



K·BRO



Q2, 2018
MANAGEMENT'S
DISCUSSION &
ANALYSIS

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 six months ended June 30, 2018 and the audited Consolidated Financial Statements, as well as the MD&A, for the year ended December 31, 2017. 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 13, 2018.

In the interest of providing current holders ("Shareholders") of common shares 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 costs, minimum wage legislation 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; (viii) changes or proposed changes to minimum wage laws in Ontario, British Columbia, Alberta and the United Kingdom (the "UK"), which could have an adverse effect on expenses in respect of employees situated in those jurisdictions and while a portion of such expenses may be passed on to or be recoverable from customers, there can be no assurances that that will occur; (ix) the availability of future financing and (x) foreign exchange rates. 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; (iii) frequency of one-time costs impacting quarterly and annual financial results; (iv) foreign exchange rates; and (v) 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. Forward looking information included in this MD&A includes the expected annual healthcare revenues to be generated from the Corporation's contracts with new customers, the anticipated capital costs for the Toronto and Vancouver facilities, calculation of costs, including one-time costs impacting the quarterly financial results, and statements with respect to future expectations on margins and volume growth.

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 and, therefore, are considered non-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

The Corporation is the largest owner and operator of laundry and linen processing facilities in Canada and a market leader for laundry and textile rental services in Scotland and the North East of England. K-Bro and its wholly owned subsidiaries, operate across Canada and the United Kingdom (“UK”), providing 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’s operations in Canada include nine processing facilities and two distribution centres under three distinctive brands: K-Bro Linen Systems Inc., Buanderie HMR, and Les Buanderies Dextraze. The Corporation operates in ten Canadian cities: Québec City, Montréal, Toronto, Regina, Saskatoon, Prince Albert, Edmonton, Calgary, Vancouver and Victoria.

The Corporation’s operations in the UK include Fishers Topco Ltd. (“Fishers”) which was acquired by K-Bro on November 27, 2017. Fishers was established in 1900 and is a leading operator of laundry and linen processing facilities in Scotland, providing linen rental, workwear hire and cleanroom garment services to the hospitality, healthcare, manufacturing and pharmaceutical sectors. The Corporation operates seven sites, including one distribution center, which are located in Cupar, Perth, Newcastle, Livingston, Inverness and Coatbridge.

Industry and Market

In Canada, K-Bro provides laundry and linen services to 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 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 Canadian laundry and linen services industry, such as uniform rental companies (which own and launder uniforms worn by their customers’ employees) typically do not offer services that significantly overlap with those offered by K-Bro.

In the UK, Fishers provides laundry and linen services to healthcare, hospitality and other commercial customers. Typical services offered by Fishers include the processing, management and distribution of general linen, workwear and clean room garment services. Other types of processors in Fishers industry in the UK include publicly traded companies, independent privately owned facilities (i.e., typically, small single facility companies), public sector central laundries and public and private sector OPLs.

Our partnerships with healthcare institutions and hospitality clients across Canada and the UK demonstrate K-Bro’s commitment to building relationships that foster continuous improvement, providing flexibility to adjust to changing circumstances as required and which incorporate incentives, penalties and the sharing of risks and rewards as circumstances warrant.

In this competitive industry, K-Bro is distinctive 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 Cyclicalities – As evidenced by the stability in the number of approved hospital beds in the healthcare system and hotel rooms in the hospitality industry. The potential for step-changes in volumes and revenues that align with contractual arrangements exists within this industry. Service relationships are generally formalized through contracts in the healthcare sector that are typically long term (from five to ten years), while contracts in the hospitality sector usually range from two to five years.

Outsourcing and Privatization – In Canada, 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 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 Canadian customers include some of the largest healthcare institutions and hospitality providers in Canada. In the UK, Fishers customers include some of the largest hotel chains operating in Scotland. Healthcare customers include acute care hospitals and long-term care facilities primarily in Canada. Most of K-Bro's hospitality customers (typically greater than 250 rooms) generate between 0.5 million and 3 million pounds of linen per year. Most healthcare customers generate between 0.5 million pounds of linen per year for a hospital and up to 41 million pounds of linen per year for a Canadian healthcare region.

SELECTED QUARTERLY FINANCIAL INFORMATION

<i>(thousands, except percentages and per share amounts)</i>	Canadian Division	UK ⁽¹⁾ Division	Three Months Ended June 30,		
	2018	2018	2018	2017 ⁽¹⁾	2016 ⁽¹⁾
Revenue	\$ 44,658	\$ 16,080	\$ 60,738	\$ 40,494	\$ 39,469
Earnings before income taxes	2,147	1,318	3,465	3,350	4,712
Net earnings	1,421	1,163	2,584	2,337	3,384
<i>Net earnings per share:</i>					
Basic	\$ 0.136	\$ 0.111	\$ 0.247	\$ 0.257	\$ 0.426
Diluted	\$ 0.135	\$ 0.111	\$ 0.246	\$ 0.256	\$ 0.425
Total assets			\$ 317,051	\$ 195,957	\$ 148,068
Long-term debt			70,505	-	7,252
<i>Weighted average number of shares outstanding:</i>					
Basic			10,462,213	9,103,510	7,951,901
Diluted			10,508,644	9,133,276	7,964,583

<i>(thousands, except percentages and per share amounts)</i>	Canadian Division	UK ⁽¹⁾ Division	Six Months Ended June 30,		
	2018	2018	2018	2017 ⁽¹⁾	2016 ⁽¹⁾
Revenue	\$ 87,950	\$ 28,172	\$ 116,122	\$ 79,452	\$ 78,281
Earnings before income taxes	3,736	770	4,506	5,120	8,358
Net earnings	2,469	762	3,231	3,587	5,916
<i>Net earnings per share:</i>					
Basic	\$ 0.236	\$ 0.073	\$ 0.309	\$ 0.420	\$ 0.744
Diluted	\$ 0.235	\$ 0.073	\$ 0.308	\$ 0.418	\$ 0.743
Total assets			\$ 317,051	\$ 195,957	\$ 148,068
Long-term debt			70,505	-	7,252
<i>Weighted average number of shares outstanding:</i>					
Basic			10,457,941	8,544,285	7,948,949
Diluted			10,496,023	8,574,839	7,957,525

(1) Prior to the acquisition of Fishers on November 27, 2017, K-Bro was reporting and operating as a single Canadian division.

SUMMARY OF INTERIM RESULTS, AND KEY EVENTS

Financial Growth

Net earnings for the second quarter were \$2.6 million or \$0.25 per share (basic). Cash used in operating activities for the quarter was \$4.6 million and distributable cash flow was \$6.5 million. Revenue increased in the second quarter of 2018 to \$60.7 million or by 50.0% compared to 2017. This increase was due to volume from the acquisition of Fishers, additional awarded healthcare volume from the Vancouver lower mainland contract, Trillium Health Partners volume, organic growth at existing customers, and new customers secured in existing markets.

