LIQUOR STORES N.A. LTD.

CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

Three months ended March 31, 2016 and 2015

(Unaudited, expressed in thousands of Canadian dollars)

Liquor Stores N.A. Ltd.

Condensed Interim Consolidated Statements of Financial Position

(in thousands of Canadian dollars)

	Note	March 31, 2016 $	December 31, 2015 $
Assets			
Current assets:			
Cash		4,276	3,790
Accounts receivable		3,574	6,020
Inventory		171,058	157,102
Prepaid expenses and deposits		10,517	11,088
		189,425	178,000
Deferred tax assets		9,850	10,474
Purchase option	3	2,592	-
Property and equipment		62,560	64,781
Intangible assets		48,918	43,312
Goodwill		170,351	158,987
		483,696	455,554
Liabilities			
Current liabilities:			
Accounts payable and accrued liabilities		53,526	61,628
Income taxes payable		923	-
Dividends payable	7	986	2,470
Derivative instrument		843	583
Current portion of long-term debt		132	114
		56,410	64,795
Long-term debt		181,361	129,566
Deferred tax liabilities		710	5,457
Non-controlling interest put option	3	13,483	-
		251,964	199,818
Shareholders' Equity			
Equity attributable to shareholders		227,763	255,659
Equity attributable to non-controlling interest		3,969	77
		231,732	255,736
		483,696	455,554

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

Liquor Stores N.A. Ltd.

Condensed Interim Consolidated Statements of Changes in Equity

(in thousands of Canadian dollars)

	Attributable to Shareholders of the Company							
	Share capital $	Equity component of convertible debentures $	Contributed surplus $	Accumulated other comprehensive income $	Deficit $	Total $	Non-controlling interest $	Total equity $
Opening balance – January 1, 2015	246,826	3,328	174,927	7,653	(68,082)	364,652	106	364,758
Net earnings (loss) for the period	-	-	-	-	(2,322)	(2,322)	9	(2,313)
Foreign currency translation adjustment	-	-	-	7,897	-	7,897	-	7,897
Comprehensive income (loss) for the period	-	-	-	7,897	(2,322)	5,575	9	5,584
Share-based payments	-	-	(2)	-	-	(2)	-	(2)
Adjustment to net proceeds on share issuance	(81)	-	-	-	-	(81)	-	(81)
Dividends declared (note 7)	-	-	-	-	(7,362)	(7,362)	-	(7,362)
Dividend reinvestment plan issuance (note 7)	564	-	-	-	-	564	-	564
Dividends declared by subsidiaries	-	-	-	-	-	-	(117)	(117)
Transactions with owners	483	-	(2)	-	(7,362)	(6,881)	(117)	(6,998)
Balance – March 31, 2015	247,309	3,328	174,925	15,550	(77,766)	363,346	(2)	363,344
Opening balance – January 1, 2016	249,303	3,328	175,761	24,460	(197,193)	255,659	77	255,736
Net earnings (loss) for the period	-	-	-	-	(1,743)	(1,743)	271	(1,472)
Foreign currency translation adjustment	-	-	-	(6,927)	-	(6,927)	(639)	(7,566)
Comprehensive loss for the period	-	-	-	(6,927)	(1,743)	(8,670)	(368)	(9,038)
Share-based payments	-	-	222	-	-	222	-	222
Reclass to share capital on settlement of equity-based payments	199	-	(199)	-	-	-	-	-
Dividends declared (note 7)	-	-	-	-	(5,778)	(5,778)	-	(5,778)
Dividend reinvestment plan issuance (note 7)	804	-	-	-	-	804	-	804
Recognition of non-controlling interest put liability (note 3)	-	-	-	-	(14,474)	(14,474)	-	(14,474)
Acquisition of Birchfield Ventures LLC (note 3)	-	-	-	-	-	-	4,854	4,854
Dividends declared by subsidiaries	-	-	-	-	-	-	(594)	(594)
Transactions with owners	1,003	-	23	-	(20,252)	(19,226)	4,260	(14,966)
Balance – March 31 , 2016	250,306	3,328	175,784	17,533	(219,188)	227,763	3,969	231,732

