shareholders.

Investing activities resulted in a use of cash of \$6.7 million in Q2, 2013 compared to \$1.2 million in Q2, 2012. Investing activities for the current quarter primarily related to the purchase of property, plant and equipment for the new Edmonton plant.

Contractual Obligations

At June 30, 2013, 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	\$ 15,338	-	15,338	-	-
Operating leases and utility commitments	\$ 29,361	2,321	7,995	6,357	12,688
Linen purchase obligations	\$ 3,268	3,268	-	-	-
Property, plant and equipment commitments	\$ 9,967	9,967	-	-	-

Scheduled lease and forward utility contract payments for 2013 are expected to be \$3.5 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>	June 30, 2013	December 31, 2012
Long term debt	\$ 15,338	\$ 5,818
Shareholders' equity	69,966	67,685
Total capitalization	\$ 85,304	\$ 73,503
Debt to total capitalization	18.0%	7.9%

For the quarter ended June 30, 2013, the Corporation had a debt to total capitalization of 18.0%, unused revolving credit facility of \$24.0 million and has not incurred any events of default under the terms of its credit facility agreement.

As at June 30, 2013, the Corporation had net working capital of \$11.0 million compared to its working capital position of \$8.1 million at December 31, 2012. The increase in working capital is attributable to the increased proceeds from the credit facility agreement, partially offset by capital expenditures associated with the new Edmonton plant.

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 believes it is also able to issue additional shares or increase its borrowing capacity, if necessary, to provide for capital spending and sustain its property, plant and equipment.

DIVIDENDS

Fiscal Period	Payment Date	# of Shares outstanding	2013		2012	
			Amount per Share	Total Amount ⁽¹⁾	Amount per Share	Total Amount ⁽¹⁾
January	February 15	7,055,207	\$ 0.09580	\$ 676	\$ 0.09167	\$ 642
February	March 15	7,055,207	0.09580	676	0.09167	642
March	April 13	7,055,207	0.09580	676	0.09167	642
Q1			\$ 0.28741	\$ 2,027	\$ 0.27501	\$ 1,927
April	May 15	7,055,207	\$ 0.09580	\$ 676	\$ 0.09167	\$ 642
May	June 15	7,095,343	0.09580	680	0.09167	676
June	July 13	7,095,343	0.09580	680	0.09167	676
Q2			\$ 0.28741	\$ 2,036	\$ 0.27501	\$ 1,994
YTD			\$ 0.28741	\$ 4,063	\$ 0.27501	\$ 3,921

⁽¹⁾ - The total amount of dividends paid was \$0.09580 per share for a total of \$675,912 per month for Jan - Apr 2013 and \$642,146 per month in 2012; when rounded in thousands \$2,027 of dividends were paid for in Q1 2013 and \$1,927 in Q1 2012, respectively.

For the three months ended June 30, 2013, the Corporation declared a \$0.288 per share dividend compared to \$0.688 per Share of Distributable Cash Flow (see *Terminology*). The payout ratio for the three months ended June 30, 2013 was 41.9%.

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>	2013		2012				2011	
	Q2	Q1	Q4	Q3	Q2	Q1	Q4	Q3
Cash provided by operating activities	\$ (1,499)	\$ 9,180	\$ 7,928	\$ 6,223	\$ 5	\$ 6,653	\$ 3,929	\$ 8,217
<i>Deduct (add):</i>								
Net changes in non-cash working capital items ⁽¹⁾	(6,956)	4,049	2,866	598	(5,518)	1,659	(583)	2,567
Share-based compensation expense	377	320	176	177	250	502	503	361
Maintenance capital expenditures	240	173	486	168	232	134	179	9
Distributable cash flow	\$ 4,840	\$ 4,638	\$ 4,400	\$ 5,280	\$ 5,041	\$ 4,358	\$ 3,830	\$ 5,280
Distributable cash flow per weighted average diluted shares outstanding	\$ 0.688	\$ 0.657	\$ 0.625	\$ 0.750	\$ 0.719	\$ 0.622	\$ 0.548	\$ 0.756
Dividends declared	2,036	2,028	2,028	2,028	1,994	1,927	1,927	1,927
Dividends declared per share	0.288	0.288	0.287	0.288	0.283	0.275	0.275	0.275
Payout ratio ⁽²⁾	41.9%	43.9%	46.0%	38.3%	39.4%	44.2%	50.2%	36.4%
Weighted average shares outstanding during the period, basic	7,020	7,019	7,020	7,007	6,979	6,932	6,932	6,930
Weighted average shares outstanding during the period, diluted	7,038	7,054	7,038	7,040	7,009	7,003	6,993	6,983
Trailing-twelve months ("TTM")								
Distributable cash flow	19,158	19,358	19,079	18,508	18,509	17,358	16,783	16,748
Dividends	8,142	8,077	7,977	7,876	7,774	7,706	7,706	7,706
Payout ratio ⁽²⁾	42.5%	41.7%	41.8%	42.5%	42.0%	44.4%	45.9%	46.0%

⁽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⁾ 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

As at June 30, the Corporation had 7,095,343 common shares outstanding, including 63,604 shares issued but held as unvested treasury shares. Basic and diluted weighted average number of common shares outstanding for the three months ended June 30, 2013 were 7,020,441 and 7,038,100, respectively, (6,979,281 and 7,009,458, respectively, for the comparative 2012 interim periods).

