

Liquor Stores N.A. Ltd.

Condensed Interim Consolidated Financial Statements

June 30, 2012 and 2011

(Unaudited, expressed in thousands of Canadian Dollars)

Liquor Stores N.A. Ltd.

Consolidated Statements of Financial Position

(in thousands of Canadian dollars)

	June 30, 2012 \$	December 31, 2011 \$
Assets		
Current assets		
Cash and cash equivalents	765	1,707
Accounts receivable	788	845
Inventory	129,889	129,842
Prepaid expenses and deposits	4,748	3,921
	136,190	136,315
Deferred income tax	2,182	1,610
Property and equipment	37,643	38,772
Intangible assets	45,950	46,145
Goodwill	280,350	280,305
	502,315	503,147
Liabilities		
Current liabilities		
Bank indebtedness	96	40,424
Accounts payable and accrued liabilities	27,154	24,478
Dividends payable to shareholders	2,058	2,040
Fair value of interest rate swap	175	390
Current portion of long-term debt (note 3)	-	55,681
	29,483	123,013
Long-term debt (note 3)	135,673	46,469
Deferred income tax	18,452	16,465
	183,608	185,947
Shareholders' Equity		
Equity attributable to shareholders	318,624	317,115
Equity attributable to non-controlling interest	83	85
	318,707	317,200
	502,315	503,147

Liquor Stores N.A. Ltd.

Consolidated Statements of Changes in Equity

(in thousands of Canadian dollars)

	Attributable to shareholders of the Company					Total	Non-controlling interest	Total shareholders' equity
	Share capital	Equity component of convertible debentures	Contributed surplus	Accumulated other comprehensive income	Deficit			
	\$	\$	\$	\$	\$	\$	\$	\$
	(note 8)							
Opening balance – January 1, 2011	180,000	37	174,632	(4,342)	(36,425)	313,902	285	314,187
Net earnings for the period	-	-	-	-	5,791	5,791	137	5,928
Foreign currency translation adjustment	-	-	-	(1,745)	-	(1,745)	-	(1,745)
Comprehensive income for the period	-	-	-	(1,745)	5,791	4,046	137	4,183
Vested long-term incentive plan units	197	-	(197)	-	(65)	(65)	-	(65)
Stock-based compensation	-	-	151	-	-	151	-	151
Dividends declared	-	-	-	-	(12,201)	(12,201)	-	(12,201)
Dividend reinvestment plan issuance	249	-	-	-	-	249	-	249
Dividends declared by subsidiaries	-	-	-	-	-	-	(164)	(164)
Transactions with shareholders	446	-	(46)	-	(12,266)	(11,866)	(164)	(12,030)
Balance – June 30, 2011	180,446	37	174,586	(6,087)	(42,900)	306,082	258	306,340
Opening balance – January 1, 2012	181,272	37	174,867	(3,174)	(35,887)	317,115	85	317,200
Net earnings for the period	-	-	-	-	7,004	7,004	168	7,172
Foreign currency translation adjustment	-	-	-	60	-	60	-	60
Comprehensive income for the period	-	-	-	60	7,004	7,064	168	7,232
Stock-based compensation	-	-	196	-	-	196	-	196
Exercise of stock options	2,404	-	(192)	-	-	2,212	-	2,212
Issuance of debentures (note 3)	-	3,328	-	-	-	3,328	-	3,328
Redemption of debentures (note 3)	30	(37)	37	-	-	30	-	30
Dividends declared (note 7)	-	-	-	-	(12,286)	(12,286)	-	(12,286)
Dividend reinvestment plan issuance (note 7)	965	-	-	-	-	965	-	965
Dividends declared by subsidiaries	-	-	-	-	-	-	(170)	(170)
Transactions with shareholders	3,399	3,291	41	-	(12,286)	(5,555)	(170)	(5,725)
Balance – June 30, 2012	184,671	3,328	174,908	(3,114)	(41,169)	318,624	83	318,707

Liquor Stores N.A. Ltd.

