

Liquidation  
World  
Quarterly  
Report  
Q3 2008

**LIQUIDATION  
WORLD®**

# 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 105 fun, friendly and no-frill Liquidation World outlets.

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

# President's Message

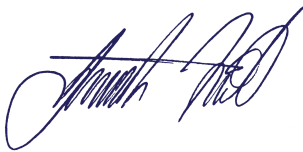
After posting disappointing results in our second quarter, we announced that we would make immediate changes to reduce operating costs and become a simpler, more agile business. During the third quarter, the following changes were implemented:

- Our buying team was reorganized and our buying processes were made more flexible, with budgets being allocated to the best deals rather than by department.
- New markdown policies were introduced to more aggressively manage aged and non-performing inventory on an ongoing basis. Operationally, our new markdown policies give store managers more authority to manage aged and non-performing inventory locally, which we believe will improve inventory turnover and cash flow.
- Corporate overhead expenses were lowered through the elimination of several positions and a thorough review of other non-store costs.
- We initiated the closure of 7 outlets to rationalize inventory and improve cash flow. The store closures will be completed by year end. The majority of these locations existed within the trade area of larger locations, helping to mitigate the negative effect on total Company sales.
- A Special Committee of independent board members was formed to investigate strategic alternatives available to the Company to increase shareholder value. The Committee continues its work with no impact on day-to-day operations.

Our third quarter results do not reflect the impact of the changes we have made. However, I am confident that the actions we have taken have created a more nimble organization that is better focused on procuring unique and exciting inventory. Furthermore, I am pleased to report that our refocused buying team has enjoyed some early success landing strong event deals which, in turn, will raise the average margin of the inventory on our shelves.

Undoubtedly, the changes implemented during the third quarter have been difficult; however, they are necessary to ensure the ongoing success of the Company. Based on these changes, we anticipate that our fourth quarter will reflect positive same store sales performance, stronger margin performance and lower absolute expense levels.

In closing, I would like to express my sincere appreciation to our shareholders for their continued support and all of our 1600 associates for their hard work and commitment during a difficult quarter.



# MD&A

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

## OVERVIEW

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

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. The Company puts a priority on merchandise from insolvencies and insurance claims, however a proportion of opportunity closeout 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 stores in Canada and the US. A typical Liquidation World store occupies between 20,000 and 25,000 square feet, although there are some smaller and some larger stores.

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

Among liquidators, Liquidation World is unique insofar as it maintains a national network of retail stores 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 capitalizes 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". The following discussion relates to continuing operations, unless otherwise noted.

A summary of results for the first quarter of fiscal 2008 ("Q3 2008"), comprising the thirteen weeks ended July 6, 2008 follows:

- Sales from continuing operations increased 5.1% to \$43,765 from \$41,650 in Q3 2007
- Same store sales increased 3.3% from Q3 2007
- Gross margin decreased to 33.6% of sales from 34.5% of sales in Q3 2007
- Selling, general and administrative expenses, including restructuring costs in the quarter, decreased to 39.1% of sales in Q3 2008 from 39.2% of sales in Q3 2007
- The Company recorded a net loss from continuing operations of \$3,783 in Q3 2008 compared to a net loss from continuing operations of \$2,069 in Q3 2007

## STRATEGIC ALTERNATIVES

On June 4, 2008, the Company announced the formation of a Special Committee of independent board members to investigate and evaluate strategic alternatives available to the Company to increase shareholder value.

The Special Committee is comprised of independent board members Craig Graham, Chairman, Jeffrey Mandel, and Bob Wiens, CA. The Special Committee has retained Capital West Partners, an independent financial advisor; to assist in the process and has also retained independent legal counsel.

The Special Committee has not established a list of strategic alternatives, nor has it endorsed any particular course of action. Furthermore, there is no guarantee that the work of the Special Committee will lead to any transaction.

## RESULTS OF OPERATIONS

### **Revenue**

Revenue for the quarter ended July 6, 2008, which includes sales of merchandise and fee revenue, increased 5.1% to \$43,765 from \$41,650 in the same quarter last year. Same store sales increased 3.3% for the quarter.