EBITDA (see Terminology) increased in the second quarter to \$8.5 million from \$6.7 million in 2017, which is an increase of 27.0%. On a consolidated basis, the EBITDA margin decreased from 16.4% in 2017 to 13.9% in 2018. For the Canadian division, the EBITDA margin decreased to 13.2% from 16.4% for the comparative quarter of 2017. The change in the Canadian EBITDA margin, relates to capacity constraints as a result of the Vancouver transition as well as rising minimum wage rates in advance of future revenue price escalators, offset with the efficiencies gained as a result of the capital expenditures made in Toronto. Management estimates the one-time costs incurred related to the Vancouver transition for the quarter were approximately \$2.0 million. After adjusting for these one-time costs, the Canadian EBITDA margin would have been 17.7% as compared to 13.2% on an unadjusted basis.

Near-Term and Long-Term Growth and Margin Impact

Management has embarked on a strategy in its Toronto and Vancouver markets that it believes will position K-Bro for accelerated growth in its healthcare and hospitality businesses. The strategy includes capital investments to build large efficient state-of-the-art facilities with meaningful additional capacity in Toronto and Vancouver. In addition, K-Bro is investing to upgrade one of its current Vancouver plants to create a more efficient facility with meaningful additional capacity.

These investments are being made because management believes that new opportunities, both current and future, justify the significant additional capacity. The construction and/or upgrade of three of our large facilities will enable us to bid on a significant amount of additional business, and create margin pressure through 2018 as K-Bro incurs one-time and transition costs associated with these large investments. While the margin pressure will vary by quarter through 2018, management believes that the one-time and transition costs incurred in 2018 will position K-Bro to achieve more growth and a lower cost structure into the future and that K-Bro will return to normalized margins closer to those achieved in 2015 in 2019.

Key events in our Toronto and Vancouver markets are summarized below.

Vancouver Facility Development

As announced on March 2, 2016, K-Bro commenced the development of a new state-of-the-art facility with projected investment of up to \$55 million. As at June 30, 2018, K-Bro has incurred \$49.1 million of the total expected capital costs. The new Vancouver plant is located in Burnaby, and K-Bro began transitioning to the new facility during the second quarter of 2018. The new facility will enable K-Bro to expand current capacity, to accommodate the additional awarded volume, and to provide the opportunity to consolidate the healthcare volume from its existing two Vancouver-area facilities. In addition to investing in the new facility, K-Bro is upgrading and replacing equipment at one of its existing Vancouver-area facilities, which will be used to process the consolidated hospitality volume. K-Bro will not be renewing the lease for the remaining Vancouver-area facility and related assets will be transferred to the other K-Bro facilities. K-Bro believes it will achieve significant operating efficiencies at its new plant. It is anticipated that transition costs associated with the new Vancouver plant will continue to negatively impact EBITDA margins over the third and fourth quarters of 2018 while the plants becomes operational.

Toronto Facility Development

Management estimates that the cost to commission the new leased facility would be \$37 million for new efficiency enhancing equipment, and leaseholds. As at June 30, 2018, K-Bro has incurred \$37 million of the total expected capital cost. K-Bro's strategy includes significant growth in its healthcare and hospitality volumes, and the additional capacity and the long-term lease enable K-Bro to grow into the additional capacity as opportunities emerge.

Alberta Contract Awards

On March 1, 2018, K-Bro was awarded a one year extension to provide laundry and linen services to Calgary Alberta Health Services. The contract extends the existing relationship between K-Bro and Alberta Health Services Calgary.

Business Acquisition

On May 9, 2018, the Corporation signed an asset purchase agreement to acquire all the assets of a private laundry and linen services company incorporated in Canada and operating in Calgary, Alberta. The acquisition is expected to close on October 1, 2018 for total consideration of \$4.7 million. The acquisition will be accounted for using the acquisition method, whereby the purchase consideration will be allocated to the net

assets acquired. The acquisition is expected to add incremental revenue and EBITDA of \$3.5 million and \$0.6 million respectively on an annual basis.

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.

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.

Effects of Economic Uncertainty

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

- Approximately 55.2% of its revenues in the quarter were from large publicly funded Canadian healthcare customers which are geographically diversified across multiple provinces;
- At June 30, 2018, K-Bro had unutilized borrowing capacity of \$27.8 million or 27.8% 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.

RESULTS OF OPERATIONS

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 in the long term. The following outlines our results on a period-to-period comparative basis in each of these areas:

<i>(thousands, except percentages and per share amounts)</i>		Canadian	UK ⁽³⁾			Canadian	UK ⁽³⁾		
Category	Indicator	Division	Division	Q2 2018	Q2 2017 ⁽⁴⁾	Division	Division	YTD 2018	YTD 2017 ⁽⁴⁾
		Q2 2018	Q2 2018			YTD 2018	YTD 2018		
Growth	EBITDA ⁽¹⁾	-11.4%		27.0%	-11.2%	0.0%		28.3%	-20.0%
	Revenue	10.3%		50.0%	2.6%	10.7%		46.2%	1.5%
	Distributable cash flow			17.1%	7.1%			16.4%	-4.0%
Profitability	EBITDA ⁽¹⁾⁽⁴⁾	\$ 5,900	\$ 2,552	\$ 8,452	\$ 6,657	\$ 11,418	\$ 3,234	\$ 14,652	\$ 11,421
	EBITDA margin	13.2%	15.9%	13.9%	16.4%	13.0%	11.5%	12.6%	14.4%
	Net earnings	\$ 1,421	\$ 1,163	\$ 2,584	\$ 2,337	\$ 2,469	\$ 762	\$ 3,231	\$ 3,587
Stability	Debt to total capitalization ⁽²⁾			26.8%	0.0%			26.8%	0.0%
	Unutilized line of credit			\$ 27,845	\$ 83,350			\$ 27,845	\$ 83,350
	Cash on hand			\$ 8,150	\$ 5,313			\$ 8,150	\$ 11,276
	Payout ratio			48.8%	51.8%			54.1%	52.6%
	Dividends declared per share			\$ 0.300	\$ 0.300			\$ 0.600	\$ 0.600
Cost containment	Wages and benefits	42.6%	35.7%	40.7%	40.9%	42.9%	36.8%	41.4%	41.5%
	Utilities	5.4%	6.8%	5.8%	5.7%	5.7%	7.1%	6.1%	6.3%
	Expenses included in EBITDA	86.8%	84.1%	86.1%	83.6%	87.0%	88.5%	87.4%	85.6%

(1) EBITDA is defined as revenue less operating expenses (which equates to net earnings before income tax, finance expense (recovery) and depreciation and amortization). See Terminology.

(2) Debt to total capitalization is defined as total debt divided by total capital. See Terminology.

(3) Prior to the acquisition of Fishers on November 27, 2017, K-Bro was reporting and operating as a single Canadian division.

(4) EBITDA in prior periods has been restated with 'gain (loss) on disposal of assets' in included expenses.

