LIQUOR STORES N.A. LTD.

CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

Three and nine months ended September 30, 2014 and 2013

(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	September 30, 2014 $	December 31, 2013 $
Assets			
Current assets:			
Cash		4,331	4,529
Accounts receivable		2,312	1,342
Inventory		135,397	131,716
Prepaid expenses and deposits		7,755	7,525
		149,795	145,112
Deferred tax assets		2,971	2,732
Property and equipment		47,617	46,782
Intangible assets		36,200	35,282
Goodwill		283,843	282,768
		520,426	512,676
Liabilities			
Current liabilities:			
Bank indebtedness	3	987	-
Accounts payable and accrued liabilities		37,076	40,746
Dividends payable to shareholders	5	2,094	2,080
Income tax payable		735	3,577
Derivative instrument		82	95
		40,974	46,498
Long-term debt	3	157,685	133,819
Deferred tax liabilities		16,288	20,437
		214,947	200,754
Shareholders' Equity			
Equity attributable to shareholders		305,433	311,828
Equity attributable to non-controlling interest		46	94
		305,479	311,922
		520,426	512,676

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 comprehen-sive income $**	**Deficit $**	**Total $**	**Non-controlling interest $**	**Total equity $**
	(note 7)							
Opening balance – January 1, 2013	185,696	3,328	174,900	(4,505)	(41,761)	317,658	92	317,750
Net earnings for the period	-	-	-	-	12,471	12,471	120	12,591
Foreign currency translation adjustment	-	-	-	2,566	-	2,566	-	2,566
Comprehensive income for the period	-	-	-	2,566	12,471	15,037	120	15,157
Share-based payments	-	-	15	-	-	15	-	15
Exercise of share options	990	-	(94)	-	-	896	-	896
Dividends declared	-	-	-	-	(18,636)	(18,636)	-	(18,636)
Dividend reinvestment plan issuance	1,580	-	-	-	-	1,580	-	1,580
Dividends declared by subsidiaries	-	-	-	-	-	-	(182)	(182)
Transactions with owners	2,570	-	(79)	-	(18,636)	(16,145)	(182)	(16,327)
Balance – September 30, 2013	188,266	3,328	174,821	(1,939)	(47,926)	316,550	30	316,580
Opening balance – January 1, 2014	188,824	3,328	174,695	342	(55,361)	311,828	94	311,922
Net earnings for the period	-	-	-	-	6,103	6,103	134	6,237
Foreign currency translation adjustment	-	-	-	4,463	-	4,463	-	4,463
Comprehensive income for the period	-	-	-	4,463	6,103	10,566	134	10,700
Share-based payments	-	-	42	-	-	42	-	42
Dividends declared (note 5)	-	-	-	-	(18,790)	(18,790)	-	(18,790)
Dividend reinvestment plan issuance (note 5)	1,787	-	-	-	-	1,787	-	1,787
Dividends declared by subsidiaries	-	-	-	-	-	-	(182)	(182)
Transactions with owners	1,787	-	42	-	(18,790)	(16,961)	(182)	(17,143)
Balance – September 30 , 2014	190,611	3,328	174,737	4,805	(68,048)	305,433	46	305,479

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 and Comprehensive Income

Three and Nine Months Ended September 30, 2014 and 2013

(in thousands of Canadian dollars)

		Three months ended		Nine months ended	
	Note	September 30, 2014 $	September 30, 2013 $	September 30, 2014 $	September 30, 2013 $
Sales		181,921	172,903	497,464	476,874
Cost of sales		134,916	129,177	371,838	356,655
Gross margin		47,005	43,726	125,626	120,219
Operating and administrative expenses	10	34,469	30,797	102,838	89,085
		12,536	12,929	22,788	31,134
Amortization					
Property and equipment		3,176	2,631	7,492	7,243
Intangible assets		97	88	242	266
		9,263	10,210	15,054	23,625
Finance costs	4	2,345	2,443	6,913	6,645
Earnings before income taxes		6,918	7,767	8,141	16,980
Income tax expense	6	1,602	1,956	1,904	4,389
Net earnings		5,316	5,811	6,237	12,591
Other comprehensive income (loss)					
Items that may be reclassified subsequently to net earnings:					
Currency translation difference on foreign subsidiaries		4,028	(1,351)	4,463	2,566
Comprehensive income		**9,344**	**4,460**	**10,700**	**15,157**
Net earnings attributable to					
Owners of the parent		5,271	5,783	6,103	12,471
Non-controlling interest		45	28	134	120
		5,316	5,811	6,237	12,591
Comprehensive income attributable to					
Owners of the parent		9,299	4,432	10,566	15,037
Non-controlling interest		45	28	134	120
		9,344	4,460	10,700	15,157
Earnings per share					
Basic	8	0.23	0.25	0.26	0.54
Diluted	8	0.23	0.25	0.26	0.54