Consolidated Statements of Earnings and Comprehensive Income For the three and six months ended June 30, 2012 and 2011

(in thousands of Canadian dollars, except for per share amounts)

	Three Months ended		Six Months ended	
	June 30, 2012 \$	June 30, 2011 \$	June 30, 2012 \$	June 30, 2011 \$
Sales	159,621	150,210	286,257	266,177
Cost of sales	119,965	113,432	214,166	200,244
Gross margin	39,656	36,778	72,091	65,933
Operating and administrative expenses (note 4)	27,569	24,530	53,070	49,006
	12,087	12,248	19,021	16,927
Amortization				
Property and equipment	1,679	1,552	3,430	3,092
Intangible assets	118	430	229	856
	10,290	10,266	15,362	12,979
Finance costs (note 5)	3,952	2,782	5,792	5,354
Earnings before income taxes	6,338	7,484	9,570	7,625
Income tax expense (note 6)	1,572	1,701	2,398	1,697
Net earnings for the period	4,766	5,783	7,172	5,928
Other comprehensive income (loss)				
Currency translation difference on foreign subsidiaries	1,228	(275)	60	(1,745)
Comprehensive income for the period	5,994	5,508	7,232	4,183
Net earnings attributable to				
Owners of the parent	4,704	5,682	7,004	5,791
Non-controlling interest	62	101	168	137
	4,766	5,783	7,172	5,928
Comprehensive income attributable to				
Owners of the parent	5,932	5,407	7,064	4,046
Non-controlling interest	62	101	168	137
	5,994	5,508	7,232	4,183
Earnings per share (note 9)				
Basic	0.21	0.25	0.31	0.26
Diluted	0.21	0.25	0.31	0.26

Liquor Stores N.A. Ltd.

Consolidated Statements of Cash Flow

For the three and six months ended June 30, 2012 and 2011

(in thousands of Canadian dollars)

	Three Months ended		Six Months ended	
	June 30, 2012 \$	June 30, 2011 \$	June 30, 2012 \$	June 30, 2011 \$
Cash provided by (used in)				
Operating activities				
Net earnings for the period	4,766	5,783	7,172	5,928
Items not affecting cash				
Amortization	1,797	1,982	3,659	3,948
Amortization of financing charges	85	199	195	399
Non-cash interest on convertible debentures	1,575	390	2,010	780
Fair value adjustment on interest rate swap	375	-	(215)	-
Deferred income tax	1,694	1,653	311	1,633
Unrealized gain on foreign currency	-	44	-	167
Share-based compensation	63	139	196	151
Cash provided by operating activities before changes in non-cash working capital	10,355	10,190	13,328	13,006
Net change in non-cash working capital items	4,329	2,670	1,582	(5,184)
	14,684	12,860	14,910	7,822
Financing activities				
(Repayment of) proceeds from bank indebtedness	(2,477)	(6,517)	(40,504)	5,957
(Repayment of) proceeds from long-term debt	(14,876)	(119)	29,120	(268)
Redemption of convertible unsecured subordinated debentures (note 3)	(57,500)	-	(57,500)	-
Issuance of convertible unsecured subordinated debentures (note 3)	64,349	-	64,349	-
Dividends paid (note 7)	(5,635)	(5,851)	(11,303)	(12,481)
Proceeds from share issuance	1,602	-	2,242	-
Distributions paid to exchangeable unit holders	-	-	-	(484)
Dividends paid to non-controlling interest by subsidiaries	(38)	(33)	(170)	(164)
	(14,575)	(12,520)	(13,766)	(7,440)
Investing activities				
Business acquisitions	(24)	-	(24)	-
Purchase of property and equipment	(1,096)	(559)	(2,066)	(1,232)
Purchase of intangible assets	(14)	(124)	(73)	(186)
	(1,134)	(683)	(2,163)	(1,418)
Foreign exchange gain (loss) on cash held in foreign currency	65	(205)	77	(221)
Increase (decrease) in cash and cash equivalents	(960)	(548)	(942)	(1,257)
Cash and cash equivalents – Beginning of period	1,725	2,106	1,707	2,815
Cash and cash equivalents – End of period	765	1,558	765	1,558

Liquor Stores N.A. Ltd.

Notes to the Consolidated Financial Statements June 30, 2012 and 2011

(Tabular amounts in thousands of Canadian dollars, except for share amounts)

1 Nature of operations and organization

Liquor Stores N.A. Ltd. (the “Company”) was incorporated under the Federal laws of Canada on November 8, 2010 and is the successor entity to Liquor Stores Income Fund. The address of the Company’s registered office is 300, 10508 – 82 Avenue, Edmonton, Alberta. The Company’s common shares and convertible unsecured subordinated debentures trade on the Toronto Stock Exchange (the “TSX”) under the symbols “LIQ” and “LIQ.DB.A”.

