

# Corporate Profile

Quality, brand name merchandise. Much of what you need for daily living - food, furniture, clothing, housewares, hardware, paint and more - Liquidation World sells it all at prices that are 30 - 70% below normal retail.

Liquidation World works closely with manufacturers, retailers, wholesalers, banks and insurance companies to help them deal with merchandise of almost every description that won't, or can't be sold through typical retail channels.

That may include merchandise from inventory overruns or packaging changes. Sometimes it means seasonal goods or goods from bankruptcies, receiverships and insurance claims. The majority of our merchandise comes from healthy, going-concern businesses who view Liquidation World as an indispensable part of their inventory management strategy.

We buy these goods at deep discounts and pass the savings along to our retail customers through 104 fun, friendly and no-frill Liquidation World outlets.

We never stop looking for a deal and neither should you.

# President's Message

In the first quarter of last year, we made the largest single inventory buy in the Company's history, which helped to drive strong same store sales in Canada. Combined with 10 grand opening sales in new locations, we set a new quarterly sales record for the Company as a whole.

Against that performance and in the absence of any similarly large deals, same store sales and profitability declined in the first quarter of this year as expected.

While our results this quarter were below those of Q1 2007, we also have reason to be encouraged.

Gross margin, which had deteriorated in the last 3 quarters showed improvement during the first quarter as a result of a greater focus on deal merchandise and more effective management of markdowns. And while the number of transactions decreased during the quarter, the average basket size increased to its highest first quarter level in recent years.

Expenses on a per store basis declined during the quarter. Non-store expenses and store labour expenses have been the focus of attention in our efforts to control costs. A new store labour management program was introduced in the first quarter that has thus far succeeded in keeping store labour expenses under budget.

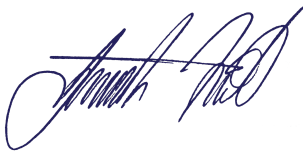
While we remain mindful of expenses, we have important initiatives under way to increase sales.

Our merchandising strategy has reduced the amount of product planning and given priority to event merchandise over closeout merchandise. Event deals are a key point of differentiation for Liquidation World and, for our customers, great deals trump great selection. During the quarter, we succeeded in improving our mix of deal merchandise and will continue to pursue unique and exciting deals that deliver great value to our customers.

During the quarter, we completed the wind-down of our US retail operations and closed 15 of 18 outlets there. Now our US based purchasing resources are fully dedicated to sourcing liquidations for our Canadian outlets. In the first quarter, our western Canadian stores benefited most from this change, as they received an increased flow of deal merchandise from the US. During the quarter, those stores outperformed stores in other areas of the country. From these early indications, we are optimistic that our US-based deal buyers can continue to have a positive impact on our Canadian store sales.

To further increase sales, late in the second quarter, we will launch a new multi-channel brand advertising campaign that has been in development for the past several months. On an annualized basis, this campaign will deliver a significant increase in total impressions that we anticipate will boost brand awareness and store traffic. Within the campaign, we are testing higher levels of advertising spend in some larger markets. We look forward to being able to communicate Liquidation World's value message in a new way and connect with a broader range of potential new customers.

In closing, I would like to express my sincere thanks to the employees of Liquidation World for your efforts this past quarter and to the shareholders for your continued support.



# MD&A

*The following discussion and analysis is effective as of February 7, 2008 and should be read together with the unaudited interim consolidated financial statements and the accompanying notes for the 13 weeks ended January 6, 2008 and the audited consolidated financial statements, MD&A and notes for the year ended October 7, 2007*

## OVERVIEW

Liquidation World Inc. ("Liquidation World" or the "Company") is the largest liquidator of opportunity inventory in Canada. Opportunity inventory results from a variety of situations including insolvencies, insurance claims, overruns, cancelled orders, and close-outs. A large proportion of opportunity inventory is made available from healthy, going-concern businesses and this is reflected in the composition of the Company's inventory. Liquidation World distributes such acquired inventory to value-oriented customers through its network of 105 corporately run outlets (102 in Canada and 3 in the US as of February 7th, 2008). A typical Liquidation World outlet occupies between 20,000 and 25,000 square feet, although there are some smaller and some larger outlets.

The success of Liquidation World's business model is predicated on its ability to service 2 key constituents, namely vendors and consumers. Manufacturers, wholesalers and retailers look to Liquidation World as a channel for effectively managing excess inventory. Consumers look to Liquidation World to provide new, quality products at excellent prices.

Among liquidators, Liquidation World is unique insofar as it maintains a national network of retail outlets and distribution centres; Liquidation World is particularly appealing to US suppliers because it is big enough to transact large buys and can effectively move merchandise away from key US markets. With its financial resources, scale and positive reputation among vendors, the Company expects to be able to capitalize on inventory opportunities as they arise.

## OVERALL PERFORMANCE

During the first quarter of fiscal 2008, the Company completed the wind up of its US retail operations, closing 15 of 18 stores there. These closed stores are now considered "discontinued operations".

