

ANNUAL REPORT  
FOR THE 52-WEEK PERIOD ENDED MARCH 29, 2014

“We are what we  
repeatedly do.  
Excellence, then,  
is not an act,  
but a habit.”

— *Aristotle*

**Indigo**  
Enrich your life™

Indigo Chapters Coles [indigo.ca](http://indigo.ca)

## The Indigo Mission

To provide our customers with the most inspiring  
retail and digital environments in the world for books  
and life-enriching products and experiences.

Indigo operates under the following banners:

*Indigo Books & Music, Chapters, Coles, SmithBooks, Indigospirit,  
The Book Company, and indigo.ca.*

The Company employs approximately 6,200 people across the country.

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# Report of the CEO

## Dear Shareholder,

In this note last year, I confirmed that we were in the early stages of a journey that is taking us from our position as Canada's leading bookseller to our vision of becoming the world's first cultural department store. 2013/14 was the year in which we made a very meaningful financial commitment to accelerate our transformation, positioning ourselves for real growth in the years ahead.

Over the course of this year we launched 37 Indigotech™ shops and meaningfully enhanced the lifestyle merchandising in almost all of our large format stores. At the same time, we made effective advances in the merchandising of our book experience reinforcing our commitment to booklovers, writers and publishers who are, without doubt, at the very core of our business.

This was also the year in which we focused investment on the digital side of our business, expanding our digital marketing and merchandising capabilities and launching a five-star rated mobile app.

Finally, just after the end of the year, we launched our first two American Girl® shops within IndigoKids, reinforcing our commitment to being the leading specialty kids' book and toy retailer in the country.

Contrary to last year, when we had the benefit of the biggest blockbuster in book history as well as some very strong performing titles, this year was one in which we had no single breakout book. We also experienced some important learning curves in our lifestyle business which impacted margin in the second half of the year.

The combination of the very significant operating investments, the pressure on margin, and some non-cash accounting requirements impacting us, result in a challenged bottom line.

I want to highlight that we are focused and committed to returning to full growth and profitability; that said, I am fully convinced that both the decisions we made and the learning in the Company are key ingredients to achieve these objectives.

In a time of industry transformation, investing to reposition is the key to success. It is also satisfying to know that as we invest in our future, we have the strength on our balance sheet to comfortably support our efforts. Even with these significant operating investments Indigo remains in a very healthy financial position.

As the year came to a close and even more so now that we are into our new year — there are several key indicators that our strategy is gaining real traction. For the first time since the advent of eReading we are seeing growth in our core book business — and not driven by a big hit but rather by efforts from our book team to create a great experience for readers both in our stores and online. We are also seeing growth in every one of our lifestyle categories (gift, paper and toys) both in sales and in margin. It is truly energizing to see our customers responding so well to what we are doing.

That said, going through a transformation is no easy task. It requires a clear vision, tenacity, incredible dedication from everyone on the team, and the willingness to take risks, make mistakes, course correct and push forward. We are totally up to the challenge.

We have a clear path forward and firm conviction that we are on the right track – one which will see Indigo grow customer affection and deliver meaningfully to both our shareholders and our employees.

As always, we have, over the course of the year, continued to support the tremendous work of the Indigo Love of Reading Foundation. This year brings to over \$15.5 million the amount we have invested in high needs schools across Canada. This is a very special initiative for us – and for those we touch. It is work in which we take great pride and to which we remain fully committed. I want to thank our customers who directly, and through their support of us, allow us to change forever the lives of the children we touch.

In closing, I want to take this opportunity to thank everyone on our team for the creativity and tremendous effort which you bring to work every day. I also want to thank our Directors and Shareholders for their continued support.

I look forward to reporting on our progress quarter-over-quarter and in this Letter next year.

A handwritten signature in black ink that reads "Heather Reisman". The script is fluid and cursive, with the first letters of "Heather" and "Reisman" being capitalized and prominent.

**Heather Reisman**

*Chair and Chief Executive Officer*

# Management's Responsibility for Financial Reporting

Management of Indigo Books & Music Inc. ("Indigo") is responsible for the preparation and integrity of the consolidated financial statements as well as the information contained in this report. The following consolidated financial statements of Indigo have been prepared in accordance with International Financial Reporting Standards, which involve management's best judgments and estimates based on available information.

Indigo's accounting procedures and related systems of internal control are designed to provide reasonable assurance that its assets are safeguarded and its financial records are reliable. In recognizing that the Company is responsible for both the integrity and objectivity of the consolidated financial statements, management is satisfied that the consolidated financial statements have been prepared according to and within reasonable limits of materiality and that the financial information throughout this report is consistent with these consolidated financial statements.

Ernst & Young LLP, Chartered Accountants, Licensed Public Accountants, serve as Indigo's auditors. Ernst & Young's report on the accompanying consolidated financial statements follows. Their report outlines the extent of their examination as well as an opinion on the consolidated financial statements. The Board of Directors of Indigo, along with the management team, have reviewed and approved the consolidated financial statements and information contained within this report.



Heather Reisman  
*Chair and Chief Executive Officer*



Kay Brekken  
*Chief Financial Officer*

# Management's Discussion and Analysis

The following Management's Discussion and Analysis ("MD&A") is prepared as at May 27, 2014 and is based primarily on the consolidated financial statements of Indigo Books & Music Inc. (the "Company" or "Indigo") for the 52-week periods ended March 29, 2014 and March 30, 2013. The Company's consolidated financial statements and accompanying notes are reported in Canadian dollars and have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") using the accounting policies described therein.

This MD&A should be read in conjunction with the consolidated financial statements and accompanying notes contained in the attached Annual Report. The Annual Report and additional information about the Company, including the Annual Information Form, can be found on SEDAR at [www.sedar.com](http://www.sedar.com).