Revenue for the thirty-nine weeks ended July 6, 2008 (year-to-date fiscal 2008) decreased 2.1% to \$138,799 from \$141,806 during the same period in fiscal 2007. Same store sales decreased 5.4% for year-to-date fiscal 2008.

### **Gross Margin**

Gross margin increased to \$14,717 in Q3 2008 or 33.6% of sales, from \$14,372 or 34.5% of sales in Q3 2007. On a year-to-date basis, gross margin was 34.6% in fiscal 2008 compared to 36.5% in fiscal 2007. Gross margin in the quarter and year-to-date was negatively impacted by reductions in carrying cost for older merchandise and higher freight costs due mainly to higher oil prices.

Gross margins can fluctuate as a result of cost of product purchased, freight costs, shrinkage, product mix sold and markdowns taken. 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 stores 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 as required.

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

Selling, general and administrative which includes all expenses of occupying, operating, and supporting stores, including opening new stores, increased to \$17,102 in Q3 2008 from \$16,342 in Q3 2007. These expenses increased in the quarter from Q3 2007 mainly due to one-time severance costs (\$485) arising from organizational restructuring. As a percentage of sales, selling, general and administrative expenses decreased to 39.1% in Q3 2008 from 39.2% in Q3 2007.

On a year-to-date basis, selling, general and administrative expenses at \$51,554, or 37.1% as a percentage of sales, were approximately flat with the prior year, and up as a percentage of sales (36.3% in fiscal 2007) due mainly to restructuring costs incurred in the third quarter.

### **Depreciation and Amortization**

Depreciation and amortization increased in Q3 2008 by 8.8% to \$994 from \$914 in Q3 2007. On a year-to-date basis, depreciation and amortization increased by 10.9% to \$3,006 in fiscal 2008 compared to \$2,711 in the same period of fiscal 2007.

### **Interest**

Total interest expense in Q3 2008 increased to \$230 compared to \$223 in Q3 2007. On a year-to-date basis, interest expenses were \$757 in fiscal 2008 compared to \$570 in the same period in fiscal 2007. Year-to-date interest expense was higher than the prior year due mainly to higher than average borrowing levels arising from higher average inventory levels in year-to-date fiscal 2008.

The Company has short-term banking facilities with a Canadian chartered bank in the amount of \$20,000, subject to margining limits on accounts receivable and inventory, bearing interest at the bank's prime rate plus 300 basis points. At the end of Q3 2008, \$7,904 was drawn (net of outstanding deposits and cheques) compared with \$7,820 at the end of Q3 2007.

### **Foreign Exchange**

During the quarter, the Company recorded a net foreign exchange loss of \$83 compared to a foreign exchange gain of \$134 in Q3 2007. On a year-to-date basis, the Company recorded a net foreign exchange loss of \$28 in fiscal 2008 as compared to a net foreign exchange gain of \$92 during the same period in fiscal 2007.

### **Income Taxes**

The statutory tax rate in effect is 31.9%, however, as a result of losses in the current and prior periods, the Company has accumulated loss carry-forwards totaling approximately \$11,000 in Canada and \$3,000 in the US. Consequently, the Company did not record any income taxes during the third quarter of 2008.

### **Net Loss from Continuing Operations**

During Q3 2008, the Company recorded a net loss from continuing operations of \$3,783 (\$0.46 per share) compared to a net loss from continuing operations of \$2,069 (\$0.25 per share) during Q3 2007. The increase in the net loss in Q3 2008 is attributable mainly to: a) severance costs incurred in Q3 2008; and b) an income tax recovery arising from a tax loss carry-back in Q3 2007.

On a year-to-date basis, the Company recorded a net loss from continuing operations of \$7,589 (\$0.92 per share) in fiscal 2008 compared to a net loss from continuing operations of \$2,329 (\$0.28 per share) during the same period in fiscal 2007. The increase in the year-to-date net loss is due mainly to: a) lower gross margin due to lower sales and lower gross margin rate; b) severance costs incurred in Q3 2008; and c) a tax recovery arising from a tax-loss carry-back in fiscal 2007.