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 and Nine Months Ended September 30, 2014 and 2013
(in thousands of Canadian dollars)

		Three months ended		Nine months ended	
	Note	**September 30, 2014 $**	**September 30, 2013 $**	**September 30, 2014 $**	**September 30, 2013 $**
Cash provided by (used in)					
Operating activities:					
Net earnings for the period		5,316	5,811	6,237	12,591
Adjustments to reconcile net income to net cash flows from operating activities:					
Amortization of property and equipment		3,176	2,631	7,492	7,243
Amortization of intangible assets		97	88	242	266
Amortization of financing charges	4	90	82	190	247
Non-cash interest on convertible debentures	4	304	281	868	801
Fair value adjustment on derivative instrument	4	(5)	185	(13)	(125)
Deferred income tax		1,602	1,985	(4,129)	(1,405)
Equity-settled share-based payments		-	(53)	42	15
Cash provided by operating activities before changes in non-cash working capital		10,580	11,010	10,929	19,633
Net change in non-cash working capital items	11	(178)	(1,728)	(9,734)	93
		10,402	9,282	1,195	19,726
Investing activities:					
Purchase of property and equipment		(3,832)	(5,297)	(7,742)	(8,803)
Purchase of intangible assets		(505)	(152)	(551)	(366)
		(4,337)	(5,449)	(8,293)	(9,169)
Financing activities:					
Proceeds (repayment) of bank indebtedness		(75)	876	933	(1,372)
Proceeds (repayment) from long-term debt		(574)	2,349	22,850	7,351
Dividends paid	5	(5,671)	(5,673)	(16,988)	(17,044)
Proceeds received on exercise of stock-options		-	-	-	896
Dividends paid to non-controlling interest by subsidiaries		(64)	(64)	(182)	(182)
		(6,384)	(2,512)	6,613	(10,351)
Foreign exchange gain on cash held in foreign currency		259	6	287	214
Increase (decrease) in cash		(60)	1,327	(198)	420
Cash – Beginning of period		4,391	4,223	4,529	5,130
Cash - End of period		4,331	5,550	4,331	5,550

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 September 30, 2014, the Company operated 246 (December 31, 2013 - 246) retail liquor stores, of which 175 (2013 - 176) were in Alberta, 35 (2013 - 36) were in British Columbia, 23 (2013 - 22) were in Alaska and 13 (2013 - 12) were in Kentucky. Of the stores operated, 201 (2013 - 202) were acquired and 45 (2013 - 44) 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 November 13, 2014.

2 Basis of preparation and significant accounting policies

These condensed interim consolidated 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 condensed interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto, for the year ended December 31, 2013.

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 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 financial statements as at and for the year ended December 31, 2013.

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 in its consolidated financial statements as at and for the year ended December 31, 2013 except as described below.

Change in Accounting Policy

The Company has adopted IFRIC 21, Levies which provides guidance on when to recognize an obligation to pay a levy other than income tax. The standard was effective January 1, 2014 and adoption of IFRIC 21 did not result in any current or retrospective adjustment.

(in thousands of Canadian dollars)

3 Bank indebtedness and long-term debt

On March 31, 2014, the Company and a syndicate of Canadian banks agreed to amend and restate the credit facility described in note 9(b) to the December 31, 2013 financial statements. Significant changes to the credit facility include an increase in the extendible revolving operating facility from $150,000 to $175,000 and an extension of the maturity date to May 31, 2016.

4 Finance costs

Finance costs comprise the following:

	Three months ended September 30,		Nine months ended September 30,	
	2014 $	2013 $	2014 $	2013 $
Interest expense				
Bank indebtedness	77	85	349	243
Long-term debt[(i)]	919	870	2,632	2,718
Convertible debenture[(ii)]	1,291	1,268	3,830	3,762
Fair value adjustment on interest rate swap	(5)	185	(13)	(125)
Net loss on foreign exchange from financing activities	63	35	115	47
	2,345	2,443	6,913	6,645

i) Included in interest expense on long-term debt for the three and nine months ended September 30, 2014 was amortization of deferred financing costs of $90 and $190 (2013 - $82 and $247), respectively.

ii) Interest expense on the convertible debentures for the three and nine months ended September 30, 2014, respectively, of $1,291 and $3,830 (2013 - $1,268 and $3,762) represents coupon interest of $987 and $2,962 (2013 – $987 and $2,961) and $304 and $868 (2013 – $281 and $801) pertaining to the impact of capitalized transaction costs and the accretion of the debt using the effective interest rate method.