## Overview

Indigo is Canada's largest book, gift and specialty toy retailer, operating stores in all ten provinces and one territory in Canada and offering online sales through its *indigo.ca* website. As at March 29, 2014, the Company operated 95 superstores under the banners *Chapters*, *Indigo* and the *World's Biggest Bookstore* and 131 small format stores, under the banners *Coles*, *Indigo*, *Indigospirit*, *SmithBooks*, and *The Book Company*. Subsequent to year end, the Company closed the *World's Biggest Bookstore*. During fiscal 2014, the Company closed two superstores and three small format stores. There were no new stores opened in fiscal 2014. The Company also has a 50% interest in Calendar Club of Canada Limited Partnership ("Calendar Club"), which operates seasonal kiosks and year-round stores in shopping malls across Canada.

Indigo operates a separate registered charity under the name Indigo Love of Reading Foundation (the "Foundation"). The Foundation provides new books and learning material to high-needs elementary schools across the country through donations from Indigo, its customers, suppliers, and employees.

The weighted average number of common shares outstanding for fiscal 2014 was 25,601,260 as compared to 25,529,035 last year. As at May 27, 2014, the number of outstanding common shares was 25,299,089 with a book value of \$203.8 million. The number of common shares reserved for issuance under the employee stock option plan is 2,029,824 as at May 27, 2014. As at March 29, 2014, there were 1,676,150 stock options outstanding of which 245,900 were exercisable.

## General Development of the Business

It has been 17 years since Indigo launched its first superstore with a commitment to enriching Canadians' lives through books and complementary products. Much has changed since then in both the book industry and the larger retail landscape that serves Indigo's customers. The online channel has expanded dramatically, offering consumers an increased number of titles at a lower cost than a traditional physical bookstore along with a broad range of general merchandise. In addition, the digital and mobile channels have provided consumers with a completely new reading platform with instant accessibility, huge selection, and lower costs.

Indigo continues to be proactive in an industry that is undergoing dramatic change and is well underway to establishing itself as the world's first cultural department store, a digital and physical place inspired by and filled with books, ideas, beautifully designed products, and the creative people who make it all happen. As such, the Company remains committed to its transformational agenda and continues to invest in Indigo's brand and the customer experience which will position the Company for sustained growth. More specifically, the Company's priorities remain focused on advancing the core retail business through adapting its physical stores, improving productivity, driving employee engagement, and expanding the Company's online and digital presence.

Indigo's entry into the digital book market began with the launch of Shortcovers in February 2009 as a new digital destination offering online and mobile service with instant access to books, articles and blogs. In December 2009, Indigo transferred the net assets of Shortcovers to a new company, Kobo Inc. ("Kobo"). During fiscal 2011 and 2012, Kobo expanded to become a global digital book leader and subsequently, in January 2012, the Company sold all the outstanding shares of Kobo to Rakuten, Inc. Notwithstanding the sale, Indigo continues to maintain a strong relationship with Kobo, supporting the products, including eInk devices and tablets, and eReading services customers have come to love, and directly benefitting from the growth of the Canadian eReading market.

Indigo has a loyal customer base. In fiscal 2012, the Company made changes to the irewards program, its fee-based loyalty program, and launched the plum rewards program ("Plum"), a free points-based loyalty program. Previously, under the irewards program, discounts were only offered on books; however, with the program changes to both irewards and Plum, discounts and points are now offered on virtually all products in the stores. Combined, the irewards and Plum programs have a total of 6.7 million members. The success of these programs creates a rich understanding of the Company's customers as well as direct marketing and communication opportunities with Indigo's best customers.

The Company's key strategies over the last three years and going forward are outlined below.

### **Adapting Our Physical Stores**

To ensure that the offerings in Indigo's physical stores are rich and compelling, the Company continues to adjust and expand its product mix, underlining Indigo's commitment to becoming the premier year-round gifting destination in Canada. The Company's main growth categories are lifestyle, paper and toy sales. This has been achieved through a reduction in the floor space allotted to books, given the erosion of physical book sales, as well as Indigo's ability to carry fewer on-hand quantities of books as a result of a more timely and efficient replenishment process.

Indigo continues to adapt and improve its physical stores to support these growth categories. Retail stores and their display fixtures are continuously being renovated and refreshed as part of the Company's transformation. During fiscal 2014, Indigo launched 37 Indigotech™ shops inside select superstores to showcase an expanded offering of electronic products. Last year, the Company expanded its lifestyle and paper offerings, and Indigo continues to expand its assortment of toys and games with either dedicated toy sections or expanded toy offerings in all of its superstores. Subsequent to year end, the Company has begun launching American Girl® specialty boutiques inside select superstores. These locations mark the first international retail presence for the iconic brand and reinforce the Company's commitment to the importance of creative play for children.

The Company also remains committed to expanding its proprietary product development capability, which primarily includes home, paper merchandise, and fashion accessories. This initiative is part of the Company's focus on providing customers with increasingly meaningful and life-enriching merchandise while improving operating margins. To support this initiative, Indigo opened a new design office in New York in fiscal 2011 and a full line of proprietary merchandise developed by this team began appearing in stores in fiscal 2012.

### **Driving Productivity Improvement**

While a key focus of the Company's business is evolving to meet the emerging needs of customers, the Company is also focused on driving productivity improvements. The challenge for the Company is to continually look for innovative ways to drive costs down while improving what Indigo delivers to customers. In particular, over the last three years the Company has focused on implementing an integrated planning system to improve merchandise management and implementing supply chain productivity initiatives designed to further reduce costs, deliver improved operating margins, and improve service to customers.

In fiscal 2014, the Company implemented an integrated planning system to improve the merchandise and financial planning for all its categories. The new integrated planning system simplifies and eliminates manual work associated with managing all categories. The Company also re-engineered all of its core general merchandising processes and streamlined employees into cross-functional category teams in order to align objectives, accelerate growth of key categories, and improve cross-functional collaboration.