Quarterly Financial Information - Consolidated

Historically, the Corporation's financial and operating results, particularly as it relates to Fishers, are stronger in the second and third quarters as a result of seasonality and the associated higher hospitality volumes. Other fluctuations in net income from quarter-to-quarter can also be attributed to hiring and labour cost trends, timing of linen purchases, utility costs, timing of repairs and maintenance expenditures, business development, capital spending patterns and changes in corporate tax rates and income tax expenses.

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

Quarterly Financial Information - Consolidated (thousands, except percentages and per share amounts)	2018		2017				2016	
	Q2	Q1	Q4	Q3	Q2	Q1	Q4	Q3
Healthcare revenue	35,400	32,065	31,385	29,021	28,499	28,053	28,374	27,333
Hospitality revenue	25,338	23,319	16,124	14,577	11,995	10,905	10,877	14,224
Total revenue	60,738	55,384	47,509	43,598	40,494	38,958	39,251	41,557
Expenses included in EBITDA ⁽⁴⁾	52,286	49,184	43,056	35,487	33,837	34,194	32,930	34,019
EBITDA ⁽¹⁾⁽⁴⁾	8,452	6,200	4,453	8,111	6,657	4,764	6,321	7,538
EBITDA as a % of revenue (EBITDA margin)	13.9%	11.2%	9.4%	18.6%	16.4%	12.2%	16.1%	18.1%
Adjusted EBITDA ⁽²⁾	8,452	6,200	7,284	8,111	6,657	4,764	6,321	7,538
Adjusted EBITDA as a % of revenue (Adjusted EBITDA margin)	13.9%	11.2%	15.3%	18.6%	16.4%	12.2%	16.1%	18.1%
Depreciation and amortization	4,271	4,283	4,105	3,213	3,246	2,809	2,866	2,748
Finance expense (recovery)	716	876	786	101	61	185	247	(11)
Earnings (loss) before income taxes	3,465	1,041	(438)	4,797	3,350	1,770	3,208	4,801
Income tax expense	881	394	849	1,379	1,013	520	1,011	1,387
Net earnings (loss)	2,584	647	(1,287)	3,418	2,337	1,250	2,197	3,414
Net earnings (loss) as a % of revenue	4.3%	1.2%	-2.7%	7.8%	5.8%	3.2%	5.6%	8.2%
Basic earnings (loss) per share	0.247	0.062	(0.132)	0.359	0.257	0.157	0.276	0.429
Diluted earnings (loss) per share	0.246	0.062	(0.132)	0.358	0.256	0.156	0.274	0.427
Adjusted net earnings ⁽³⁾	2,584	647	1,544	3,418	2,337	1,250	2,197	3,414
Basic adjusted earnings (loss) per share ⁽³⁾	0.247	0.062	0.159	0.359	0.257	0.157	0.276	0.429
Diluted adjusted earnings (loss) per share ⁽³⁾	0.246	0.062	0.158	0.358	0.256	0.156	0.274	0.427
Total assets	317,051	312,193	295,213	199,452	195,957	180,583	168,289	153,923
Total long-term financial liabilities	86,675	72,189	57,594	9,205	8,407	41,134	33,949	17,596
Funds provided by (used in) operations	(4,629)	4,625	6,395	3,788	2,297	6,300	6,071	7,581
Long-term debt	70,505	56,356	42,780	-	-	32,363	25,800	10,338
Dividends declared per share	0.300	0.300	0.300	0.300	0.300	0.300	0.300	0.300

- (1) EBITDA is defined as revenue less operating expenses (which equates to net earnings before income tax, finance expense (recovery) and depreciation and amortization). See Terminology.
- (2) Adjusted EBITDA is defined as EBITDA (defined above) with the exclusion of certain material items that are unusual in nature, infrequently occurring or not considered part of our core operations. See Terminology for a complete description of the adjusted items.
- (3) Adjusted net earnings is defined as net earnings with the exclusion of certain material items that are unusual in nature, infrequently occurring or not considered part of our core operations. See Terminology for a complete description of the adjusted items.
- (4) EBITDA in prior periods has been restated with 'gain (loss) on disposal of assets' in included expenses.

Quarterly Financial Information – Canadian Division

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

Quarterly Financial Information - Canadian Division (thousands, except percentages and per share amounts)	2018		2017				2016	
	Q2	Q1	Q4	Q3	Q2	Q1	Q4	Q3
Healthcare revenue	32,193	32,010	31,375	29,021	28,499	28,053	28,374	27,333
Hospitality revenue	12,465	11,282	11,406	14,577	11,995	10,905	10,877	14,224
Total revenue	44,658	43,292	42,781	43,598	40,494	38,958	39,251	41,557
Expenses included in EBITDA ⁽⁴⁾	38,758	37,774	35,820	35,487	33,837	34,194	32,930	34,019
EBITDA ⁽¹⁾⁽⁴⁾	5,900	5,518	6,961	8,111	6,657	4,764	6,321	7,538
EBITDA as a % of revenue (EBITDA margin)	13.2%	12.7%	16.3%	18.6%	16.4%	12.2%	16.1%	18.1%
Adjusted EBITDA ⁽²⁾	5,900	5,518	6,961	8,111	6,657	4,764	6,321	7,538
Adjusted EBITDA as a % of revenue (Adjusted EBITDA margin)	13.2%	12.7%	16.3%	18.6%	16.4%	12.2%	16.1%	18.1%
Depreciation and amortization	3,040	3,058	3,708	3,213	3,246	2,809	2,866	2,748
Finance expense (recovery)	713	871	768	101	61	185	247	(11)
Earnings before income taxes	2,147	1,589	2,485	4,797	3,350	1,770	3,208	4,801
Income tax expense	726	541	891	1,379	1,013	520	1,011	1,387
Net earnings	1,421	1,048	1,594	3,418	2,337	1,250	2,197	3,414
Net earnings as a % of revenue	3.2%	2.4%	3.7%	7.8%	5.8%	3.2%	5.6%	8.2%
Basic earnings per share	0.136	0.100	0.164	0.359	0.257	0.157	0.276	0.429
Diluted earnings per share	0.135	0.100	0.163	0.358	0.256	0.156	0.274	0.427
Adjusted net earnings ⁽³⁾	1,421	1,048	1,594	3,418	2,337	1,250	2,197	3,414
Basic adjusted earnings per share ⁽³⁾	0.136	0.100	0.164	0.359	0.257	0.157	0.276	0.429
Diluted adjusted earnings per share ⁽³⁾	0.135	0.100	0.163	0.358	0.256	0.156	0.274	0.427

- (1) EBITDA is defined as revenue less operating expenses (which equates to net earnings before income tax, finance expense (recovery) and depreciation and amortization). See Terminology.
- (2) Adjusted EBITDA is defined as EBITDA (defined above) with the exclusion of certain material items that are unusual in nature, infrequently occurring or not considered part of our core operations. See Terminology for a complete description of the adjusted items.
- (3) Adjusted net earnings is defined as net earnings with the exclusion of certain material items that are unusual in nature, infrequently occurring or not considered part of our core operations. See Terminology for a complete description of the adjusted items.
- (4) EBITDA in prior periods has been restated with 'gain (loss) on disposal of assets' in included expenses.