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

Liquor Stores N.A. Ltd.
Condensed Interim Consolidated Statements of Earnings (Loss) and Comprehensive Income (Loss)
Three Months Ended March 31, 2016 and 2015
(in thousands of Canadian dollars)

	Note	**March 31, 2016 $**	**March 31, 2015 $**
Sales		172,034	147,426
Cost of sales		128,420	109,403
Gross margin		43,614	38,023
Operating and administrative expenses		41,528	36,542
		2,086	1,481
Amortization			
Property and equipment		3,081	2,249
Intangible assets		130	78
		(1,125)	(846)
Finance costs	4	2,521	1,922
Net loss (gain) on foreign exchange from financing activities		(1,963)	149
Fair value adjustments	5	355	189
Loss before income taxes		(2,038)	(3,106)
Income tax recovery	8	(566)	(793)
Net loss		(1,472)	(2,313)
Other comprehensive income			
Items that may be reclassified subsequently to net earnings:			
Currency translation difference on foreign subsidiaries		(8,997)	7,897
Net investment hedge		1,431	-
Comprehensive income (loss)		**(9,038)**	**5,584**
Net earnings (loss) attributable to			
Owners of the parent		(1,743)	(2,322)
Non-controlling interest		271	9
		(1,472)	(2,313)
Comprehensive income (loss) attributable to			
Owners of the parent		(8,670)	5,575
Non-controlling interest		(368)	9
		(9,038)	5,584
Loss per share			
Basic	10	(0.06)	(0.09)
Diluted	10	(0.06)	(0.09)

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

Liquor Stores N.A. Ltd.
Condensed Interim Consolidated Statements of Cash Flow
Three Months Ended March 31, 2016 and 2015
(in thousands of Canadian dollars)

	Note	March 31, 2016 $	March 31, 2015 $
Cash provided by (used in)			
Operating activities:			
Net loss for the period		(1,472)	(2,313)
Adjustments to reconcile net loss to net cash flows from operating activities:			
Amortization of property and equipment		3,081	2,249
Amortization of intangible assets		130	78
Amortization of financing charges	4	104	109
Non-cash interest on convertible debentures	4	328	295
Unrealized foreign exchange gain		(2,208)	-
Fair value adjustments	5	355	189
Deferred income tax		(4,751)	(4,400)
Equity-settled share-based payments		222	(2)
Cash used in operating activities before changes in non-cash working capital		(4,211)	(3,795)
Net change in non-cash working capital items	12	(13,597)	(8,274)
		(17,808)	(12,069)
Investing activities:			
Purchase of property and equipment		(4,213)	(6,987)
Purchase of intangible assets		(501)	(1,350)
Acquisition, net of cash acquired	3	(20,912)	-
		(25,626)	(8,337)
Financing activities:			
Proceeds from long-term debt		51,390	29,803
Proceeds from sale and leaseback of assets		-	5,664
Dividends paid	7	(6,617)	(6,794)
Dividends paid to non-controlling interest by subsidiaries		(339)	(117)
		44,434	28,556
Foreign exchange gain (loss) on cash held in foreign currency		(514)	207
Increase in cash		486	8,357
Cash – Beginning of quarter		3,790	3,003
Cash – End of quarter		4,276	11,360

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

1 Nature of the business

Liquor Stores N.A. Ltd. (the “Company”) was incorporated under the Canada Business Corporations Act. 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 March 31, 2016, the Company operated 254 (2015 - 246) retail liquor stores, of which 180 (2015 - 175) were in Alberta, 35 (2015 - 35) were in British Columbia, 22 (2015 - 23) were in Alaska, 15 (2015 - 13) were in Kentucky and two (2015 - none) were in New Jersey. Of the stores operated, 198 (2015 - 199) were acquired and 56 (2015 - 47) were developed by the Company.