A summary of results for the first quarter of fiscal 2008, comprising 13 weeks ended January 6, 2008:

- Sales from continuing operations decreased 9.2% to \$52.8 million from \$58.2 million in Q1 2007
- Same store sales decreased 11.9% from Q1 2007
- Gross margin decreased to 37.2% of sales from 39.8% of sales in Q1 2007
- Selling, general and administrative expenses increased to 32.6% of sales in Q1 2008 from 31.7% of sales in Q1 2007
- 3 new stores were opened during the quarter
- Earnings from continuing operations totaled \$1,155 compared to \$2,473 in Q1 2007
- Net earnings of \$0.1 million were recorded for the first quarter, including a \$1.0 million loss from discontinued operations, versus net income of \$1.8 million in Q1 2007

## RESULTS OF OPERATIONS

### Revenue

Revenue for the quarter ended January 6, 2008, which includes sales of merchandise and fee revenue, decreased 9.2% to \$52,812,000 from \$58,171,000 in the same quarter last year. Same store sales decreased 11.9% for the quarter.

During the quarter, the Company closed 15 of its 18 US outlets, which are henceforth classified as discontinued operations. Revenues from discontinued operations in Q1 2008 totaled \$745,000 during the final three weeks of wind-up compared to \$6,500,000 during the full 13 weeks of Q1 2007. Three US stores remain in Washington State in Spokane, Richland and Renton and are not included in discontinued operations.

Historically, the first quarter accounts for 28% of annual revenue.

### **Gross Margin**

Gross margin decreased in Q1 2008 to 37.2% of sales, or \$19,657,000 from 39.8% of sales or \$23,163,000 in Q1 2007.

Gross margins can fluctuate as a result of product mix sold. Liquidation World's pricing policies and strategy are to ensure prices for comparable products are lower than any other in the market, including discount stores, warehouse type outlets and special promotions. Gross margins are subject to pressure under this policy and can fluctuate as a result. Where specific price matching is concerned, Liquidation World will continue to mark down product.

### **Selling, General and Administrative**

Selling, general and administrative, which includes all costs of occupying, operating, and supporting outlets, including opening new outlets, decreased to \$17,230,000 in Q1 2008 from \$18,448,000 in Q1 2007. As a percentage of sales, selling, general and administrative expenses increased to 32.6% in Q1 2008 from 31.7% in Q1 2007.

### **Depreciation and Amortization**

Depreciation and amortization increased in Q1 2008 by 19.7% to \$1,027,000 from \$858,000 in Q1 2007. This change reflects capital investments over the past year in new stores, equipment and offices.

### **Interest**

Total interest expenses in Q1 2008 increased to \$240,000 compared to \$171,000 in Q1 2007. The Company has short-term banking and operating facilities of \$25,000,000. At the end of Q1 2008, \$10,401,000 was drawn compared with \$2,157,000 at the end of Q1 2007.

### **Foreign Exchange**

During the quarter, the Company recorded a net foreign exchange gain of \$86,000 compared to a foreign exchange loss of \$118,000 in Q1 2007.

### **Income Taxes**

The statutory tax rate in effect is 34.7%, however, as a result of losses in prior periods, the Company has accumulated loss carry-forwards totaling approximately \$9 million in Canada and \$4 million in the US. Consequently, the Company did not record any income taxes during the first quarter of 2008. In Q1 2007 the Company recorded income tax expense of \$1,008,000.

### **Net Earnings from Continuing Operations**

During Q1 2008, net earnings from continuing operations decreased 53.3% to \$1,155,000 (\$0.14 per share) from \$2,473,000 (\$0.30 per share) during Q1 2007.

### **Discontinued Operations**

During Q1 2008, the Company ceased operations of its wholly owned US subsidiary, including the closing of 15 of its 18 US stores. These closed outlets are now considered 'discontinued operations'. During the quarter, the Company recorded a loss from discontinued operations of \$1,043,000 compared to a loss from discontinued operations of \$677,000 in Q1 2007. Approximately \$0.4 million of the loss from discontinued operations relates to lease obligations for the insolvent subsidiary. While accounting standards dictate that these obligations must be recorded, the insolvent status of the subsidiary precludes their payment.

### **Net Earnings and Comprehensive Earnings**

The net earnings and comprehensive earnings for Q1 2008 total \$112,000 (\$0.01 per share) compared with net earnings of \$1,796,000 (\$0.21 per share) in Q1 2007.