Quarterly Financial Information – UK Division

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

Quarterly Financial Information - UK Division (in reporting currency Canadian \$) (thousands, except percentages and per share amounts)	2018		2017			2016		
	Q2	Q1	Q4	Q3	Q2	Q1	Q4	Q3
Healthcare revenue	3,207	55	10	-	-	-	-	-
Hospitality revenue	12,873	12,037	4,718	-	-	-	-	-
Total revenue	16,080	12,092	4,728	-	-	-	-	-
Expenses included in EBITDA	13,528	11,410	7,236	-	-	-	-	-
EBITDA ⁽¹⁾	2,552	682	(2,508)	-	-	-	-	-
EBITDA as a % of revenue (EBITDA margin)	15.9%	5.6%	-53.0%	-	-	-	-	-
Adjusted EBITDA ⁽²⁾	2,552	682	323	-	-	-	-	-
Adjusted EBITDA as a % of revenue (Adjusted EBITDA margin)	15.9%	5.6%	6.8%	-	-	-	-	-
Depreciation and amortization	1,231	1,225	397	-	-	-	-	-
Finance expense (recovery)	3	5	18	-	-	-	-	-
Earnings (loss) before income taxes	1,318	(548)	(2,923)	-	-	-	-	-
Income tax expense (recovery)	155	(147)	(42)	-	-	-	-	-
Net earnings (loss)	1,163	(401)	(2,881)	-	-	-	-	-
Net earnings (loss) as a % of revenue	7.2%	-3.3%	-60.9%	-	-	-	-	-
Basic earnings (loss) per share	0.111	(0.038)	(0.296)	-	-	-	-	-
Diluted earnings (loss) per share	0.111	(0.038)	(0.295)	-	-	-	-	-
Adjusted net earnings (loss) ⁽³⁾	1,163	(401)	(50)	-	-	-	-	-
Basic adjusted earnings (loss) per share ⁽³⁾	0.111	(0.038)	(0.005)	-	-	-	-	-
Diluted adjusted earnings (loss) per share ⁽³⁾	0.111	(0.038)	(0.005)	-	-	-	-	-

Quarterly Financial Information - UK Division (in local currency Sterling £) (thousands, except percentages and per share amounts)	2018		2017			2016		
	Q2	Q1	Q4	Q3	Q2	Q1	Q4	Q3
Healthcare revenue	1,824	31	6	-	-	-	-	-
Hospitality revenue	7,329	6,835	2,755	-	-	-	-	-
Total revenue	9,153	6,866	2,761	-	-	-	-	-
Expenses included in EBITDA	7,700	6,480	4,227	-	-	-	-	-
EBITDA ⁽¹⁾	1,453	386	(1,466)	-	-	-	-	-
EBITDA as a % of revenue (EBITDA margin)	15.9%	5.6%	-53.1%	-	-	-	-	-
Adjusted EBITDA ⁽²⁾	1,453	386	188	-	-	-	-	-
Adjusted EBITDA as a % of revenue (Adjusted EBITDA margin)	15.9%	5.6%	6.8%	-	-	-	-	-
Depreciation and amortization	700	696	232	-	-	-	-	-
Finance expense (recovery)	2	3	(3)	-	-	-	-	-
Earnings (loss) before income taxes	751	(313)	(1,695)	-	-	-	-	-
Income tax expense (recovery)	89	(84)	(25)	-	-	-	-	-
Net earnings (loss)	662	(229)	(1,670)	-	-	-	-	-
Net earnings (loss) as a % of revenue	7.2%	-3.3%	-60.5%	-	-	-	-	-
Basic earnings (loss) per share	0.063	(0.022)	(0.172)	-	-	-	-	-
Diluted earnings (loss) per share	0.063	(0.022)	(0.171)	-	-	-	-	-
Adjusted net earnings (loss) ⁽³⁾	660	(229)	(16)	-	-	-	-	-
Basic adjusted earnings (loss) per share ⁽³⁾	0.063	(0.022)	(0.002)	-	-	-	-	-
Diluted adjusted earnings (loss) per share ⁽³⁾	0.063	(0.022)	(0.002)	-	-	-	-	-

- (1) EBITDA is defined as revenue less operating expenses (which equates to net earnings before income tax, finance expense (recovery) and depreciation and amortization). See Terminology.
- (2) Adjusted EBITDA is defined as EBITDA (defined above) with the exclusion of certain material items that are unusual in nature, infrequently occurring or not considered part of our core operations. See Terminology for a complete description of the adjusted items.
- (3) Adjusted net loss is defined as net earnings with the exclusion of certain material items that are unusual in nature, infrequently occurring or not considered part of our core operations. See Terminology for a complete description of the adjusted items.

Revenue, Earnings and EBITDA

For the three months ended June 30, 2018, K-Bro's revenue increased by 50.0% to \$60.7 million from \$40.5 million in the comparative period, and on a year-to-date basis K-Bro's revenue increased by 46.2% to \$116.1 million from \$79.5 million in the comparative period. This increase was due to the acquisition of Fishers, additional awarded healthcare volume from the Vancouver lower mainland contract signed in 2016, Trillium Health Partners volume, organic growth at existing customers, and new customers secured in existing markets.

For the three months ended June 30, 2018, approximately 58.3% of K-Bro's revenue was generated from healthcare institutions compared to 70.4% in Q2, 2017. On a year-to-date basis, approximately 58.0% of K-Bro's revenue was generated from healthcare institutions compared to 71.2% in Q2, 2017. This decrease is primarily related to Fishers' volume being concentrated within the hospitality sector.

EBITDA increased to \$8.5 million for the three months ended June 30, 2018, compared to \$6.7 million in the comparative period of 2017, and on a year-to-date basis EBITDA increased to \$14.7 million compared to \$11.4 million in 2017. The change in EBITDA and margin is primarily associated with the efficiencies gained as a result of the capital expenditures made in Toronto, volume related to the acquisition of Fishers, offset by Vancouver transition costs and rising minimum wage rates the timing of which is not offset by price increases. Management estimates the one-time costs incurred related to the Vancouver transition for the quarter were approximately \$2.0 million. After adjusting for these one-time costs, the Canadian EBITDA margin would have been 17.7% as compared to 13.2% on an unadjusted basis.

For the three months ended June 30, 2018, net earnings increased by \$0.3 million or 10.6% from \$2.3 million in 2017 to \$2.6 million in 2018, and net earnings as a percentage of revenue decreased by 1.5% to 4.3% in 2018 from 5.8% in 2017. On a year-to-date basis, net earnings decreased by \$0.4 million or 9.9% from \$3.6 million in 2017 to \$3.2 million in 2018, and net earnings as a percentage of revenue decreased by 1.7% to 2.8% in 2018 from 4.5% in 2017. This decrease in net earnings is primarily due to the flow through items in EBITDA discussed above, higher finance costs related with the revolving credit facility, higher depreciation of property, plant and equipment associated with new plant builds and the acquisition of Fishers, offset by a lower income tax expense.