5 Dividends

Dividends are determined in accordance with the Board of Directors periodic review of Company performance. During the three months ended September 30, 2014, the Company declared monthly dividends of $0.09 per share or $6,278 (2013 - $0.09 per share or $6,227). Dividends of $6,273 (2013 - $6,224) were paid during the period, of which $602 (2013 - $551) was paid in shares pursuant to the Company's dividend reinvestment plan.

During the nine months ended September 30, 2014, the Company declared monthly dividends of $0.09 per share or $18,790 (2013 - $0.09 per share or $18,636). Dividends of $18,775 (2013 - $18,624) were paid during the period, of which $1,787 (2013 - $1,580) was paid in shares pursuant to the Company's dividend reinvestment plan.

(in thousands of Canadian dollars)

Dividends of $2,094 were payable as at September 30, 2014 (2013 - $2,080). Dividends are paid mid-month following the month of declaration.

Dividends were declared on October 15, 2014 in the amount of $0.09 per common share and will be paid on November 14, 2014 to the holders of common shares as at the close of the record date of October 31, 2014.

6 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 2014 is 24% (the effective tax rate for the year ended December 31, 2013 was 22.5%).

7 Share capital

a) Authorized:

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

b) Issued and outstanding:

	#	$
Balance – January 1, 2013	22,924,591	185,696
Exercised stock options	57,750	896
Transfer from contributed surplus for share options exercised	-	94
Shares issued under dividend reinvestment plan	92,039	1,580
Balance – September 30, 2013	23,074,380	188,266
Balance – January 1, 2014	23,113,172	188,824
Shares issued under dividend reinvestment plan	154,059	1,787
Balance –September 30, 2014	23,267,231	190,611

(in thousands of Canadian dollars)

8 Earnings per share

	Three months ended September 30,		Nine months ended September 30,	
	2014 **$**	**2013** **$**	**2014** **$**	**2013** **$**
Net earnings attributable to owners of the parent	5,271	5,783	6,103	12,471
	2014 **#**	**2013** **#**	**2014** **#**	**2013** **#**
Weighted average number of common shares outstanding – Basic	23,241,958	23,057,008	23,188,955	23,001,665
Effect of dilutive securities				
Equity-settled share-based payment awards	-	12,243	-	27,753
Weighted average number of common shares outstanding - Diluted	23,241,958	23,069,251	23,188,955	23,029,418
	2014 **$**	**2013** **$**	**2014** **$**	**2013** **$**
Basic earnings per share	0.23	0.25	0.26	0.54
Diluted earnings per share	0.23	0.25	0.26	0.54

Due to their anti-dilutive effect, the equity-settled share options and potential shares issuable in exchange for convertible debentures were not included in the diluted earnings per share calculation for the three and nine months ended September 30, 2014 and the three and nine months ended September 30, 2013.

9 Share-based payments

During the nine months ended September 30, 2014, the Company granted 64,020 restricted share units with a value of $776. Compensation expense of $163 and $271 related to these awards was recognized for the three and nine months ended September 30, 2014, respectively. No performance share units were awarded during the period.

(in thousands of Canadian dollars)

10 Related party transactions

The following transactions were carried out with related parties:

a) Operating and administrative expenses

	Three months ended September 30,		Nine months ended September 30,	
	2014 **$**	**2013** **$**	**2014** **$**	**2013** **$**
Professional fees[(i)]	19	40	61	115
Rent expense[(ii)]	-	127	194	360
	19	167	255	475

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

(ii) Rent includes amounts paid to entities controlled by a former Director of the Company up until May 15, 2014 when the Director retired from the Company's Board and ceased to be a related party. The commitment remaining under this lease agreement as at September 30, 2014 is $1,164 for the remaining term ending on March 31, 2017.

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

There was $3 included in accounts payable and accrued liabilities (December 31, 2013 – $12) relating to these transactions.

b) Included in operating and administrative expenses for the nine months ended September 30, 2014 are payments of $617 related to the departure of the Company's former Chief Financial Officer. This expense has been included in the Canadian operating segment (note 13).