### Discontinued Operations

During Q1 2008, the Company ceased operations of its wholly-owned US subsidiary, which included closing 15 of its 18 US stores. These closed stores are now considered 'discontinued operations'. During Q3 2008, the Company recorded no earnings or losses related to the discontinued operations. During Q3 2007, losses from discontinued operations totaled \$827 or \$0.10 per share.

### Net Loss and Comprehensive Loss

The Company recorded a net loss and comprehensive loss for Q3 2008 of \$3,783 (\$0.46 per share) compared with net loss and comprehensive loss of \$2,896 (\$0.35 per share) in Q3 2007. On a year-to-date basis, the Company recorded a net loss and comprehensive loss of \$8,632 (\$1.05 per share) in fiscal 2008 compared with a net loss and comprehensive loss of \$4,132 (\$0.50 per share) during the same period in fiscal 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	July 6 2008	April 6 2008	January 6 2008	October 7 2007
Revenue	\$ 43,765	\$ 42,222	\$ 52,812	\$ 46,456
Net earnings (loss) from continuing operations	(3,783)	(4,961)	1,155	(3,922)
Net earnings (loss) from continuing operations per common share				
Basic	(0.46)	(0.60)	0.14	(0.48)
Diluted	(0.46)	(0.60)	0.14	(0.48)
Net earnings (loss) and comprehensive income (loss)	(3,783)	(4,961)	112	(7,588)
Net earnings (loss) per common share				
Basic	(0.46)	(0.60)	0.01	(0.92)
Diluted	(0.46)	(0.60)	0.01	(0.92)

Quarter Ended	July 1 2007	April 1 2007	December 31 2006	October 1 2006
Revenue	\$ 41,650	\$ 41,985	\$ 58,185	\$ 47,200
Net earnings (loss) from continuing operations	(2,069)	(2,733)	2,473	(1,356)
Net earnings (loss) from continuing operations per common share				
Basic	(0.25)	(0.33)	0.30	(0.16)
Diluted	(0.25)	(0.33)	0.30	(0.16)
Net earnings (loss) and comprehensive income (loss)	(2,896)	(3,032)	1,796	(1,131)
Net earnings (loss) per common share				
Basic	(0.35)	(0.36)	0.21	(0.14)
Diluted	(0.35)	(0.36)	0.21	(0.14)

Note: (1) Due to the Company's floating year end (first Sunday in October) the quarter ended October 7, 2007 consisted of fourteen weeks. All others presented consist of thirteen 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 consumed by operations totaled \$2,698 in Q3 2008 compared with cash consumed of \$1,039 in Q3 2007. Net working capital changes generated cash of \$9,527 in Q3 2008 as compared to \$196 in Q3 2007. As a result, cash generated by operating activities was \$6,829 in Q3 2008 compared to cash consumed of \$843 in Q3 2007.

Working capital decreased to \$21,402 at the end of Q3 2008 compared to \$29,207 at the end of fiscal 2007. At July 6, 2008 the Company had short-term banking and operating facilities of \$20,000 of which the Company had drawn down \$10,338 (\$7,904 net of outstanding deposits and cheques). The short-term borrowing facilities should sufficiently fund its planned activities for the balance of 2008.

The Company incurred capital expenditures net of disposals of \$95 during Q3 2008 compared to \$641 in Q3 2007 which included capital expenditures for new and existing stores, and for a portion of the software and hardware costs of the merchandise management system (MMS project).

On a year-to-date basis, capital expenditures were \$927 in fiscal 2008 compared to \$2,746 in the same period in fiscal 2007 which included capital expenditures for new stores and information technology investments.

