LIQUOR STORES N.A. LTD.

MANAGEMENT'S DISCUSSION AND ANALYSIS

For the Year Ended December 31, 2015

Dated as at March 9, 2016

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1. Basis of Presentation

Management's Discussion and Analysis ("MD&A") provides a comparison of Liquor Stores N.A. Ltd.'s performance for the three months and year ended December 31, 2015 with the three months and year ended December 31, 2014. This discussion should be read in conjunction with the Company's annual audited consolidated financial statements and notes thereto (the "financial statements") for the years ended December 31, 2015 and 2014, and the Annual Information Form of the Company for the year ended December 31, 2015 dated March 9, 2016. The information in this MD&A is current to March 9, 2016, unless otherwise noted.

In this MD&A, all references to "we", "us", "our", "Liquor Stores", and "the Company" refer to Liquor Stores N.A. Ltd. and its subsidiaries. All references to "Management" refer to the directors and senior officers of the Company.

Unless otherwise stated, financial information is expressed in Canadian dollars and has been prepared in accordance with International Financial Reporting Standards ("IFRS"), as set out in the Handbook of the Chartered Professional Accountants – Part I ("CPA Handbook"), for financial statements. Certain dollar amounts have been rounded to the nearest hundred thousand dollars or thousand dollars.

Throughout this MD&A references are made to non-IFRS financial measures, including same-store sales, operating margin, operating margin as a percentage of sales, adjusted operating margin, adjusting items, adjusted net earnings, adjusted basic and diluted earnings per share, cash provided by operating activities before changes in non-cash working capital, cash provided by operating activities before changes in non-cash working capital on a per share basis, cash provided by operating activities before changes in non-cash working capital and adjusted items, and cash provided by operating activities before changes in non-cash working capital and adjusted items on a per share basis. A description of these measures and their limitations are discussed under *"Non-IFRS Financial Measures",* along with a reconciliation to the nearest IFRS financial measure.

Additional information relating to Liquor Stores can be found at www.liquorstoresna.ca. The Company's continuous disclosure materials, including its annual and quarterly MD&A, audited annual and unaudited interim financial statements, its Annual Information Form, Information Circulars, and various news releases issued by the Company are also available on its website or directly through the SEDAR system at www.sedar.com.

2. Forward Looking Statements

This MD&A contains forward looking statements or information (collectively "forward-looking statements") within the meaning of the "safe harbour" provisions of applicable securities legislation. All statements and information other than statements of historical fact contained in this MD&A are forward-looking statements. In particular, this MD&A contains forward-looking statements, including, without limitation, statements regarding the future financial position, cash dividends, business strategy, proposed acquisitions, budgets, litigation, government regulation and laws, projected costs and plans and objectives of or involving Liquor Stores N.A. Ltd. Prospective investors can identify many of these statements by looking for words such as "believes", "expects", "will", "intends", "projects", "anticipates", "estimates", "continues" or similar words and the negative thereof.

Forward-looking statements reflect the Company's current plans, intentions, and expectations, which are based on Management's perception of historical trends, current conditions and expected future developments, as well as other factors it believes are appropriate in the circumstances. The Company's plans, intentions, and expectations are inherently subject to significant business, economic, competitive and other uncertainties and contingencies regarding future events and as such, are subject to change. There is no assurance that the plans, intentions, or expectations upon which these forward-looking statements are based will occur. Forward looking statements are subject to risks, uncertainties and assumptions, including, but not limited to, those discussed elsewhere in this MD&A. Although Management believes that the expectations represented in such forward looking statements are reasonable there can be no assurance that such expectations will prove to be correct and such forward-looking statements included in this MD&A should not be unduly relied upon.

Some of the factors that could affect future results and could cause results to differ materially from those expressed in the forward looking statements contained herein include, but are not limited to: risks relating to government regulation and changes thereto (whether by court decisions, citizen referenda, or otherwise); competition; the state of the economy including general economic conditions in Canada (including Alberta) and the U.S.; the unpredictability and volatility of Liquor Store's common share price; restrictions on potential growth; restrictions on the potential growth of Liquor Stores as a consequence of the payment of cash dividends by Liquor Stores representing a substantial amount of its operating cash flow; availability of sufficient financial resources to fund the Company's capital expenditures; changes in commodity tax rates and government mark-ups; risks relating to future acquisitions and development of new stores; the ability of management to execute the Company's business and strategic plans; Liquor Stores' ability to locate and secure acceptable store sites and to adapt to changing market conditions; poor weather conditions; dependence on key personnel; labour costs, shortages and labour relations including Liquor Stores' ability to hire and retain staff at current wage levels and the risk of possible future unionization; supply interruption or delays; dependence on suppliers; reliance on information and control systems; income tax changes; leverage and restrictive covenants in agreements relating to current and future indebtedness of Liquor Stores; credit risks arising from operations; dilution and future sales of Liquor Stores common shares; and the potential lack of an active trading market for Liquor Stores' common shares and convertible debentures. These factors should not be construed as exhaustive. The information contained in this MD&A, including the information set forth under "Risk Factors", and as disclosed in other filings made by the Company with Canadian securities regulatory authorities and available on SEDAR at www.sedar.com, identifies additional factors that could affect the operating results and performance of Liquor Stores. Readers are cautioned that this list of risk factors should not be construed as exhaustive.

The forward looking statements contained herein are expressly qualified in their entirety by this cautionary statement. The forward looking statements included in this MD&A are made as of the date of this MD&A and Liquor Stores assumes no obligation to update or revise them to reflect new events or circumstances except as expressly required by applicable securities law.

3. Performance Overview

The following table summarizes highlights of the Company's financial performance for the three months ended December 31, 2015 and 2014:

	Three months ended December 31,					
	2015		2014		Variance	
(Cdn $000's unless otherwise noted)	$	%	$	%	$	%
	(unaudited)		(unaudited)			
Sales						
Canadian same-stores[3]	132,000	61.6%	131,615	66.9%	385	0.3%
Other Canadian stores [1]	6,776	3.2%	3,681	1.9%	3,095	84.1%
Canadian wholesale	7,620	3.6%	6,663	3.4%	957	14.4%
Total Canadian store sales	146,396	68.4%	141,959	72.2%	4,437	3.1%
U.S. same-stores (US$)[3]	41,688	19.5%	41,471	21.1%	217	0.5%
Other U.S. stores (US$)[2]	9,065	4.2%	6,736	3.4%	2,329	34.6%
Foreign exchange on U.S. store sales	17,017	7.9%	6,556	3.3%	10,461	159.6%
Total U.S. store sales	67,770	31.6%	54,763	27.8%	13,007	23.8%
Total sales	214,166	100.0%	196,722	100.0%	17,444	8.9%
Gross margin	54,638	25.5%	50,725	25.8%	3,913	7.7%
Operating and administrative expense	42,760	20.0%	36,983	18.8%	5,777	15.6%
Operating margin	11,878	5.5%	13,742	7.0%	(1,864)	(13.6)%
Adjusted operating margin[3]	13,971	6.5%	13,742	7.0%	229	1.7%
Net earnings (loss)	(105,808)	(49.4)%	6,714	3.4%	(112,522)	nm
Adjusted net earnings [3]	6,589	3.1%	6,714	3.4%	(125)	(1.9)%
Cash provided by operating activities	15,680		19,639		(3,959)	(20.2)%
Cash provided by operating activities before changes in non-cash working capital and adjusting items [3]	12,804		11,148		1,656	14.9%
Dividends paid in cash	6,694		5,675		1,019	18.0%
Total assets	455,554		525,865		(70,311)	(13.4)%
Total equity	255,736		364,758		(109,022)	(29.9)%
Basic and diluted earnings (loss) per share	(3.86)		0.28		(4.14)	nm
Basic and diluted adjusted earnings per share [3]	0.24		0.28		(0.04)	(14.3)%

nm – not meaningful

The following table summarizes highlights of the Company's financial performance for the year ended December 31, 2015 and 2014:

	Year ended December 31,					
	2015		2014		Variance	
(Cdn $000's, unless otherwise noted)	$	%	$	%	$	%
	(unaudited)		(unaudited)			
Sales						
Canadian same-stores(3)	466,942	62.6%	460,541	66.3%	6,401	1.4%
Other Canadian stores (1)	33,590	4.5%	28,368	4.1%	5,222	18.4%
Canadian wholesale	28,188	3.7%	25,048	3.6%	3,140	12.5%
Total Canadian store sales	528,720	70.8%	513,957	74.0%	14,763	2.9%
U.S. same-stores (US$)(3)	141,984	19.0%	140,600	20.3%	1,384	1.0%
Other U.S. stores (US$)(2)	27,610	3.7%	22,329	3.2%	5,281	23.7%
Foreign exchange on U.S. store sales	48,070	6.5%	17,300	2.5%	30,770	177.9%
Total U.S. store sales	217,664	29.2%	180,229	26.0%	37,435	20.8%
Total sales	746,384	100.0%	694,186	100.0%	52,198	7.5%
Gross margin	191,389	25.6%	176,351	25.4%	15,038	8.5%
Operating and administrative expense	154,519	20.7%	139,821	20.1%	14,698	10.5%
Operating margin(3)	36,870	4.9%	36,530	5.3%	340	0.9%
Adjusted operating margin(3)	40,894	5.5%	37,916	5.5%	2,978	7.9%
Net earnings (loss)	(99,392)	(13.3)%	12,949	1.9%	(112,341)	nm
Adjusted net earnings (3)	15,722	2.1%	13,988	2.0%	1,734	12.4%
Cash provided by operating activities	16,373		20,834		(4,461)	(21.4)%
Cash provided by operating activities before changes in non-cash working capital and adjusting items (3)	30,924		23,463		7,461	31.8%
Dividends paid in cash	26,994		22,663		4,331	19.1%
Total assets	455,554		525,865		(70,311)	(13.4)%
Total equity	255,736		364,758		(109,022)	(29.9)%
Basic and diluted earnings (loss) per share	(3.64)		0.54		(4.18)	nm
Basic and diluted adjusted earnings per share (3)	0.57		0.59		(0.02)	(3.4)%

nm – not meaningful

Notes:

(1) *Sales for Other Canadian stores for the three months ended December 31, 2015 and 2014 include those of ten stores opened, five stores closed, three stores within close proximity to the opened and closed stores, and one store that was closed for a significant portion of time due to destruction by fire subsequent to September 30, 2014.*

Sales for Other Canadian stores for the year ended December 31, 2015 and 2014 include those of fifteen stores opened, twelve stores closed, four stores within close proximity to the opened and closed stores, and one store that was closed for a significant portion of time due to destruction by fire subsequent to December 31, 2013.

(2) *Sales for Other U.S. stores for the three months ended December 31, 2015 and 2014 include the following changes subsequent to September 30, 2014: (i) Kentucky: three new stores opened, one store closed and two stores within close proximity to the opened stores; and (ii) Alaska: one store closed and one store within close proximity to the closed store.*

Sales for Other U.S. stores for the year ended December 31, 2015 and 2014 include the following changes subsequent to December 31, 2014: (i) Kentucky: four new stores opened, one store closed and two stores within close proximity to the opened stores; and (ii) Alaska: one store opened, one store closed and one store within close proximity to the closed store.

(3) *Same-store sales, operating margin, adjusting items, adjusted operating margin, adjusted net earnings, cash provided by operating activities before changes in non-cash working capital and adjusting items, and adjusted earnings per share are non-IFRS measures that do not have any standardized meaning prescribed by IFRS. For more information and a reconciliation of non-IFRS measures to the closest IFRS measure see the 'Non-IFRS Financial Measures' section of this MD&A.*

Fourth Quarter 2015 Operating Results Compared to Fourth Quarter 2014 Operating Results

Sales

Total sales increased by $17.4 million or 8.9% to $214.2 million in the fourth quarter of 2015 (Q4 2014 - $196.7 million). The increase is primarily the result of the sales contribution from same-stores, new store expansion in the United States and Canada offsetting store closures (thirteen new stores opened and seven stores closed since September 30, 2014), and a $10.5 million positive change in foreign exchange on the translation of U.S. dollar denominated sales to Canadian dollars.

Same-Store Sales[1]

- Canadian same-store sales increased by $0.4 million, or 0.3%.
  - Same-store sales in British Columbia, Edmonton and Calgary (which account for approx. 75% of our Canadian same-stores) continued to grow in the fourth quarter of 2015 compared to the same period in 2014. In particular, we had strong growth in stores that were renovated during the previous two years. We also saw same-store sales growth in British Columbia in spite of increased competition faced from government-owned stores as a result of the regulatory changes implemented by the province on April 1, 2015 as described in the *'Risk Factors'* section of this document.
  - However, as a result of the deteriorating economic conditions in Alberta which saw a sharp and rapid decline in the price of oil and increase in unemployment levels in the province, the growth in Edmonton and Calgary in Q4 2015 decelerated from the growth rates that we achieved earlier in 2015.
  - Our stores located in the resource and rural markets of Alberta also faced increased pressure in the fourth quarter from the weakening economic conditions compared with the first half of

[1] See the 'Non-IFRS Financial Measures' section of this MD&A

    2015, with regional same-store sales declines of between 5% and 15% depending on the market.

- U.S. same-store sales increased by $0.2 million or 0.5%.
    - Same-store sales in the United States were negatively impacted by a continued slowdown in the Alaska economy as a result of a decline in oil and gas exploration activity and were impacted by unfavourable weather in Kentucky during the quarter.

Other Sales

- Canadian wholesale sales, which include sales to licensee customers in Alberta (restaurants, lounges, hotels, etc.), were $7.6 million for the three months ended December 31, 2015, representing an increase of $1.0 million or 14.4% from the prior year (2014 - $6.7 million). Our sales increased due to the addition of new licensee customer accounts over the past year, which were partly offset by a decline in sales to existing customers in rural and resource markets.
- Sales for the Other Canadian stores have increased $3.1 million compared to the prior year, primarily as a result of the sales from the ten new stores opened contributing more than the lost contribution from the five stores closed since September 30, 2014. Sales for Other U.S. stores have increased by $2.3 million compared to 2014, primarily as a result of three new large-format stores opened in Kentucky more than offsetting the sales decline in the two stores in close proximity to the new stores since September 30, 2014.

Gross Margin

For the three months ended December 31, 2015, gross margin was $54.6 million, up 7.7% from $50.7 million for the same period last year. The increase in our gross margin was primarily attributable to the margin increase from new stores net of store closures ($1.1 million), margin growth from the Canadian wholesale business ($0.3 million), and a positive change in foreign exchange on translation of the U.S dollar denominated gross margin to Canadian dollars ($2.5 million).

Gross margin as a percentage of sales for the period has decreased to 25.5% (2014 – 25.8%), which was primarily attributable to the pricing and promotional strategies applied to the new stores opened in 2015 to drive a more rapid increase to customer count in these new locations and growth in our Canadian wholesale sales, which attracts a lower gross margin percentage than our retail sales. We have also been mindful of our pricing strategy to ensure our products remained priced appropriately considering the economic slowdown being experienced in Alberta and Alaska, and the competitive pressures being faced in British Columbia.

Operating and Administrative Expenses

Operating and administrative expenses for the three months ended December 31, 2015 were $42.8 million, up 15.6% from $37.0 million a year earlier. Excluding adjusting items of $2.1 million (summarized under the 'Non-IFRS Financial Measures' section of this MD&A), these expenses increased by 10.0% or $3.7 million.