## QUARTERLY INFORMATION

The following selected financial information is derived from the consolidated financial statements of the Company and should be read in conjunction with such financial statements and related notes. (amounts in thousands of Canadian dollars, except per share amounts):

Quarter Ended	January 6 2008	October 7 2007	July 1 2007	April 1 2007
Revenue	\$ 52,812	\$ 46,456	\$ 41,650	\$ 41,972
Net earnings (loss) from continuing operations	1,155	(3,922)	(2,459)	(2,733)
Net earnings (loss) from continuing operations per common share				
Basic	0.14	(0.48)	(0.30)	(0.33)
Diluted	0.14	(0.48)	(0.30)	(0.33)
Net earnings (loss) and comprehensive income (loss)	112	(7,588)	(2,887)	(3,032)
Net earnings (loss) per common share				
Basic	0.01	(0.92)	(0.35)	(0.37)
Diluted	0.01	(0.92)	(0.35)	(0.37)

Quarter Ended	December 31 2006	October 1 2006	July 2 2006	April 2 2006
Revenue	\$ 58,171	\$ 47,200	\$ 43,782	\$ 44,639
Net earnings (loss) from continuing operations	2,473	(1,356)	273	1,382
Net earnings (loss) from continuing operations per common share				
Basic	0.30	(0.16)	0.03	0.16
Diluted	0.30	(0.16)	0.03	0.16
Net earnings (loss) and comprehensive income (loss)	1,796	(1,131)	42	663
Net earnings (loss) per common share				
Basic	0.21	(0.14)	0.01	0.08
Diluted	0.21	(0.14)	0.00	0.08

Note: (1) Due to the Company's floating year end (first Sunday in October) the quarter ended October 7, 2007 consisted of 14 weeks. All others presented consist of 13 weeks.

## LIQUIDITY AND CAPITAL RESOURCES

Bank borrowings and cash flow from operations have been the primary funding sources of working capital and capital expenditures over the past several years. Cash flow from operations totaled \$2,273,000 in Q1 2008 compared with \$3,418,000 in Q1 2007. Working capital consumed cash of \$1,308,000 in Q1 2008 versus cash provided of \$728,000 in Q1 2007. As a result, cash provided by operating activities totaled \$965,000 in Q1 2008 compared to \$4,146,000 in Q1 2007.

Working capital increased modestly to \$29,494,000 at the end of Q1 2008 compared to \$29,246,000 at the end of fiscal 2007. At January 6, 2008 the Company had short-term banking and operating facilities of \$25,000,000 of which \$10,401,000 was drawn. The short-term borrowing facilities should sufficiently fund its planned activities of 2008 including a reserve to fund potential inventory acquisitions.

The Company incurred capital expenditures net of disposals of \$627,000 during Q1 2008 compared to \$1,463,000 in Q1 2007 to provide furniture, fixtures and equipment and make necessary leasehold improvements to new facilities, upgrade or provide new equipment to existing locations and acquire software and hardware.

During fiscal 2008, the Company expects to invest approximately \$1,800,000 in capital equipment, reflecting a modest maintenance program for computer equipment and pre-existing commitments for 5 new locations, 3 of which were opened during the first quarter.

## Contractual Obligations

Payments due by period (\$000's)	Less than 1 year	1 to 3 years	4 to 5 years	After 5 years	Total
Financial Commitments					
Long-term debt	\$ nil	\$ nil	\$ nil	\$ nil	\$ nil
Capital leases	1,344	1,714	46	nil	3,104
Contractual Obligations					
Outlet leases	11,918	18,966	13,935	18,455	63,274
Vehicle and equipment leases	126	59	nil	nil	185
Other long-term obligations	nil	nil	nil	nil	nil
Total	\$ 13,388	\$ 20,739	\$ 13,981	\$ 18,455	\$ 66,563

## RISKS AND UNCERTAINTIES

The Company is principally engaged in the sale of goods through 105 leased retail outlets located across Canada and in the US state of Washington. The Company's business is subject to a number of factors, which directly impact retail sales over which it has no control, namely fluctuations in weather patterns, swings in consumer confidence and buying habits and the changes in goods available for purchase.

Geographically, the Company's stores are located in cities and towns of various sizes. The Company has good relationships with its suppliers and has no reason to believe that it is exposed to any material risk that would prevent the Company from acquiring, distributing and/or selling its merchandise on an ongoing basis.

### Source of Supply of Inventory

All inventory is acquired from opportunistic situations, so those conditions must exist to provide an occasion to acquire inventory. While surpluses of inventory exist in the global economy, the Company must successfully identify each opportunity and negotiate a price that enables the inventory to be sold for a profit. Certain brands, categories and sources of inventory are more desirable and create more customer traffic in the outlets.

### Valuation of Inventory

The Company routinely buys merchandise resulting from closeouts, bankruptcies and insurance claims, and often bids for inventory on a lot basis, without the benefit of complete product details. Company representatives typically view the merchandise and, based on their expertise, draw subjective conclusions about its liquidated value and potential realizable value at retail. Lot purchases are routinely made on the basis of these subjective evaluations.

Over time, the Company's realized revenue and margin, determined using the retail inventory method (see "CRITICAL ACCOUNTING ESTIMATES") in conjunction with periodic physical inventory counts, serve to validate its assumptions about inventory value. On a historic basis, these measures have proven the subjective inventory valuations to be reasonably accurate; however, it still remains a possibility that, in the future, realizable inventory value may differ from its recorded value.