In fiscal 2012, the Company upgraded its retail distribution facility to more efficiently support its retail stores. The project scope included replacing the warehouse management system and upgrading the material handling equipment. The completion of this project allowed the Company to handle the increased demands of the new growth categories while also sending more overall product through its distribution centres, thus improving overall margins.

During fiscal 2012, the Company also launched the Galileo project to identify productivity opportunities and initiatives. To date, under the umbrella of Galileo, the Company has implemented hundreds of initiatives that have improved operating efficiency while also enhancing employee and customer engagement. These initiatives support the continued investments in the Company's overall business transformation. One of the key Galileo projects in fiscal 2014 was systematically organizing retail store backrooms in order to drive retail productivity and improve merchandise management.

Going forward, the Company continues to target processes for re-engineering, cost rationalization, and improving customer value. Fiscal 2015 will focus on continuing to drive end-to-end productivity, including supply chain projects to improve the flow of merchandise and margin expansion initiatives.

### **Employee Engagement**

Indigo's strategic efforts continue to focus on building and maintaining high levels of employee engagement. In fiscal 2014, the Company conducted an employee engagement survey which showed year-over-year increases in engagement. In May 2014, Indigo's employee engagement focus was also recognized outside of the Company, with Indigo being named as the top Canadian retail employer brand by Randstad Canada for the second year in a row. The award is based on the polling of job seekers in search of employment opportunities in Canada's leading organizations.

The Company realizes that sustaining high levels of employee engagement is an ongoing responsibility and continues to commit resources to specific initiatives designed to make Indigo one of the best places to work. Efforts to boost employee satisfaction include the continuous improvement of core work process design and the implementation of systems upgrades; improvements to communication, training and development, and performance management are also ongoing. In fiscal 2014, the Company's employee engagement efforts focused on improving the core work processes, tools and structure of Indigo's general merchandising teams. During fiscal 2014, the Company also launched a new training module to all new and seasonal store staff to accelerate sales and service capabilities.

In addition to identifying productivity opportunities, the Galileo project, discussed above, also drives employee engagement by empowering all employees to participate in improving the customer and employee experiences. All employees can interact with the internal Galileo social media platform. This platform is designed to capture and cultivate innovation by providing the opportunity for employees to submit, review, vote, and comment on ideas for improving the employee and customer experiences. The Galileo project and the social media platform have been embraced by employees, and project successes are recognized and celebrated internally. Based on employee feedback, improvements to the Galileo processes and social media platform were implemented in fiscal 2014 and will continue to be implemented going forward.

### **Online Development and Redesign**

Reshaping Indigo's physical store offerings means the online store must also continue to adapt and change. The website redesign completed at the end of fiscal 2013 included much richer visual presentations of lifestyle, paper and toy categories, a simplified checkout experience, a much enhanced mobile experience, a comprehensive gift finder, and an innovative drag and drop capability to ease online shopping. Social media integration, including Facebook, Pinterest, and Twitter, also remain a priority.

To further improve the online customer experience, Indigo launched "buy online, ship to store" in fiscal 2013, an initiative that allows customers to buy products online and have the items shipped to one of our stores for free. This service provides customers with additional flexibility to decide where and when purchases are picked up and reduces Indigo's shipping costs.

In fiscal 2014, the Company launched a new mobile application for the iOS and Android platforms to offer a truly integrated and rich experience across Indigo's retail and online channels. Customers can use the mobile application to shop-on-the-go by making purchases online or to check retail inventory prior to visiting a store. Additionally, the application allows customers to scan a product barcode in-store, purchase the product online, and have it shipped to the location of their choice.

Personalization is also a key feature of the application, allowing users to create wish lists and access their plum rewards data. Going forward, the Company will continue to focus on increasing integration across its channels to provide a rich omni-channel shopping experience.

## Results of Operations

The following three tables summarize selected financial and operational information for the Company for the periods indicated. The classification of financial information presented below is specific to Indigo and may not be comparable to that of other retailers. The selected financial information is derived from the audited consolidated financial statements for the 52-week periods ended March 29, 2014, March 30, 2013, and March 31, 2012.

Key elements of the consolidated statements of earnings (loss) and comprehensive earnings (loss) for the periods indicated are shown in the following table:

| (millions of Canadian dollars)             | 52-week<br>period ended<br>March 29,<br>2014 | %<br>Revenues | 52-week<br>period ended<br>March 30,<br>2013 | %<br>Revenues |
|--------------------------------------------|----------------------------------------------|---------------|----------------------------------------------|---------------|
| Revenues                                   | 867.7                                        | 100.0         | 878.8                                        | 100.0         |
| Cost of sales                              | (494.0)                                      | 56.9          | (495.1)                                      | 56.3          |
| Cost of operations                         | (280.2)                                      | 32.3          | (273.7)                                      | 31.1          |
| Selling, administrative and other expenses | (93.4)                                       | 10.8          | (81.5)                                       | 9.3           |
| <b>Adjusted EBITDA<sup>1</sup></b>         | <b>0.1</b>                                   | <b>0.0</b>    | <b>28.5</b>                                  | <b>3.2</b>    |

1 Earnings before interest, taxes, depreciation, amortization, impairment, and equity investment. Also see "Non-IFRS Financial Measures".