Operating Expenses

Wages and benefits in the second quarter increased to \$24.7 million in 2018 from \$16.6 million in 2017, and decreased as a percentage of revenue from 40.9% in 2017 to 40.7% in the same period of 2018. This includes \$5.7 million related to our UK Division. On a year-to-date basis, wages and benefits increased to \$48.1 million in 2018 from \$32.9 million in 2017, and decreased as a percentage of revenue from 41.5% in 2017 to 41.4% in the same period of 2018. This includes \$10.4 million related to our UK Division. The remaining increase in wages and benefits in the period is due to the incremental labour required to process the higher volumes, significant overtime costs and one-time costs related to the Vancouver transition, and rising labour costs from incremental increases in the wage rate.

Linen expenses in the second quarter increased to \$6.8 million in 2018 from \$4.5 million in 2017, and increased as a percentage of revenue to 11.2% from 11.1% in 2017. This includes \$1.8 million related to our UK Division. On a year-to-date basis, linen expenses increased to \$13.2 million in 2018 from \$8.9 million in 2017, and increased as a percentage of revenue to 11.4% from 11.2% in 2017. This includes \$3.1 million related to our UK Division. The remaining increase is a result of increased healthcare volumes from new Canadian customers and the associated linen costs.

Utility costs in the second quarter increased to \$3.5 million compared to \$2.3 million in 2017 and increased as a percentage of revenue to 5.8% from 5.7% in 2017. This includes \$1.1 million related to our UK Division. On a year-to-date basis, utility costs increased to \$7.0 million compared to \$5.0 million in 2017 and decreased as a percentage of revenue to 6.1% from 6.3% in 2017. This includes \$2.0 million related to our UK Division. The

remaining variance is primarily due to the incremental volume processed, higher carbon levy rates in Alberta, offset by improved efficiencies in the new Toronto facility.

Delivery costs in the second quarter increased to \$7.4 million and to 12.2% as a percentage of revenues compared to \$4.1 million and 10.2% in Q2, 2017. This includes \$2.7 million related to our UK Division. On a year-to-date basis, delivery costs increased to \$14.8 million and to 12.7% as a percentage of revenues compared to \$8.3 million and 10.5% in 2017. This includes \$5.3 million related to our UK Division. The remaining increase is a result of increased business activity, measures to address temporary capacity constraints at our Vancouver facilities, higher carbon levy rates in Alberta, and higher cost of diesel and external freight charges tied to diesel price.

Occupancy costs in the second quarter increased to \$2.5 million and to 4.1% as a percentage of revenue, compared to \$1.7 million and 4.1% in Q2, 2017. This includes \$0.7 million related to our UK Division. On a year-to-date basis, occupancy costs increased to \$4.8 million and to 4.1% as a percentage of revenue, compared to \$3.1 million and 3.9% in 2017. This includes \$1.3 million related to our UK Division. The remaining increase is a result of 2018 being reflective of a full year of the occupancy costs related to the new Toronto facility and additional occupancy costs in Vancouver related to our plant build out strategy.

Materials and supplies in the second quarter increased to \$2.0 million and to 3.3% as a percentage of revenue, compared to \$1.2 million and 3.0% in Q2, 2017. This includes \$0.7 million related to our UK Division. On a year-to-date basis, materials and supplies increased to \$4.0 million and to 3.4% as a percentage of revenue, compared to \$2.7 million and 3.4% in 2017. This includes \$1.3 million related to our UK Division. Materials and supplies as a percent of revenue increased primarily related to higher costs due to the transition of our Vancouver facilities and certain one-time set-up costs that were required.

Repairs and maintenance in the second quarter increased to \$2.3 million and to 3.8% as a percentage of revenues, compared to \$1.2 million and 3.0% in Q2, 2017. This includes \$0.3 million related to our UK Division. On a year-to-date basis, repairs and maintenance increased to \$4.1 million and to 3.5% as a percentage of revenues, compared to \$2.6 million and 3.3% in 2017. This includes \$0.7 million related to our UK Division. Changes in repairs and maintenance are primarily due to the timing of scheduled maintenance activities and one-time costs related to the transition of our Vancouver facilities.

Corporate costs in the second quarter increased to \$3.0 million and to 5.0% as a percentage of revenues compared to \$2.2 million and 5.5% in Q2, 2017. This includes \$0.4 million related to our UK Division. On a year-to-date basis, corporate costs increased to \$5.5 million and to 4.7% as a percentage of revenues compared to \$4.4 million and 5.5% in 2017. This includes \$0.9 million related to our UK Division. Changes in corporate costs are primarily related to the timing of costs and initiatives to support the Corporation's growth and business strategies across the plants.

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. The increase during the quarter is related to the completion of the new Toronto and Vancouver facilities and the acquisition of Fishers.

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 provision on the earnings of the Corporation.

LIQUIDITY AND CAPITAL RESOURCES

For the six months ended June 30, 2018, the Corporation's distributable cash flow was \$11.7 million with a debt to total capitalization of 26.8%. Due to the strategic plans K-Bro expects to execute in the coming fiscal year, management expects the debt to total capitalization to increase, mainly as a result of strategic capital expenditures as part of the investment in the new Vancouver facility. Management believes the unutilized balance of \$27.8 million with respect to its revolving credit facility is sufficient for the Corporation's operations in the foreseeable future. However, management intends to continually assess its opportunities to maintain a conservative amount of leverage and balance sheet flexibility in the short and long-term basis in order to ensure that sufficient capital is available for future growth needs.

In Q2, 2018 cash used in operating activities was \$4.6 million, compared to cash generated by operating activities \$2.3 million during Q2, 2017. On a year-to-date basis, cash used in operating activities was \$0.0 million, compared to cash generated by operating activities of \$8.6 million in 2017. The change in cash from operations is primarily due to the change in working capital items driven mainly from the timing of business activity.

During Q2, 2018, cash generated by financing activities was \$11.0 million compared to \$19.9 million in Q2, 2017. On a year-to-date basis, cash generated by financing activities was \$21.4 million compared to \$24.1 million in 2017. Financing activities in Q2, 2018 consisted of net proceeds from the revolving credit facility, offset by dividends paid to shareholders.

During Q2, 2018, cash used in investing activities was \$7.6 million compared to \$16.9 million in Q2, 2017. On a year-to-date basis, cash used in investing activities was \$24.8 million compared to \$27.4 million in 2017. Investing activities related primarily to the purchase of plant equipment for the new Vancouver plant and the purchase of equipment in existing plants to facilitate strategic growth.