### Seasonality

As a retailer, the Company experiences its strongest sales in its first quarter, buoyed by the holiday shopping season. Sales during the second and third quarters are typically weakest, although large inventory deals can skew the results in any given quarter.

### Competition

As a retailer, Liquidation World competes with other retailers in offering the best value for products it has on hand. There is no effective barrier to prevent entry into the retailing marketplace or the liquidation retailing marketplace by any potential competitor, foreign or domestic. Accordingly, when retailers offer significant savings through price reductions, the Company's competitive advantage is diminished and may need to be addressed by reducing prices, which reduces margins and profitability.

This risk is mitigated somewhat by the scale, scope and reputation of the Company. The liquidation industry is characterized by numerous small regional players. Liquidation World's country-wide base of retail outlets gives it the scale to purchase very large deals and the channel to effectively liquidate them. Its core Canadian operations enable the Company to move goods away from US suppliers' local markets. Liquidation World's 21-year history of respecting its suppliers' brands along with its status as a public company provide a level of comfort and transparency that makes the Company an attractive business partner over lesser known startups and regional players. The unique opportunistic circumstances under which Liquidation World acquires its products enable the Company to purchase inventory at lower cost than other retailers. This cost advantage allows the Company to discount its prices further than most competitors when necessary.

### **Real Estate Leases**

The Company is opportunistic as it leases outlets and pays less than market rates in most cases. If the Company is unable to extend or replace existing leases, it may face increasing costs or a reduction in its number of outlets.

### **Foreign Currency Risk**

The Company acquires more inventory denominated in US dollars than it sells in US dollars, so it is exposed to fluctuations in the value of the US dollar relative to the Canadian dollar. Since inventory is acquired and sold in a relatively short period of time, such fluctuations have limited impact. The Company has assets in its US subsidiaries that, when converted to Canadian dollars on consolidation, are impacted by changes in the exchange rate, creating gains or losses. The Company has determined that such fluctuations are not material to its overall operations and, accordingly, has not adopted a hedging strategy to mitigate those risks.

## **TRANSACTIONS WITH RELATED PARTIES**

The Company does not have any transactions with related parties.

## **CRITICAL ACCOUNTING ESTIMATES**

The Company uses the retail method to estimate the value of its inventory. Under the retail method, inventory on hand is counted and totaled at its retail value net of adjustments for markdowns and obsolescence. The ratio of inventory on hand at its retail value to total inventory available for sale during the course of the quarter at retail is used to determine the portion of inventory remaining at cost as a portion of total inventory available for sale at cost. Accordingly, the costs attributed to inventory are apportioned between inventory remaining and cost of sales.

### **New Accounting Pronouncements**

On December 1, 2006, the CICA issued three new accounting standards: Handbook Section 1535 "Capital Disclosures"; Handbook Section 3862 "Financial Instruments – Disclosures"; Handbook Section 3863 "Financial Instruments – Presentation". These standards are effective for interim and annual financial statements for the Company's reporting period beginning on January 1, 2008. Section 1535 specifies the disclosure of (i) an entity's objectives, policies and processes for managing capital; (ii) quantitative data about what the entity regards as capital; (iii) whether the entity has complied with any capital requirements; and (iv) if it has not complied, the consequences of such non-compliance. The new Handbook Sections 3862 and 3863 replace Handbook Section 3861 "Financial Instruments - Disclosure and Presentation", revising and enhancing its disclosure requirements, and carrying forward unchanged its presentation requirements. These new sections place increased emphasis on disclosures about the nature and extent of risks arising from financial instruments and how the entity manages those risks. The application of Sections 3862 and 3863 do not have any material impact on the Company's financial statements.

### **Future Accounting Pronouncements**

In March 2007, the CICA approved Handbook Section 3031 "Inventories" which replaces the existing Handbook Section 3030 "Inventories". This standard is effective for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2008, with earlier application encouraged. The standard establishes guidance on the determination of cost and its subsequent recognition as an expense including any write down to net realizable value. It also provides guidance in the cost formulas that are used to assign costs to inventories.

The Company is currently assessing the impact of these new accounting standards on its financial statements.

## **OUTSTANDING SHARE DATA**

As of January 6, 2008, the Company has authorized for issuance unlimited common shares of which 8,248,042 are issued and outstanding. As of December 31, 2006 the Company had 8,246,242 shares outstanding. Further, the Company has reserved 751,684 options to acquire common shares of which 672,400 have been granted. At December 31, 2006, 742,950 options were outstanding.

## **DISCLOSURE CONTROLS AND PROCEDURES**

Disclosure controls and procedures are designed to provide reasonable assurance that all relevant information is gathered and reported to senior management, including the Chief Executive Officer and the Chief Financial Officer, on a timely basis so that appropriate decisions can be made regarding public disclosure.