- The increase primarily related to an increase in the foreign exchange on translation of U.S. dollar denominated store level operating expense and head office administrative expenses to Canadian dollars ($2.7 million), rent escalations related to the renewal of long-term lease arrangements in the past twelve months ($1.0 million), a liability recognized for the remaining lease costs on the closure of an underperforming store ($0.4 million), and the increased costs associated with running our thirteen new stores opened since September 30, 2014 net of seven store closures ($1.2 million).

- These increases were partially offset by decreases in operating costs associated with running our same stores ($0.7 million) and a decrease in head office administrative expenses ($0.7 million) compared to the prior year due to a decline in stock-based compensation expense (primarily due to our lower share price at December 31, 2015 which reduced the value of our cash settled awards recognized in the current quarter) and management more tightly controlling these expenditures in response to the economic slowdown being experienced in Alberta as discussed in our analysis of same-store sales above.

Operating Margin

Operating margin for the three months ended December 31, 2015 decreased by $1.9 million to $11.9 million or 5.5% as a percentage of sales (Q4 2014 – 7.0%). However, adjusted operating margin for the three months ended December 31, 2015 increased by $0.2 million to $14.0 million due to the increases in gross margin partially offset by the increases in the foreign exchange on translation of U.S. dollar denominated store level operating expense and head office administrative expenses to Canadian dollars as explained above. Adjusted operating margin[2] as a percentage of sales was 6.5%, down from 7.0% in the prior year.

Since September 30, 2014, the Company has added thirteen new stores in Canada and the United States. New stores generally take up to three years to mature and fully contribute to operating margin, and as such, these new stores have contributed to the decline in the adjusted operating margin as a percentage of sales. Management believes that this impact is temporary and that these new stores will positively contribute to adjusted operating margin as a percentage of sales as they mature. The Company has also closed seven stores since September 30, 2014, which has impacted operating margins due in part to costs associated with closing the stores.

Amortization

Amortization expense of $2.9 million for the fourth quarter of 2015 was up $0.4 million from the prior year (Q4 2014 - $2.5 million). Additional amortization in the current year related to the new stores opened in the past year.

Finance Costs

Finance costs are comprised of cash interest on bank indebtedness, long-term debt and convertible debentures of $1.8 million (Q4 2014 - $2.0 million); non-cash interest of $0.4 million (Q4 2014 - $0.3 million), an unrealized loss on the mark-to-market adjustments related to an interest rate swap of $0.4 million (Q4 2014 - insignificant), and a $0.4 million loss on foreign exchange from financing activities (Q4 2014 - insignificant). Cash interest expense has declined compared with Q4 2014 as a result of our lower average long-term debt balances compared to the prior year due to our common share issuance which occurred near the end of Q4 2014, from which we used the proceeds to repay long-term debt. Average borrowing rates during the period have been relatively consistent with the prior year.

Impairment

During the three months ended December 31, 2015, the Company recorded an aggregate $116.8 million impairment charge to the goodwill allocated to the Canadian CGU as well as a $12.6 million impairment charge to the goodwill allocated to the Alaska CGU. The recoverable amounts of the CGUs declined in 2015 primarily due to downward adjustments to Management's forecasted sales and profitability as a result of a

[2] See the 'Non-IFRS Financial Measures' section of this MD&A

rapid and significant economic slowdown in these markets. The Company also recorded a $1.6 million impairment provision on retail liquor licenses, which are classified as indefinite life intangible assets, related to two stores in British Columbia (Canadian operating segment). The impairment primarily related to a change in Management's forecasted sales and profitability as a result of increased competition in the areas that these stores operate. A reversal of previously recorded impairment charges was recorded during the quarter in the amount of $0.7 million. This reversal related to a retail liquor license of one store where Management's forecasted sales and profitability increased due to a sustained improvement in operating results.

Also see the 'Risk Factors' section later in this MD&A for further discussion of potential changes in the regulatory and economic environment for all regions that we operate in.

Income Taxes

In the fourth quarter of 2015, we recorded an income tax recovery of $18.6 million for an effective rate of 15.0% (Q4 2014 - $2.2 million expense).

Our effective tax rate for the period differs from the statutory rate due to a portion of the provision for impairment of goodwill that is not deductible for tax purposes.

In addition, our estimated annual effective rate of tax will fluctuate based on the estimated proportion of income/loss attributable to each jurisdiction that the Company operates in for 2015 compared to 2014.

Net Earnings

For the three months ended December 31, 2015, a net loss of $105.8 million was recorded (Q4 2014 – earnings of $6.7 million). Excluding after-tax adjusting items of $112.4 million (summarized under the 'Non-IFRS Financial Measures' section of this MD&A), adjusted net earnings[3] were $6.6 million, a decrease of $0.1 million or 1.9% compared to Q4 2014.

The decrease in adjusted net earnings is due the increase in amortization expense and finance costs as discussed above partially offset by the increase in adjusted operating margin and recoveries on income taxes.

Year ended December 31, 2015 Operating Results Compared to the Year ended December 31, 2014 Operating Results

Sales

Total sales increased by $52.2 million or 7.5% to $746.4 million in 2015 (2014 - $694.2 million). The increase is the result of the growth in same-stores sales in both Canada and the U.S., sales contribution from the new store expansion in Canada and the United States offsetting sales lost from store closures (twenty new stores opened and fourteen stores closed since December 31, 2013), and a $30.8 million positive change in foreign exchange on translation of U.S. dollar denominated sales to Canadian dollars.

Same-Store Sales[2]

- Canadian same-store sales increased by $6.4 million, or 1.4%.

[3] See the 'Non-IFRS Financial Measures' section of this MD&A

- The increase in Canadian same-store sales for the year ended December 31, 2015 was primarily the result of growth in average basket sizes. We believe that these positive improvements were related to changes that were made to our pricing and marketing strategies over the last year, and the introduction of enhanced store level training programs in late 2014 as part of our seven point plan.
- The increase in Canadian same-store sales is also attributable to: (i) increased sales contribution from those stores that have been renovated over the last 18 months, and (ii) newer stores that are now included in same-store sales (i.e. those that have been open for 13 months to 36 months) contributing higher than average sales increases as they continue to mature.
- The increases in Canadian same-store sales were in spite of an economic slowdown in resource and rural markets in Alberta, where we have seen declines in same-store sales as discussed in the analysis of the three months ended December 31, 2015.

- U.S. same store sales increased by $1.4 million, or 1.0%.
    - Same-store sales in the United States have been positively impacted by same-store sales growth in Kentucky. The increase in Kentucky is in part the result of making changes to our pricing and marketing strategies and store level training programs, similar to Canada, which drove an increase in our basket size compared to the prior year.
    - The increase in Kentucky was offset by a decrease in same-store sales in Alaska during the year. This market has been negatively impacted by a slowdown in the economy as a result of a decline in oil and gas exploration activity. Throughout 2015, we have been adjusting our pricing and marketing strategies to combat the impact of the economic slowdown, and we replaced the local leadership team in the Alaska region early in 2015. As a result of these changes, our results steadily improved as the year progressed.

Other Sales

- Canadian wholesale sales, which include sales to licensee customers in Alberta, were $28.2 million for the year ended December 31, 2015, representing an increase of $3.1 million or 12.5% from the prior year (2014 - $25.0 million), primarily due to adding new licensee customer accounts in the current year. This increase was partially offset by the declines we have seen to our existing customer base who have been impacted by the economic slowdown in Alberta.
- Sales for the Other Canadian stores have increased $5.2 million compared to the prior year primarily as a result of the sales from the fifteen new stores opened in the period contributing more than the lost contribution from the closure of twelve stores since December 31, 2013. Sales for Other U.S. stores have increased by $5.3 million compared to 2014 primarily as a result of the sales from the five new stores opened in the United States contributing more than the lost contribution from the closure of two stores since December 31, 2013.

Gross Margin

For the year ended December 31, 2015, gross margin was $191.4 million, up $15.0 million or 8.5% from $176.4 million for the same period last year. Gross margin as a percentage of sales for the year has increased to 25.6% (2014 – 25.4%). The increase in our gross margin was primarily attributable to the gross margin increase from new stores net of store closures ($2.6 million), the increase in the gross margin as a percentage of sales ($3.1 million), the gross margin impact from the increase in same-stores ($1.7 million), the gross margin increase due to the growth in our Canadian wholesale sales ($0.5 million), and a positive change in foreign exchange on translation of the U.S dollar denominated gross margin to Canadian dollars ($7.1 million).

As a result of changes we have made to our pricing and marketing strategies starting in the beginning half of the year, our gross margin as a percentage of sales increased compared to the prior year. The aggregate of the increases in the first three quarters of 2015 were partially offset by the decline in gross margin as a percentage of sales that we recorded in the last quarter of 2015, which was primarily attributable to the pricing and promotional strategies applied to the new stores opened in 2015 to drive a more rapid increase to customer count in these new locations, and growth in our Canadian wholesale sales, which attracts a lower gross margin percentage than our retail sales. We have also been mindful of our pricing strategy to ensure our products remained priced appropriately considering the economic slowdown being experienced in Alberta and Alaska, and the competitive pressures being faced in British Columbia.

Operating and Administrative Expenses

Operating and administrative expenses for the year ended December 31, 2015 were $154.5 million, up 10.5% from $139.8 million a year earlier. Excluding adjusting items of $4.0 million in the current period and $1.4 million in the prior year (summarized under the 'Non-IFRS Financial Measures' section of this MD&A), these expenses increased by 8.7% or $12.1 million.

- The increases related to the operation of our stores includes a $6.9 million increase in the foreign exchange on translation of U.S. dollar denominated store level operating expense and head office administrative expenses to Canadian dollars, rent escalations related to the renewal of long-term lease arrangements in the past twelve months ($2.2 million), the increased costs associated with running our 20 new stores opened since December 31, 2013 net of fourteen store closures ($2.2 million), a liability recognized for the remaining lease costs on the closure of an underperforming store ($0.4 million), and increases in operating costs associated with running same-stores, including the use of additional various forms of media in our marketing plans ($0.4 million).
- Administrative expenses, excluding adjusting items, were flat compared to the prior year, primarily due to inflationary increases in this spend being offset by a decline in stock-based compensation expense primarily due to our lower share price at December 31, 2015 which reduced the value of our cash settled awards recognized at the current year-end.

Operating Margin

Operating margin for the year ended December 31, 2015 increased by $0.3 million to $36.9 million, but decreased as a percentage of sales to 4.9% (2014 – 5.3%).

Adjusted operating margin[4] for the year ended December 31, 2015 increased by $3.0 million to $40.9 million, primarily due to the increases in gross margins as explained above offset by increases to operating and administrative expenses. Adjusted operating margin as a percentage of sales remained consistent with the prior year at 5.5%.

Since December 31, 2013, the Company has added 20 new stores in Canada and the United States, and as such, these new stores have contributed to the increase in the adjusted operating margin as a percentage of sales. The Company has also closed fourteen stores since December 31, 2013, which has impacted operating margins due to costs associated with closing the stores.

[4] See the 'Non-IFRS Financial Measures' section of this MD&A

Amortization

Amortization expense of $11.1 million for 2015 increased by $0.8 million from the prior year (2014 - $10.3 million). The increase related primarily to the new stores opened in the previous year.

Finance Costs

Finance costs during the year ended December 31, 2015 have increased by $0.3 million compared to the prior year. Finance costs are comprised of cash interest on bank indebtedness, long-term debt and convertible debentures of $6.5 million (2014 - $7.6 million); non-cash interest of $1.6 million (2014 - $1.5 million), realized foreign exchange losses of $1.0 million (2014 - $0.2 million loss), and a $0.5 million unrealized loss on the mark-to-market adjustments related to an interest rate swap (2014 - $0.1 million loss). Our average long-term debt balances and average borrowing rates were fairly consistent during the year compared to the prior year.

Impairment

During the year ended December 31, 2015, the Company recorded an aggregate $116.8 million impairment charge to the Canadian CGU as well as a $12.6 million impairment charge to the Alaska CGU. The recoverable amounts of the CGUs declined in 2015 primarily due to Management's forecasted sales and profitability as a result of the significant economic slowdown in these markets. The Company also recorded a $1.6 million impairment provision on retail liquor licenses, which are classified as indefinite life intangible assets, related to two stores in British Columbia (Canadian operating segment). A reversal of previously recorded impairment charges was recorded during the year in the amount of $0.7 million. This reversal related to a retail liquor license of one store where Management's forecasted sales and profitability increased due to a sustained improvement in operating results.

Also see the 'Risk Factors' section later in this MD&A for further discussion of potential changes in the regulatory and economic environment for all regions that we operate in.

Income Taxes

In 2015, an income tax recovery of $14.7 million (2014 - $4.1 million expense) was recorded for an effective rate of approximately 12.9% (2014 - 24.0%).

Effective July 1, 2015, the Alberta corporate income tax rate increased from 10 percent to 12 percent, which will increase our Canadian statutory tax rate in future periods by the proportion of our taxable income attributable to the province of Alberta.

Our effective tax rate for the period differs from the statutory rate due to:

- A portion of the provision for impairment of goodwill is not deductible for tax purposes.

- a one-time re-measurement of our deferred income tax liability arising from the Alberta corporate income tax rate increase. As a result of this re-measurement, a deferred tax expense of $1.3 million was recorded in the second quarter of 2015.

In addition, our estimated annual effective rate of tax will fluctuate based on the estimated proportion of income/loss attributable to each jurisdiction that the Company operates in for 2015 compared to 2014.

Net Earnings

For the year ended December 31, 2015, a net loss of $99.4 million was recorded (2014 – $12.9 million earnings). Excluding after-tax adjusting items of $113.8 million (summarized under the 'Non-IFRS Financial Measures' section of this MD&A; 2014 - $1.0 million), adjusted net earnings[5] were $15.7 million, an increase of $1.7 million or 12.4% compared to 2014.

The increase in adjusted net earnings in 2015 is primarily the result of the increases in gross margin in the current year ($15.0 million) and recoveries on income taxes in the year, partially offset by an increase in operating and administrative expenses (a significant portion of this increase was driven by foreign exchange), increased amortization expense, and increased income tax expense.

4. Liquidity and Capital Resources

Summary of Consolidated Cash Flows

	Three months ended December 31,		Year ended December 31,	
(expressed in thousands)	2015 (unaudited)	2014 (unaudited)	2015	2014
Changes in non-cash working capital	$4,969	$8,491	($10,527)	($1,243)
Cash provided by operating activities	15,680	19,639	16,373	20,834
Cash used in investing activities	(10,432)	(3,212)	(30,557)	(11,505)
Cash provided by (used in) financing activities	(4,490)	(17,791)	14,502	(11,178)
Effect of exchange rate on changes in cash	242	36	469	323
Net increase (decrease) in cash	1,000	(1,328)	787	(1,526)

Operating activities

In reviewing the Company's financial statements, users should consider that the statement of earnings and comprehensive income includes significant provisions for impairment losses, amortization of property and equipment and for intangible assets resulting from store acquisitions, deferred taxes and non-cash interest. Amortization and other non-cash transactions have a major impact on the basic and diluted earnings per share calculation.