Contractual Obligations

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	\$ 70,505	-	70,505	-	-
Operating lease commitments	\$ 64,017	5,251	15,084	11,390	32,292
Utility commitments	\$ 6,840	2,991	2,575	1,274	-
Linen purchase obligations	\$ 7,973	7,973	-	-	-
Property, plant and equipment commitments	\$ 11,095	11,095	-	-	-

The operating lease obligations are secured by automotive equipment and plants, 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

	Six months ended June 30,	Year ended December
<i>(thousands, except percentages)</i>	2018	2017
Cash and cash equivalents	\$ (8,150)	\$ (11,276)
Long-term debt	70,505	42,780
Shareholders' equity	201,068	201,587
Total capitalization	\$ 263,423	\$ 233,091
Debt to total capitalization (see <i>Terminology</i> for definition)	26.8%	18.4%

For the quarter ended June 30, 2018, the Corporation had a debt to total capitalization of 26.8%, unused revolving credit facility of \$27.8 million and has not incurred any events of default under the terms of its credit facility agreement.

As at June 30, 2018, the Corporation had net working capital of \$46.6 million compared to its working capital position of \$32.0 million at December 31, 2017. The increase in working capital is primarily attributable to, timing differences related to the cash settlement of new plant equipment, timing of income tax recovery, the seasonality of hospitality volume processed at Fishers, and deposits related to the acquisition of equipment related across the plants.

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	2018		2017	
			Amount per Share	Total Amount (1)(3)	Amount per Share	Total Amount (2)(4)
January	February 15	10,508,502	\$ 0.10000	\$ 1,051	\$ 0.10000	\$ 802
February	March 15	10,508,502	0.10000	1,051	0.10000	802
March	April 13	10,508,502	0.10000	1,051	0.10000	802
Q1			\$ 0.30000	\$ 3,153	\$ 0.30000	\$ 2,407
April	May 15	10,508,502	\$ 0.10000	\$ 1,051	\$ 0.10000	\$ 954
May	June 15	10,559,936	0.10000	1,056	0.10000	958
June	July 13	10,559,936	0.10000	1,056	0.10000	958
Q2			\$ 0.30000	\$ 3,163	\$ 0.30000	\$ 2,871
YTD			\$ 0.60000	\$ 6,315	\$ 0.60000	\$ 5,278

- (1) The total amount of dividends declared was \$0.10000 per share for a total of \$1,050,850 per month for January - March 2018; when rounded in thousands, \$3,153 of dividends were declared for the quarterly period.
- (2) The total amount of dividends declared was \$0.10000 per share for a total of \$802,348 per month for January - March 2017; when rounded in thousands, \$2,407 of dividends were declared for the quarterly period.
- (3) The total amount of dividends declared was \$0.10000 per share for a total of \$1,050,850 for April 2018, and \$1,055,994 per month for May - June 2018. When rounded in thousands, \$3,163 of dividends were declared for the quarterly period.
- (4) The total amount of dividends declared was \$0.10000 per share for a total of \$954,148 for April 2017, \$958,390 for May 2017, and \$958,390 for June 2017. When rounded in thousands, \$2,871 of dividends were declared for the quarterly period.

For the three months ended June 30, 2018, the Corporation declared a \$0.300 per share dividend compared to \$0.617 per Share of Distributable Cash Flow (see *Terminology*). The payout ratio for the three months ended June 30, 2018 was 48.8%.

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 percentages and per share amounts)</i>	2018		2017				2016	
	Q2	Q1	Q4	Q3	Q2	Q1	Q4	Q3
Cash provided by (used in) operating activities	\$ (4,629)	\$ 4,625	\$ 6,395	\$ 3,788	\$ 2,297	\$ 6,300	\$ 6,071	\$ 7,581
<i>Deduct (add):</i>								
Net changes in non-cash working capital items ⁽¹⁾	(12,167)	(1,471)	2,942	(3,917)	(4,161)	1,214	(336)	1,102
Share-based compensation expense	625	409	333	276	494	405	368	337
Maintenance capital expenditures ⁽²⁾	430	488	349	192	427	179	264	289
Distributable cash flow	\$ 6,483	\$ 5,199	\$ 2,771	\$ 7,237	\$ 5,537	\$ 4,502	\$ 5,775	\$ 5,853
Dividends declared	3,163	3,153	2,968	2,875	2,871	2,407	2,407	2,407
Dividends declared per share	0.300	0.300	0.300	0.300	0.300	0.300	0.300	0.300
Payout ratio ⁽³⁾	48.8%	60.6%	107.1%	39.7%	51.8%	53.5%	41.7%	41.1%
Weighted average shares outstanding during the period, basic	10,462	10,454	9,718	9,511	9,104	7,979	7,965	7,957
Weighted average shares outstanding during the period, diluted	10,509	10,491	9,755	9,548	9,133	7,999	8,004	7,991
Trailing-twelve months ("TTM")								
Distributable cash flow	21,690	20,744	20,047	23,051	21,667	21,298	22,081	20,908
Dividends	12,159	11,867	11,121	10,560	10,092	9,624	9,613	9,602
Payout ratio ⁽³⁾	56.1%	57.2%	55.5%	45.8%	46.6%	45.2%	43.5%	45.9%

(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) Maintenance capital expenditures include costs required to maintain or replace assets which do not have a discrete return on investment.

(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 divided by the distributable cash flow.

OUTSTANDING SHARES

As at June 30, and August 13, 2018, the Corporation had 10,559,936 common shares outstanding. Basic and diluted weighted average number of common shares outstanding for the three months ended June 30, 2018 were 10,462,213 and 10,508,644, respectively (9,103,510 and 9,133,276, respectively, for the comparative 2017 interim periods).

In accordance with the LTI plan and in conjunction with the performance of the Corporation in the 2017 fiscal year, on April 16, 2018 the Compensation, Nominating and Corporate Governance Committee of the Board of Directors approved LTI compensation of \$1.6 million (2017 – \$1.7 million) to be paid as shares issued from treasury. As at June 30, 2018, the value of the shares held in trust by the LTI trustee was \$3.4 million (December 31, 2017 – \$2.3 million) which was comprised of 89,681 in vested common shares (December 31, 2017 – 54,880) with a nil aggregate cost (December 31, 2017 – \$nil).

As at August 13, 2018 there were 10,559,936 common shares issued and outstanding including 89,681 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. For the three month period ended June 30, 2018, the Corporation incurred fees totaling \$34,500 compared to \$34,500 for the same period of fiscal 2017. For the Six month period ended June 30, 2018, the Corporation incurred fees totaling \$69,000 compared to \$69,000 for the same period of fiscal 2017.

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, 2017.

TERMINOLOGY

EBITDA

K-Bro reports EBITDA (Earnings before interest, taxes, depreciation and amortization) as a key measure used by management to evaluate performance. EBITDA is utilized to measure compliance with debt covenants and to make decisions related to dividends to Shareholders. We believe EBITDA assists investors to assess 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, and income taxes.

EBITDA is a sub-total presented within the statement of earnings in accordance with the amendments made to IAS 1 which became effective January 1, 2016. EBITDA is not considered an alternative to net earnings in measuring K-Bro's performance. 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.