An evaluation of the effectiveness of the design and operation of disclosure controls and procedures was conducted as of October 1, 2006, by and under the supervision of management, including the Chief Executive Officer and the Chief Financial Officer. Based on this evaluation, the Chief Executive Officer and the Chief Financial Officer have concluded that disclosure controls and procedures, as defined under Multilateral Instrument 52-109 – Certification of Disclosure in Issuers' Annual and Interim Filings, are effective to ensure that information required to be disclosed in reports filed or submitted under Canadian securities legislation is recorded, processed, summarized and reported within the time periods specified in those rules.

An evaluation of the design of internal controls over financial reporting was conducted as of October 1, 2006 by and under the supervision of management, including the Chief Executive Officer and the Chief Financial Officer. Based on this evaluation, the Chief Executive Officer and the Chief Financial Officer have concluded that internal controls and procedures, defined under Multilateral Instrument 52-109, have been designed to reasonably ensure the reliability of financial reporting and that the preparation of financial statements for external purposes are in accordance with those rules.

In the process of evaluating the design of the internal controls over financial reporting, certain weaknesses were identified related to the implementation of the Merchandise Management System. Management has since instituted a number of changes to address these weaknesses and is continuing to monitor and refine its internal processes to ensure the accuracy of reported gross margins and inventory values. Furthermore the Company performs semi-annual physical inventory counts to confirm data provided by the information systems.

## **OTHER ITEMS**

Additional information relating to Liquidation World is available on the SEDAR website at [www.sedar.com](http://www.sedar.com).

## **OUTLOOK**

The Company has undergone significant change over the past two years in order to build a stronger foundation for the future. The primary objective in the current fiscal year is to slow the pace of change and to focus on tactical initiatives related to buying merchandise, operating stores and promoting the business. Above all, the Company will aggressively pursue a larger, stronger, more compelling mix of deal merchandise and continue to offer the greatest possible value proposition available to consumers in all the markets it services.

## **FORWARD LOOKING STATEMENTS**

The foregoing includes forward-looking statements and potential future circumstances and developments. Forward-looking statements regarding future performance are subject to risks and uncertainties and actual results may differ materially.

See accompanying notes to consolidated financial statements.

# Consolidated Financial Statements

## CONSOLIDATED BALANCE SHEETS

As at January 6, 2008 and October 7, 2007

Unaudited

(In thousands of Canadian dollars)

	January 6, 2008	October 7, 2007 <small>Restated (see note 5)</small>
<b>Assets</b>		
Current assets		
Cash and equivalents	\$ 205	\$ 216
Accounts receivable	222	293
Inventory	53,704	48,816
Prepaid expenses	1,415	1,719
Income taxes recoverable	2,246	2,221
<u>Current assets of discontinued operations (note 5)</u>	-	1,237
	57,792	54,502
Property and equipment	12,877	12,542
Long-term assets of discontinued operations (note 5)	-	172
	<u>\$ 70,669</u>	<u>\$ 67,216</u>
<b>Liabilities and Shareholders' Equity</b>		
Current liabilities		
Bank indebtedness	\$ 8,336	\$ 7,820
Accounts payable and accrued liabilities	18,184	14,954
Current portion of obligations under capital leases	1,344	1,256
<u>Current liabilities of discontinued operations (note 5)</u>	434	1,265
	28,298	25,295
Obligations under capital leases	1,759	1,512
Shareholders' equity		
Share capital (note 3)	15,518	15,518
Contributed surplus (note 3)	1,250	1,159
<u>Retained earnings</u>	23,844	23,732
	40,612	40,409
	<u>\$ 70,669</u>	<u>\$ 67,216</u>

See accompanying notes.

## CONSOLIDATED STATEMENTS OF EARNINGS (LOSS) AND COMPREHENSIVE INCOME (LOSS) AND RETAINED EARNINGS

For the thirteen weeks ended January 6, 2008 and December 31, 2006

Unaudited

(In thousands of Canadian dollars, except per share amounts)

	2008	2007 Restated (see note 5)
Revenue	\$ 52,812	\$ 58,171
Cost of sales	33,155	35,008
	19,657	23,163
Expenses		
Selling, general and administrative	17,230	18,448
Depreciation and amortization	1,027	858
Stock based compensation	91	86
Interest		
Short Term	199	122
Long Term	41	49
Foreign exchange	(86)	118
	18,502	19,681
Earnings before income taxes	1,155	3,482
Income taxes		
Current	-	1,008
Future	-	1
	-	1,009
Net earnings from continuing operations	1,155	2,473
Loss from discontinued operations (note 5)	(1,043)	(677)
Net earnings and comprehensive income	112	1,796
Retained earnings, beginning of period	23,732	35,443
Retained earnings, end of period	\$ 23,844	\$ 37,239
Basic and diluted earnings (loss) per share		
From continuing operations	\$ 0.14	\$ 0.30
From discontinued operations	(0.13)	(0.09)
	\$ 0.01	\$ 0.21

See accompanying notes.