Cash provided by operating activities before changes in non-cash working capital is a non-IFRS financial measure which the Company believes provides useful information to investors and Management by providing an indication of cash flow available for sustaining its current annual dividend, investment in working capital, the replacement of existing fixed assets or the purchase of new fixed assets, acquisitions and debt repayment. Users of the Company's financial statements often compare basic and diluted earnings per share amounts to the Company's annual dividend. The basic and diluted loss per share for the three months and year ended December 31, 2015 was $3.86 and $3.64, respectively (2014 – $0.28 and $0.54 earnings per share). The Company believes that cash provided in operating activities before changes in non-cash working capital, excluding one-time adjusting items, provides a better indicator of the Company's ability to sustain its current annual dividend than basic and diluted earnings per share.

The following table provides a reconciliation of cash provided by operating activities before changes in non-cash working capital to its nearest IFRS alternative, cash provided by operating activities:

[5] See the 'Non-IFRS Financial Measures' section of this MD&A

	Three months ended December 31,		Year ended December 31,	
(expressed in thousands, except per share amounts)	2015	2014	2015	2014
Cash provided by operating activities	$ 15,680	$ 19,639	$ 16,373	$ 20,834
Changes in non-cash working capital (2)	4,969	8,491	(10,527)	(1,243)
Cash provided by operating activities before changes in non-cash working capital (1)	10,711	11,148	26,900	22,077
Adjusting items(1) (3)	2,093	-	4,024	1,386
Cash provided by operating activities before changes in non-cash working capital and adjusting items (1)	12,804	11,148	30,924	23,463
Weighted average number of common shares outstanding – basic	27,409,088	23,803,430	27,329,145	23,343,836
Per share amount	0.39	0.47	0.98	0.95
Per share amount before adjusting items	0.47	0.47	1.13	1.01
Cash dividends per share	0.27	0.27	1.08	1.08

Notes:

(1) *Cash provided by operating activities before changes in non-cash working capital, and cash provided by operating activities before changes in non-cash working capital and adjusting items are non-IFRS measures that do not have any standardized meaning prescribed by IFRS. For more information on non-IFRS measures see the 'Non-IFRS Measures' section of this MD&A.*

(2) *Changes in non-cash working capital is excluded in the calculation of cash provided by operating activities before changes in non-cash working capital as Management believes that it would introduce significant cash flow variability that can be caused by such factors as timing of disbursements (such as the payment for large inventory purchases, income taxes, etc.) and foreign exchange on translation of U.S. dollar denominated working capital to Canadian dollars. As well, significant increases in working capital are generally required when new stores are developed or acquired.*

(3) *Adjusting items are summarized under the 'Non-IFRS Financial Measures' section of this MD&A.*

Cash provided by operating activities before changes in non-cash working capital and adjusting items for the three months ended December 31, 2015 has increased by $1.7 million primarily due to the increase in adjusted operating margins and lower cash interest costs compared to the prior year. The $7.5 million increase in cash provided by operating activities before changes in non-cash working capital and adjusting items for the year ended December 31, 2015 as compared to the same period in 2014 is primarily due to the increase in adjusted operating margin (see further discussion earlier in the MD&A in the *'Performance Overview'* section).

Investing activities

For the three months ended December 31, 2015, cash used in investing activities was $10.4 million, a $7.2 million increase from $3.2 million used for the same period a year ago.

- Cash used for the purchase of property and equipment for the three months ended December 31, 2015 of $8.1 million (2014 - $3.1 million) related to six new stores opened, and store renovations.
- Cash used for the purchase of intangible assets during the fourth quarter of $2.3 million (2014 - $0.1 million) primarily related to the implementing of our enterprise resource planning (ERP) system.

For the year ended December 31, 2015, cash used in investing activities was $30.6 million, a $19.1 million increase from $11.5 million used for the same period a year ago.

- Cash used for the purchase of property and equipment for the year ended December 31, 2015 of $25.9 million (2014 - $10.9 million) related to new stores opened in 2015 and the acquisition of a retail liquor store in Edmonton in June 2015. The increase compared to the prior year is a result of developing and acquiring more stores compared to the prior year (thirteen stores opened in 2015 compared to seven in 2014), and as a result of a larger proportion of destination and mid-size format stores having been constructed in the current year as compared to the prior year (five in 2015 compared to one in 2014).
- Cash used for the purchase of intangible assets during the period of $4.6 million (2014 - $0.6 million) primarily related to the implementation of our ERP system, the acquisition of a retail liquor license in Massachusetts, and a lease at below market rates obtained in the acquisition of a retail liquor store in Edmonton in the current quarter.

Financing activities

For the three months ended December 31, 2015, cash used for repayment of debt and return of capital to shareholders was $4.5 million, compared to $17.8 million from the same period a year ago. This change primarily relates to:

- Higher total proceeds from long term debt compared to the prior year, which was due to the investment made in the construction of new stores and expenditures on the implementation of our ERP system.
- In the prior year, including the repayment of bank indebtedness, we had a net repayment of debt included in financing activities as a result of the proceeds from the common share issuance completed in the fourth quarter of 2014 being used to repay debt.

For the year ended December 31, 2015, cash provided by financing activities was $14.5 million, compared to cash used for repayment of debt and return of capital to shareholders of $11.2 million from the same period a year ago. This is primarily as a result of:

- Cash received on the disposal of a property in Fairbanks, Alaska related to a sale-leaseback transaction for net proceeds of $5.7 million.
- Higher proceeds from long-term debt compared to the prior year, which was due to the investment made in the construction of new stores and renovations of existing stores, the acquisition of a retail liquor store in Edmonton, expenditures on the implementation of our enterprise resource planning system, and dividends paid that were $4.3 million higher in the period compared to the prior year as a result of the common share issuance completed by the Company in the fourth quarter of 2014.

Foreign currency translation gain on cash

The accounts of the Company's subsidiaries with a U.S. dollar functional currency are translated into Canadian dollars as follows:

- Assets and liabilities are translated at the rate of exchange in effect at the balance sheet date; and
- Revenue and expense items (including amortization) are translated at the average rate of exchange for the period.

The resulting unrealized exchange gains and losses from these translation adjustments are included as a separate component of shareholders' equity in accumulated other comprehensive income. The effect of exchange rate changes on cash balances held in foreign currencies is separately reported as part of the reconciliation of the change in cash balances for the period. The U.S. dollar experienced increases and decreases against the Canadian dollar at times during the three months and twelve months ended December 31, 2015, and based on the timing and level of cash held in U.S. dollars, the Company has recorded a $0.2 million and $0.5 million gain on cash held in foreign currency in the three and twelve months ended December 31, 2015, respectively.

Due to a significant increase in the rate of exchange to translate the assets and liabilities of the Company's subsidiaries with a U.S. dollar functional currency at the current year-end date (2015 – 1.38; 2014 – 1.16) coupled with an increase in the net assets of these subsidiaries, the Company recorded a $16.8 million currency translation gain in other comprehensive income (2014 - $7.3 million gain).

Credit Facilities and Subordinated Debentures

On June 30, 2015, the Company and a syndicate of Canadian banks agreed to amend and restate the credit facility available to the Company, which is effective until September 30, 2017 and consists of a $175 million extendible revolving operating loan. At March 8, 2016, there was approximately $122 million drawn on the credit facility. Pursuant to the terms of the credit facility, the Company has the ability to request an additional $50 million of loan availability (to be provided by the lenders on a best-effort basis).

The Company's credit facility is subject to a number of financial covenants. Under the terms of the Company's credit facility, the following ratios are monitored: funded debt to EBITDA, adjusted debt to EBITDAR, and fixed coverage ratio. There are no financial covenants attributable to the Company's convertible unsecured subordinated debentures due April 30, 2018.

<u>Funded debt to EBITDA ratio</u>

Funded debt is all the Company's obligations, liabilities and indebtedness which would, in accordance with IFRS, be classified on a consolidated balance sheet of the Company as indebtedness for borrowed money of the Company, but excludes subordinated debt, deferred taxes and accounts payable incurred in the ordinary course of the Company's business.

EBITDA is defined under the amended and restated credit facility as the net income of the Company plus the following: interest expense, provision for income taxes, any portion of expense in respect of non-cash items including any long-term incentive plan amounts not to be settled in cash, depreciation, amortization, deferred taxes, and non-recurring losses to a maximum of $4.5 million in any fiscal year, write down of goodwill and other restructuring charges for store closures, and amortization of inventory fair value adjustments. EBITDA is also less any non-recurring extraordinary or one-time gains from any capital asset sales or certain foreign currency transactions.

Adjusted debt to EBITDAR

Adjusted debt is defined as the Company's debt plus seven times aggregate rent expense. EBITDAR is defined as EBITDA plus aggregate rent expense.

Fixed charge coverage ratio

Fixed charge coverage ratio is the ratio of EBITDAR less the aggregate amount of unfunded capital expenditures and cash taxes divided by the sum of all interest expense and scheduled repayment of debt for the relevant period, cash dividends and rent.

As at December 31, 2015, the Company was in compliance with all financial covenants.

Ratio	**Covenant**	**As at December 31, 2015**
Funded debt to EBITDA	< 3.50:1.00	1.61
Adjusted debt to EBITDAR	< 5.00:1.00	3.89
Fixed charge coverage	> or = 0.90:1.00(1)	1.00

(1) *Effective March 31, 2016 and thereafter, the fixed charge covenant will be greater than or equal to 1.00:1.00.*

The funded debt to EBITDA, adjusted debt to EBITDAR and fixed charge coverage ratios are calculated quarterly based on the latest rolling four quarter period completed, including acquired stores.

The Company has $67.5 million in aggregate principal amount of convertible unsecured subordinated debentures due April 30, 2018 (the "Debentures"). The Debentures bear interest at a rate of 5.85% per annum, payable semi-annually in arrears on April 30 and October 31 of each year, the first interest payment having been paid on October 31, 2012. The Debentures are convertible at any time at the option of the holders into common shares of the Company at a conversion price of $24.90 per share.

On and after April 30, 2015 and prior to April 30, 2017, the Debentures may be redeemed by the Company, in whole or in part from time to time, on not more than 60 days and not less than 30 days prior notice at a redemption price equal to their principal amount plus accrued and unpaid interest, if any, up to but excluding the date set for redemption, provided that the volume-weighted average trading price of the Common Shares on the TSX for the 20 consecutive trading days ending five trading days prior to the date on which notice of redemption is provided is at least 125% of the Conversion Price. On or after April 30, 2017 and prior to the maturity date, the Company may, at its option, redeem the Debentures by way of cash payment or through the issuance of common shares, in whole or in part, from time to time at par plus accrued and unpaid interest.

Liquidity Risk

Liquidity ensures the Company has sufficient financial resources available at all times to meet its obligations. The Company manages liquidity risk by ensuring it has a variety of alternatives available to fund acquisitions, new store development and ongoing operations, which include cash provided by operations, bank indebtedness, issuance of new equity or debt instruments or a combination thereof. The decision to utilize a specific alternative is dependent upon capital market conditions and interest rate levels. The degree to which the Company is leveraged may impact its ability to obtain additional financing for working capital or to finance acquisitions.

Management continuously monitors the marketplace for acquisitions and new store development opportunities and has developed financing strategies to support this growth in the current economic environment. Management believes the Company has managed liquidity risk appropriately and does not anticipate that the current economic environment will prevent the Company from being able to fund operating and liquidity needs in the near term. As at March 8, 2016, the Company has undrawn credit of approximately $36 million under its credit facility available to finance operating requirements, growth opportunities and for general corporate purposes.

Interest Rate Risk and Sensitivity

The Company's indebtedness in respect of its credit facility bears interest at floating rates. The Company manages its interest rate risk through credit facility negotiations and by identifying upcoming credit requirements based on strategic plans. The Company was party to an interest rate swap with a Canadian Schedule I bank that matured December 14, 2015 whereby the interest rate paid by the Company on $60.0 million was equivalent to 1.388% per annum. To replace the expiring swap, the Company entered into a forward starting interest rate swap on August 31, 2015 effective on December 14, 2015 and expiring December 14, 2019, to fix the effective interest rate on a notional $60 million of principal debt with a rate equivalent to 1.23% plus the applicable credit spread determined with reference to the credit facility. At March 9, 2016, the fixed rate paid by the Company on the notional amount of the interest rate swap is 2.98% per annum after taking into account the applicable credit spread determined with reference to the credit facility. The Company is not using hedge accounting for this swap, and accordingly, its fair value is recorded on the statement of financial position, with changes in fair value recorded in earnings.

Assuming an outstanding long-term debt of $65.4 million, of which $60.0 million is subject to the interest rate swap, the following table presents a sensitivity analysis to changes in market interest rates on floating rate indebtedness and their potential annual impact on the Company as at December 31, 2015:

(expressed in thousands)	*+ 1.00%*	*- 1.00%*
Increase (decrease) in interest expense	54	(54)
Increase (decrease) in net earnings (loss)	(40)	40

An increase/decrease of 1.00% in market interest rates would result in a nominal decrease/increase in the Company's net loss per share.

Credit Risk

The Company's financial assets that are exposed to credit risk consist primarily of cash and cash equivalents and accounts receivable. The Company maintains its cash and cash equivalents with a major Canadian chartered bank. The Company, in its normal course of operations, is exposed to credit risk from its wholesale customers in Alberta; however, wholesale customer purchases represent less than 5% of the Company's sales. Risk associated with accounts receivable is mitigated by credit management policies. Historically, bad debts from these accounts have been insignificant. The Company is not subject to significant concentration of credit risk with respect to its customers; primarily all receivables are due from businesses in the Alberta hospitality industry. Bad debts are insignificant in relation to total sales.

Foreign Exchange Risk

The Company is subject to fluctuations in the value of the Canadian dollar relative to the U.S. dollar in the normal course of business. A portion of cash flows are realized in U.S. dollars and as such, fluctuations in the exchange rate between the Canadian dollar and U.S. dollar may have an effect on financial results.

Transactions denominated in foreign currencies are recorded at the rate of exchange on the transaction date. Monetary assets and liabilities are translated into Canadian dollars at the rate of exchange prevailing at the balance sheet date, with any resulting gain or loss being included in earnings. This exposure primarily relates to U.S. intercompany management fees and interest payments which totalled US$4,363 million for the year ended December 31, 2015.

The accounts of the Company's subsidiaries with a U.S. dollar functional currency are translated into Canadian dollars as follows:

- Assets and liabilities are translated at the rate of exchange in effect at the balance sheet date; and
- Revenue and expense items (including amortization) are translated at the average rate of exchange for the period.

The resulting unrealized exchange gains and losses from these translation adjustments are included as a separate component of shareholders' equity in accumulated other comprehensive income. The Company manages this exposure by funding significant investments in these subsidiaries in USD borrowings where possible.

Other than as noted above, foreign currency transactions are generally not material.

Contractual Obligations

The table below sets forth, as of December 31, 2015, the contractual obligations of the Company due in the years indicated and relate to various premises operating leases, finance leases for a portion of our vehicles, software licenses and maintenance, long-term debt and convertible unsecured subordinated debentures.