The Company’s principal activity is the retailing of wines, beers and spirits. As at June 30, 2012, the Company operated 242 (2011 - 236) retail liquor stores, of which 176 (2011 - 172) were in Alberta, 35 (2011 - 35) were in British Columbia, 20 (2011 - 20) were in Alaska and 11 (2011 - 9) were in Kentucky. Of the stores operated, 206 (2011 - 206) were acquired by the Company and 36 (2011 - 30) were developed by the Company.

These unaudited condensed interim consolidated financial statements (“interim financial statements”) have been approved and authorized for issue by the Board of Directors on August 8, 2012.

2 Basis of preparation and significant accounting policies

These interim financial statements have been prepared in accordance with IFRS applicable to the preparation of interim financial statements, including International Accounting Standard (“IAS”) 34, Interim Financial Reporting and do not include all of the information required for full annual financial statements.

The preparation of interim financial statements requires management to make judgements, estimates, and assumptions that affect the application of accounting policies and the reported amounts of assets and liabilities, income and expense. Actual results may differ from these estimates. In preparing these interim financial statements, the significant judgements made by management in applying the Company’s accounting policies and the key sources of estimation uncertainty were the same as those that applied to the consolidated financial statements as at and for the year ended December 31, 2011.

The Company’s operations are seasonal in nature. Accordingly, sales will vary based on consumer spending behaviour, which tends to result in relatively higher sales in the third and fourth quarters. The Company is able to adjust certain variable costs in response to seasonal revenue patterns; however, costs such as occupancy are fixed, causing the Company to report a higher level of earnings in the third and fourth quarters. This business seasonality results in quarterly performance that is not necessarily indicative of the year’s performance.

The accounting policies applied by the Company in these interim financial statements are the same as those applied by the Company in its consolidated financial statements as at and for the year ended December 31, 2011. Accordingly, these interim financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto, for the year ended December 31, 2011.

Liquor Stores N.A. Ltd.

Notes to the Consolidated Financial Statements June 30, 2012 and 2011

(Tabular amounts in thousands of Canadian dollars, except for share amounts)

3 Long-term debt

On April 23, 2012, the Company issued \$67,500,000 aggregate principal amount of convertible unsecured subordinated debentures due April 30, 2018 (the "2012 Debentures") at a price of \$1,000 per 2012 Debenture. The 2012 Debentures are subordinated, unsecured obligations of the Company and bear interest at a rate of 5.85% per annum, payable semi-annually in arrears on April 30 and October 31 of each year, commencing October 31, 2012. The 2012 Debentures are convertible at any time at the option of the holders into common shares of the Company at a conversion price (the "Conversion Price") of \$24.90 per share.

The 2012 Debentures will not be redeemable prior to April 30, 2015. On and after April 30, 2015 and prior to April 30, 2017, the 2012 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 2012 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.

The value of the conversion feature, which was determined to be \$4,437,000, net of \$207,096 in transaction costs, has been recorded as equity with the remaining \$59,912,432 (net of \$2,943,471 in transaction costs) recorded as long-term debt. A deferred income tax liability of \$1,109,000 related to the conversion feature was recorded directly to the carrying amount of the equity component. The debentures are being accreted such that the liability at maturity will be equal to the face value of \$67,500,000.

On May 28, 2012, the Company also redeemed the outstanding 6.75% convertible unsecured subordinated debentures (the "2007 Debentures") with a maturity date of December 31, 2012, a principal amount of \$57,500,000, and accrued interest of \$1,458,614. When redeemed, the 2007 Debentures had a carrying value of \$56,393,285 and accordingly an additional \$1,106,715 was charged to interest expense.

4 Operating and administrative expenses

Operating and administrative expenses include a \$1,242,556 charge for costs associated with a store investment (with a prospective partner) that was not completed, and which costs were determined by the Company not to be recoverable. This expense has been included in the US operating segment (note 12).

Liquor Stores N.A. Ltd.