(in thousands of Canadian dollars)

11 Supplementary disclosure of cash flow information

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

	Three months ended September 30,		Nine months ended September 30,	
	2014 $	**2013 $**	**2014 $**	**2013 $**
Accounts receivable	(434)	46	(962)	1,490
Inventory	1,602	2,377	(1,808)	6,010
Prepaid expenses and deposits	587	(4,046)	(167)	(416)
Accounts payable and accrued liabilities	(350)	471	(4,018)	(8,763)
Income tax payable	(1,583)	(576)	(2,779)	1,772
	(178)	(1,728)	(9,734)	93

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

	Three months ended September 30,		Nine months ended September 30,	
	2014 $	**2013 $**	**2014 $**	**2013 $**
Interest paid	933	2,229	4,867	7,095
Income taxes paid	1,604	530	9,019	3,961

12 Fair value of financial instruments

a) Financial instruments measured at fair value

Financial instruments recognized at fair value include deferred share and restricted awards, which are level 1 measurements and the interest rate swap, which is a level 2 measurement. There have been no transfers of instruments between levels in the hierarchy.

The fair values of interest rate swaps are calculated as the net present value of the future cash flows expected to arise on the variable and fixed legs, determined using applicable yield curves at each measurement date.

Fair value hierarchy

Financial instruments recognized on the statement of financial position at fair value are classified in a hierarchy based on the significance of the estimates used in their measurement, as follows:

Level 1 – Quoted prices in active markets for identical assets or liabilities.

Level 2 – Inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly or indirectly.

Level 3 – Inputs for the asset or liability that are not based on observable market data.

b) Financial instruments measured at other than fair value

Financial assets that are measured at other than fair value on the consolidated statements of financial position include cash and accounts receivable. The carrying value less impairment provision of trade receivables approximates fair value due to the short-term nature of the instruments.

Financial liabilities that are valued at other than fair value are comprised of bank indebtedness, accounts payable and accrued liabilities, dividends payable to shareholders, and long-term debt.

The carrying value of trade payables and dividends payable approximates their fair value due to the short-term nature of the instruments. The carrying value of bank indebtedness and long-term debt approximates the fair value, as the interest rate affecting these instruments is at a variable market rate. Debentures with a face value of $67,500 have a fair value of $70,538 (December 31, 2013 – $69,525), determined based on market trading values at the balance sheet date.

13 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, as included in the internal management reports that are reviewed regularly by the Company's Chief Executive Officer (the Company's chief operating decision maker) 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 Condensed Interim 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. 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.

(in thousands of Canadian dollars)

Operating segments (continued)

			Three months ended September 30, 2014
	Canadian Operations $	US Operations $	Consolidated $
Sales	137,917	44,004	181,921
Operating margin	10,844	1,692	12,536
Property and equipment amortization			3,176
Intangible asset amortization			97
Finance costs			2,345
Earnings before income taxes			6,918
Other information			
Expenditures for additions to:			
Property and equipment	2,729	739	3,468
Intangible assets	-	508	508
Total assets at September 30, 2014	425,328	95,098	520,426

			Three months ended September 30, 2013
	Canadian Operations $	US Operations $	Consolidated $
Sales	133,565	39,338	172,903
Operating margin	10,931	1,998	12,929
Property and equipment amortization			2,631
Intangible asset amortization			88
Finance costs			2,443
Earnings before income taxes			7,767
Other information			
Expenditures for additions to:			
Property and equipment	1,510	2,784	4,293
Intangibles	275	-	275
Total assets at December 31, 2013	422,118	90,558	512,676

(in thousands of Canadian dollars)

Operating segments (continued)

	Nine months ended September 30, 2014		
	Canadian Operations $	**US Operations $**	**Consolidated $**
Sales	371,997	125,467	497,464
Operating margin	19,007	3,781	22,788
Property and equipment amortization			7,492
Intangible asset amortization			242
Finance costs			6,913
Earnings before income taxes			8,141
Other information			
Expenditures for additions to:			
Property and equipment	6,978	1,234	8,212
Intangible assets	-	513	513
Total assets at September 30, 2014	425,328	95,098	520,426

	Nine months ended September 30, 2013		
	Canadian Operations $	**US Operations $**	**Consolidated $**
Sales	366,398	110,476	476,874
Operating margin	26,031	5,103	31,134
Property and equipment amortization			7,243
Intangible asset amortization			266
Finance costs			6,645
Earnings before income taxes			16,980
Other information			
Expenditures for additions to:			
Property and equipment	4,275	5,775	10,050
Intangibles	347	146	493
Total assets at December 31, 2013	422,118	90,558	512,676