(expressed in thousands)	**2016**	**2017**	**2018**	**2019**	**2020**	**2021 and thereafter**
Operating leases	32,920	29,871	26,430	22,300	18,852	69,845
Finance leases	113	111	119	119		
5.85% Debentures	-	-	67,500	-	-	-
Long-term bank indebtedness	-	65,412	-	-	-	-
Software licenses and maintenance	511	587	293	297	99	-
Total	33,544	95,981	94,342	22,716	18,951	69,845

5. Analysis of Consolidated Financial Position

Selected accounts (Cdn $000's)	As at December 31, 2015	As at December 31, 2014
Cash	3,790	3,003
Accounts receivable	6,020	2,099
Inventory	157,102	135,363
Total current assets	178,000	149,618
Property and equipment	64,781	51,008
Intangible assets	43,312	36,714
Goodwill	158,987	284,607
Total assets	455,554	525,865
Accounts payable and accrued liabilities	61,628	48,629
Dividends payable	2,470	2,452
Total current liabilities	64,795	51,124
Long-term debt	129,566	92,037
Total liabilities	199,818	161,107

The Company has a significant investment in working capital that is primarily due to the Company being required, consistent with other liquor retailers, to pay for inventory prior to receiving it in Alberta and British Columbia. As we do not have traditional payment terms on our inventory, our working capital is higher in these regions compared to that in Kentucky and Alaska where we generally have 30 day trade payment terms. At December 31, 2015, net working capital (current assets, excluding cash, less current liabilities) was $109.4 million, a $13.9 million increase from the comparative period last year (2014 - $95.5 million). This increase is primarily attributable to the change in foreign exchange on translation of U.S. dollar denominated working capital to Canadian dollars, offset by a reduction in inventory on a same-store basis.

- Accounts receivable increased $3.9 million to $6.0 million as at December 31, 2015 primarily as a result of an increase in our wholesale business with licensee customers on account, an increase in income taxes recoverable and an increase in tenant improvement allowances receivable related to new stores and store renovations completed in 2015.

- Inventory increased by $21.7 million to $157.1 million as at December 31, 2015 primarily due to an $8.5 million increase related to the strengthening of the U.S. dollar vs. the Canadian dollar in 2015 and $10.7 million increase for inventory used to stock new stores that opened during the year. The remaining increase related to increased inventory purchases towards year end compared to the prior year end to increase our stock of preferred label products. This increase in inventory was partially offset by a continued reduction in inventory on a same-store basis, which is attributable to Management's focus on increasing inventory turns.

- Accounts payable and accrued liabilities increased by $13.0 million to $61.6 million as at December 31, 2015 primarily due to a $6.9 million increase related to the strengthening of the U.S. dollar vs. the Canadian dollar in 2015. The remaining increase related to increased accruals related to expenditures on the implementation of our new enterprise resource planning system in the fourth quarter and increased inventory purchases in the U.S. compared to the prior year end.

- The carrying value of property and equipment was $64.8 million, a $13.8 million increase from the prior year end (December 31, 2014 - $51.0 million). Additions during the period of $27.0 million (2014 - $12.8 million) were related primarily to the thirteen new stores opened in the year (2014 – nine) and maintenance capital expenditures. These additions were offset by amortization of $10.8 million (2014 - $10.0 million) and the disposition of a property in Fairbanks, Alaska with carrying value of $5.5 million at the time of disposal (via a sale lease back transaction). Foreign exchange differences on property and equipment assets held in the U.S. resulted in an increase in the carrying value of $3.4 million (2014 - $1.4 million). The increase in additions in the period is a result of developing and acquiring more stores compared to the prior year (thirteen stores opened in 2015 compared to seven in 2014), of which a larger proportion of destination and mid-size format stores (five in 2015 compared to one in 2014) were constructed or acquired in the current year.

- Long-term debt was $129.6 million at December 31, 2015, a $37.6 million increase from the prior year (2014 - $92.0 million). During the year, there were net proceeds of long-term debt of $36.1 million (2014 – net repayments of $42.9 million), finance costs paid of $0.5 million in 2015 (2014 – $0.4 million) that were recognized against the carrying value of long-term debt, $1.6 million was recognized as accretion of the subordinated convertible debentures and amortization of deferred financing charges (2014 - $1.5 million), and a finance lease obligation of $0.4 million from new lease agreements entered into during 2015. The increase in long-term debt from the prior year primarily related to the Company using the net proceeds of a common share issuance in December 2014 to repay long term debt, with subsequent draws on our credit facility throughout 2015 to finance capital expenditures and the execution of the Company's business strategies.

As at December 31, 2015 and March 9, 2016, the Company did not have any off-balance sheet arrangements in place, other than the operating leases identified under the heading Contractual Obligations.

6. Shareholders' Equity

At December 31, 2015, the Company had 27,449,891 common shares outstanding. The basic and diluted weighted average number of common shares outstanding for the year ended December 31, 2015 was 27,329,145 and 27,376,270, respectively (compared to 23,343,836 for the comparative period for both basic and diluted weighted average number of common shares outstanding). As at March 9, 2016, 27,523,677 common shares of the Company were issued and outstanding.

7. Dividends

Dividend Policy

Up to and including the dividend declared on February 15th, 2016, which is payable on March 15, 2016 to shareholders on record on February 29, 2016, the Company paid a monthly dividend of $0.09 per Common Share. On March 9, 2016 the Company announced a reduction in its dividend to $0.03 per Common Share. Dividends are paid, if declared, on or about the 15th day of each month to Shareholders of record at the end of the previous month.

The amount of future cash dividends, if any, will be subject to the discretion of the Board of Directors and may vary depending on a variety of factors and conditions existing from time to time, including the prevailing economic and competitive environment, Liquor Stores' results of operations and earnings, financial requirements for Liquor Stores' operations and the execution of its growth strategy, fluctuations in working capital, capital expenditures and debt service requirements, contractual restrictions and financing agreement covenants, the satisfaction of solvency tests imposed by the CBCA for the declaration and payment of dividends, and other factors and conditions existing from time to time. Depending on these and various other factors, many of which are beyond the control of the Board and Liquor Stores' management team, the Board may change our dividend policy from time to time, and as a result, future cash dividends could be reduced or suspended entirely. The market value of the Common Shares may deteriorate if the Board reduces or suspends the amount of cash dividends that Liquor Stores pays in the future and such deterioration may be material. See "*Risk Factors*".

Although it is expected that dividends declared and paid by us will qualify as "eligible dividends" for the purposes of the Tax Act, and thus qualify for the enhanced gross-up and tax credit regime available to certain holders of Common Shares, no assurances can be given that all dividends will be designated as "eligible dividends" or qualify as "eligible dividends".

The agreement governing Liquor Stores' Credit Facility contains provisions which restrict its ability to pay dividends to Shareholders in the event of the occurrence of certain events of default. The full text of the agreement governing Liquor Stores' Credit Facility is available on SEDAR at www.sedar.com. For additional information regarding the Credit Facility, see note 10 to Liquor Stores' audited consolidated financial statements for the year ended December 31, 2015, and "Liquidity and Capital Resources" section within this MD&A.

Dividend Reinvestment Plan

The Company has a Dividend Reinvestment Plan (the "DRIP" or the "Plan") which provides shareholders with a cost-effective and convenient method of reinvesting their monthly cash dividends into additional common shares of the Company. Presently, shares issued pursuant to the DRIP are issued at a discount of 3% from the market price (as such term is defined in the Plan) and no brokerage or administration fees are charged by the Company for participating in the Plan.

As at February 29, 2016, shareholders enrolled in the DRIP held approximately 3.2 million shares.

Further information concerning the DRIP, including enrolment forms for the Plan, is available on the Company's website at www.liquorstoresna.ca.

8. Related Party Transactions

The Company has a conflict of interest policy that requires the disclosure of potential conflicts and excludes persons with a material conflict of interest from any related decisions.

During the year ended December 31, 2015, the Company incurred expenses in the normal course of business for professional fees of $86 thousand (2014 - $85 thousand) paid to a law firm of which a director of the Company is a partner and recognized professional fees of $50 thousand from this same firm in the carrying value of long-term debt. The amounts charged are recorded at their exchange amounts and are subject to normal trade terms.

9. Financial Instruments

The Company, as part of its operations, is party to a number of financial instruments. These financial instruments consist of cash and cash equivalents, accounts receivable, foreign exchange currency contracts, an interest rate swap, bank indebtedness, accounts payable and accrued liabilities, dividends payable and long-term debt including convertible unsecured subordinated debentures. Financial assets are classified as loans and receivables. Financial liabilities are classified as other financial liabilities, other than derivatives which are held for trading. Refer to *"Liquidity and Capital Resources"* for discussion of risks associated with financial instruments.

10. Business Overview

Liquor Stores is a leading liquor retailer in the North American marketplace. We have a strong base in western Canada and we are a market leader in Kentucky and Alaska. Management believes the Company is the largest liquor store operator in Alberta, Canada's largest private liquor retailer and North America's largest publicly-traded liquor retailer (based upon number of stores and revenue). We have positioned our business to attract customers who are focused on convenience and those who are looking for a destination-type shopping experience.

The Company primarily operates under the brand names: "Liquor Depot", "Liquor Barn" and "Wine and Beyond" in Alberta; "Liquor Depot", "Liquor Barn", and "Wine Cellar" in British Columbia; "Brown Jug" in Alaska; and "Liquor Barn, The Ultimate Party Source" and "Liquor Barn Express" in Kentucky.

Effective January 4, 2016, the Company acquired a 51% ownership interest in Birchfield Ventures, LLC. Birchfield Ventures, LLC operates two stores in New Jersey under the banner "Joe Canal's Discount Liquor Outlets". These stores are large destination/large format stores with areas of 17,000 and 25,000 square feet respectively.

As of March 9, 2016, the Company operated 254 stores in Alberta, British Columbia, Alaska, Kentucky and New Jersey, comprised of 16 destination/large-format stores, 236 full liquor stores, and two wine only stores. Product selection is tailored to each location. Stores in Canada generally range in size from 2,000 to 5,000 square feet. Our U.S. stores are larger in size. The Company's stores in Alaska range in size from 1,400 to 14,000 square feet and we have one combined store and warehouse in excess of 40,000 square feet. Our Kentucky stores range in size from 2,700 to 30,000 square feet along with a flagship store of 44,000 square feet. Our three Wine & Beyond stores, our destination/large-format stores in Alberta, with areas of approximately 17,000 and 20,000 square feet, respectively, are the largest liquor retail stores in western Canada.

The following provides a summary of the Company's locations as at December 31, 2015:

	2015			
	1-Jan-15	**Opened[5]**	**Closed[6]**	**31-Dec-15**
Alberta				
Edmonton[1]	79	5	(1)	83
Calgary[1]	43	2	-	45
Other[2]	50	2	-	52
	172	9	(1)	180
British Columbia				
Interior	11	-	-	11
Lower Mainland	13	1	(1)	13
Vancouver Island	11	-	-	11
	35	1	(1)	35
Alaska				
Anchorage	19	-	(1)	18
Other[3]	4	-	-	4
	23	-	(1)	22
Kentucky				
Lexington	6	-	-	6
Louisville	4	2	-	6
Other[4]	3	1	(1)	3
	13	3	(1)	15
Total	**243**	**13**	**(4)**	**252**

As at March 9, 2016, there have been no changes to the above other than for the acquisition of a 51% interest in Birchfield Ventures, LLP on January 4, 2016, as discussed above.

Notes:

(1) *References to Edmonton and Calgary are to stores located in or near those urban centres.*

(2) *Other stores in Alberta by region: Northern (26), Southern (nine), Central (15) and resort communities (two).*

(3) *Other communities served in Alaska include Wasilla (three) and Fairbanks (one).*

(4) *Other communities served in Kentucky include Danville, Bowling Green and Elizabethtown.*

(5) *All stores opened were developed by the Company with the exception of one retail liquor store acquired by the Company in the Edmonton region in June 2015.*

(6) *The stores closed by region:*

  a. *Edmonton – one store closed due to underperformance*

  b. *Lower Mainland BC – one store closed as part of a planned relocation to another site within the same municipality*

  c. *Anchorage – one store closed due to underperformance*

  d. *Other Kentucky – one store closed as part of a planned relocation to another site within the same trade area*

Competitive Differentiation

Management focuses on differentiating the Company's stores from the competition by promoting a broad selection of products, by emphasizing our in-store customer experience, and through continued marketing and development of well-known industry-leading brands. Management believes that its emphasis on offering a range of stores from large-format/destination-type stores (with a strong focus on product selection and customer experience) to convenience-focused stores (convenient and high-traffic locations) assists the Company in differentiating itself from its competitors.

Seasonality

The retail liquor industry is subject to seasonal variations. The Company's sales are typically lowest early in the year and increase in the latter half. In 2015, 20% (2014 - 20%) of annual same store sales occurred in the first quarter, 26% (2014 - 26%) in the second quarter, 26% (2014 - 26%) in the third quarter, and 28% (2014 - 28%) in the fourth quarter. Our working capital requirements are greatest in the second and third quarters as we ramp up inventory for the summer and the holiday seasons, respectively.

Policy on Same-Store Sales Comparisons

Comparable same-store sales, a measure that is generally used by retailers, includes sales for stores that have been open 12 full months at the beginning of the reporting period. This is one of the key metrics that we use to assess our performance and provides a useful comparison between periods. Same-store sales exclude: (i) all sales to wholesale customers, (ii) stores where same-store sales have been negatively impacted due to sales being shifted to closely-located convenience-focused stores we've opened in the last 12 full months, and (iii) stores where same-store sales have increased due to the closure of closely-located stores in the last 12 full months.

11. Business Strengths

We attribute our success to the following competitive strengths:

Our Brands - The retail liquor store industry in Alberta, British Columbia, Kentucky, Alaska and New Jersey is a fragmented market. We operate some of the leading liquor retail brands in our respective markets. Our brands include:

- *Liquor Depot/Liquor Barn* – Convenience-focused stores located in Alberta and British Columbia, focused on convenient locations and store layouts, and great selection at fair prices.
- *Wine and Beyond* – Destination/large-format stores located in Alberta that are dedicated to having the best selection of wine, spirits and beer and strong customer service.
- *Wine Cellar* – Wine centric stores located in British Columbia, with a unique wine selection and a staff as passionate as our customers about the product that we sell.
- *Brown Jug* - Convenience-focused stores located in Alaska, focused on convenient locations and store layouts, and great selection at fair prices.
- *Liquor Barn, The Ultimate Party Source* - Destination/large-format stores located in Kentucky that are dedicated to having the best selection of wine, spirits, beer, and party supplies and strong customer service.
- *Liquor Barn Express* - Convenience-focused stores located in Kentucky, focused on convenient locations and store layouts, and great selection at fair prices.
- *Joe Canal's Discount Liquor Outlets* - Destination/large-format stores located in New Jersey, focused on high-traffic locations, having the best selection of wine, spirits, beer at fair prices.

Location - Liquor Stores' business model is based on highly visible and accessible store locations. We endeavour to locate our stores in areas where access to customers is maximized such as near grocery stores or on main arteries in or near residential areas. Approximately 60% of Liquor Stores' Canadian outlets are located in or near shopping centres with major grocery stores or other anchor tenants. With respect to its U.S. operations, Management believes that location is a key factor in the success of a liquor store and consequently we endeavour to locate our stores in high-traffic areas and major thoroughfares. Although very few of Liquor Stores' U.S. outlets are located in or near shopping centers with grocery stores and large anchor tenants, Management believes its U.S. stores enjoy easy-customer access and enhanced street visibility.