Selected financial information of the Company for the last three fiscal years is shown in the following table:

| (thousands of Canadian dollars, except per share data)                                                      | 52-week<br>period ended<br>March 29,<br>2014 | 52-week<br>period ended<br>March 30,<br>2013 | 52-week<br>period ended<br>March 31,<br>2012 |
|-------------------------------------------------------------------------------------------------------------|----------------------------------------------|----------------------------------------------|----------------------------------------------|
| <b>Revenues</b>                                                                                             |                                              |                                              |                                              |
| Superstores                                                                                                 | 617,791                                      | 626,628                                      | 656,530                                      |
| Small format stores                                                                                         | 127,388                                      | 137,642                                      | 145,247                                      |
| Online (including store kiosks)                                                                             | 102,016                                      | 91,907                                       | 91,279                                       |
| Other                                                                                                       | 20,473                                       | 22,608                                       | 27,093                                       |
|                                                                                                             | <b>867,668</b>                               | <b>878,785</b>                               | <b>920,149</b>                               |
| Earnings (loss) and comprehensive earnings (loss)<br>for the period from continuing operations <sup>1</sup> | (30,999)                                     | 4,288                                        | (27,827)                                     |
| Net earnings (loss) and comprehensive earnings (loss)<br>for the period                                     | (30,999)                                     | 4,288                                        | 66,189                                       |
| Total assets                                                                                                | 512,588                                      | 569,140                                      | 591,752                                      |
| Long-term debt (including current portion)                                                                  | 811                                          | 1,478                                        | 2,201                                        |
| Working capital                                                                                             | 189,696                                      | 224,343                                      | 223,701                                      |
| Basic earnings (loss) per share from continuing operations <sup>1</sup>                                     | \$(1.21)                                     | \$0.17                                       | \$(1.10)                                     |
| Basic earnings (loss) per share                                                                             | \$(1.21)                                     | \$0.17                                       | \$3.68                                       |
| Diluted earnings (loss) per share                                                                           | \$(1.21)                                     | \$0.17                                       | \$3.64                                       |

1 Excludes Kobo discontinued operations.

Selected operating information of the Company for the last three fiscal years is shown in the following table:

|                                                          | 52-week<br>period ended<br>March 29,<br>2014 | 52-week<br>period ended<br>March 30,<br>2013 | 52-week<br>period ended<br>March 31,<br>2012 |
|----------------------------------------------------------|----------------------------------------------|----------------------------------------------|----------------------------------------------|
| <b>Comparable Store Sales<sup>1</sup></b>                |                                              |                                              |                                              |
| Superstores                                              | (0.9%)                                       | (4.6%)                                       | (1.9%)                                       |
| Small format stores                                      | (5.0%)                                       | (2.4%)                                       | (0.8%)                                       |
| <b>Stores Opened</b>                                     |                                              |                                              |                                              |
| Superstores                                              | —                                            | —                                            | —                                            |
| Small format stores                                      | —                                            | —                                            | —                                            |
|                                                          | —                                            | —                                            | —                                            |
| <b>Stores Closed</b>                                     |                                              |                                              |                                              |
| Superstores                                              | 2                                            | —                                            | —                                            |
| Small format stores                                      | 3                                            | 9                                            | 7                                            |
|                                                          | 5                                            | 9                                            | 7                                            |
| <b>Number of Stores Open at Year-End</b>                 |                                              |                                              |                                              |
| Superstores                                              | 95                                           | 97                                           | 97                                           |
| Small format stores                                      | 131                                          | 134                                          | 143                                          |
|                                                          | 226                                          | 231                                          | 240                                          |
| <b>Selling Square Footage at Year-End</b> (in thousands) |                                              |                                              |                                              |
| Superstores                                              | 2,200                                        | 2,235                                        | 2,235                                        |
| Small format stores                                      | 370                                          | 379                                          | 400                                          |
|                                                          | 2,570                                        | 2,614                                        | 2,635                                        |

1 See "Non-IFRS Financial Measures".

## Revenue Decreased

Total consolidated revenues for the 52-week period ended March 29, 2014 decreased \$11.1 million or 1.3% to \$867.7 million from \$878.8 million for the 52-week period ended March 30, 2013. The decrease was driven by declining book and eReader sales, higher sales discounts, reduced loyalty card sales, and the Company operating five fewer stores than last year. The decrease was partially offset by double-digit growth in lifestyle, paper, and toy sales along with continued growth in online sales. Book sales decreased mainly due to the phenomenal success of the *Fifty Shades* and *Hunger Games* trilogies in the prior year. Excluding the impact of these blockbuster titles, total consolidated revenues increased by 1.3% compared to last year.

Comparable store sales for the fiscal year decreased 0.9% in superstores and 5.0% in small format stores. The decrease was mainly driven by the reasons mentioned above. Excluding the blockbuster titles, comparable store sales increased 1.3% in superstores and 0.4% in small format stores. Comparable store sales are defined as sales generated by stores that have been open for more than 12 months on a 52-week basis. It is a key performance indicator for the Company as this measure excludes sales fluctuations due to store closings, permanent relocation, and chain expansion. As at March 29, 2014, the Company operated two fewer superstores and three fewer small format stores compared to March 30, 2013.

Online sales increased by \$10.1 million or 11.0% to \$102.0 million for the 52-week period ended March 29, 2014 compared to \$91.9 million last year. Although in-store physical book sales have declined, online book sales continue to increase as more customers purchase books online instead of in-store. Additionally, online sales of lifestyle, paper, and toy products continue to grow, benefiting from the Company's investments in growing its online customer base and from IT enhancements, such as the website redesign launched at the end of the last fiscal year and the launch of the mobile application in fiscal 2014.

Revenues from other sources include revenues generated through irewards card sales, revenue from unredeemed gift cards (“gift card breakage”), revenue from unredeemed plum points (“Plum breakage”), and revenue-sharing with Kobo. Revenues from other sources decreased \$2.2 million or 9.7% to \$20.5 million for the 52-week period ended March 29, 2014 compared to \$22.7 million last year primarily as a result of lower irewards membership income. irewards card sales have decreased by \$2.4 million compared to last year. This decrease is consistent with the Company’s expectations as members moved to the free plum rewards program. As more members participate in Plum and earn more points, the Company recognizes increased revenue from Plum breakage. The reduction in irewards revenue has been partially offset by higher revenues earned from Plum breakage. Plum breakage revenue increased by \$0.7 million compared to last year.