In accordance with the LTI plan and in conjunction with the performance of the Corporation in the 2012 fiscal year, on April 24, 2013 the Compensation, Nominating and Corporate Governance Committee of the Board of Directors approved LTI compensation of \$1.2 million (2012 – \$1.2 million) to be paid as shares issued from treasury. As at June 30, 2013, the value of the shares held in trust by the LTI trustee was \$2.3 million (December 31, 2012 – \$1.4 million) which was comprised of 63,604 in unvested common shares (December 31, 2012 – 48,191) with a nil aggregate cost (December 31, 2012 – \$0.3 million).

As at August 9, 2013, there were 7,095,343 common shares issued and outstanding including 63,604 shares issued but held as unvested treasury shares.

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 three month period ended June 30, 2013, the Corporation incurred fees totaling \$34,500, compared to \$34,500 for the same period of fiscal 2012.

CRITICAL ACCOUNTING ESTIMATES

The preparation of the financial statements, in conformity with IFRS, requires K-Bro to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported period. Management regularly evaluates these estimates and assumptions which are based on past experience and other factors that are deemed reasonable under the circumstances. This involves varying degrees of judgment and uncertainty and, therefore, amounts currently reported in the financial statements could differ in the future. There have been no changes in the accounting estimates from those reported at December 31, 2012.

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 June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Net earnings	\$ 2,886	\$ 2,963	\$ 5,648	\$ 5,432
<i>Add:</i>				
Income tax expense	1,226	1,121	2,271	1,829
Interest expense and financial charges, net	127	67	250	150
Depreciation of property, plant and equipment	1,411	1,590	2,834	3,125
Amortization of intangible assets	529	673	1,080	1,346
Loss on disposal of property, plant and equipment	78	(10)	78	119
EBITDA	\$ 6,257	\$ 6,404	\$ 12,161	\$ 12,001

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 June 30, 2013 interim condensed consolidated financial statements in accordance with IAS 34, *Interim Financial Reporting*, as issued by the IASB and incorporated the same accounting principles and methods used in the preparation of the audited annual Consolidated Financial Statements. See Note 2 of the Corporation’s audited annual Consolidated Financial Statements for more information regarding the significant accounting principles used to prepare the interim Consolidated Financial Statements.

The Corporation has adopted the following new and revised standards, along with any consequential amendments, effective January 1, 2013. These changes were made in accordance with the applicable transitional provisions.

- IFRS 10, *Consolidated Financial Statements*, replaces the guidance on control and consolidation in IAS 27, *Consolidated and Separate Financial Statements*, and SIC-12, *Consolidation - Special Purpose Entities*. IFRS 10 requires consolidation of an investee only if the investor possesses power over the investee, has exposure to variable returns from its involvement with the investee and has the ability to use its power over the investee to affect its returns. Detailed guidance is provided on applying the definition of control. The accounting requirements for consolidation have remained largely consistent with IAS 27. The Corporation assessed its consolidation conclusions on January 1, 2013 and determined that the adoption of IFRS 10 did not result in any change in the consolidation status of any of its subsidiaries and investees.
- IFRS 13, *Fair value measurement*, provides a single framework for measuring fair value. The measurement of the fair value of an asset or liability is based on assumptions that market participants would use when pricing the assets or liability under current market conditions, including assumptions about risk. The Corporation adopted IFRS 13 on January 1, 2013 on a prospective basis. The adoption of IFRS did not require any adjustments to valuation techniques used by the Corporation to measure fair value and did not result in any measurement adjustments as at January 1, 2013.

CRITICAL RISKS AND UNCERTAINTIES

As at June 30, 2013, there are no material changes in the Corporation’s risks or risk management activities since December 31, 2012. 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 three months ended June 30, 2013, and have concluded that they are effective.

Internal Controls over Financial Reporting

There were no changes in internal controls over financial reporting (“ICFR”) during the three month period ended June 30, 2013 that materially affected, or are reasonably likely to materially affect, the Corporation’s ICFR. The CEO and the CFO have evaluated these controls for the three months ended June 30, 2013 and have concluded that the controls are operating effectively. A discussion of the internal controls over financial reporting can be found under the MD&A that accompany the audited consolidated financial statements for the year ended December 31, 2012.

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 »).