K·BRO

Q3, 2013 Condensed Consolidated Financial Statements

dependable.

K-Bro Linen Inc.

www.k-brolinen.com | inquiries@k-brolinen.com

Condensed Consolidated Statements of Financial Position

(unaudited, thousands of Canadian dollars)

	September 30, 2013	December 31, 2012
ASSETS		
Current assets		
Accounts receivable	$ 14,816	$ 14,197
Linen in service	9,101	8,888
Prepaid expenses and deposits	1,335	1,071
	25,252	24,156
Property, plant and equipment (note 3)	52,800	39,175
Intangible assets	9,403	11,013
Goodwill	20,456	20,456
	$ 107,911	$ 94,800
LIABILITIES		
Current liabilities		
Accounts payable and accrued liabilities (note 4)	$ 13,720	$ 13,001
Income taxes payable	217	2,415
Dividends payable to shareholders	680	676
	14,617	16,092
Long-term debt (note 5)	17,028	5,818
Unamortized lease inducements	341	415
Deferred income taxes	5,147	4,790
	$ 37,133	$ 27,115
SHAREHOLDERS' EQUITY		
Share capital	72,158	71,444
Contributed surplus	1,472	1,209
Deficit	(2,852)	(4,968)
	$ 70,778	$ 67,685
Contingencies and commitments (note 6)		
	$ 107,911	$ 94,800

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

Condensed Consolidated Statements of Earnings & Comprehensive Income

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	**2013**	2012
Revenue	**$ 34,551**	$ 33,013	**$ 98,858**	$ 94,704
Expenses				
Wages and benefits	**16,169**	15,523	**45,739**	43,673
Linen	**3,476**	3,126	**10,180**	9,443
Utilities	**2,073**	2,216	**6,250**	6,107
Delivery	**1,520**	1,422	**4,468**	4,116
Occupancy costs	**2,125**	960	**4,043**	2,905
Materials and supplies	**1,174**	1,026	**3,162**	2,914
Repairs and maintenance	**1,016**	931	**3,091**	2,844
Corporate	**1,263**	1,070	**4,029**	3,962
	28,816	26,274	**80,962**	75,964
EBITDA	**5,735**	6,739	**17,896**	18,740
Other expenses				
Depreciation of property, plant and equipment	**1,357**	1,609	**4,191**	4,734
Amortization of intangible assets	**530**	674	**1,610**	2,020
Financial charges	**169**	272	**419**	422
Loss on disposal of property, plant and equipment	**5**	1	**83**	120
	2,061	2,556	**6,303**	7,296
Earnings before income taxes	**3,674**	4,183	**11,593**	11,444
Current income tax expense	**1,046**	1,007	**3,017**	3,045
Deferred income tax expense	**57**	217	**357**	8
Income tax expense	**1,103**	1,224	**3,374**	3,053
Net earnings and Comprehensive income	**2,571**	2,959	**8,219**	8,391
Net earnings per share:				
Basic	**$ 0.37**	$ 0.42	**$ 1.17**	$ 1.20
Diluted	**$ 0.36**	$ 0.42	**$ 1.17**	$ 1.20
Weighted average number of shares outstanding:				
Basic	**7,031,487**	7,007,015	**7,019,737**	6,972,843
Diluted	**7,054,936**	7,040,017	**7,041,823**	7,005,845

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

Condensed Consolidated Statements of Changes in Equity

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

	Issued Capital						
	Number of shares	Amount	Shares held in trust	Total Share Capital	Contributed surplus	Deficit	Total equity
	#	$	$	$	$	$	$
As at December 31, 2012	7,018,581	71,725	(281)	71,444	1,209	(4,968)	67,685
Net earnings	-	-	-	-	-	8,219	8,219
Dividends declared (note 7)	-	-	-	-	-	(6,103)	(6,103)
Employee share based compensation expense	40,136	1,351	-	1,351	(374)	-	977
Unvested treasury shares held in trust	(26,978)	(918)	-	(918)	918	-	-
Vested shares held in trust	-	-	281	281	(281)	-	-
As at September 30, 2013	7,031,739	72,158	-	72,158	1,472	(2,852)	70,778