Revenues by channel are highlighted below:

| (millions of Canadian dollars)  | 52-week<br>period ended<br>March 29,<br>2014 | 52-week<br>period ended<br>March 30,<br>2013 | % increase<br>(decrease) | Comparable<br>store sales<br>% increase<br>(decrease) |
|---------------------------------|----------------------------------------------|----------------------------------------------|--------------------------|-------------------------------------------------------|
| Superstores                     | 617.8                                        | 626.6                                        | (1.4)                    | (0.9)                                                 |
| Small format stores             | 127.4                                        | 137.6                                        | (7.4)                    | (5.0)                                                 |
| Online (including store kiosks) | 102.0                                        | 91.9                                         | 11.0                     | N/A                                                   |
| Other                           | 20.5                                         | 22.7                                         | (9.7)                    | N/A                                                   |
|                                 | 867.7                                        | 878.8                                        | (1.3)                    | (1.6)                                                 |

Revenues by product line are as follows:

|                                  | 52-week<br>period ended<br>March 29,<br>2014 | 52-week<br>period ended<br>March 30,<br>2013 |
|----------------------------------|----------------------------------------------|----------------------------------------------|
| Print <sup>1</sup>               | 67.4%                                        | 69.8%                                        |
| General merchandise <sup>2</sup> | 27.7%                                        | 23.6%                                        |
| eReading <sup>3</sup>            | 2.9%                                         | 4.1%                                         |
| Other <sup>4</sup>               | 2.0%                                         | 2.5%                                         |
| Total                            | 100.0%                                       | 100.0%                                       |

1 Includes books, calendars, magazines, and newspapers.

2 Includes lifestyle, paper, toys, music, DVDs, and electronics.

3 Includes eReaders, eReader accessories, and Kobo revenue share.

4 Includes cafés, irewards, gift card breakage, and Plum breakage.

A reconciliation between total revenues and comparable store sales is provided below:

|                                                      | Superstores                                  |                                              | Small format stores                          |                                              |
|------------------------------------------------------|----------------------------------------------|----------------------------------------------|----------------------------------------------|----------------------------------------------|
| (millions of Canadian dollars)                       | 52-week<br>period ended<br>March 29,<br>2014 | 52-week<br>period ended<br>March 30,<br>2013 | 52-week<br>period ended<br>March 29,<br>2014 | 52-week<br>period ended<br>March 30,<br>2013 |
| Total revenues                                       | 617.8                                        | 626.6                                        | 127.4                                        | 137.6                                        |
| Adjustments for stores not in<br>both fiscal periods | (1.1)                                        | (4.3)                                        | (1.3)                                        | (4.9)                                        |
| <b>Comparable store sales</b>                        | <b>616.7</b>                                 | <b>622.3</b>                                 | <b>126.1</b>                                 | <b>132.7</b>                                 |

### **Cost of Sales (as a Percent of Revenues) Remained Flat**

Cost of sales includes the landed cost of goods sold, online shipping costs, inventory shrink and damage reserve, less all vendor support programs. Cost of sales decreased \$1.1 million to \$494.0 million, compared to \$495.1 million last year. The decrease was driven by lower retail sales volumes, as discussed above. This decrease was partially offset by a \$1.6 million increase in vendor support. Cost of sales as a percent of total revenues increased by 0.6% to 56.9%, compared to 56.3% last year. The percentage increase was mainly due to increased discounting and higher markdowns to clear seasonal merchandise.

### **Cost of Operations Increased Over Last Year**

Cost of operations includes all store, online, and distribution centre costs. Cost of operations increased \$6.5 million to \$280.2 million this year, compared to \$273.7 million last year. As a percent of total revenues, cost of operations increased by 1.2% to 32.3% this year, compared to 31.1% last year. The increase was primarily driven by a \$4.8 million, or 25.8%, increase in online costs compared to last year. Higher online costs were driven by higher fulfilment costs resulting from the increase in online sales volumes, increased digital marketing spend to drive sales and continued growth of the Company's customer base, and technical improvements to the Company's website. Store occupancy costs were also \$2.2 million higher compared to last year as a result of contractual increases in leasing costs.

### **Selling, Administrative and Other Expenses Increased Compared to Last Year**

Selling, administrative and other expenses include retail marketing, head office costs, and operating expenses associated with the Company's transformation. These expenses increased \$11.9 million to \$93.4 million, compared to \$81.5 million last year. Expenses increased as the Company continued its transformational journey by investing in all areas of home office. Specifically, the Company made operating investments in expanding merchandising space within its existing superstores to support growth categories, in launching its new Indigotech™ business and in exiting certain businesses, in marketing to drive consumer awareness of new products in key growth categories, and in additional talent to enhance its digital capabilities and to support the growth of the general merchandise categories. The Company also recognized higher severance costs due to a reorganization of its workforce during the fourth quarter. As a percent of total revenues, selling, administrative and other expenses increased by 1.5% to 10.8%, compared to 9.3% last year.