(thousands)	Three Months Ended June 30,		Six Months Ended June 30,	
	2018	2017	2018	2017
Net earnings	\$ 2,584	\$ 2,337	\$ 3,231	\$ 3,587
Add:				
Income tax expense	881	1,013	1,275	1,533
Finance expense	716	61	1,592	246
Depreciation of property, plant and equipment	3,565	2,842	7,016	5,223
Amortization of intangible assets	706	404	1,538	832
EBITDA	\$ 8,452	\$ 6,657	\$ 14,652	\$ 11,421

Non-GAAP Measures

Adjusted EBITDA

Adjusted EBITDA is a measure which has been reported in order to assist in the comparison of historical EBITDA to current results. Adjusted EBITDA is defined as EBITDA (defined above) with the exclusion of certain material items that are unusual in nature, infrequently occurring or not considered part of our core operations.

Adjusted Net Earnings and Adjusted Net Earnings per Share

Adjusted net earnings and adjusted net earnings per share are measures which have been reported in order to assist in the comparison of historical net earnings to current results. Adjusted net earnings is defined as net earnings with the exclusion of certain material items that are unusual in nature, infrequently occurring or not considered part of our core operations. The calculation of adjusted net earnings normalizes the impact of the transaction costs related to the acquisition of Fishers, and the related impact on net earnings and net earnings per share. The normalization of this net expense in the calculation of adjusted net earnings and adjusted net earnings per share is considered by management to be a more accurate representation of the net earnings from core operations.

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. Management refers to "Distributable cash flow" as to cash provided by (used in) operating activities with the addition of net changes in non-cash working capital items, less share-based compensation, and maintenance capital expenditures.

Payout Ratio

Payout ratio is defined by management as the actual cash dividend divided by distributable cash. This is a key measure used by investors to value K-Bro, assess its performance and provide an indication of the sustainability of dividends. The payout ratio depends on the distributable cash and the Corporation's dividend policy.

Debt to Total Capitalization

Debt to total capitalization is defined by management as the total long-term debt less cash and cash equivalents divided by the Corporation's total shareholder's equity. This is a measure used by investors to assess the Corporation's financial structure.

Distributable Cash Flow, Payout Ratio, Debt to Total Capitalization, Adjusted EBITDA, Adjusted net earnings, and Adjusted net earnings per share are not calculations based on IFRS and are not considered an alternative to IFRS measures in measuring K-Bro's performance. Distributable Cash Flow, Payout Ratio, Adjusted EBITDA, Adjusted net earnings, and Adjusted net earnings per share do not have standardized meanings in IFRS and are therefore not likely to be comparable with similar measures used by other issuers.

Off Balance Sheet Arrangements

As at June 30, 2018, the Corporation has not entered into any off balance sheet arrangements.

ADOPTION OF NEW ACCOUNTING STANDARDS

The Corporation has prepared its June 30, 2018 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 IFRS 15 and IFRS 9, which has resulted in the inclusion of additional depth for the Corporation's existing accounting policies.

Revenue recognition

A laundry services contract is a contract specifically negotiated for the provision of laundry and linen services. Revenue is based on contractually set pricing on a consistent unit-of-weight or price-per-piece basis for each service over the term of the contract. The Corporation reports revenue under two revenue categories: healthcare and hospitality services. When determining the proper revenue recognition method for contracts, the Corporation evaluates whether two or more contracts should be combined and accounted for as one single contract and whether the combined or single contract should be accounted for as more than one performance obligation. This evaluation requires significant judgment and the decision to combine a group of contracts or to separate a single contract into multiple performance obligations could affect the amount of revenue and profit recorded in a given period. The Corporation accounts for a contract when, it has commercial substance, the parties have approved the contract in accordance with customary business practices and are committed to their obligations, the rights of the parties and payment terms are identified, and collectability of consideration is probable.

1. Identifying the Contract

The Corporation's policy for revenue recognition requires an appropriately authorized contract, with sign-off by representatives from all respective parties, before any services are provided to a customer. Contained within the terms of these contracts is detailed information identifying each party's rights regarding the laundry and linen services to be provided, as well as associated payment terms (i.e. service pricing, early payment discounts, invoicing requirements, etc.). In addition, the Corporation's contracts have commercial substance as the services to be provided will directly impact the Corporation's future cash flows via incoming revenue and related outgoing expenditures.

As part of the Corporation's analysis in reviewing and accepting a contract, the Corporation assesses the likelihood of collection from all prospective customers and only transacts with those customers from which payment is probable. As the Corporation's significant customer contracts are generally with government-funded health agencies and large volume hotels, it is probable that the Corporation will collect the consideration to which is entitled for the performance of these contracts.

For services provided following the expiration of a contract and subsequent renewal negotiations, the terms of the original contract carry forward until the new agreement has been appropriately authorized. This is confirmed through verbal approval, and is consistent with customary business practices.

2. Identifying performance obligations in a contract

Linen services are provided to the Corporation's customers consecutively over a period of time (i.e. daily deliveries over the contract term) and the same method is used to measure the

Corporation's progress in satisfying the performance of the contract (i.e. revenue is based on contractually set pricing on a consistent unit-of-weight or price-per-piece basis for each service over the term of the contract). Additionally, these services generally include integrated processing and delivery, consist of a single deliverable (clean processed volume), and in the case of rental linen, are not offered individually (rental linen is used as an input in the provision of standard laundry and linen services). Therefore, the services provided under one service agreement constitute a single performance obligation.

3. Determining the transaction price

The majority of the Corporation's contracts utilize a fixed pricing model. These contracts stipulate a fixed rate to be charged to customers on a price-per-unit basis, including either weight-based or item-based billing. For these types of arrangements, revenue is recognized over time as each unit of linen is processed and delivered using the fixed consideration rate per the contract. In addition to the above pricing methodology, some contracts have additional components which meet the definition of variable consideration per IFRS 15 which are accounted for using the most likely amount method. The estimates of variable consideration and determination of whether to include estimated amounts in the transaction price are based largely on an assessment of the Corporation's anticipated performance and all information, historical, current and forecasted, that is reasonably available.

4. Allocating the Transaction Price

Each of the Customer's individual customer contracts represents a single performance obligation. As a result, the transaction price for each contract (based contractually stipulated fixed and variable pricing for a single deliverable) is allocated to each processed item based on the agreed upon rate.

5. Performance obligations satisfied over time

The Corporation typically transfers control of goods or services, and satisfies performance obligations, over time. Therefore, the Corporation recognizes revenue over time as once clean linen has been provided to the customer, and the customer has accepted delivery of the processed items.

Financial Instruments

From January 1, 2018, the Corporation classifies its financial assets in the following measurement categories:

- Those to be measured subsequently at fair value (either through other comprehensive income, or through profit or loss), and
- Those to be measured at amortized cost.

The classification depends on the Corporation's business model for managing the financial assets and contractual terms of the cash flows.

At initial recognition, the Corporation measures a financial asset at fair value plus, in the case of a financial asset not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition of the financial asset.