### **Contractual Obligations**

Payments due by period (\$000's)	Less than 1 year	1 to 3 years	4 to 5 years	After 5 years	Total
<b>Financial Commitments</b>					
Capital leases	\$ 1,844	\$ 564	\$ nil	\$ nil	\$ 2,408
<b>Contractual Obligations</b>					
Store leases	10,795	18,124	14,281	17,792	60,992
Vehicle and equipment leases	79	9	nil	nil	88
<b>Total</b>	<b>\$ 12,718</b>	<b>\$ 18,697</b>	<b>\$ 14,281</b>	<b>\$ 17,792</b>	<b>\$ 63,488</b>

### **RISKS AND UNCERTAINTIES**

The Company is principally engaged in the sale of goods through 105 leased retail stores 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 landlords and 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 stores.

#### **Valuation of Inventory**

The Company routinely buys merchandise resulting from closeouts, bankruptcies and insurance claims, and often bids for inventory on a lot basis, often 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 stores

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 stores 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 stores.

#### **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. 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 historically not adopted a hedging strategy to mitigate those risks.

#### **Financing Risk**

The Company is currently negotiating a long-term asset-based loan facility with its bank to replace the current demand credit facility. This new facility is expected to be completed in the fourth quarter.

### **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 year 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 CICA 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 the Company in the fiscal year beginning October 6, 2008. 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.

CICA Handbook Section 1400, General Standards of Financial Statement Presentation, was amended to include requirements to assess and disclose an entity's ability to continue as a going concern. This standard is effective for the Company in the fiscal year beginning October 6, 2008.

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

## OUTSTANDING SHARE DATA

As of July 6, 2008, the Company has authorized for issuance unlimited common shares of which 8,248,122 are issued and outstanding. Further, the Company has reserved 751,684 options to acquire common shares of which 560,800 have been granted as at July 6, 2008. Subsequent to the end of the quarter 190,884 options were granted and 20,000 cancelled.

## 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 in the last year in order to build a stronger foundation for the future. The primary objective in the current fiscal year is to improve processes, to control costs and to focus on 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 July 6, 2008 and October 7, 2007

Unaudited

(In thousands of Canadian dollars)

	July 6, 2008	October 7, 2007 <small>Restated (see note 5)</small>
<b>Assets</b>		
Current assets		
Cash and equivalents	\$ 199	\$ 216
Accounts receivable	557	293
Inventory	45,140	48,816
Prepaid expenses	1,407	1,719
Income taxes recoverable	270	2,221
<u>Current assets of discontinued operations (note 5)</u>	<u>-</u>	<u>1,237</u>
	47,573	54,502
Property and equipment	11,213	12,542
Long-term assets of discontinued operations (note 5)	-	172
	<u>\$ 58,786</u>	<u>\$ 67,216</u>
<b>Liabilities and Shareholders' Equity</b>		
Current liabilities		
Bank indebtedness	\$ 7,904	\$ 7,820
Accounts payable and accrued liabilities	15,989	14,954
Current portion of obligations under capital leases	1,843	1,256
<u>Current liabilities of discontinued operations (note 5)</u>	<u>434</u>	<u>1,265</u>
	26,171	25,295
Obligations under capital leases	564	1,512
Shareholders' equity		
Share capital	15,518	15,518
Contributed surplus (note 3)	1,433	1,159
<u>Retained earnings</u>	<u>15,100</u>	<u>23,732</u>
	32,051	40,409
	<u>\$ 58,786</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 July 6, 2008 and July 1, 2007