### **Adjusted EBITDA Decreased Versus Last Year**

Adjusted EBITDA, defined as earnings before interest, taxes, depreciation, amortization, impairment, and equity investment decreased \$28.4 million to \$0.1 million for the 52-week period ended March 29, 2014, compared to \$28.5 million for the 52-week period ended March 30, 2013. Adjusted EBITDA as a percent of revenues decreased 3.2% to 0.0% this year from 3.2% last year. The decrease was driven by lower book sales in the first half of the current fiscal year due to a lack of blockbuster titles compared to sales of the *Fifty Shades* and *Hunger Games* trilogies last year, along with higher current year expenses related to the Company's transformational strategy to become the premier year-round gifting destination in Canada

### **Depreciation, Amortization, and Asset Impairments Increased Compared to Last Year**

Depreciation and amortization for the 52-week period ended March 29, 2014 decreased by \$0.4 million to \$27.5 million compared to \$27.9 million last year. Capital expenditures in fiscal 2014 totalled \$29.3 million and included \$15.2 million for store construction, renovations and equipment, \$10.5 million for intangible assets (primarily application software and internal development costs), and \$3.6 million for technology equipment. Of the \$3.6 million expenditure in technology equipment, \$0.1 million was financed through finance leases. The increase in capital expenditures in the current year was due to greater spending on capital projects as the Company continues to implement its transformation strategy.

The Company assesses at each reporting date whether there is any indication that capital assets may be impaired. The Company identified impairment and reversal indicators for certain cash-generating units (“CGUs”) and groups of CGUs. For capital assets which can be reasonably and consistently allocated to individual stores, the store level is used as the CGU. As a result of identifying impairment and reversal indicators, the Company performed testing which could result in the recognition and reversal of impairment losses. Recoverable amounts for CGUs being tested are based on value in use, which is calculated from discounted cash flow projections over the remaining lease terms, plus any renewal options where renewal is likely.

The Company had \$2.6 million of capital asset impairments and no capital asset impairment reversals during fiscal 2014. Last year, the Company recognized \$1.3 million in capital asset impairments and \$1.0 million in impairment reversals. For both years, impairment losses arose due to stores performing at lower-than-expected profitability and impairment reversals arose due to improved store performance and the likelihood of lease term renewals. All of the impairment losses and reversals were spread across a number of CGUs at the store level.

#### **Net Interest Income Remained Flat**

The Company recognized net interest income of \$2.3 million this year compared to \$2.5 million last year. The Company nets interest income against interest expense.

#### **Earnings from Equity Investment Decreased**

The Company uses the equity method to account for its investment in Calendar Club and recognizes its share of Calendar Club’s earnings and losses as part of consolidated net earnings and losses. Indigo recognized net earnings from Calendar Club of \$0.8 million this year compared to net earnings of \$1.3 million last year. Total sales remained nearly flat to last year, but Calendar Club operated 16 additional kiosks in fiscal 2014, which increased operating costs. In addition, Calendar Club had less favourable locations in premier malls this year, which impacted their earnings.

#### **Income Tax Expense Increased Due to Valuation Allowance**

The Company recognized income tax expense of \$4.1 million this year compared to an income tax recovery of \$0.1 million last year. The higher income tax expense was driven by an \$11.6 million valuation allowance recorded against deferred tax assets in fiscal 2014. The valuation allowance was determined under IAS 12, “Income Taxes,” based on management’s best estimate of future taxable income that the Company expects to achieve from reviewing its latest forecast. The time period used to determine the valuation allowance under IAS 12 was significantly shorter than the expiration period of the tax loss carryforwards. As such, the economic benefits of the deferred tax assets have not decreased, as management expects to fully utilize all deferred tax assets prior to expiry. The Company’s effective tax rate was (15.2)% this year compared to (2.3)% last year.

#### **Net Earnings Decreased from Last Year**

The Company recognized net loss of \$31.0 million for the 52-week period ended March 29, 2014 (\$1.21 net loss per common share), compared to net earnings of \$4.3 million (\$0.17 net earnings per common share) last year. As discussed above, the decrease was driven by lower revenues, increases in cost of operations and selling, administrative and other expenses, and higher income tax expense.

## Seasonality and Fourth Quarter Results

Indigo's business is highly seasonal and follows quarterly sales and profit (loss) fluctuation patterns, which are similar to those of other retailers that are highly dependent on the December holiday sales season. A disproportionate amount of revenues and profits are earned in the third quarter. As a result, quarterly performance is not necessarily indicative of the Company's performance for the rest of the year. The following table sets out revenues, net earnings (loss) attributable to shareholders of the Company, basic and diluted earnings (loss) per share for the preceding eight fiscal quarters.

| (thousands of Canadian dollars,<br>except per share data) | Fiscal quarters      |                      |                      |                      |                      |                      |                      |                      |
|-----------------------------------------------------------|----------------------|----------------------|----------------------|----------------------|----------------------|----------------------|----------------------|----------------------|
|                                                           | Q4<br>Fiscal<br>2014 | Q3<br>Fiscal<br>2014 | Q2<br>Fiscal<br>2014 | Q1<br>Fiscal<br>2014 | Q4<br>Fiscal<br>2013 | Q3<br>Fiscal<br>2013 | Q2<br>Fiscal<br>2013 | Q1<br>Fiscal<br>2013 |
| Revenues                                                  | 184,333              | 332,393              | 179,417              | 171,525              | 183,976              | 322,620              | 185,563              | 186,626              |
| Total net earnings (loss)                                 | (14,378)             | 8,497                | (10,070)             | (15,048)             | (8,247)              | 22,035               | (4,013)              | (5,487)              |
| Basic earnings (loss) per share                           | \$(0.56)             | \$0.33               | \$(0.39)             | \$(0.59)             | \$(0.32)             | \$0.86               | \$(0.16)             | \$(0.22)             |
| Diluted earnings (loss) per share                         | \$(0.56)             | \$0.33               | \$(0.39)             | \$(0.59)             | \$(0.32)             | \$0.86               | \$(0.16)             | \$(0.22)             |

The Company saw an improvement in consolidated revenues in the fourth quarter of fiscal 2014 against last year due to strong growth in online revenue. Revenues increased by \$0.3 million to \$184.3 million compared to \$184.0 million in the same quarter last year. Online sales increased by \$2.8 million, or 13.1%, to \$24.1 million compared to \$21.3 million in the same quarter last year. Comparable store sales increased 1.4% in superstores and decreased 3.1% in small format stores.