Product Selection - Our stores offer an impressive selection of wine, spirits, coolers, liqueurs, beer, and specialty products. Product selection is individually tailored to our store brands and formats. In our convenience-focused stores, product selection varies between 1,000 and 4,000 wine, spirit, cooler and beer items, which management believes is a larger product selection and inventory than the industry average. Our Wine and Beyond large-format "destination" stores offer over 10,000 items. New, exclusive and preferred label varieties and products arrive in our stores throughout the year. Similar to our Wine and Beyond stores, our U.S. stores offer a significantly larger product selection than our convenience-focused stores, and although selection is again location-specific, alcoholic product selection in certain U.S. stores generally exceeds 7,000 items. In addition, we sell non-alcoholic beverages including pop, juice, bottled water and mixes, along with accessories for gift giving and everyday use such as gift bags, wine charms, bottle stoppers, aerators, bar supplies and unique items. In Kentucky we have a specialty grocery offering focused on party and entertainment food items such as cheese, deli meats, olives, chips and crackers, desserts, and select frozen food items.

Effective Sales Staff - We pride ourselves on our customer service with employees who are well-versed in each liquor category to best serve our customers. We strive to have dedicated staff with product knowledge that they are enthusiastic to share. Liquor Stores endeavours to maintain product knowledgeable managers, assistant managers and line staff through frequent seminars and training. In 2013, we implemented a new company-wide training program called Liquor Stores University offered in person and online, with a goal of further fostering a customer-focused sales-driven culture in our stores. All new staff members receive training in Company policies and basic product knowledge, selling skills, operations overview, loss prevention and robbery prevention. In the destination/large-format stores, store staff includes well-trained wine, beer, and spirits specialists.

Strategic Markets - Management's primary strategy in Canada and the United States is to focus on urban centres such as the Calgary, Edmonton, Vancouver, and the Anchorage, Louisville, Lexington and Princeton metropolitan areas. Here we find the best opportunities for larger per store revenues and likelihood of population increases. The Company is also exploring potential growth opportunities in other U.S. cities. While our focus is primarily on urban centres, we also have stores in other communities including rural or smaller urban centres where demographic and economic conditions warrant, such as those with resource-based economies. Such communities include Ft. McMurray, Alberta (seven stores), Grande Prairie (nine stores) and the destination/large-format store in Fairbanks, Alaska.

Store Design and Format - Liquor Stores generally designs its stores to optimize traffic flow and present its products in an upscale environment. Management has recently initiated a store "refresh" program and intends to update, modernize and refurbish a large number of stores. Our stores feature wooden cases and tasteful shelving as a primary display mechanism. Innovative new store layouts feature a fresh, contemporary design and interactive experiences. In certain stores, we offer in-store tasting sessions, seminars, recipes, social events and other in-store initiatives to enhance our customers' experience and to promote new products.

Economies of Scale - Liquor Stores' leading market position, large-scale operations (relative to most other industry participants), and cross-border presence provide it with a number of competitive advantages including: the benefit of operating efficiencies relative to non-liquor expenses (including finance, marketing, human resources, and corporate); and greater access to capital. In our US markets, we benefit from purchasing efficiencies and we have the ability to negotiate volume-discounts on our liquor purchases. As we continue to expand in these U.S. jurisdictions, and possibly others, we expect our competitive purchasing advantage to increase.

Stable and Growing Industry - The retail liquor business in our current geographic markets is characterized by relatively stable demand. Total wholesale liquor sales in Alberta grew by 4.4%[6], and was down by 0.2%[1] in British Columbia during the year ended March 31, 2014. Comparable annual sales information is not available for either of Alaska or Kentucky.

12. Company Strategy

As previously communicated in our 2014 MD&A, we are focused on the following Seven Point Plan (the "Plan") to build on our competitive position, invest in opportunities to support long-term profitability and drive growth across our business:

- Enhance the Senior Leadership Team
- Invest in our People

[6] *Source: Statistics Canada, May 2015*

- Implement an Industry Leading Information Technology Platform
- Invest in our Store Network
- Increase Brand Awareness and Loyalty
- Increase Operating Margins
- Pursue Expansion

In 2015, the Company achieved or partially achieved its objectives against this plan. In 2016, Liquor Stores intends to build on the success to date with expansion of initiatives related to investment in people, brand awareness and loyalty and product selection designed to increase operating margins.

Liquor Stores intends to adopt a measured approach to growth that will be scaled up or down depending on market conditions. The goal is to advance the seven point plan initiatives to invest in the store network and pursue expansion, while ensuring that the Company can withstand a prolonged period of economic pressure in Alberta as discussed further in the Outlook section later in this document.

The following is a summary of the 2015 goals as included in our 2014 MD&A and progress made in 2015, along with a summary of our 2016 goals.

Business Strategy	Goals for 2015	2015 Progress	Goals for 2016
1. Enhance the Senior Leadership Team We have an opportunity to drive sales and further improve profitability of the current business, and further position the Company for growth in new markets by hiring certain key executives with deep retail experience in both Canada and the United States.	We are targeting to hire two new executives in the next six to twelve months who come from leading Canadian or U.S. companies to lead our Marketing and Real Estate teams. The costs associated with these positions are anticipated to be cost neutral, as a result of offsetting cost savings in these departments.	**Status:** **Achieved** We have successfully completed the required enhancements to our Senior Leadership team. Working out of our corporate headquarters in Edmonton and Louisville, Kentucky, our team is leading the implementation of refined business processes and strategies to optimize and scale Liquor Stores' existing platform and support the future growth of our enterprise in our existing markets and new markets, primarily in the United States.	N/A – completed in 2015
2. Invest in our People We have an opportunity to attract more customers to existing locations and increase sales per customer by improving our customer service. Our investments will include enhancing our hiring and retention strategies, the introduction of industry leading training programs, implementing competitive store level compensation and benefit programs, and a focus on providing our employees with career and performance management.	Deliver the next phase of our sales, workforce management and store operational training programs to at least 75% of our store managers by the end of 2015. Enhance our current store level incentive program to further align our store teams with our strategy related to preferred label products.	**Status:** **Achieved** During the year we continued developing and delivered new training material to our staff and met our goal to deliver this training program to over 75% of our store managers. We also implemented planned refinements to our store level incentive plan where our store teams have a portion of their incentive plan determined based on sales of our preferred label products.	Program Expansion Deliver our sales, workforce management and store operational training programs to at least 90% of our store managers by the end of 2016. Enhance our current store level incentive program to continue to further align our store teams with our strategy related to preferred label products by adding further stretch goals to increase our preferred label penetration even further.

Business Strategy	Goals for 2015	2015 Progress	Goals for 2016
3. Implement an Industry Leading Information Technology Platform We have an opportunity to build on our competitive position by implementing a new enterprise resource planning ("ERP") system that will drive new efficiencies into our organization, provide enhanced visibility into business operations that will drive down costs, and provide a scalable growth platform that will allow us to grow organically and smoothly integrate newly acquired business.	Achieve significant milestones in the implementation of the Company's new ERP system with little or no impact on customers. Milestones include completing the planning and design phase of the implementation process by the end of 2016, implementation of the financial modules by mid-2017, and the remainder of the core modules by the end of 2017.	**Status:** **Partially Achieved** In Q4 2015, we completed the blue-printing and design phase of the project, on-schedule and on-budget. To adjust to current economic conditions, the Company is revising its expectation to introduce a new enterprise resource planning system, which was previously expected to be implemented by the end of 2017. The implementation will be delayed and a revised schedule has not yet been set.	Deferred - Dependent on Market Conditions Continue to evaluate economic conditions throughout the year, and if they show a sustained improvement, develop a revised implementation schedule.
4. Invest in our Store Network We have an opportunity to attract more customers to existing locations and increase sales per customer through renovating and refreshing our existing stores, and by implementing a consistent store layout and design across our network to further enhance our brand with our customers.	Renovate/refresh 5% to 8% of our existing stores in 2015. This range has been set to allow for the number of projects to be scaled up or down depending on economic conditions and the Company's financial position.	**Status:** **Partially Achieved** The Company completed renovations for nine stores in 2015 and has noted a measured increase in same-stores sales as a result of these renovated stores. However, in response to the decline in Alberta economy discussed earlier in the MD&A, Management made the decision to defer several planned renovations until economic conditions stabilize.	Measured Growth - Dependent on Market Conditions Invest approximately $2.5 million on store refurbishments. This spend could adjust higher or lower depending on volatility of economic conditions in our key markets Continue to evaluate economic conditions throughout the year, and if they show a sustained improvement, develop a revised store renovation schedule.
5. Increase Brand Awareness and Loyalty We will continue to increase our brand awareness and customer loyalty through investment in our store network, our marketing strategy, our digital marketing initiatives, and our brand advertising and public relations efforts.	Hire a Senior Vice President of Marketing to lead the enhancement and execution of our marketing and promotions strategies. Continue to enhance our customer relationship management strategy, and grow the number of customers enrolled in this program in 2015. Continue to increase selection and promotion of private label and control brands that customers enjoy and will only find in our stores.	**Status:** **Achieved** Our new Senior Vice President of Marketing was hired in early Q2 2015. We continue to enhance our marketing and promotion strategies, with a focus on digital forms of advertising to increase our brand awareness and sign-ups in our customer relationship management program, the Celebration Members Club. Our merchants have remained focused on sourcing exclusive and control brands from our suppliers. We continue to introduce a selection of new items and have provided all of our store managers with training on how to merchandise and sell these items.	Expansion Continue to enhance our customer relationship management strategy, and grow the number of customers enrolled in this program in 2016. Continue to increase selection and promotion of private label and control brands that customers enjoy and will only find in our stores.

Business Strategy	Goals for 2015	2015 Progress	Goals for 2016
6. Increase Operating Margins We have the opportunity to continue to improve our operating margins by leveraging our fixed occupancy costs and scalable infrastructure.	Continue to implement product assortment plans (i.e. planograms) into our store locations in 2015. Continue to grow our control/exclusive brands ("preferred label") across all regions as a percentage of their respective categories.	**Status:** Achieved We are currently implementing product assortment plans into all new and renovated stores, and into a selection of our existing stores. Our merchants have been focused on sourcing exclusive and control brands from our suppliers. Control/exclusive brand sales as a percentage of their respective categories continue to grow.	Expansion Continue to implement product assortment plans (i.e. planograms) into our store locations in 2016. Continue to increase selection and promotion of private label and control brands that customers enjoy and will only find in our stores.
7. Pursue Expansion We plan to strategically expand our business in existing markets in Canada and the United States, and into select new markets in the United States over the next several years. We believe that brand positioning and emphasis on in-store experience for our customers will have a strong appeal.	Targeting a 2% to 3% organic store growth rate per year for the next two to three years. Strategically invest in new square footage in our existing regions as a result of population growth and, in the case of Kentucky, capitalize on opportunities resulting from certain counties going from 'dry' to 'wet'. The Company continually explores opportunities to develop and/or acquire stores in Alberta, British Columbia and the United States where regulatory regimes permit private liquor stores. Management will continue to evaluate and assess potential store development and store acquisition opportunities for their ability to add accretive cash flow and shareholder value. Developing new destination-focused/large-format stores in our current regions to complement our existing convenience-focused store network and expand market share. Sourcing opportunities to expand geographically through new store development and/or acquisitions to capitalize on opportunities in new regions and to reduce the concentration risk of any particular region. Based on a proven track record of success, the Company anticipates it will invest significantly in large format expansion in both Canada and the United States.	**Status:** Achieved In 2015, we opened 10 new convenience-format stores in Canada and 3 large-format stores in Kentucky in the United States. We also completed the acquisition of Birchfield Venture LLC, operating two large format stores in New Jersey, a new region for the Company.	Measured Growth – Dependent on Market Conditions To adjust to current economic conditions, the Company expects to open four to seven new stores over the next 24 months. The Company will continue to monitor economic conditions and evaluate plans for 2017 new store constructions in due course. Management will continue to evaluate and assess potential store acquisitions for their ability to add accretive cash flow and create shareholder value.

13. Industry Regulation and Competitive Environment

Alberta is the only province in Canada that has a fully privatized retail distribution system for adult beverages. We currently operate 180 liquor stores in Alberta where there are 1,401 retail liquor stores and 91 agency stores[7]. Our "Liquor Depot" and "Liquor Barn" trade names are well recognized throughout the province as leading alcoholic beverage retailers.

We operate 35 stores in British Columbia. British Columbia's model for liquor distribution is a blend of 730 private stores and 196 government operated stores[8].

We operate 22 stores in Alaska, with 18 stores in the greater Anchorage area, three stores in Wasilla, and one in Fairbanks. Save for limited community liquor stores operated by certain municipal governments, there are no government owned or operated liquor stores and the state limits the number of liquor stores in the state to one per 3,000 people in urban areas. In Alaska, there are 363 retail liquor stores with 113 stores in the greater Anchorage, Wasilla and Fairbanks areas[9]. The Company's "Brown Jug" trade name is well recognized throughout the state as a leading alcoholic beverage retailer.

We operate fifteen stores in Kentucky of which seven are large format stores with six stores in Lexington (Fayette County), six stores in Louisville (Jefferson County), and one store in each of Danville (Boyle County), Bowling Green (Warren County), and Elizabethtown (Hardin County). In Kentucky, there are no government owned or operated liquor stores. Liquor licenses are permitted based on whether the sale of alcoholic beverages is allowed in each county (wet or dry). The Alcoholic Beverage Control Board limits the number of retail liquor package licenses issued in wet counties to one per 2,300 persons with the exception of counties containing cities of first class such as Louisville, where liquor licenses are limited to one for every 1,500 persons. Grocery stores and gas stations are able to sell beer, but a retail liquor package license is required to sell beer, wine and spirits. There are 921 package retail license stores in Kentucky with 272 in Jefferson County, 82 in Fayette County, 8 in Boyle County, 22 in Warren County, 22 in Hardin County[10].

14. Critical Accounting Estimates and Accounting Policies

The Company's summary of significant accounting policies are contained in note 3 to the audited consolidated financial statements.

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

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[7] Source: Alberta Gaming and Liquor Commission, as at February 2016.
[8] Source: British Columbia Liquor Distribution Branch, as at February 2016.
[9] Source: Alaska's Alcoholic Beverage Control Board, as at February 2016.
[10] Source: Kentucky's Alcoholic Beverage Control Board, as at February 2016.

The Company has:

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

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

- A mandate that includes ongoing development of procedures, standards and systems to allow staff to make the best decisions possible and ensuring those decisions are in compliance with the Company's policies.

Preparation of the Company's financial statements requires Management to make estimates and assumptions that affect (i) goodwill and intangible assets subsequent to acquisition, (ii) deferred income taxes, (iii) expense related to equity-settled share-based payments, and (iv) inventory. Below is a summary of how we apply these critical accounting estimates in our significant accounting policies:

Valuation of Goodwill and Intangible Assets

The Company accounts for intangible assets and goodwill in accordance with IFRS 3, Business Combinations and IAS 38, Intangible Assets. Subsequent to acquisition, goodwill and intangible assets with indefinite lives are not amortized, however they are periodically assessed for impairment in accordance with IAS 36. The Company reviews goodwill and intangible assets with indefinite lives at least annually, and other non-financial assets when there is any indication that the asset may be impaired. The recoverable amounts of cash-generating units have been determined using discounted cash flow models that require assumptions about future cash flows, margins and discount rates.