	Issued Capital						
	Number of shares	Amount	Shares held in trust	Total Share Capital	Contributed surplus	Deficit	Total equity
	#	$	$	$	$	$	$
As at December 31, 2011	7,006,365	71,400	(1,907)	69,493	1,580	(8,140)	62,933
Net earnings	-	-	-	-	-	8,391	8,391
Dividends declared (note 7)	-	-	-	-	-	(5,949)	(5,949)
Employee share based compensation expense	48,842	1,178	1,626	2,804	(549)	-	2,255
Unvested treasury shares held in trust	(36,626)	(853)	-	(853)	-	-	(853)
As at September 30, 2012	7,018,581	71,725	(281)	71,444	1,031	(5,698)	66,777

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

Condensed Consolidated Statements of Cash Flow

(unaudited, thousands of Canadian dollars)

	Three Months Ended September 30, 2013	Three Months Ended September 30, 2012	Nine Months Ended September 30, 2013	Nine Months Ended September 30, 2012
OPERATING ACTIVITIES				
Net earnings	$ 2,571	$ 2,959	$ 8,219	$ 8,391
Depreciation of property, plant and equipment	1,357	1,609	4,191	4,734
Amortization of intangible assets	530	674	1,610	2,020
Amortization of lease inducements	(25)	(12)	(74)	(60)
Share-based compensation expense	279	177	977	929
Loss on disposal of property, plant and equipment	5	1	83	120
Deferred income taxes	57	217	357	8
	4,774	5,625	15,363	16,142
Change in non-cash balances relating to operations (note 8)	332	598	(2,576)	(3,261)
Cash provided by operating activities	5,106	6,223	12,787	12,881
FINANCING ACTIVITIES				
Net proceeds from revolving credit facility	1,690	674	11,210	1,692
Dividends paid to shareholders	(2,039)	(2,028)	(6,099)	(5,915)
Cash used in financing activities	(349)	(1,354)	5,111	(4,223)
INVESTING ACTIVITIES				
Purchase of property, plant and equipment	(4,757)	(4,869)	(17,942)	(8,716)
Proceeds from disposal of property, plant and equipment	-	-	44	58
Cash used in investing activities	(4,757)	(4,869)	(17,898)	(8,658)
Change in cash during the period	-	-	-	-
Cash, beginning of year	-	-	-	-
Cash, end of period	$ -	$ -	$ -	$ -
Supplementary cash flow information				
Interest paid	$ 119	$ 37	$ 288	$ 103
Income taxes paid	$ 974	$ 343	$ 5,215	$ 3,140

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

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 eight processing facilities in seven major cities across Canada from Victoria, British Columbia to Québec City, Québec.

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 November 12, 2013.

1 Basis of Presentation

These unaudited interim condensed consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"), 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, 2012 which have been prepared in accordance with IFRS, as issued by the International Accounting Standards Board. 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, 2013

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 13 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.

(unaudited, thousands of Canadian dollars except share and per share amounts,
three and nine months ended September 30, 2013 and 2012)