Net loss in the fourth quarter of fiscal 2014 was \$14.4 million compared to a loss of \$8.2 million in the same quarter last year. Although fourth quarter revenues increased by \$0.3 million compared to the same period last year, the Company collected \$1.1 million less vendor support and cost of operations and selling, administrative and other expenses increased \$3.9 million. As previously discussed, the higher expenses were primarily driven by investments made in relation to the Company's ongoing transformational strategy.

## Overview of Consolidated Balance Sheets

### Total Assets

As at March 29, 2014, total assets decreased \$56.5 million to \$512.6 million, compared to \$569.1 million as at March 30, 2013. The decrease was primarily due to a \$53.0 million decrease in cash and cash equivalents. The Company used its cash to make significant investments in capital assets and working capital as part of its transformation strategy. Capital asset purchases in fiscal 2014 totalled \$29.3 million compared to \$19.1 million last year as the Company made significant investments in store renovations and updated information systems as part of its transformation strategy. The Company also used \$19.2 million of cash towards working capital in the current year compared to generating \$1.1 million of cash from working capital last year. The Company's changing product assortment now includes more items with shorter payment terms, which drove the increased use of cash towards working capital.

### Total Liabilities

As at March 29, 2014, total liabilities decreased \$17.9 million to \$200.9 million, compared to \$218.8 million as at March 30, 2013. The decrease was primarily the result of a \$14.9 million decrease in current and long-term accounts payable and accrued liabilities. As discussed above, the Company's changing product assortment now includes more items with shorter payment terms, which drove the decrease in current and long-term accounts payable and accrued liabilities. Changes to the Company's product assortment is a significant component of the Company's transformation strategy.



## Total Equity

Total equity at March 29, 2014 decreased \$38.6 million to \$311.7 million, compared to \$350.3 million as at March 30, 2013. The decrease in total equity was primarily due to net loss of \$31.0 million and \$8.3 million of dividend payments. Share capital increased by less than \$0.1 million due to the exercise of stock options. Contributed surplus increased \$0.7 million as the expensing of employee stock options and Directors' deferred share units was partially offset by the Company's one-time options repurchase. In the first quarter of fiscal 2014, the Company offered a one-time cash repurchase to certain option holders. Unamortized expense related to repurchased options was immediately recognized and increased contributed surplus by \$0.5 million. The increase was offset by the \$1.0 million cash payment made to the option holders.

## Working Capital and Leverage

The Company reported working capital of \$189.7 million as at March 29, 2014, compared to \$224.3 million as at March 30, 2013. The decrease was driven by the \$53.0 million decrease in cash and cash equivalents discussed above, as the Company had significant expenditures related to its transformation strategy.

The Company's leverage position (defined as Total Liabilities to Total Equity) remained flat at 0.6:1 year-over-year as both total liabilities and total equity decreased by a similar percentage.

## Overview of Consolidated Statements of Cash Flows

Cash and cash equivalents decreased \$53.0 million during fiscal 2014 compared to an increase of \$3.8 million last year. The decrease in fiscal 2014 was driven by cash flows used in operating activities of \$17.3 million, investing activities of \$25.6 million, financing activities of \$10.2 million, and the effect of foreign currency exchange rate changes on cash and cash equivalents of \$0.1 million.

## Cash Flows from Operating Activities

The Company used cash flows of \$17.3 million from operating activities in fiscal 2014 compared to generating \$30.4 million last year, a decrease of \$47.7 million. The Company used \$19.2 million of cash for working capital this year compared to generating \$1.1 million of cash from working capital last year and had a net loss of \$31.0 million this year compared to net earnings of \$4.3 million last year. The Company also had \$2.6 million of capital asset impairments in the current year compared to \$0.3 million last year. For both years, impairment losses arose due to stores performing at lower-than-expected profitability.

## Cash Flows from Investing Activities

Total cash spent on capital projects in fiscal 2014 was \$29.2 million compared to \$19.1 million spent last year, as outlined below:

| (millions of Canadian dollars)                                                       | 52-week<br>period ended<br>March 29,<br>2014 | 52-week<br>period ended<br>March 30,<br>2013 |
|--------------------------------------------------------------------------------------|----------------------------------------------|----------------------------------------------|
| Store construction, renovations and equipment                                        | 15.2                                         | 7.1                                          |
| Intangible assets (primarily application software<br>and internal development costs) | 10.5                                         | 9.6                                          |
| Technology equipment                                                                 | 3.5                                          | 2.4                                          |
|                                                                                      | 29.2                                         | 19.1                                         |

The Company used cash flows of \$25.6 million for investing activities in fiscal 2014 compared to \$15.1 million used by investing activities last year, an increase of \$10.5 million. The increase was due to greater spending on capital projects as the Company continues to implement its transformation strategy. Distributions from the equity investment in Calendar Club were \$1.2 million in the current year compared to \$1.3 million last year. The Company also received \$2.5 million of interest in the current year compared to \$2.7 million last year.



## Cash Flows from Financing Activities

The Company used cash flows of \$10.2 million for financing activities in fiscal 2014 compared to using \$12.0 million last year, a decrease of \$1.8 million. The Company paid \$8.3 million of dividend payments in fiscal 2014 compared to \$11.1 million of dividend payments last year. The decrease in dividend payments resulted from the suspension of quarterly dividend payments beyond December 3, 2013. This decrease was partially offset by an increased use of cash in fiscal 2014 as a result of the Company's options repurchase, as previously discussed. The cash payment for the options repurchase was \$1.0 million.