Although intangible assets with definite lives are amortized over their useful life, if the estimated value of an intangible asset has declined below its amortized book value, a write-down would be recorded in the period in which the event causing the decline in value occurred, which would increase amortization expense and decrease the intangible assets balance.

Deferred income taxes

Determining deferred income taxes involves a number of assumptions and variables that could reasonably change, including: the useful lives of recorded property and equipment and intangible assets that determine the amount of amortization recorded thereon; the amount of discretionary tax deductions the Company will claim from its existing tax depreciation pools, the rates of tax applicable to various jurisdictions in which the Company is taxable and the allocation of taxable income to those jurisdictions; and the acceptance of the Company's tax filing positions by the taxation authorities. Changes in these assumptions and variables, which are re-evaluated at each balance sheet date, could result in changes in the recorded amount of deferred income taxes, and these changes could be material.

Deferred income tax assets are assessed to determine the likelihood that they will be realized from future taxable income. Details of tax losses expected to be utilized on the basis of future taxable income are provided in note 13 of the 2015 consolidated financial statements.

Fair value of equity-settled share-based payments

The Company uses a pricing model to determine the fair value of certain share-based payments in accordance with IFRS 2 and IFRS 13. Inputs to the model are subject to various estimates relating to volatility, interest rates, dividend yields and expected life of the units issued. Fair value inputs are subject to market factors as well as internal estimates. The Company considers historic trends together with any new information to determine the best estimate of fair value at the date of the grant.

Separate from the fair value calculation, the Company is required to estimate the expected forfeiture rate of equity-settled share based payments.

Net realizable value of inventory

Inventories are carried at the lower of cost and net realizable value which requires the Company to utilize estimates related to fluctuations in future retail prices, seasonality and costs necessary to sell the inventory.

15. Non-IFRS Financial Measures

Same-store sales, operating margin, operating margin as a percentage of sales, adjusted operating margin, adjusting items, adjusted net earnings, adjusted basic and diluted earnings per share, cash provided by operating activities before changes in non-cash working capital, cash provided by operating activities before changes in non-cash working capital on a per share basis, cash provided by operating activities before changes in non-cash working capital and adjusted items, and cash provided by operating activities before changes in non-cash working capital and adjusted items on a per share basis are not measures recognized by IFRS and do not have a standardized meaning prescribed by IFRS. Investors are cautioned that these measures should not replace net earnings or loss (as determined in accordance with IFRS) as an indicator of the Company's performance, of its cash flows from operating, investing and financing activities or as a measure of its liquidity and cash flows. The Company's method of calculating the aforementioned non-IFRS measures may differ from the methods used by other issuers. Therefore, these measures may not be comparable to similar measures presented by other issuers.

- Same-store sales include sales for stores that have been open 12 full months at the beginning of the reporting period. This is one of the key metrics that we use to assess our performance and provides a useful comparison between periods. Same-store sales exclude: (i) all sales to wholesale customers, (ii) stores where same-store sales have been negatively impacted due to sales being shifted to closely-located convenience-focused stores we've opened in the last 12 full months, and (iii) stores where same-store sales have increased due to the closure of closely-located stores in the last 12 full months.

- Operating margin for purposes of disclosure under "Operating Results" has been derived by subtracting Operating and Administrative expenses from Gross Margin. Operating margin as a percentage of sales is calculated by dividing operating margin by sales.

- Adjusted operating margin represents operating margin adjusted for unusual, non-recurring or non-operating factors on both a consolidated and segmented basis. These factors, referred to as adjusting items, are reconciled and discussed in the *'Performance Overview'* section.

- Adjusted net earnings is calculated as net earnings or loss less the tax effected adjusting items. The tax effect of the adjusting items is calculated by multiplying the adjusting items by the statutory rate of income tax of the applicable jurisdiction. Adjusted basic and diluted earnings per share is calculated as adjusted net earnings divided by basic or diluted weighted average number of common shares outstanding.

Management believes the presentation of adjusted operating margin, adjusted net earnings, and adjusted basic and diluted earnings per share provides for useful information to investors and shareholders as it provides increased transparency and predictive value. Management uses adjusted operating margin to set targets and assess performance of the Company.

Cash provided by operating activities before changes in non-cash working capital and adjusting items is a non-IFRS financial measure that does not have a standardized meaning prescribed by IFRS and therefore is unlikely to be comparable to similar measures presented by other issuers. Investors are cautioned that this should not be construed as an alternative measure of profitability.

EBITDA and EBITDAR, which are used by Management only with reference to the calculation of covenants under the Company's credit facility, have been defined in the Liquidity and Capital Resources section of this MD&A.

Refer below for a reconciliation of operating margin and net earnings (loss) to adjusted operating margin and adjusted net earnings:

	Three months ended December 31,		**Year ended December 31,**	
(expressed in thousands)	**2015** (unaudited)	**2014** (unaudited)	**2015**	**2014**
Operating margin	$11,878	$13,742	$36,870	$36,530
Adjusting items:				
Costs associated with implementing a new enterprise resource system	465	-	1,240	-
Onerous contracts associated with delayed implementation of new enterprise resource management system	1,170	-	1,170	-
Legal, professional and travel fees incurred in evaluating potential acquisitions	458	-	719	-
Payments to a former member of senior management team upon departure from the Company	-	-	675	617
Payments made to members of a regional operations team upon termination	-	-	220	-
Settlement with vendor for software license fees	-	-	-	385
Legal and tax professional related to changes to the corporate structure	-	-	-	284
Early termination of a lease in conjunction with a store closure	-	-	-	100
Total adjusting items	2,093	-	4,024	1,386
Adjusted operating margin	13,971	13,742	40,894	37,916

(expressed in thousands)	Three months ended December 31, 2015 (unaudited)	Three months ended December 31, 2014 (unaudited)	Year ended December 31, 2015	Year ended December 31, 2014
Net earnings (loss)	($105,808)	$6,714	($99,392)	$12,949
Adjusting items:				
Costs associated with implementing a new enterprise resource system	465	-	1,240	-
Onerous contracts associated with delayed implementation of new enterprise resource management system	1,170	-	1,170	-
Legal, professional and travel fees incurred in evaluating potential acquisitions	458	-	719	-
Impairment loss related to goodwill and intangible assets	130,313	-	130,313	-
Payments to a former member of senior management team upon departure from the Company	-	-	675	617
Payments made to members of a regional operations team upon termination	-	-	220	-
Settlement with vendor for software license fees	-	-	-	385
Legal and tax professional related to changes to the corporate structure	-	-	-	284
Early termination of a lease in conjunction with a store closure	-	-	-	100
Total adjusting items	132,406	-	134,337	1,386
Tax effect of adjusting items	(20,009)	-	(20,513)	(347)
Total adjusting items, after tax	112,397	-	113,824	1,039
Re-measurement of opening net deferred tax liabilities for change in Alberta corporate tax rate on July 1, 2015	-	-	1,290	-
Adjusted net earnings	6,589	6,714	15,722	13,988

16. Risk Factors

The following is a summary of certain risk factors relating to the affairs and business of Liquor Stores. The following information is a summary only of certain risk factors and is qualified in its entirety by reference to, and must be read in conjunction with, the detailed information appearing elsewhere in this MD&A and our Annual Information Form. Shareholders and potential Shareholders (and other security holders) should consider carefully the information contained herein and, in particular, the following risk factors. These risks and uncertainties are not the only ones facing Liquor Stores. Additional risks and uncertainties not currently known to Liquor Stores, or that Liquor Stores currently considers immaterial, may also impair the business and operations of Liquor Stores. If any of these risks actually occur, the business, sales, financial condition, liquidity or results of operations of Liquor Stores could be materially adversely affected, with a resulting decrease in or elimination of the dividends paid on, and the market price of, the Common Shares.

Government Regulation

Liquor Stores operates in the highly regulated retail liquor industry in the Provinces of Alberta and British Columbia and the States of Alaska, Kentucky and New Jersey. Decisions by the Alberta Gaming and Liquor Commission ("AGLC"), British Columbia Liquor Control and Licensing Branch ("BCLCLB"), Alaska Alcoholic Beverage Control Board ("ABCB"), the New Jersey Division of Alcoholic Beverage Control (the "NJABC") and Kentucky Department of Alcoholic Beverage Control ("KYABC") and rules enacted by them or by other governmental authorities (including state, provincial, county, municipal or other local governments), new legislation, regulations, rules, or bylaws, or changes to existing legislation, regulations, rules, or bylaws, can materially impact the operations of Liquor Stores, both favourably and unfavourably. Changes in legislation, regulations, rules or bylaws may arise as a result of a multitude of factors, including but not limited to citizen referenda.

There is no assurance that the operations or licensing of Liquor Stores (or the amount of cash available to Liquor Stores for the payment of dividends) will not be adversely affected by: i) new legislation, regulations, rules, or bylaws; ii) changes and court challenges to existing legislation, regulations, rules, or bylaws; iii) new interpretations of existing legislation, regulations, rules or bylaws; or iv) decisions of the AGLC, the BCLCLB, the ABCB, the KYABC, the NJABC or other governmental entities (including state, provincial, county, municipal, or other local governments) or applicable courts.

Of particular note:

Alberta

City of Edmonton

- The existing bylaw regulations require liquor stores to be located at least 500 metres away from each other (subject to grandfathering).

- On October 5th, 2015, the Executive Committee of the Edmonton City Council instructed City Administration to construct a comprehensive plan to ease restrictions on this 500m separation distance between liquor stores in big box shopping complexes. The Executive Committee has deferred this discussion until Spring/Summer of 2016.

British Columbia

- On April 1st, 2015, the 73 recommendations from the Liquor Policy Review Report were, or are in the process of being, implemented. Management believes these changes will assist in creating greater business efficiencies including: new rules permitting the warehousing of inventory, the ability to transfer inventory between stores, the retention of the existing "1 km rule" that requires that no new liquor retailer be located within 1 km of an existing liquor retailer, and the elimination of the existing "5 km rule" that currently limits liquor retailers from relocating their license outside of a 5 km radius of their current location. The Report also included recommendations that could lead to, over the long-term, increased competition for liquor retail sales in that province, including a recommendation to introduce liquor sales into grocery stores. While grocery stores have been permitted to sell liquor since April 1st, 2015, as of the date hereof Liquor Stores is not aware of any currently doing so with a full service "store-within-store" concept. The impact thus far on Liquor Stores has not been significant. While this policy change will add to competition in the marketplace, Liquor Stores will also be in a position to participate in that limited expansion. In the near term, we continue to anticipate competition will not increase significantly as no new retail liquor licenses are expected to be issued by the province and therefore should grocery stores want to sell beer, wine and spirits, they will need to acquire licenses from existing operators and comply with the 1 km rule.

Kentucky

- It is anticipated that a Wine in Grocery Bill, allowing wine sales in grocery stores, will be introduced in the State Legislature during the 2016 legislative session. Given the uncertainties surrounding the actual timing of introduction of the legislation and the details of the regulatory model, it is difficult to quantify the potential impacts that this may have on our Kentucky stores at this time.

New Jersey

Pennsylvania Privatization

- Relevant to New Jersey liquor retailers is the possibility of the privatization of the Liquor retail system in Pennsylvania. Considering Liquor Stores acquisition of 51% of Birchfield, and the close proximity of its two Joe Canal's Discount Liquor Outlet stores to the Pennsylvania border, we believe that privatization in Pennsylvania would have an impact on sales in New Jersey. Privatization in Pennsylvania may impact stores in New Jersey. However, this could also provide Liquor Stores with the opportunity to expand into a new market.

License Cap

- Legislation is anticipated to be introduced in New Jersey in 2016 pertaining to the proposed expansion of the number of liquor licenses that can be held in New Jersey. Currently in New Jersey, a single person/company can only hold two off premise licenses. Increasing the number of licenses that can be held may impact current stores in New Jersey but will provide Liquor Stores with the opportunity to open and/or consider additional opportunities and stores in New Jersey.

Retail Licenses

All of Liquor Stores' Alberta stores are operated pursuant to licenses issued by the AGLC, which must be re-applied for annually. Similar to the process in Alberta, all B.C. stores are operated pursuant to licenses issued by the BCLCLB, which must be re-applied for annually.

All of Liquor Stores' Alaska stores are operated pursuant to licenses issued by the ABCB, which must be renewed bi-annually, and its Kentucky stores are operated pursuant to licenses issued by the KYABC, which are due for renewal on an annual basis. New Jersey licenses are issued by the NJABC in conjunction with municipalities and must be renewed annually.

Since its inception in 2004, Liquor Stores has never had a store license revoked or not reissued. Management is not aware of any retail liquor store licensee having a license revoked. The AGLC, the BCLCLB, ABCB and KYABC have certain discretion in the granting or revocation of a license to operate a liquor store.

State of Economy

Liquor Stores' success depends on numerous factors affecting discretionary consumer spending, including economic conditions, disposable consumer income and consumer confidence. Adverse changes in these factors could reduce customer traffic or impose practical limits on pricing, either of which could reduce sales and other operating results, which in turn could adversely affect the availability of cash for the payment of dividends.

Deteriorating economic conditions in Alberta resulting from a sharp and rapid decline in the price of oil and increase in unemployment levels in the province (unemployment rate per Statistics Canada at January 2016: 7.6%; January 2015: 4.6%), have had, and may continue to have, an impact on Liquor Stores' business.

Competition

The private retail distribution of alcoholic beverages in the Provinces of Alberta and British Columbia and the States of Alaska, New Jersey and Kentucky is both competitive and fragmented. Competition exists mainly on a local basis with the main competitive factors being location, convenience, price and service. Changes in the regulatory regime in a particular jurisdiction may increase competition which in turn could materially adversely affect Liquor Stores' business and results of its operations.

In Alberta, Liquor Stores competes with other local single store operators, other local and regional chain operators, and liquor stores associated with national and regional grocery store chains. The current regulatory regime in Alberta limits certain of the potential competitive advantages of large scale retailers by, among other things, requiring liquor stores to be operated as a separate business and prohibiting the sale of liquor in stores selling other goods and by requiring all retailers to pay the same wholesale price and a uniform "postage stamp" delivery charge.

In British Columbia, Liquor Stores competes with government owned and operated liquor stores, local independent stores, and wine stores. In February 2010, the British Columbia government amended certain liquor control and licensing regulations, including an amendment that increased the relocation distance such that a retail liquor store is not permitted to be relocated anywhere within 1.0 kilometre of an existing retail liquor store, or the site of an application to license a new retail liquor store (subject to certain "grandfathering" exceptions). This arrangement limits the number of entrants who are able to enter into the market. As noted above, changes to the British Columbia regulatory regime may have significant changes on competition and value of licenses in that province. Liquor Stores has not yet experienced any significant impact from the new British Columbia laws and regulations.