These condensed interim consolidated financial statements (the “financial statements”) were approved and authorized for issuance by the Board of Directors on May 9, 2016.

2 Basis of preparation and significant accounting policies

These financial statements have been prepared in accordance with International Accounting Standard (“IAS”) 34, Interim Financial Reporting, and do not include all of the information required for full annual financial statements. Accordingly, these financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto, for the year ended December 31, 2015.

The preparation of condensed interim consolidated 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, 2015, with the exception of the following new significant estimates and judgements were made in the current interim period:

i) Liability related to non-controlling interest put option

Estimates and assumptions used to calculate the value of the liability related to the non-controlling put option include the discount rate used to measure the present value of the exercise price of the option, the expected timing of exercise of the put option, and the forecasted gross settlement amount of the put option, which will vary depending on the trailing earnings of Birchfield Ventures LLC (“Birchfield”) at the time of exercise.

The put option is classified as a financial liability .Non-controlling interest continues to be recognized because the non-controlling shareholders have access to the returns associated with their underlying ownership interests. As such, the impact of recognizing the financial liability has been included in the Deficit of the Company at the acquisition date and had no impact on the measurement of non-controlling interest. The liability will be remeasured each period with gains and losses recorded in fair value adjustments in the Consolidated Statement of Earnings.

ii) Purchase option asset

Estimates and assumptions were used to calculate the value of the asset related to the Company's purchase option to acquire the remaining 49% of Birchfield for a fixed price in the first 18 months subsequent to January 4, 2016. Fair value was determined using a Black-Scholes option pricing model, and estimates and assumptions were made with respect to the strike price compared to current price of the option, and expected volatility of Birchfield's earnings.

iii) Consolidation of Birchfield (note 3)

Based on current degree of ownership and voting rights, and considering substantive potential voting rights available through exercise of the purchase option, the Company has determined that it controls Birchfield and as such, has consolidated Birchfield in the financial statements.

The Company's operations are seasonal in nature. Accordingly, sales will vary by quarter based on consumer spending behaviour. 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 and there have been no changes to critical accounting estimates or judgements made from those as described in its consolidated financial statements as at and for the year ended December 31, 2015.

3 Business Combination

Effective January 4, 2016, the Company acquired a 51% ownership interest in Birchfield Ventures LLC and the right to acquire the remaining 49% interest at pre-negotiated terms. Birchfield operates two stores in New Jersey under the banner "Joe Canal's Discount Liquor Outlets". The aggregate consideration paid to the sellers in consideration of the transfer of the purchased units and other undertakings is an aggregate amount in cash equal to USD $15 million plus or minus a closing net working capital adjustment. The acquisition was funded by the Company's existing credit facilities, and has been accounted for using the acquisition method. The Company is using USD borrowings to manage its exposure to foreign currency fluctuations associated with the net assets of the acquired business. The purchase of this business is consistent with the Company's U.S. growth strategy. The acquisition costs associated with the business combination were $539, which were recognised in the Statement of Earnings and Comprehensive Income. Included in the Consolidated Statement of Earnings and Comprehensive Income for the interim reporting period is $11,794 of sales and $380 of net earnings of Birchfield since acquisition, of which $186 of the net earnings are attributable to the non-controlling interest.

The following table summarizes the preliminary purchase consideration and estimated preliminary purchase price allocation for the acquisition, subject to completion of a closing working capital audit and finalization of a third party valuation report to assist with the estimation of the fair values of assets acquired and liabilities at the date of acquisition:

(in thousands of Canadian dollars)

	Preliminary Fair Value As at January 4, 2016
Fair value of consideration transferred ($15,000 USD)	20,912
Fair value of purchase option	(2,782)
Non-controlling interest	4,854
	22,984
Net identifiable asset or liability:	
Current assets net of current liabilities	774
Property and equipment	1,177
Intangible asset – non compete agreement	971
Intangible asset – liquor licenses	6,986
Fair value of net identifiable assets acquired and liabilities assumed	9,908
Goodwill	13,076

The goodwill recognized is attributable mainly to the synergies expected to be achieved through integrating Birchfield into the Company's US operations. The entire amount of goodwill is deductible for U.S. tax purposes.