Unaudited

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

	13 weeks ended July 6, 2008	13 weeks ended July 1, 2007	39 weeks ended July 6, 2008	39 weeks ended July 1, 2007
		Restated (see note 5)		Restated (see note 5)
Revenue	\$ 43,765	\$ 41,650	\$ 138,799	\$ 141,806
Cost of sales	29,048	27,278	90,769	90,094
Gross Margin	14,717	14,372	48,030	51,712
Expenses				
Selling, general and administrative	17,102	16,342	51,554	51,507
Depreciation and amortization	994	914	3,006	2,711
Stock based compensation	91	94	274	291
Interest				
Short Term	169	198	610	433
Long Term	61	25	147	137
Foreign exchange	83	(134)	28	(92)
	18,501	17,439	55,620	54,987
Loss before income taxes	(3,783)	(3,067)	(7,589)	(3,275)
Income taxes				
Current	-	(1,020)	-	(984)
Future	-	22	-	38
	-	(998)	-	(946)
Net loss from continuing operations	(3,783)	(2,069)	(7,589)	(2,329)
Loss from discontinued operations	-	(827)	(1,043)	(1,803)
Net loss and comprehensive loss	(3,783)	(2,896)	(8,632)	(4,132)
Retained earnings, beginning of period	18,883	34,207	23,732	35,443
Retained earnings, end of period	\$ 15,100	\$ 31,311	\$ 15,100	\$ 31,311
Basic and diluted earnings (loss) per share	\$ (0.46)	\$ (0.25)	\$ (0.92)	\$ (0.28)
From continuing operations	\$ -	\$ (0.10)	\$ (0.13)	\$ (0.22)
From discontinued operations	\$ (0.46)	\$ (0.35)	\$ (1.05)	\$ (0.50)

See accompanying notes.

## CONSOLIDATED STATEMENTS OF CASH FLOWS

For the thirteen weeks ended July 6, 2008 and July 1, 2007

Unaudited

(In thousands of Canadian dollars)

	13 weeks ended July 6, 2008	13 weeks ended July 1, 2007 Restated (see note 5)	39 weeks ended July 6, 2008	39 weeks ended July 1, 2007 Restated (see note 5)
<b>Operating activities</b>				
Net loss from continuing operations	\$ (3,783)	\$ (2,069)	\$ (7,589)	\$ (2,329)
Add (deduct) non-cash items:				
Depreciation and amortization	994	914	3,006	2,711
Loss (gain) on disposal of capital asset	-	-	12	(118)
Stock based compensation	91	94	274	291
Future income taxes	-	22	-	38
	(2,698)	(1,039)	(4,297)	593
Changes in non-cash operating working capital				
Accounts receivable	177	(75)	(264)	99
Inventory	4,010	1,170	3,676	(4,951)
Prepaid expenses	(140)	(510)	312	(345)
Accounts payable and accrued liabilities	3,340	653	1,035	3,665
Income taxes recoverable	2,140	(1,042)	1,951	(1,311)
	6,829	(843)	2,413	(2,250)
<b>Investing activities</b>				
Purchase of capital assets	(95)	(641)	(927)	(2,746)
Proceeds on disposal of capital assets	-	-	2	156
	(95)	(641)	(925)	(2,590)
<b>Financing activities</b>				
Increase (decrease) in bank indebtedness	(6,390)	845	84	7,476
Repayment of capital lease	(348)	(294)	(1,125)	(972)
Proceeds on issuance of common shares	-	8	-	8
	(6,738)	559	(1,041)	6,512
Cash provided by (applied to) discontinued operations (note 5)	-	992	(465)	(1,643)
Increase (decrease) in cash	(3)	(3)	(17)	29
Cash and equivalents, beginning of period	202	216	216	184
Cash and equivalents, end of period	\$ 199	\$ 213	\$ 199	\$ 213
<b>Supplemental disclosure of cash paid for:</b>				
Income taxes	\$ 26	\$ 90	\$ 221	\$ 397
Interest	229	255	769	655
	\$ 255	\$ 345	\$ 990	\$ 1,052

See accompanying notes.

# Notes to Interim Financial Statements

July 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 property and equipment. 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

CICA Handbook Section 3031 "Inventories" replaces the existing Handbook Section 3030 "Inventories". This standard is effective for the Company in the fiscal year beginning October 6, 2008. 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.

CICA Handbook Section 1400 "General Standards of Financial Statement Presentation" was amended to include requirements to assess and disclose an entity's ability to continue as a going concern this standard is effective for the Company in the fiscal year beginning October 6, 2008.

## 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 thirteen 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 July 6, 2008 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	(195,050)	5.52
Granted	40,000	2.26
Balance, end of period	560,800	\$ 5.03

#### (b) Contributed Surplus

The Company recognizes stock-based compensation expense using the fair value method, when options are granted 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.