Notes to the Consolidated Financial Statements June 30, 2012 and 2011

(Tabular amounts in thousands of Canadian dollars, except for share amounts)

5 Finance costs

	Three months ended June 30		Six months ended June 30	
	2012 \$	2011 \$	2012 \$	2011 \$
Interest expense				
Bank indebtedness	57	860	365	1,571
Long-term debt	648	553	1,338	1,051
Convertible debentures	2,882	1,357	4,294	2,715
Fair value adjustment on interest rate swap	375	-	(215)	-
Net (gain) loss on foreign exchange from financing activities	(10)	12	10	17
	3,952	2,782	5,792	5,354

6 Income taxes

Income tax is recognized based on management's estimate of the weighted average annual effective tax rate expected for the full financial year. The estimated average annual effective tax rate for 2012 is 25% (the effective tax rate for the year ended December 31, 2011 was 23%). The increase in the rate is primarily related to an expected change in the relative proportions of income earned in the various tax jurisdictions that the Company operates in compared to the prior year.

7 Dividends

Dividends are determined in accordance with the Board of Directors periodic review of Company performance.

Date dividends declared	Declared \$	Paid	
		Shares \$	Cash \$
December 15, 2011	-	145	1,895
January 13, 2012	2,040	148	1,892
February 15, 2012	2,041	160	1,881
March 15, 2012	2,046	172	1,874
April 13, 2012	2,047	169	1,878
May 15, 2012	2,054	171	1,883
June 15, 2012	2,058	-	-
	12,286	965	11,303

Dividends paid in shares are pursuant to the Company's dividend reinvestment plan. Dividends are paid mid-month following the month of declaration.

Liquor Stores N.A. Ltd.

Notes to the Consolidated Financial Statements

June 30, 2012 and 2011

(Tabular amounts in thousands of Canadian dollars, except for share amounts)

7 Dividends (continued)

Monthly dividends of \$0.09 per share have been proposed from July 2012 to December 2012. As these dividends have not yet been declared as of June 30, 2012, they have not been recognized as a distribution for the three and six months ended June 30, 2012.

8 Share capital

	#	\$
Balance – January 1, 2011	22,577,088	180,000
Vested shares	13,015	197
Issued for Dividend Reinvestment Plan	16,884	249
Balance – June 30, 2011	22,606,987	180,446
Balance – January 1, 2012	22,665,902	181,272
Exercised stock options	142,500	2,212
Transfer from contributed surplus for stock options exercised	-	192
Shares issued under dividend reinvestment plan	58,356	965
Conversion of subordinated debentures	1,052	30
Balance – June 30, 2012	22,867,810	184,671

9 Earnings per share

	Three months ended June 30,		Six months ended June 30,	
	2012 \$	2011 \$	2012 \$	2011 \$
Net income attributable to shareholders of the Company	4,704	5,682	7,004	5,791
Weighted average number of common share outstanding - Basic	22,783,941	22,598,575	22,733,077	22,593,859
Dilutive effect of stock options	50,669	-	36,681	-
Weighted average number of common share outstanding - Diluted	22,834,610	22,598,575	22,769,758	22,593,859
Basic earnings per share	0.21	0.25	0.31	0.26
Diluted earnings per share	0.21	0.25	0.31	0.26

Potential shares issuable in exchange for convertible debentures for both periods have not been included in the diluted earnings per share calculation due to their anti-dilutive effect.

Liquor Stores N.A. Ltd.

Notes to the Consolidated Financial Statements June 30, 2012 and 2011

(Tabular amounts in thousands of Canadian dollars, except for share amounts)

10 Related party transactions

	Three months ended June 30,		Six months ended June 30,	
	2012 \$	2011 \$	2012 \$	2011 \$
Professional fees ⁽ⁱ⁾	33	66	85	159
Rent expense ⁽ⁱⁱ⁾	144	135	290	275
Consulting fees ⁽ⁱⁱⁱ⁾	-	33	-	33
	177	234	375	467

⁽ⁱ⁾A Director of the Company is a partner in a law firm to which the Company incurred professional fees for legal services.

⁽ⁱⁱ⁾The Company paid rent to entities controlled by a Director of the Company.

⁽ⁱⁱⁱ⁾The Company paid consulting fees to an entity controlled by a Director of the Company for real estate services.

These operating and administrative expenses were incurred in the normal course of business at terms similar to those applicable to unrelated parties.

There was \$522 (December 31, 2011 – \$9,485) included in accounts payable and accrued liabilities relating to these transactions.