In each of Alaska, Kentucky and New Jersey, Liquor Stores competes with local single store operators, other local and regional chain operators (in so far as license caps permit in New Jersey) and liquor stores associated with U.S. national grocery store chains (and in some instances, with U.S. national drug store chains who also offer alcoholic products for sale). Under the Alaska, Kentucky and New Jersey regulatory environments, stores purchase product directly from distributors and are able to negotiate large volume discounts with suppliers; as such, competitors with greater financial resources are able to maintain a competitive advantage over smaller operators.

Restrictions on Potential Growth

The payout by Liquor Stores of a substantial amount of its operating cash flow makes additional capital and operating expenditures dependent on increased cash flow or additional financing in the future. Lack of those funds could limit the future growth of Liquor Stores and its cash flow.

Commodity Taxes & Government Mark-Ups

Changes in tax rates or government mark-ups, and their corresponding effect on product pricing could affect sales and/or earnings. If taxes or government mark-ups increase and Liquor Stores increases prices by the full amount of the tax or the mark-up, as the case may be, sales volumes could be adversely impacted. If Liquor Stores is not able to pass the full amount of the tax or mark-up increase on to consumers, then margins and earnings could be adversely impacted. There can be no assurance that governments will not change tax or mark-up rates in the future.

Acquisition and Development Risks

Acquisitions have been a significant part of Liquor Stores' growth strategy. Liquor Stores expects to continue to selectively seek strategic acquisitions in both Canada and the U.S. Liquor Stores' ability to consummate and to integrate effectively any future acquisitions on terms that are favourable to it may be limited by the number of attractive acquisition targets, internal demands on Liquor Stores' resources and, to the extent necessary, Liquor Stores' ability to obtain financing on satisfactory terms for larger acquisitions, if at all. Acquisitions may expose Liquor Stores to additional risks, including: difficulties in integrating administrative, financial reporting, operational and information systems and managing newly acquired operations and improving their operating efficiency; difficulties in negotiating lease renewal terms; difficulties in maintaining uniform standards, controls, procedures and policies through all of Liquor Stores' stores; entry into markets or development of new store formats in which Liquor Stores has little or no direct prior experience; difficulties in retaining key employees of the acquired operations; disruptions to Liquor Stores' ongoing business; and diversion of management time and resources.

Liquor Stores expects that new store development will also continue to be a significant part of Liquor Stores' growth strategy. The development of new stores is subject to many of the same risks as acquisitions including but not limited to limitations on the number of attractive development opportunities and competition for such opportunities and internal demands on Liquor Stores' resources. The rate of new store developments may be impacted by factors outside of Liquor Stores' control such as the availability of suitable site locations and the availability of contractors to perform development work. In addition, the development of new stores requires an outlay of capital and profitability is based on management's projections of future store performance (which may prove to be incorrect).

Ability to Locate, Secure and Maintain Acceptable Store Sites and to Adapt to Changing Market Conditions

The success of Liquor Stores' retail stores is significantly influenced by location. There can be no assurance that current locations will continue to be attractive, or that additional locations can be located and secured, as demographic patterns change. It is possible that the current locations or economic conditions where Liquor Stores' retail stores are located could decline in the future including as a result of the opening of stores by competitors, resulting in potentially reduced sales in those locations. There is also no assurance that future store locations will produce the same results as existing locations. To the extent that Liquor Stores enters into long-term leases for its store locations, Liquor Stores' ability to respond in a timely manner to changes in the demographic or retail environment at any location may be limited.

Weather

Weather conditions in Canada and the United States play an important role in Liquor Stores' success. Prolonged poor weather conditions in both the summer and winter months reduce overall customer counts and consequently may have a material effect on Liquor Stores' operating results.

Key Personnel

Liquor Stores' success depends on the skills, experience and effort of its key employees. The loss of services of one or more members of Liquor Stores' key employees could significantly weaken Liquor Stores' management expertise and its ability to deliver its services efficiently and profitably.

Labour Costs and Shortages and Labour Relations

The success of Liquor Stores' business depends on a large number of both hourly and salaried employees. Changes in the general conditions of the labour markets in which Liquor Stores operates could affect the ability of Liquor Stores to hire or retain staff at current wage levels. The occurrence of either of these events could have an adverse effect on Liquor Stores' results of operations.

On October 1, 2015 Alberta's minimum wage was raised to $11.20 per hour (up from $10.20) for most employees in Alberta. The current Government of Alberta has announced a notional target to reach $15.00 per hour by 2018 (with increases in the interim). As noted above, this change could have an effect on store level labour costs.

Liquor Stores does not currently have any unionized staff; however there is no assurance that some or all of the employees of Liquor Stores will not unionize in the future. Such an occurrence could increase labour costs and thereby have an adverse effect on Liquor Stores' results of operations.

Supply Interruption or Delay

Liquor Stores is dependent upon a limited number of distributors for a substantial majority of its products. Specifically, liquor store operators in Alberta are dependent on the Connect Logistics Service warehouse and Brewers Distributor Ltd. ("BDL") for the substantial majority of their products. In British Columbia, liquor store operators are dependent on the BCLDB and BDL for the majority of their products. With respect to Liquor Stores' U.S. operations, a limited number of private distributors serve the jurisdictions in which Liquor Stores operates. Any significant disruptions in the operations of these companies (for example, an organized work stoppage) and a resulting interruption in supply may have a material adverse effect on liquor stores operations, including the operations of Liquor Stores and its subsidiaries.

Importance of Information and Control Systems

Information and control systems play an important role in the support of Liquor Stores' core business processes, including store operations, finance, human resources, supply and inventory management and loss prevention. Liquor Stores' ability to maintain and regularly upgrade its information systems capabilities is important to its future performance.

Changes in Income Tax Legislation and Other Laws

Income tax laws, such as the treatment of dividends, may in the future be changed or interpreted in a manner that adversely affects Liquor Stores and our Shareholders (both Canadian and U.S. Shareholders). Furthermore, tax authorities having appropriate jurisdiction over Liquor Stores or our Shareholders may disagree with how we calculate our income for tax purposes or could change administrative practises to our detriment or the detriment of our Shareholders (including, without limitation, the interpretation of certain cross-border tax rules).

Leverage and Restrictive Covenants

The Company has a credit facility with a syndicate of Canadian banks, which is effective until September 30, 2017 and consists of a $175 million extendible revolving operating loan (the "Credit Facility"). At March 8, 2016 there was approximately $122 million drawn on the Credit Facility. Pursuant to the terms of the Credit Facility, the Company has the ability to request an additional $50 million (to be provided by the lenders on a best-effort basis). The company also has a $5 million US operating facility.

The Company's Credit Facility is subject to a number of financial covenants, all of which are met by Liquor Stores. Under the terms of the Company's Credit Facility, the following ratios are monitored: funded debt to EBITDA, adjusted debt to EBITDAR, and fixed coverage ratio.

The Company has $67.5 million in aggregate principal amount of convertible unsecured subordinated debentures due April 30, 2018 (the "Convertible Debentures" or the "Debentures"). The Debentures bear interest at a rate of 5.85% per annum, payable semi-annually in arrears on April 30 and October 31 of each year, which commenced on October 31, 2012. The Debentures are convertible at any time at the option of the holders into common shares of the Company at a conversion price of $24.90 per share.

There are no financial covenants attributable to the Company's convertible unsecured subordinated debentures due April 30, 2018.

In the event that our Credit Facility is not extended past its current maturity date (or in the event the credit is renewed on different terms) it could adversely affect the Company's ability to fund our ongoing operations and, as repayment of such indebtedness has priority over the payment of dividends to Shareholders, to pay cash dividends to Shareholders.

The degree to which Liquor Stores is leveraged could have important consequences to the holders of the Common Shares, including: (i) a portion of Liquor Stores' cash flow from operations is dedicated to the payment of interest on its indebtedness, thereby reducing funds available for the payment of dividends; and (ii) certain of Liquor Stores' borrowings are at variable rates of interest, which exposes Liquor Stores to the risk of increased interest rates. Liquor Stores' ability to make scheduled payments of principal and interest on, or to refinance, its indebtedness depends on its future operating performance and cash flow, which are subject to prevailing economic conditions, prevailing interest rate levels, and financial, competitive, business and other factors, many of which are beyond its control.

Our Credit Facility contains certain customary operating covenants that limit the discretion of management with respect to certain business matters. These covenants place restrictions on, among other things, the ability of Liquor Stores to incur additional indebtedness, to create liens or other encumbrances, to pay dividends or make certain other payments, investments, loans and guarantees and to sell or otherwise dispose of assets and merge or consolidate with another entity. A failure to comply with the obligations in the agreements in respect of the Credit Facility could result in an event of default which, if not cured or waived, could permit acceleration of the indebtedness. If the indebtedness under this Credit Facility were to be accelerated, there can be no assurance that Liquor Stores' assets would be sufficient to repay in full that indebtedness.

Credit Risk

Liquor Stores' financial assets that are exposed to credit risk consist primarily of cash and cash equivalents and accounts receivable. The Company maintains its cash and cash equivalents with a major Canadian chartered bank. Liquor Stores, in its normal course of operations, is exposed to credit risk from its wholesale customers in Alberta whose purchases represent less than 5% of the Company's sales. Risk associated with accounts receivable is mitigated by credit management policies. Historically, bad debts from these accounts have been insignificant. Liquor Stores is not subject to significant concentration of credit risk with respect to its customers; however, all trade receivables are due from businesses in the Alberta hospitality industry. Bad debts are insignificant in relation to total sales.

Conflicts of Interest

Certain directors of Liquor Stores are associated with other companies or entities, including entities engaged in the commercial real estate development, leasing and services businesses, as well as information technology, which may give rise to conflicts of interest. In accordance with the Canada Business Corporations Act, directors who have a material interest in any person who is a party to a material contract or proposed material contract with Liquor Stores are required, subject to certain exceptions, to disclose that interest and abstain from voting on any resolution to approve that contract.

Risks Related to the Common Shares

Unpredictability and Volatility of Share Price

A publicly traded company will not necessarily trade at values determined by reference to the underlying value of its business. The prices at which the Common Share will trade cannot be predicted. The market price of the Common Shares could be subject to significant fluctuations in response to variations in quarterly operating results and other factors. The annual yield on the Common Shares as compared to the annual yield on other financial instruments may also influence the price of Common Shares in the public trading markets. An increase in market interest rates will result in higher yield on other financial instruments, which could adversely affect the market price of the Common Shares.

In addition, the securities markets have experienced significant market wide and sector price and volume fluctuations from time to time that often have been unrelated or disproportionate to the operating performance of particular issuers. Such fluctuations may adversely affect the market price of the Common Shares.

Cash Dividends are not Guaranteed

The actual cash flow available for the payment of cash dividends to Shareholders can vary significantly from period to period for a number of reasons, including among other things: (i) our operational and financial performance; (ii) the amount of cash required or retained for debt service or repayment; (iii) amounts required to fund capital expenditures and working capital requirements. Certain of these amounts are, in part, subject to the discretion of the Board of Directors, which regularly evaluates Liquor Stores' dividend payout with respect to anticipated cash flows, debt levels, capital expenditures plans and amounts to be retained to fund acquisitions and expenditures. In addition, our level of dividend per Common Share will be affected by the number of outstanding Common Shares. Cash dividends may be increased, reduced or suspended entirely depending on our operations and financial performance. The market value of the Common Shares may deteriorate if we are unable to meet dividend expectations in the future, and that deterioration may be material.

Dilution and Future Sales of Common Shares

Liquor Stores is authorized to issue an unlimited number of Common Shares for the consideration and on terms and conditions as are established by the Board of Directors without the approval of any Shareholders. In the normal course of making capital investments to maintain and expand our business operations, additional Common Shares may be issued. Additionally, from time to time, we may issue Common Shares from treasury in order to reduce debt and maintain a more optimal capital structure. As well, additional new Common Shares are issued on a monthly basis pursuant to the Company's dividend reinvestment plan. Conversely, to the extent that external sources of capital, including the issuance of additional Common Shares, becomes limited or unavailable, our ability to make the necessary capital investments to maintain or expand our business operations will be impaired. To the extent that we are required to use additional cash flow to finance capital expenditures or acquisitions, or to pay debt service charges or reduce debt, the amount of cash dividends paid to Shareholders could be reduced. Any further issuances of Common Shares will also dilute the interests of existing Shareholders. Shareholders have no pre-emptive rights in connection with such future issuances.

The Company may determine to redeem outstanding Convertible Debentures for Common Shares or repay outstanding principal amounts of the Convertible Debentures at maturity by issuing additional Common Shares. Accordingly, holders of Common Shares may suffer dilution.

Active Trading Market for the Common Shares

While there is currently an active trading market for the Common Shares, we cannot guarantee that an active trading market will be sustained. If an active trading market in the Common Shares is not sustained, the trading liquidity of the Common Shares will be limited and the market value of the Common Shares may be reduced.

Risks Related to the Convertible Debentures

Active Trading Market for the Convertible Debentures

Although the Convertible Debentures trade on the Toronto Stock Exchange, there is not currently an active trading market for the Convertible Debentures, and we cannot guarantee that an active trading market will develop. If an active trading market in the Convertible Debentures does not develop, the trading liquidity of the Convertible Debentures will remain limited and the market value of the Convertible Debentures may be adversely affected.

The market price of the Convertible Debentures may be volatile and subject to wide fluctuations and will be based on a number of factors, including: (i) the prevailing interest rates being paid by companies similar to the Company; (ii) the overall condition of the financial and credit markets; (iii) interest rate volatility; (iv) the markets for similar securities; (v) actual or anticipated fluctuations in the financial condition, results of operations and prospects of the Company; (vi) the publication of earnings estimates or other research reports and speculation in the press or investment community; (vii) the market price and volatility of the Common Shares; (viii) changes in the industry in which the Company operates and competition affecting the Company; and (ix) general market and economic conditions in North America and globally.

The condition of the financial and credit markets and prevailing interest rates have fluctuated in the past and are likely to fluctuate in the future. Fluctuations in these factors could have an adverse effect on the market price of the Convertible Debentures.

Prior Ranking Indebtedness

The Convertible Debentures are subordinate to all Senior Indebtedness (as defined in the Debenture Indenture[11]) of the Company and to any indebtedness of trade creditors of the Company. The Convertible Debentures are also effectively subordinate to claims of creditors of the Company's subsidiaries for payment of which the Company is responsible or liable, whether absolutely or contingently. Therefore, if the Company becomes bankrupt, liquidates its assets, reorganizes or enters into certain other transactions, the Company's assets will be available to pay its obligations with respect to the Convertible Debentures only after it has paid all of its senior and secured indebtedness in full. There may be insufficient assets remaining following such payments to pay amounts due on any or all of the Convertible Debentures then outstanding.

Absence of Covenant Protection

The Debenture Indenture does not restrict the Company from incurring additional indebtedness for borrowed money or from mortgaging, pledging or charging its properties to secure any indebtedness. Nor does the Debenture Indenture prohibit or limit the ability of the Company to pay dividends, except where an event of default has occurred and such default has not been cured or waived. The Debenture Indenture does not contain any provision specifically intended to protect holders of the Convertible Debentures in the event of a future leveraged transaction involving the Company.

Prevailing Yields on Similar Securities

Prevailing yields on similar securities will affect the market value of the Convertible Debentures. Assuming all other factors remain unchanged, the market value of the Convertible Debentures will decline as prevailing yields for similar securities rise, and will increase as prevailing yields for similar securities decline.