## CONSOLIDATED STATEMENTS OF CASH FLOWS

For the thirteen weeks ended January 6, 2008 and December 31, 2006

Unaudited

(In thousands of Canadian dollars)

	2008	2007
		Restated (see note 5)
Operating activities		
Net earnings from continuing operations	\$ 1,155	\$ 2,473
Add (deduct) non-cash items:		
Depreciation and amortization	1,027	858
Stock based compensation	91	86
Future income taxes	-	1
	<u>2,273</u>	<u>3,418</u>
Changes in non-cash operating working capital		
Accounts receivable	71	67
Inventory	(4,888)	(6,496)
Prepaid expenses	304	1,379
Accounts payable and accrued liabilities	3,230	5,053
Income taxes recoverable / payable	(25)	725
	<u>965</u>	<u>4,146</u>
Investing activities		
Purchase of capital assets	(627)	(1,463)
Proceeds on disposal of capital assets	2	-
	<u>(625)</u>	<u>(1,463)</u>
Financing activities		
Increase in (repayment of) bank indebtedness	516	(1,639)
Repayment of capital lease	(402)	(285)
	114	(1,924)
Cash applied to discontinued operations (note 5)	(465)	(723)
	<u>(11)</u>	<u>36</u>
Increase (decrease) in cash	(11)	36
Cash and equivalents, beginning of period	216	184
Cash and equivalents, end of period	<u>\$ 205</u>	<u>\$ 220</u>
Supplemental disclosure of cash paid for:		
Income taxes	\$ 27	\$ 285
Interest	240	137
	<u>\$ 267</u>	<u>\$ 422</u>

See accompanying notes.

# Notes to Interim Financial Statements

January 6, 2008

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

## I. Basis of Presentation

### (a) Significant Accounting Policies

The accompanying unaudited interim consolidated financial statements for Liquidation World Inc. (the "Company") have been prepared in accordance with Canadian generally accepted accounting principles for interim financial statements. These interim financial statements follow the same accounting policies and methods of application as the most recent annual audited consolidated financial statements dated October 7, 2007 except as noted below. These interim financial statements should be read in conjunction with the annual statements.

### (b) Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets at the date of the financial statements. In determining the cost amount of inventories, management uses the retail inventory method, which is by its nature subjective. Other significant areas requiring the use of estimates relate to the determination of future tax assets and liabilities, provisions relating to returns, obsolete inventory, and the remaining useful life of capital assets. Actual results could differ from those estimates.

### (c) Comparative Information

Certain comparative figures have been reclassified to conform with the current financial statement presentation.

### (d) New Accounting Pronouncements

On December 1, 2006, the CICA issued three new accounting standards: Handbook Section 1535 "Capital Disclosures"; Handbook Section 3862 "Financial Instruments – Disclosures"; Handbook Section 3863 "Financial Instruments – Presentation". These standards are effective for interim and annual financial statements for the Company's reporting period beginning on October 8, 2007. Section 1535 specifies the disclosure of (i) an entity's objectives, policies and processes for managing capital; (ii) quantitative data about what the entity regards as capital; (iii) whether the entity has complied with any capital requirements; and (iv) if it has not complied, the consequences of such non-compliance. The new Handbook Sections 3862 and 3863 replace Handbook Section 3861 "Financial Instruments - Disclosure and Presentation", revising and enhancing its disclosure requirements, and carrying forward unchanged its presentation requirements. These new sections place increased emphasis on disclosures about the nature and extent of risks arising from financial instruments and how the entity manages those risks. The application of sections 3862 and 3863 do not have any material impact on the Company's financial statements.

### (e) Future Accounting Pronouncements

In March 2007, the CICA approved Handbook Section 3031 "Inventories" which replaces the existing Handbook Section 3030 "Inventories". This standard is effective for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2008, with earlier application encouraged. The standard provides more guidance on the measurement and disclosure requirements for inventories. The Company is currently assessing the impact of this new accounting standard on its consolidated financial statements.

## 2. Seasonality

As a retailer, the Company experiences stronger sales in its first quarter (particularly in December) and lower sales in its second and third quarters due in part to consumer buying patterns over the holiday season. Additionally, large inventory deals may skew the results in any given quarter. Therefore, the performance of this 13-week period is not necessarily indicative of the performance for the balance of the fiscal year.

### 3. Share Capital

#### (a) Stock Options:

A summary of the status of the Company's share option plan as of October 7, 2007 and changes during the fiscal period are presented below:

	Number of options	Weighted average exercise price
Stock options outstanding, October 7, 2007	715,850	\$ 5.32
Cancelled/expired	(43,450)	5.46
Balance, January 6, 2008	672,400	\$ 5.31

#### (b) Contributed Surplus

The Company recognizes stock-based compensation expense using the fair value method, when options are issued to employees. Such cost is recorded as an expense and an increase to contributed surplus, on a straight-line basis, over the vesting period related to such options. The amount is included in contributed surplus on the consolidated balance sheets and selling, general and administrative expenses on the consolidated statement of operations.