The Corporation's financial assets consist of cash and cash equivalents and accounts receivable, which are measured at amortized cost under IFRS 9 and were previously measured at amortized cost under IAS 39.

Long term debt

No retrospective adjustments were required in relation to amendments made to the Corporation's credit facility prior to January 1, 2018, as the amendments were considered to be an extinguishment. The Corporation considers both quantitative and qualitative factors to assess if an amendment should be accounted for as an extinguishment or a modification.

Impairment of financial assets

As discussed in note 2 of the Corporation's unaudited interim condensed Consolidated Financial Statements for the six months ended June 30, 2018, the Corporation has adopted IFRS 9, which expands on the guidance and disclosure requirements on the impairment of loans and receivables, and credit risk disclosure. The Corporation has adopted the application of the simplified approach to providing for expected credit losses prescribed by IFRS 9, which permits the use of the lifetime expected loss provision for all trade receivables. To measure the expected credit losses, the Corporations' trade receivables have been grouped based on operating segment, shared credit risk characteristics and days past due. Significant accounting judgment and estimate is required in the assessment of the lifetime expected default rate of each trade receivables grouping. The lifetime expected default rates are reviewed at least annually and are updated if expectations change.

In the prior year, the impairment of trade receivables was assessed based on the incurred loss model. Individual receivables which were known to be uncollectible were written off by reducing the carrying amount directly. The other receivables were assessed collectively, to determine whether there was objective evidence that impairment had been incurred but not yet been identified. For these receivables, the estimated impairment losses were recognized in a separate provision for impairment. The group considered that there was evidence of impairment if any of the following indicators were present:

- significant financial difficulties of the debtor
- probability that the debtor will enter bankruptcy or financial reorganization, and
- default or delinquency in payments (more than 30 days overdue).

While cash and cash equivalents are also subject to the impairment requirements of IFRS9, the identified impairment loss was immaterial. The Corporation's adoption of the simplified approach for credit losses prescribed by IFRS 9, effective January 1, 2018, did not result in any changes to the measurement, presentation or disclosures in the financial statements.

RECENT ACCOUNTING PRONOUNCEMENTS

Significant accounting policies adopted January 1, 2018

The following standards have been applied in preparing the interim condensed consolidated financial statements.

- IFRS 9, Financial Instruments, was issued in July 2014 by the IASB and supersedes IAS 39, "Financial Instruments: Recognition and Measurement". IFRS 9 addresses the classification, measurement and recognition of financial assets and financial liabilities. IFRS 9 retains but simplifies the mixed measurement model and establishes three primary measurement categories for financial assets: amortized cost, fair value through OCI and fair value through P&L. IFRS 9 is to be applied retrospectively and is effective for annual periods beginning on or after January 1, 2018, with earlier application permitted. The Corporation adopted the requirements of IFRS 9 using the retrospective approach without restating comparative information effective January 1, 2018. The adoption of IFRS 9 had no impact on the Corporation's financial position or results of operations.
- IFRS 15, Revenue from Contracts with Customers, was issued in May 2014 by the IASB and

supersedes IAS 18, "Revenue", IAS 11 "Construction Contracts" and other interpretive guidance associated with revenue recognition. IFRS 15 establishes a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. IFRS 15 is to be applied using a full retrospective or a modified retrospective approach and is effective for annual periods beginning on or after January 1, 2018, with earlier application permitted. The core principle of IFRS 15 is that an entity should recognize revenue based on the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Specifically, IFRS 15 introduces a 5-step approach to revenue recognition:

- Step 1: Identify the contract(s) with a customer.
- Step 2: Identify the performance obligations in the contract.
- Step 3: Determine the transaction price.
- Step 4: Allocate the transaction price to the performance obligations in the contract.
- Step 5: Recognize revenue when (or as) the entity satisfies a performance obligation.

Under IFRS 15, an entity recognizes revenue as a performance obligation is satisfied, i.e. when control of the goods or services underlying the particular performance obligation is transferred to the customer. The Corporation adopted the requirements of IFRS 15 using the modified retrospective approach, effective January 1, 2018, for any accounting or disclosure changes required under this standard. The adoption of IFRS 15 had no impact on the Corporation's financial position or results of operations.

- On June 20, 2016 the IASB issued an amendment to IFRS 2 "Share based Payment" addressing three classification and measurement issues. The amendment clarifies the measurement basis for cash-settled, share based payments and the accounting for modifications that change an award from cash-settled to equity settled. It also introduces an exception to the principles in IFRS 2 that will require an award to be treated as if it was wholly-equity settled, where an employer is obliged to withhold an amount for the employee's tax obligation associated with a share based payment and pay that amount to the tax authority. The amendments are effective for periods beginning on or after January 1, 2018. The Corporation adopted the amended requirements of IFRS 2 effective January 1, 2018, for any accounting or disclosure changes required under this standard. Adoption of the amendments did not result in any changes to the presentation or disclosures in the financial statements.

New Standards and interpretations not yet adopted

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

- IFRS 16, Leases, was issued in January 2016 and applies to annual reporting periods beginning on or after January 1, 2019. IFRS 16 specifies how an IFRS reporter will recognize, measure, present and disclose leases. The standard provides a single lessee accounting model, requiring lessees to recognize assets and liabilities for all leases unless the lease term is 12 months or less or the underlying asset has a low value. Lessors continue to classify leases as operating or finance, with IFRS 16's approach to lessor accounting substantially unchanged from its predecessor, IAS 17. The Corporation is in the process of evaluating the impact that IFRS 16 may have on the financial statements. The standard will affect primarily the accounting for the Corporation's operating leases. The Corporation has not yet determined to what extent these commitments will result in the recognition of assets and liabilities for future payments and how this will affect EBITDA, net earnings and classification of cash flows.

CRITICAL RISKS AND UNCERTAINTIES

As at June 30, 2018, there are no material changes in the Corporation's risks or risk management activities since December 31, 2017. 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 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.

Internal Controls over Financial Reporting

There were no changes in internal controls over financial reporting ("ICFR") during the three month period ended June 30, 2018 that materially affected, or are reasonably likely to materially affect, the Corporation's ICFR.

The Corporation's CEO and CFO have determined that there is not a material weakness in the design of disclosure controls and procedures and internal controls over financial reporting which existed as at June 30, 2018.

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, 2017.

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.

Limitation on Scope of Design

K-Bro has limited the scope of design of DCP and our Internal Controls over Financial Reporting (ICFR) to exclude controls, policies and procedures of Fishers acquired on November 27, 2017. The scope limitation is in accordance with section 3.3(1)(b) of NI 52-109 which allows an issuer to limit its design of ICFR to exclude controls, policies and procedures of a business that the issuer acquired not more than 365 days before the end of the fiscal period.

Fishers (millions)	As at June 30, 2018
Current assets	\$ 29.2
Non-current assets	51.8
Current liabilities	9.8
Non-current liabilities	3.9

Fishers (millions)	Six Months Ended June 30, 2018
Revenue	\$ 28.2
Expense	(27.4)
Income from operations	\$ 0.8

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 »).