Credit Risk

The likelihood that purchasers of the Convertible Debentures will receive payments owing to them under the terms of the Convertible Debentures will depend on the financial health of the Company and its creditworthiness.

Redemption Prior to Maturity

The Convertible Debentures may be redeemed, at the option of the Company, in whole or in part at any time, subject to certain conditions in the case of redemptions prior to April 30, 2017, at a price equal to the principal amount thereof plus accrued and unpaid interest. Holders of Convertible Debentures should understand that this redemption option may be exercised if the Company is able to refinance at a lower interest rate or it is otherwise in the interests of the Company to redeem the Convertible Debentures.

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[11] "Debenture Indenture" refers to the trust indenture dated as of December 21, 2007 between Liquor Stores Fund (the predecessor to Liquor Stores) and CIBC Mellon Trust Company (the predecessor to Valiant Trust Company), as supplemented by a first supplemental trust indenture dated as of December 31, 2010 among Liquor Stores, Valiant Trust Company and BNY Trust Company of Canada (successor to CIBC Mellon Trust Company), and as further supplemented by a second supplemental indenture dated April 23, 2012, creating and setting forth the terms of the Convertible Debentures to be entered into between Liquor Stores and the Debenture Trustee;

Change of Control

The Company will be required to make an offer to purchase all of the outstanding Convertible Debentures for cash in the event of certain transactions that would constitute a Change of Control (as defined in the Debenture Indenture). The Company cannot assure holders of Convertible Debentures that, if required, it would have sufficient cash or other financial resources at that time or would be able to arrange financing to pay the purchase price of the Convertible Debentures in cash. The Company's ability to purchase the Convertible Debentures in such an event may be limited by law, by the Debenture Indenture governing the Convertible Debentures, by the terms of other present or future agreements relating to the Company's credit facilities and other indebtedness and agreements that the Company may enter into in the future which may replace, supplement or amend the Company's future debt. The Company's future credit agreements or other agreements may contain provisions that could prohibit the purchase by the Company of the Convertible Debentures without the consent of the lenders or other parties thereunder. If the Company's obligation to offer to purchase the Convertible Debentures arises at a time when the Company is prohibited from purchasing or redeeming the Convertible Debentures, the Company could seek the consent of lenders to purchase the Convertible Debentures or could attempt to refinance the borrowings that contain this prohibition. If the Company does not obtain a consent or refinance these borrowings, the Company could remain prohibited from purchasing the Convertible Debentures. The Company's failure to purchase the Convertible Debentures would constitute an event of default under the Debenture Indenture, which might constitute a default under the terms of the Company's other indebtedness at that time.

In the event that Debenture holders holding 90% or more of the Convertible Debentures have tendered their Convertible Debentures for purchase pursuant to such an offer, the Company may redeem the remaining Convertible Debentures on the same terms. In such event, the conversion privilege associated with the Convertible Debentures would be eliminated.

Conversion Following Certain Transactions

Pursuant to the Debenture Indenture, in the event of certain transactions each Convertible Debenture will become convertible into the securities, cash or property receivable by a Shareholder in accordance with such transactions. This change could substantially reduce or eliminate any potential future value of the conversion privilege associated with the Convertible Debentures. For example, if the Company were acquired in a cash merger, each Convertible Debenture would become convertible solely into cash and would no longer be convertible into securities whose value would vary depending on the Company's future prospects and other factors.

Volatility of Market Price of Common Shares

The market price of the Common Shares may be volatile. The volatility may affect the ability of holders of Convertible Debentures to sell the Convertible Debentures at an advantageous price and may result in greater volatility in the market price of the Convertible Debentures than would otherwise be expected for non-convertible securities. Market price fluctuations in the Common Shares may be due to actual or anticipated fluctuations in the financial condition, results of operations and prospects of the Company, the Company's operating results failing to meet the expectations of securities analysts or investors in any quarter, downward revision in securities analysts' estimates, governmental regulatory action, adverse change in general market conditions or economic trends, acquisitions, dispositions or other material public announcements by the Company or its competitors, along with a variety of additional factors. In addition, the market price for securities in the stock markets has recently experienced significant price and trading fluctuations. These fluctuations have resulted in volatility in the market prices of securities that often has been unrelated or disproportionate to changes in operating performance. These broad market fluctuations may adversely affect the market prices of the Convertible Debentures and the Common Shares.

Change in Tax Laws

The Debenture Indenture does not contain a requirement that the Company increase the amount of interest or other payments to holders of Convertible Debentures in the event that the Company is required to withhold amounts in respect of income or similar taxes on payment of interest or other amounts on the Convertible Debentures. At present, no amount is required to be withheld from such payments to holders of Convertible Debentures resident in Canada or in the United States who deal at arm's length with the Company, but no assurance can be given that applicable income tax laws or treaties will not be changed in a manner that may require the Company to withhold amounts in respect of tax payable on such amounts.

Withholding Tax

Effective January 1, 2008, the Income Tax Act (Canada) (the "Tax Act") was amended to generally eliminate withholding tax on interest paid or credited to non-residents of Canada with whom the payor deals at arm's length. However, Canadian withholding tax continues to apply to payments of "participating debt interest". For purposes of the Tax Act, participating debt interest is generally interest that is paid on an obligation where all or any portion of such interest is contingent or dependent on the use of or production from property in Canada or is computed by reference to revenue, profit, cash flow, commodity price or any similar criterion.

Under the Tax Act, when a debenture or other debt obligation issued by a person resident in Canada is assigned or otherwise transferred by a non-resident person to a person resident in Canada (which would include a conversion of the obligation or payment on maturity), the amount, if any, by which the price for which the obligation was assigned or transferred exceeds the price for which the obligation was issued is deemed to be a payment of interest on that obligation made by the person resident in Canada to the non-resident (an "excess"). The deeming rule does not apply in respect of certain "excluded obligations", although it is not clear whether a particular convertible debenture would qualify as an "excluded obligation". If a convertible debenture is not an "excluded obligation", issues that arise are whether any excess would be considered to exist, whether any such excess which is deemed to be interest is "participating debt interest", and if the excess is participating debt interest, whether that results in all interest on the obligation being considered to be participating debt interest.

The Canada Revenue Agency (the "CRA") has stated that no excess, and therefore no participating debt interest, would in general arise on the conversion of a "traditional convertible debenture" and therefore, there would be no withholding tax in such circumstances (provided that the payor and payee deal at arm's length for purposes of the Tax Act). The CRA has published guidance on what it believes to be a "traditional convertible debenture" for these purposes. The Convertible Debentures should generally meet the criteria set forth in CRA's published guidance; however, there can be no assurance that amounts paid or payable by the Company to a holder of Convertible Debentures on account of interest or any "excess" amount will not be subject to Canadian withholding tax at 25% (subject to any reduction in accordance with a relevant tax treaty).

Investment Eligibility

The Company will endeavour to ensure that the Convertible Debentures continue to be qualified investments for trusts governed by registered retirement savings plans, registered retirement income funds, deferred profit sharing plans, registered education savings plans, registered disability savings plans and tax free savings accounts. No assurance can be given in this regard. The Tax Act imposes penalties for the acquisition or holding of non-qualified investments by such plans.

17. Disclosure Controls and Procedures

The Company's disclosure controls and procedures are designed to provide reasonable assurance that information required to be disclosed by the Company is recorded, processed, summarized and reported within the time periods specified under Canadian securities laws and include controls and procedures designed to ensure that information is accumulated and communicated to Management, including the Chief Executive Officer and the Chief Financial Officer, to allow timely decisions regarding required disclosure.

Management, including the Chief Executive Officer and Chief Financial Officer, are responsible for establishing and maintaining adequate internal controls over financial reporting, as such term is defined in National Instrument 52-109. A material weakness in internal controls over financial reporting exists if the deficiency is such that there is a reasonable possibility that a material misstatement of the Company's annual or interim consolidated financial statements will not be prevented or detected on a timely basis.

The Chief Executive and Chief Financial Officers certified that disclosure controls and procedures and internal controls over financial reporting were properly designed and effective for the year ended December 31, 2015. There have been no changes in the design of the Company's disclosure controls and procedures or internal control over financial reporting that occurred during the three months or year ended December 31, 2015 that have materially affected, or are reasonably likely to materially affect, the Company's disclosure controls and procedures or internal control over financial reporting.

18. Outlook

Economic Conditions

Liquor Stores anticipates further downward pressure on same-store sales in all Alberta markets in 2016. Management is right-sizing the organization to reflect these economic conditions. To save costs and drive efficiencies, it is streamlining operations and eliminating or restructuring approximately 20% of the positions at its Edmonton and Louisville Store Support Centres. These changes are largely complete and expected to result in approximately $2.5 million in annual savings in operating and administrative expenses. We anticipate recording a one-time charge of approximately $0.7 million related to this restructuring in our financial results for the three months ended March 31, 2016.

Future Growth

Liquor Stores is taking a measured approach to growth that will be scaled up or down dependent on market conditions. The goal is to advance the seven point plan initiatives to invest in the store network and pursue expansion, while ensuring that the Company can withstand a prolonged period of economic pressure in Alberta.

As discussed earlier in this document, Liquor Stores has taken steps to ensure that it has sufficient capital to fund the strategic growth initiatives, including the dividend revision, organizational restructuring and the decision to delay the implementation of the new enterprise resource planning system.

Liquor Stores expects to drive increased levels of profitability of the business over both near and long-term through the opening of strategically placed greenfield stores in the US as well as store remodelling and measured growth in select Canadian markets:

- Liquor Stores currently expects to open four to seven new stores over the next 24 months, at an estimated aggregate cost of between approximately $5 million to $10 million, depending on format (destination vs. convenience sized). This target reflects current economic conditions and is a downward revision from the previous expectation to open ten stores over the next 24 months. The Company will continue to monitor economic conditions and evaluate plans for 2017 new store constructions in due course.

- In 2016, Liquor Stores intends to invest approximately $2.5 million on store refurbishments, but could adjust this spend higher or lower depending on the volatility of economic conditions in key markets. Liquor Stores believes that this approach will attract more customers and increase sales per customer. Stores remodelled since 2013 have, on average, delivered a 20% return on invested capital.

Furthermore, we believe we may have the opportunity to augment this growth by executing upon selective strategic acquisitions. These acquisitions would provide us with access to new and growing markets while diversifying our revenue base. Liquor Stores will continue to evaluate and assess potential store acquisitions for their ability to add accretive cash flow and create shareholder value.

Management believes that this approach contemplates the most efficient and effective use of our capital to continue to realize our strategic growth objectives in light of the economic conditions we currently face, as discussed above. With these adjustments to our capital allocation strategy, Management believes that its cash flow from existing operations, its current available credit and access to new capital are sufficient to finance the execution of the Company’s business strategies.

19. Condensed Quarterly Information

(expressed in thousands of Canadian dollars, except per share amounts and number of stores)

	2015				2014			
	Dec 31	**Sep 30**	**June 30**	**Mar 31**	**Dec 31**	**Sep 30**	**Jun 30**	**Mar 31**
Statement of Financial Position								
Cash	3,790	$ 2,790	$4,057	$ 11,360	$ 3,003	$ 4,331	$ 4,391	$ 5,197
Total assets	455,554	562,400	546,351	545,810	525,865	520,426	517,128	520,410
Current bank indebtedness	-	-	-	-	-	987	932	4,462
Total current liabilities	64,795	52,522	44,458	45,872	51,124	40,974	43,514	45,178
Long-term debt	129,566	127,017	124,670	122,244	92,037	157,685	157,907	155,670
Total liabilities	199,818	198,145	186,244	182,466	161,107	214,947	215,258	213,642
Shareholders' equity	255,736	364,255	360,127	363,344	364,758	305,479	301,809	306,738
Non-controlling interest	77	15	60	(2)	106	46	61	30
Statement of Earnings								
# stores, end of period	252	247	247	246	243	246	245	243
Sales	214,166	194,186	190,606	147,426	196,722	181,921	178,168	137,375
Adjusted operating margin [(1)]	13,971	11,507	12,805	2,611	13,742	12,536	10,642	996
Net earnings (loss) attributable to owners of the parent	(105,897)	4,142	4,490	(2,322)	6,612	5,271	3,355	(2,525)
Net earnings (loss)	(105,808)	4,169	4,560	(2,313)	6,714	5,316	3,417	(2,498)
Basic earnings (loss) per share	($3.86)	$0.15	$0.16	($ 0.09)	$ 0.28	$ 0.23	$ 0.14	($ 0.11)
Dividends declared per share	$0.27	$0.27	$0.27	$ 0.27	$0.27	$0.27	$0.27	$ 0.27

[(1)] Adjusted operating margin is a non-IFRS measure that does not have any standardized meaning prescribed by IFRS. For more information on non-IFRS measures see the 'Non-IFRS Financial Measures' section of this MD&A.

20. Condensed Annual Information

(expressed in thousands of Canadian dollars, except per share amounts, number of stores and US store sales)

	As at and for the year ended December 31,				
	2015	**2014**	**2013**	**2012**	**2011**
Statement of Financial Position					
Cash and cash equivalents	3,790	$ 3,003	$ 4,529	$ 5,724	$ 1,707
Total current assets (excluding cash)	174,210	146,615	140,583	157,047	134,608
Total assets	455,554	525,865	512,676	533,681	503,147
Total current liabilities	64,795	51,124	46,498	47,227	123,013
Total non-current liabilities	135,023	109,983	154,256	168,704	62,934
Total liabilities	199,818	161,107	200,754	215,931	185,947
Shareholders' equity	255,736	364,758	311,922	317,750	317,200
Statement of Earnings					
# stores, end of year	252	243	246	249	239
Canadian store sales	528,720	513,957	503,527	481,081	452,390
US store sales (US$)	169,594	162,929	152,604	149,164	140,317
Total sales	746,384	694,186	660,979	630,106	591,502
Gross margin	191,389	176,351	165,824	159,511	146,528
Operating and administrative expense	154,519	139,821	122,583	113,840	100,629
Amortization expense	11,068	10,276	9,759	7,744	7,839
Finance costs	9,545	9,234	8,838	9,718	10,449
Impairment provision	130,313	-	9,823	2,500	-
Net earnings (loss) attributable to owners of the parent	(99,587)	12,713	11,273	18,778	24,802
Net earnings (loss)	(99,392)	12,949	11,483	19,056	24,802
Statement of Cash Flow					
Cash provided by operating activities	16,373	20,834	50,802	30,819	31,776
Cash used in investing activities	(30,557)	(11,505)	(12,241)	(15,513)	(5,696)
Cash provided by (used in) financing activities	14,502	(11,178)	(40,076)	(11,385)	(26,140)
Basic earnings (loss) per share(1)	($3.64)	$ 0.54	$ 0.49	$ 0.82	$ 1.08
Dividends declared per share	$1.08	$ 1.08	$ 1.08	$ 1.08	$ 1.08

(1) *Adjusted earnings per share were $0.57 for the year ended December 31, 2015 (2014 - $0.59, 2013 - $0.90; 2012 - $1.02; 2011 - $0.96). Adjusted basic and diluted earnings per share are non-IFRS measures that do not have any standardized meaning prescribed by IFRS. For more information on non-IFRS measures see the 'Non-IFRS Financial Measures' section of this MD&A.*