	Jan 6, 2008
Balance, beginning of period	\$ 1,159
Stock-based compensation expense	91
Balance, end of period	\$ 1,250

### 4. Income Tax

The provision for income taxes differs from the amount obtained by applying the combined applicable income tax rate to earnings before income taxes. The difference relates to the following items:

	2008
Statutory income tax rate	34.7%
Calculated tax expense (recovery)	\$ 401
Capital taxes	15
Stock option benefit	32
Change in valuation allowance	(358)
Difference in enacted rates on future taxes	(86)
Other items	(4)
	\$ -

The tax effects of temporary differences that give rise to significant portions of the future tax asset (liability) at are presented below:

	Assets (Liability)		Jan 6, 2008	Oct 7, 2007
	Canada	United States		
Non-capital loss carryforwards	\$ 2,738	\$ 1,204	\$ 3,942	\$ 4,476
Capital assets	(660)	-	(660)	(836)
Inventory of US subsidiaries	-	-	-	-
	2,078	1,204	3,282	3,640
Valuation allowance	(2,078)	(1,204)	(3,282)	(3,640)
	\$ -	\$ -	\$ -	\$ -

## 5. Discontinued Operations

The Company operated 18 stores in the US which were reported in segmented information under Geographical Information as US at fiscal year end. During the fourth quarter of fiscal 2007, the Company announced that it would wind down its US operations and subsequently closed 15 of 18 stores in the first quarter of fiscal 2008, and which are now described as discontinued operations. The following table provides additional information regarding the stores that are now closed.

The assets and liabilities of discontinued operations presented in the accompanying interim consolidated balance sheets were as follows:

	January 6, 2008	October 7, 2007
Inventory	\$ -	\$ 1,104
Prepaid expenses	-	133
Current assets of discontinued operations	\$ -	\$ 1,237
Property and equipment	-	172
Long-term assets of discontinued operations	\$ -	\$ 172
Accounts payable and accrued liabilities	434	1,265
Liabilities of discontinued operations	\$ 434	\$ 1,265

The results of discontinued operations, previously reported in the US segment, for the thirteen week statement of operations were as follows:

	January 6, 2008	December 31, 2006
Revenue	\$ 745	\$ 6,500
Loss from discontinued operations, net of nil tax	\$ (1,043)	\$ (677)

There was no gain or loss on the sale of capital assets.

Net cash used in discontinued operations during the thirteen week periods were as follows:

	January 6, 2008	December 31, 2006
Operating activities:		
Net loss from discontinued operations	\$ (1,043)	\$ (677)
Add (deduct) non-cash items:		
Depreciation and amortization	-	57
Change in working capital items	406	(75)
	(637)	(695)
Investing activities:		
Purchase of capital assets	-	(28)
Proceeds on disposal of capital assets	172	-
	172	(28)
Net cash used in discontinued operations	\$ (465)	\$ (723)

## 6. Commitments and Contingencies

The Company leases properties and equipment under operating leases covering various years up to 2037 and are reported in the F2007 Annual Report.

The Company is involved and potentially subject to various claims by third parties arising out of the normal course and conduct of its business. Management assesses such claims and where it is considered likely that the claim will result in a material loss and where the amount of the loss is quantifiable, provisions for loss are made based on management's assessment of the likely outcome. The Company does not provide for claims that are considered unlikely to result in a significant loss, claims for which the outcome is not determinable or claims where the amount of the loss cannot be reasonably estimated. Any settlements or awards under such claims are provided for when reasonably determinable. Although such matters cannot be predicted with certainty, management currently considers the exposure to such claims and litigation, to the extent not covered by the Company's insurance policies or otherwise provided for, not to be material to these consolidated financial statements.

## 7. Capital Management

The Company's objective when managing its capital is to safeguard the Company's assets while at the same time maximizing the growth of its business and the returns to its shareholders. The Company's capital consists of debt and share capital.

This objective is achieved by prudently managing the capital generated through internal growth, optimizing the use of lower cost capital (capital leases and bank debt) and raising share capital when required to fund growth initiatives. Short term borrowings are managed through managing inventory purchases and balancing inventory levels, reducing inventory levels to reduce debt when prudent.

Consistently with others in the industry, the Corporation monitors capital on the basis of the ratio of debt to shareholders' equity (debt divided by the book value of shareholders' equity). Although the Company has no mandated range or ceiling for its ratio of debt to equity, it currently would not anticipate exceeding a ratio of .7 to 1. The Company's ratio of debt to shareholders equity on a book and current value basis is as follows:

(\$000's)	January 6, 2008	October 7, 2007
Bank indebtedness	\$ 8,336	\$ 7,820
Capital leases	3,103	2,768
Debt	11,439	10,588
Capital stock	15,518	15,518
Contributed surplus	1,250	1,159
Retained earnings	23,844	23,732
Shareholders' equity	\$ 40,612	\$ 40,409
Debt to equity ratio	0.28:1	0.26:1

Shares are listed on the Toronto Stock Exchange under the symbol LQW.