Non-controlling interest of $4,854 has been recognized on the basis of a 49% interest in the fair value of the net identifiable assets acquired and liabilities assumed.

The terms of the purchase option to acquire the remaining 49% are as follows:

i) If the Company exercises the purchase option within the first 18 months subsequent to the acquisition date, the purchase price will be a fixed USD$12.5 million;

ii) If the Company exercises the purchase option between 18 and 36 months subsequent to the acquisition date, the purchase price will be calculated at 4.5 times store level earnings before interest, tax, depreciation and amortization ("EBITDA") for the trailing twelve months;

iii) If the Company exercises the purchase option more than 36 months subsequent to the acquisition date, the purchase price will be calculated at 4.5 times average annual store level EBITDAfor the trailing 36 months with a floor price of 4.5 times 10% of gross sales for the trailing twelve months.

In addition, the Company has provided the non-controlling interest shareholders a put option whereby if the Company has not exercised the above call option in the first 36 months subsequent to the acquisition date, the non-controlling interest can, at their option, require the Company to purchase the remaining 49% interest in Birchfield at a price of 4.5 times average annual store level EBITDA for the trailing 36 months. This put option has been presented as a liability related to non-controlling interest put option in the Statement of Financial Position.

(in thousands of Canadian dollars)

4 Finance costs

Finance costs comprise the following:

	Three months ended March 31, 2016 $	2015 $
Interest expense		
Long-term debt[(i)]	1,206	640
Convertible debenture[(ii)]	1,315	1,282
	2,521	1,922

i) Included in interest expense on long-term debt was amortization of deferred financing costs of $104 (2015 - $109).

ii) Interest expense on the convertible debentures of $1,315 (2015 - $1,282) represents coupon interest of $987 (2015 – $987) and $328 (2015 – $295) pertaining to the impact of capitalized transaction costs and the accretion of the debt using the effective interest rate method.

5 Fair value adjustments

Fair value adjustments comprise the following:

	Fair Value Hierarchy	Three months ended March 31, 2016 $	2015 $
Fair value adjustment to interest rate swap	Level 2	260	189
Fair value adjustment to non-controlling interest put option	Level 3	95	-
Fair value adjustment to purchase option	Level 2	-	-
		355	189

6 Hedge of a net investment in foreign operation

The Company is applying hedge accounting to foreign currency differences arising between the $USD functional currency of Birchfield (note 3) and the $CAD functional currency of the Company. The Company has therefore designated a portion of the principal amount outstanding of the $USD borrowings made by the Company as a net investment hedge of the net assets of Birchfield. The Company’s investments in other subsidiaries are not hedged.

No ineffectiveness was recognized in the current period from the net investment hedge.

(in thousands of Canadian dollars)

7 Dividends

	Three months ended March 31, 2016 $	2015 $
Dividends declared	5,778	7,362
Dividends paid		
Dividends paid in cash	6,617	6,794
Dividends paid in shares	804	564

Dividends were declared on April 15, 2016 in the amount of $0.03 per common share (previously $0.09 per month up to and including the dividend declared on March 15, 2016) and will be paid on May 13, 2016 to the holders of common shares as at the close of the record date of April 29, 2016. Dividends are paid mid-month following the month of declaration.

8 Income tax

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 2016 is 27.8%.