11 Supplementary disclosure of cash flow information

Interest and taxes paid are included in cash flows from operating activities in the statement of cash flows.

	Three months ended June 30,		Six months ended June 30,	
	2012 \$	2011 \$	2012 \$	2011 \$
Interest paid	1,927	2,371	3,505	4,557
Income taxes paid	14	58	14	121

Liquor Stores N.A. Ltd.

Notes to the Consolidated Financial Statements

June 30, 2012 and 2011

(Tabular amounts in thousands of Canadian dollars, except for share amounts)

12 Operating segments

The Company has two reportable segments: Canadian Operations and US Operations. Segmentation is based on differences in the regulatory environments of Canada and the US and reflects the basis on which management measures performance and makes decisions regarding the allocation of resources. Both segments operate retail liquor stores in their respective jurisdictions.

Financial information regarding the results of each reportable segment is included below. Performance is measured based on operating margin, which is defined as earnings before amortization, finance costs and income tax expense (recovery), as included in the internal management reports that are reviewed regularly by the Company's President and Chief Executive Officer (the Company's chief operating decision maker) and follow the organization, management and reporting structure of the Company. Management uses operating margin to establish performance benchmarks for incentive compensation for employees and to evaluate the performance of its operating segments. A reconciliation of operating margin to earnings before income taxes, an earnings measure used in the Company's Consolidated Statement of Earnings and Comprehensive Income, has been included in the table below.

Operating margin is not an earnings measure recognized by International Financial Reporting Standards ("IFRS") and does not have a standardized meaning prescribed by IFRS. Therefore, operating margin may not be comparable to similar measures presented by other issuers. Investors are cautioned that operating margin should not be construed as an alternative to earnings before income tax as determined in accordance with IFRS, as an indicator of performance or as an alternative to cash flows from operating, investing and financing activities as a measure of liquidity and cash flows.

Liquor Stores N.A. Ltd.

Notes to the Consolidated Financial Statements June 30, 2012 and 2011

(Tabular amounts in thousands of Canadian dollars, except for share amounts)

12 Operating segments (continued)

	Three months ended June 30, 2012		
	Canadian Operations \$	US Operations \$	Consolidated \$
Sales to external customers	121,257	38,364	159,621
Operating margin (note 4)	10,630	1,457	12,087
Property and equipment amortization			1,679
Intangible asset amortization			118
Finance costs			3,952
Earnings before income taxes			6,338
Other information			
Expenditures for additions to			
Property and equipment	981	339	1,320
Intangible assets	12	2	14
Total assets at June 30, 2012	432,045	70,270	502,315
	Three months ended June 30, 2011		
	Canadian Operations \$	US Operations \$	Consolidated \$
Sales to external customers	116,041	34,169	150,210
Operating margin	10,151	2,097	12,248
Property and equipment amortization			1,552
Intangible asset amortization			430
Finance costs			2,782
Earnings before income taxes			7,484
Other information			
Expenditures for additions to			
Property and equipment	431	128	559
Intangibles	110	14	124
Total assets at December 31, 2011	430,388	72,759	503,147

Liquor Stores N.A. Ltd.

Notes to the Consolidated Financial Statements June 30, 2012 and 2011

(Tabular amounts in thousands of Canadian dollars, except for share amounts)

12 Operating segments (continued)

	Six months June 30, 2012		
	Canadian Operations \$	US Operations \$	Consolidated \$
Sales to external customers	216,397	69,860	286,257
Operating margin (note 4)	16,191	2,830	19,021
Property and equipment amortization			3,430
Intangible asset amortization			229
Finance costs			5,792
Earnings before income taxes			9,570
Other information			
Expenditures for additions to			
Property and equipment	1,586	704	2,290
Intangible assets	69	4	73
Total assets at June 30, 2012	432,045	70,270	502,315
	Six months ended June 30, 2011		
	Canadian Operations \$	US Operations \$	Consolidated \$
Sales to external customers	203,821	62,356	266,177
Operating margin	13,671	3,256	16,927
Property and equipment amortization			3,092
Intangible asset amortization			856
Finance costs			5,354
Earnings before income taxes			7,625
Other information			
Expenditures for additions to			
Property and equipment	1,040	192	1,232
Intangibles	162	24	186
Total assets at December 31, 2011	430,388	72,759	503,147