3 Property, plant and equipment

	Land	Buildings	Laundry Equipment[1]	Office Equipment	Delivery Equipment	Computer Equipment	Leasehold Improvements[2]	Spare Parts	Total
Year ended, December 31, 2012									
Opening net book amount	$ 125	$ 1,122	$ 24,528	$ 200	$ 641	$ 100	$ 5,687	$ 692	$ 33,095
Additions	-	103	12,249	15	-	95	107	81	12,650
Disposals	-	-	(184)	-	(34)	(2)	-	-	(220)
Depreciation charge	-	(85)	(4,737)	(63)	(90)	(88)	(1,287)	-	(6,350)
Closing net book amount	$ 125	$ 1,140	$ 31,856	$ 152	$ 517	$ 105	$ 4,507	$ 773	$ 39,175
At December 31, 2012									
Cost	$ 125	$ 1,377	$ 58,637	$ 617	$ 913	$ 1,636	$ 11,544	$ 773	$ 75,622
Accumulated depreciation	-	(237)	(26,781)	(465)	(396)	(1,531)	(7,037)	-	(36,447)
Net book amount	$ 125	$ 1,140	$ 31,856	$ 152	$ 517	$ 105	$ 4,507	$ 773	$ 39,175
Nine month period ended, September 30, 2013									
Opening net book amount	**$ 125**	**$ 1,140**	**$ 31,856**	**$ 152**	**$ 517**	**$ 105**	**$ 4,507**	**$ 773**	**$ 39,175**
Additions	**-**	**23**	**10,812**	**64**	**99**	**109**	**6,738**	**97**	**17,942**
Disposals	**-**	**-**	**(74)**	**-**	**(52)**	**-**	**-**	**-**	**(126)**
Transfers	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
Depreciation charge	**-**	**(66)**	**(3,131)**	**(26)**	**(54)**	**(69)**	**(845)**	**-**	**(4,191)**
Closing net book amount	**$ 125**	**$ 1,097**	**$ 39,463**	**$ 190**	**$ 510**	**$ 145**	**$ 10,400**	**$ 870**	**$ 52,800**
At September 30, 2013									
Cost	**$ 125**	**$ 1,400**	**$ 69,164**	**$ 681**	**$ 943**	**$ 1,745**	**$ 18,282**	**$ 870**	**$ 93,210**
Accumulated depreciation	**-**	**(303)**	**(29,701)**	**(491)**	**(433)**	**(1,600)**	**(7,882)**	**-**	**(40,410)**
Net book amount	**$ 125**	**$ 1,097**	**$ 39,463**	**$ 190**	**$ 510**	**$ 145**	**$ 10,400**	**$ 870**	**$ 52,800**

[1] Included in additions to laundry equipment are assets under development in the amount of $8,393. These assets are not available for service and accordingly are not presently being depreciated.

[2] Included in additions to leasehold improvements are assets under development in the amount of $6,699. These assets are not available for service and accordingly are not presently being depreciated.

4 Accounts payable and accrued liabilities

As at September 30, 2013, the Corporation has recognized a liability for the remaining lease payments for decommissioned facilities as a result of the transition to the new Edmonton plant as follows:

- In 2009 the Corporation entered into a non-cancellable lease for corporate office space which, due to the transition to the new Edmonton facility, the Corporation had ceased to use by September 30, 2013. The lease for the office space expires in January 2014.

- In 2004 the Corporation entered into a non-cancellable lease for the building used by the Edmonton plant. In September 2013, the corporation had begun to transition the Edmonton operations to the new Edmonton facility. The lease for the prior building space expires in November 2014.

The charge to occupancy costs as a result of the decommissioned facilities is $713 for the period ended September 30, 2013.

(unaudited, thousands of Canadian dollars except share and per share amounts,
three and nine months ended September 30, 2013 and 2012)

5 Long-term debt

	Bankers Acceptances[1]	Prime Rate Loan[2]	Total Long Term Debt
At January 1, 2012	$ 4,000	$ 2,095	$ 6,095
Repayment of debt	-	(277)	(277)
Closing Balance at December 31, 2012	4,000	1,818	5,818
At January 1, 2013	**$ 4,000**	**$ 1,818**	**$ 5,818**
Draws	**-**	**11,210**	**11,210**
Closing Balance at September 30, 2013	**4,000**	**13,028**	**17,028**

[1] Bankers' Acceptances bear interest at 30 day BA rates plus 1.75% depending on certain financial ratios, renewable monthly until July 31, 2016. As at September 30, 2013, the interest rate was 2.91%.

[2] Prime rate loan, collateralized by a general security agreement, interest at prime plus 1.0% depending on certain financial ratios, monthly repayment of interest only, maturing on July 31, 2016. As at September 30, 2013, the interest rate was 4.0%.

The Corporation has a revolving credit facility of up to $40,000 of which $17,678 is drawn (including letters of credit totaling $650) as at September 30, 2013.