9 Share capital

a) Authorized:

An unlimited number of voting common shares are authorized to be issued.

b) Issued and outstanding:

	#	$
Balance – January 1, 2015	27,240,760	246,826
Shares issued under dividend reinvestment plan	38,900	564
Adjustment to net proceeds on share issuance	-	(81)
Balance – March 31, 2015	27,279,660	247,309
Balance – January 1, 2016	27,449,891	249,303
Shares issued under dividend reinvestment plan	110,029	804
Shares issued on settlement of equity based compensation awards	14,056	199
Balance – March 31, 2016	27,573,976	250,306

(in thousands of Canadian dollars)

10 Loss per share

	Three months ended March 31, 2016 $	2015 $
Loss attributable to owners of the parent	(1,743)	(2,322)

	2016 #	2015 #
Weighted average number of common shares outstanding – Basic	27,464,008	27,260,508
Effect of dilutive securities		
Equity-settled share-based payment awards	20,654	7,902
Weighted average number of common shares outstanding - Diluted	27,484,662	27,268,410

	2016 $	2015 $
Basic loss per share	(0.06)	(0.09)
Diluted loss per share	(0.06)	(0.09)

Due to their anti-dilutive effect, the potential shares issuable in exchange for convertible debentures were not included in the diluted earnings per share calculation for the three months ended March 31, 2016 and 2015.

11 Related party transactions

The following transactions were carried out with related parties:

a) Operating and administrative expenses

	Three months ended March 31, 2016 $	2015 $
Professional fees[(i)]		
Recognized in operating and administrative expenses	10	29
	10	29

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

(in thousands of Canadian dollars)

b) Included in operating and administrative expenses for the three months ended March 31, 2015 are payments of $675 related to the departure of the Company's former Executive Vice President, Business Development, General Counsel and Corporate Secretary. These expenses have been included in the corporate operating segment (note 13).

12 Supplementary disclosure of cash flow information

Changes in non-cash working capital items comprise the following:

	Three months ended March 31, 2016 $	2015 $
Accounts receivable	5,270	727
Inventory	(6,979)	(3,796)
Prepaid expenses and deposits	667	571
Accounts payable and accrued liabilities	(13,478)	(7,407)
Income tax payable	923	1,631
	(13,597)	(8,274)

Interest and income taxes paid are included in cash provided by operating activities in the Statements of Cash Flows.

	Three months ended March 31, 2016 $	2015 $
Interest paid	1,102	531
Income taxes paid	265	1,817

13 Operating segments

The Company has three reportable segments: Canadian Operations, US Operations, and Corporate. 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. The Canada and US 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, net loss(gain) on foreign exchange activities, fair value adjustments, 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, or "CODM") and follow the organization, management and reporting structure of the Company. Operating margin is one of the primary benchmarks used by management 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 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. Users 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.

(in thousands of Canadian dollars)

13 Operating segments (continued)

	Three months ended March 31, 2016			
	Canadian Operations $	**US Operations $**	**Corporate $**	**Consolidated $**
Sales to external customers	110,428	61,606	-	172,034
Operating margin	6,881	2,515	(7,310)	2,086
Property and equipment amortization				3,081
Intangible asset amortization				130
Finance costs				2,521
Net loss (gain) on foreign exchange from financing activities				(1,963)
Fair value adjustments				355
Earnings before income taxes				(2,038)
Other information				
Expenditures for additions to				
Property and equipment(i)	654	455	-	1,109
Intangible assets(i)	56	1	-	57
Total assets at March 31, 2016(i)	334,807	148,889	-	483,696

	Three months ended March 31, 2015			
	Canadian Operations $	**US Operations $**	**Corporate $**	**Consolidated $**
Sales to external customers	104,790	42,636	-	147,426
Operating margin	7,504	1,450	(7,473)	1,481
Property and equipment amortization				2,249
Intangible asset amortization				78
Finance costs				1,922
Net loss (gain) on foreign exchange from financing activities				149
Fair value adjustments				189
Earnings before income taxes				(3,106)
Other information				
Expenditures for additions to				
Property and equipment(i)	3,882	1,878	-	5,760
Intangible assets(i)	1,464	-	-	1,464
Total assets at March 31, 2015(i)	431,833	113,977	-	545,810

(i) Total corporate assets are not regularly reported to the CODM but rather, a split between US and Canadian assets is provided. The disclosure above reflects what is regularly provided to the CODM.