	13 weeks ended July 6, 2008	39 weeks ended July 6, 2008
Balance, beginning of period	\$ 1,342	\$ 1,159
Stock-based compensation expense	91	274
Balance, end of period	\$ 1,433	\$ 1,433

### 4. Income Tax

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

	13 weeks ended July 6, 2008	13 weeks ended July 1, 2007	39 weeks ended July 6, 2008	39 weeks ended July 1, 2007
Statutory income tax rate	31.9%	34.7%	31.9%	34.7%
Calculated tax expense (recovery)	\$ (1,207)	\$ (1,045)	\$ (2,421)	\$ (1,117)
Capital taxes	19	22	49	52
Stock option benefit	29	31	87	99
Change in valuation allowance	1,281	42	1,440	54
Difference in enacted rates on future taxes	(97)	-	125	160
Other items	(25)	(48)	720	(194)
	\$ -	\$ (998)	\$ -	\$ (946)

The tax effects of temporary differences that give rise to significant portions of the future tax asset (liability) are presented below (loss carryforward includes discontinued operations):

	Assets (Liability)		Total	
	Canada	United States	2008	2007
Non-capital loss carryforwards	\$ 4,312	\$ 1,609	\$ 5,921	\$ 4,476
Capital assets	(182)	-	(182)	(836)
	4,130	1,609	5,739	3,640
Valuation allowance	4,130	1,609	5,739	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:

	July 6, 2008	October 7, 2007
Inventory	\$ -	\$ 1,104
Prepaid expenses	-	133
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 and thirty nine week periods ended July 6, 2008 and July 1, 2007 presented in the accompanying interim consolidated statement of operations were as follows:

	13 weeks ended July 6, 2008	13 weeks ended July 1, 2007	39 weeks ended July 6, 2008	39 weeks ended July 1, 2007
Revenue	\$ -	\$ 4,890	\$ 745	\$ 16,984
Loss from discontinued operations, net of nil tax	\$ -	\$ (827)	\$ (1,043)	\$ (1,803)

There was no gain or loss on the sale of capital assets arising from discontinued operations.

Net cash applied to discontinued operations for the thirteen and thirty nine week periods ended July 6, 2008 and July 1, 2007 presented in the accompanying interim consolidated statement of cash flows was as follows:

	13 weeks ended July 6, 2008	13 weeks ended July 1, 2007	39 weeks ended July 6, 2008	39 weeks ended July 1, 2007
Operating activities:				
Net loss from discontinued operations	\$ -	\$ (827)	\$ (1,043)	\$ (1,803)
Add non-cash items:				
Depreciation and amortization	-	33	-	149
Change in working capital items	-	1,716	406	113
	-	922	(637)	(1,541)
Investing activities:				
Purchase of capital assets	-	-	-	(102)
Proceeds on disposal of capital assets	-	-	172	-
	-	-	172	(102)
Net cash provided by (applied to) discontinued operations	\$ -	\$ 922	\$ (465)	\$ (1,643)

## 6. Commitments and Contingencies

The Company leases properties and equipment under operating leases covering various years up to 2019 and one to 2037 and are reported in the fiscal 2007 Annual Report.

The Company is involved in 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 capital consists of debt and share capital. 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. 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, scheduling payments and balancing inventory levels and reducing inventory levels to reduce debt when prudent.

The Company is subject to margining requirements under its bank credit facility which limit its borrowings to the lesser of its credit limit and its available borrowing base that is determined mainly by eligible inventory on hand. As at July 6, 2008, the Company was in compliance with these margining requirements.