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 $650 (December 31, 2012 – $400) 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:

	September 30, 2013	December 31, 2012
Remainder of 2013	**1,164**	4,160
2014	**4,272**	4,234
2015	**3,723**	3,693
2016	**3,351**	3,323
2017	**3,003**	3,003
Subsequent	**12,688**	12,688
	$ 28,201	$ 31,101

(ii) Linen purchase commitments

At September 30, 2013, the Corporation was committed to linen expenditure obligations in the amount of $3,099 (December 31, 2012 – $2,551) to be incurred within the next year.

(unaudited, thousands of Canadian dollars except share and per share amounts,
three and nine months ended September 30, 2013 and 2012)

(iii) Property, plant and equipment commitments

At September 30, 2013, the Corporation was committed to capital expenditure obligations in the amount of $7,018 (December 31, 2012 – $20,332) to be incurred within the next year.

7 Dividends to shareholders

During the three months ended September 30, 2013, the Corporation declared total dividends to shareholders of $2,039 or $0.288 per share (September 30, 2012 - $2,028 or $0.288 per share). During the nine months ended September 30, 2013, the Corporation declared total dividends to shareholders of $6,103 or $0.862 per share (2012 - $5,949 or $0.825 per share).

8 Net change in non-cash working capital items

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	**2013**	2012
Accounts receivable	**$ (439)**	$ (477)	**$ (619)**	$ 241
Linen in service	**(108)**	(382)	**(213)**	(1,010)
Prepaid expenses and deposits	**(273)**	(217)	**(264)**	(188)
Accounts payable and accrued liabilities	**1,072**	1,010	**718**	(2,209)
Income taxes payable	**80**	664	**(2,198)**	(95)
	$ 332	$ 598	**(2,576)**	$ (3,261)

9 Fair value of financial instruments

The Corporation’s financial instruments at September 30, 2013 consist of accounts receivable, accounts payable and accrued liabilities, dividends payable to shareholders, and long-term debt. The carrying value of accounts receivable, accounts payable and accrued liabilities, and dividends payable to shareholders approximate fair value due to the immediate or short-term maturity of these financial instruments. The fair value of the Corporation’s interest-bearing debt approximates the respective carrying amount due to the floating rate nature of the debt.

10 Related party transactions

The Corporation incurred expenses in the normal course of business for advisory consulting services provided by a Director primarily relating to acquisitions. The amounts charged are recorded at their exchange amounts and are subject to normal trade terms. For the three months ended September 30, 2013, the Corporation incurred such fees totaling $35 (2012 – $35). For the nine months ended September 30, 2013, the Corporation incurred such fees totaling $104 (2012 – $104).

(unaudited, thousands of Canadian dollars except share and per share amounts,
three and nine months ended September 30, 2013 and 2012)

11 Segmented information

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

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. This contract currently expires March 31, 2023. In Calgary, the major customer is contractually committed to February 28, 2018 and in Vancouver a portion of the major customer is contractually committed to November 12, 2015, with the remaining volume committed to November 30, 2020. For the nine months ended September 30, 2013, the Corporation has recorded revenue of $44,050 (2012 – $44,309) from these three major customers, representing 44.6% (2012 – 46.8%) of total revenue.

	Three Months Ended September 30, 2013			Three Months Ended September 30, 2012		
Healthcare	$	21,874	63.3%	$	21,418	64.9%
Hospitality	$	12,677	36.7%		11,595	35.1%
	$	34,551	100.0%	$	33,013	100.0%

	Nine Months Ended September 30, 2013			Nine Months Ended September 30, 2012		
Healthcare	$	66,286	67.1%	$	64,388	68.0%
Hospitality		32,572	32.9%		30,316	32.0%
	$	98,858	100.0%	$	94,704	100.0%

12 Subsequent events

On October 15, 2013, the Board declared an eligible dividend of $0.0958 per common share of the Corporation payable on November 15, 2013 payable to shareholders of record October 31, 2013.

On November 12, 2013, the Board declared an eligible dividend of $0.0958 per common share of the Corporation payable on December 15, 2013 payable to shareholders of record November 30, 2013.