# Corporate Information

## DIRECTORS

### *Leslie Landes, Chairman*

Les is a former Director and Chairman of publicly listed Stockgroup Information Systems Inc., as well as a consultant in his private company, Landes Enterprises, which provides interim and turn around management services in a number of industries. Les is a former director of TIR Systems Ltd., and formerly held various senior executive positions with the Jim Pattison Group.

### *Jonathan Hill, President and CEO since February, 2005*

Jonathan joined Liquidation World in 1991 and has been responsible for building the eastern operations. In February of 2005 he was appointed president and sole CEO.

### *Darren Gillespie, Senior Executive VP and President, LQW Traders Inc.*

Darren joined Liquidation World in 1993 and led the Company's expansion in British Columbia before relocating to Seattle to launch the Company's US retail and buying operations. Today, as President of LQW Traders Inc., Darren develops and manages key supply relationships within US retail, freight, insurance, legal and banking channels to provide inventory for Liquidation World's Canadian outlets. Prior to joining Liquidation World, Darren spent 10 years with a startup consumer electronics business in Canada and helped build it into a nation-wide chain.

### *Herb Lukofsky, CA, Corporate Director, Business Consultant*

Herb was a partner with Arthur Andersen where he was in charge of the firm's tax practice. In 1984 he established Lukofsky, Lajoie and Associates, a business consulting firm specializing in mergers and acquisitions. Herb joined the Board of Directors for Liquidation World in January 2001.

### *Charles M. (Chad) Murray, President, Chad Murray Sales and Marketing Inc.*

Chad is a long-time shareholder in Liquidation World and has a solid understanding of retailing in Canada. He served in numerous capacities with Erie Industries Inc., eventually becoming President, CEO and a member of the board before founding his own company.

### *Robert Thomson, QC, President, Rovalex Investments Inc.*

Robert, now President of Rovalex Investments Inc. practiced corporate law with the firm of Fraser Milner in mergers and acquisitions until his retirement in 1999.

### *Bob Weins, CA, Business Consultant*

Bob was CFO of D-Wave Systems Inc., until March 2005. Previously Bob was President and CEO of FACS Record Centre Inc., and managing partner with Arthur Andersen in Ottawa and Vancouver. Currently Bob is involved with a number of charitable organizations.

## MANAGEMENT

Jonathan Hill, President and CEO

Darren Gillespie, Senior Executive VP and President, LQW Traders Inc.

Andrew Searby, CA, Executive VP and CFO

Maurice Chelli, SVP Merchandising

Darryl Chenoweth, SVP Operations

## **SOLICITORS**

Miller Thomson, LLP  
#3000, 700 - 9th Ave. SW, Calgary, AB T2P 3T3

## **AUDITORS**

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One London Place, Suite 1800,  
255 Queens Ave., London, ON N6A 5S7

## **BANK**

Royal Bank of Canada  
P.O. Box 50, 200 Bay St. Toronto, ON M5J 2W7

## **TRANSFER AGENT**

Computershare Investor Services  
100 University Ave. 8th Floor, Toronto ON M5J 2Y1

## **CORPORATE OFFICE**

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Phone: 519-758-8878

Web: [www.liquidationworld.com](http://www.liquidationworld.com)

# Outlet Locations

## BRITISH COLUMBIA

Abbotsford  
Aldergrove  
Chilliwack  
Coquitlam  
Courtenay  
Cranbrook  
Duncan  
Gibsons  
Kamloops  
Langley  
Maple Ridge  
Merritt  
Mission  
Nanaimo  
Penticton  
Powell River  
Prince George  
Quesnel  
Richmond  
Surrey (2)  
Terrace  
Trail  
Vernon

## ALBERTA

Calgary (3)  
Camrose  
Cold Lake  
Drumheller  
Edmonton  
Fort Saskatchewan  
Grande Prairie  
Hinton  
Lethbridge  
Medicine Hat  
Peace River  
Ponoka  
St. Paul  
Taber  
Westlock  
Wetaskiwin

## ONTARIO

Ajax  
Arthur  
Belleville  
Blenheim  
Bolton  
Brantford  
Cambridge  
Campbellford  
Chatham  
Cobourg  
Hamilton (2)  
Hawkesbury  
Ingersoll  
Keswick  
Kingston  
Leamington  
London (2)  
Mississauga  
Oakville  
Orillia  
Oshawa  
Paris  
Petawawa  
Port Colborne  
Prescott  
Renfrew  
Sarnia  
Sault Ste. Marie  
Smiths Falls  
St. Catharines (2)  
Sudbury  
Thunder Bay  
Trenton  
Wallaceburg  
Welland  
Windsor (2)

## YUKON

Whitehorse

## SASKATCHEWAN

Lloydminster  
Moose Jaw  
Prince Albert  
Regina  
Saskatoon  
Swift Current  
Yorkton

## MANITOBA

Steinbach  
Swan River  
Winnipeg (3)

## ATLANTIC

Amherst, NS  
Dartmouth, NS  
Fredericton, NB  
Halifax, NS  
Saint John, NB  
Truro, NS

## US

Spokane, WA  
Richland, WA  
Renton, WA