The Company monitors capital on the basis of the ratio of debt to shareholders' equity (debt divided by the book value of shareholders' equity). The Company has no mandated range or ceiling for its ratio of debt to equity. The Company's ratio of debt to shareholders' equity on a book and current value basis is as follows:

(\$000's)	July 6, 2008	October 7, 2007
Bank indebtedness	\$ 7,904	\$ 7,820
Capital leases	2,408	2,768
Debt	10,312	10,588
Capital stock	15,518	15,518
Contributed surplus	1,433	1,159
Retained earnings	15,100	23,732
Shareholders' equity	\$ 32,051	\$ 40,409
Debt to equity ratio	0.32:1	0.26:1

## 8. Financial Instruments

The Company has designated cash and bank indebtedness as held for trading as the fair value can be reliably measured. Accounts receivable are designated as receivables and accounts payable and accrued liabilities are designated as other financial liabilities. These financial instruments are initially measured at fair value. Receivables and accounts payable and accrued liabilities are subsequently measured on the basis of amortized cost using the effective interest rate method. Assets and liabilities held for trading are revalued on the reporting date based on relevant market information and information about the financial instrument.

[a] Credit risk is the risk of an unexpected loss if a customer or third party to a financial instrument fails to meet its contractual obligations. Cash is composed of financial instruments issued primarily by large Canadian financial institutions. The Company's receivables consist primarily of amounts due from one reputable customer in relation to store closure services.

[b] Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in the market prices and is comprised primarily of interest rate risk for the Company. Interest rate risk arises because of changes in market interest rates. The Company's bank indebtedness is subject to risk of changes in cash flow due to its variable rate nature. The impact of a 50 basis point increase in the bank's prime rate throughout the quarter would have increased the loss for the 13 weeks ended July 6, 2008 by \$16.

[c] Liquidity risk is the risk that the Company will not be able to meet its obligations associated with financial liabilities as they fall due. The Company's borrowing policy is to acquire the liquidity necessary to settle other financial liabilities as they mature. Accounts payable and accrued liabilities are all current.

[d] Foreign exchange risk arises because the amount of the local payable for transactions denominated in foreign currencies may vary due to changes in exchange rates ("transaction exposures") and because the non-Canadian dollar denominated financial statements of the Company may vary on revaluation into the Canadian dollar reporting currency ("translation exposures"). The Company's exposure relates to the fact that a significant portion of its inventory purchases is transacted in U.S. dollars. As a result, the Company may experience transaction and translation exposures because of the volatility in the exchange rate between the U.S. dollar and the Canadian dollar. Based on the Company's U.S. dollar denominated purchases from continuing operations in Q3 2008, fluctuations of +/- 1% would have an effect on the loss from continuing operations before income taxes of approximately \$100.

[e] Financing risk is the risk that the Company's bank credit facility may be removed or reduced by the bank. The Company is currently negotiating a long-term asset-based loan facility with its bank to replace the current demand credit facility. This new facility is expected to be completed in the fourth quarter.

**9. Bank Indebtedness**

The Company has a bank credit facility with a Canadian chartered bank in the amount of \$20,000, subject to margining limits on accounts receivable and inventory, bearing interest at the bank's rate plus 300 basis points.

# Corporate Information

## DIRECTORS

### ***Craig Graham, Chairman***

Craig is currently a director and investor in a number of companies including Executive Risk Services Limited, Norsim Equipment Limited, and Twenty First Century Investments Inc. Mr. Graham is also a trustee of Specialty Food Income Fund.

### ***Jonathan Hill, President and CEO***

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

### ***Eric Beutel***

Eric is a Director, Vice President and Secretary of Oakwest Corporation Limited, a private investment company in Toronto. Mr. Beutel also sits on the Board of Directors and Investment Committee of The Equitable Group, a TSX listed company.

### ***Jeffrey Mandel***

Jeffrey is the President of AMR Securities Services Inc. and Vice President, Israel Opportunity Inc. He also is a director of Mitec Telecom (TSX), Goldbard Capital (TSXV) and privately owned companies Tiltan Pharma and Datex Billing Services Inc.

### ***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.

Ken Wightman, CA, SVP Finance and CFO

Mark Vella, Director Operations

Carol Ryan, Director Merchandising

## SOLICITORS

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## BANK

Royal Bank of Canada

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## AUDITORS

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# Outlet Locations

## BRITISH COLUMBIA

Abbotsford  
Aldergrove  
Campbell River  
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  
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  
St. Stephen, NB  
Truro, NS

## US

Spokane, WA  
Richland, WA  
Renton, WA