## Liquidity and Capital Resources

The Company has a highly seasonal business which generates the majority of its revenues and cash flows during the December holiday season. Indigo has minimal accounts receivable and a significant portion of book products are purchased on trade terms with the right to return. Indigo's main sources of capital are cash flows generated from operations, long-term debt, and cash and cash equivalents.

The Company's contractual obligations due over the next five years are summarized below:

| (millions of Canadian dollars) | Less than 1 year | 1-3 years | 4-5 years | After 5 years | Total |
|--------------------------------|------------------|-----------|-----------|---------------|-------|
| Operating leases               | 57.6             | 89.7      | 51.6      | 6.9           | 205.8 |
| Finance lease obligations      | 0.6              | 0.2       | —         | —             | 0.8   |
| Total obligations              | 58.2             | 89.9      | 51.6      | 6.9           | 206.6 |

Based on the Company's liquidity position and cash flow forecast, management expects its current cash position and cash flows generated from operations to be sufficient to meet its working capital needs and debt service requirements for fiscal 2015. As a result, the Company cancelled its revolving line of credit on June 12, 2013. In addition, Indigo has the ability to reduce capital spending to fund debt requirements if necessary; however, a long-term decline in capital expenditures may negatively impact revenues and profit growth. In order to maintain sufficient capital resources to fund the Company's transformation, management and the Company's Board of Directors decided to suspend quarterly dividend payments beyond December 3, 2013. Future declaration of quarterly dividends and the establishment of future record and payment dates are subject to the final determination of the Company's Board of Directors.

There can be no assurance that operating levels will not deteriorate over the ensuing fiscal year, which could result in the Company being unable to meet its current working capital and debt service requirements. In addition, other factors not presently known to management could materially and adversely affect Indigo's future cash flows. In such events, the Company would be required to obtain additional capital as is necessary to satisfy its working capital and debt service requirements from other sources. Alternative sources of capital could result in increased dilution to shareholders and may be on terms that are not favourable to the Company.

## Accounting Policies

### Critical Accounting Judgments and Estimates

The discussion and analysis of Indigo's operations and financial condition are based upon the consolidated financial statements, which have been prepared in accordance with IFRS. The preparation of the consolidated financial statements in conformity with IFRS requires the Company to use judgment and estimation to assess the effects of several variables that are inherently uncertain. These judgments and estimates can affect the reported amounts of assets, liabilities, revenues, and expenses. The Company bases its judgments and estimates on historical experience and other assumptions which management believes to be reasonable under the circumstances. The Company also evaluates its judgments and estimates on an ongoing basis. Methods for determining all material judgments and estimates are consistent with those used in prior periods. The critical accounting judgments and estimates and significant accounting policies of the Company are described in notes 3 and 4 of the consolidated financial statements.

The following items in the consolidated financial statements involve significant judgment or estimation.

#### Use of judgment

The preparation of the consolidated financial statements in conformity with IFRS requires the Company to make judgments, apart from those involving estimation, in applying accounting policies that affect the recognition and measurement of assets, liabilities, revenues, and expenses. Actual results may differ from the judgments made by the Company. Information about judgments that have the most significant effect on recognition and measurement of assets, liabilities, revenues, and expenses are discussed below. Information about significant estimates is discussed in the following section.

#### *Impairment*

An impairment loss is recognized for the amount by which the carrying amount of an asset or a cash-generating unit (“CGU”) exceeds its recoverable amount. The Company uses judgment when identifying CGUs and when assessing for indicators of impairment.

#### *Intangible assets*

Initial capitalization of intangible asset costs is based on the Company’s judgment that technological and economic feasibility are confirmed and the project will generate future economic benefits by way of estimated future discounted cash flows that are being generated.

#### *Leases*

The Company uses judgment in determining whether a lease qualifies as a finance lease arrangement that transfers substantially all the risks and rewards incidental to ownership.

#### *Deferred tax assets*

The recognition of deferred tax assets is based on the Company’s judgment. The assessment of the probability of future taxable income in which deferred tax assets can be utilized is based on management’s best estimate of future taxable income that the Company expects to achieve from reviewing its latest forecast. This estimate is adjusted for significant non-taxable income and expenses and for specific limits to the use of any unused tax loss or credit. Deferred tax assets are recognized to the extent that it is probable that taxable profit will be available against which the deductible temporary differences and the carryforward of unused tax credits and unused tax losses can be utilized. Any difference between the gross deferred tax asset and the amount recognized is recorded on the balance sheet as a valuation allowance. If the valuation allowance decreases as the result of subsequent events, the previously recognized valuation allowance will be reversed. The recognition of deferred tax assets that are subject to certain legal or economic limits or uncertainties are assessed individually by the Company based on the specific facts and circumstances.

#### Use of estimates

The preparation of the consolidated financial statements in conformity with IFRS requires the Company to make estimates and assumptions in applying accounting policies that affect the recognition and measurement of assets, liabilities, revenues, and expenses. Actual results may differ from the estimates made by the Company, and actual results will seldom equal estimates. Information about estimates that have the most significant effect on the recognition and measurement of assets, liabilities, revenues, and expenses are discussed below.

### *Revenues*

The Company recognizes revenue from gift card breakage if the likelihood of gift card redemption by the customer is considered to be remote. The Company estimates its average gift card breakage rate based on historical redemption rates. The resulting revenue is recognized over the estimated period of redemption based on historical redemption patterns commencing when the gift cards are sold.

The Indigo plum rewards program allows customers to earn points on their purchases. The fair value of Plum points is calculated by multiplying the number of points issued by the estimated cost per point. The estimated cost per point is based on many factors, including the expected future redemption patterns and associated costs. On an ongoing basis, the Company monitors trends in redemption patterns (redemption at each reward level), historical redemption rates (points redeemed as a percentage of points issued) and net cost per point redeemed, adjusting the estimated cost per point based upon expected future activity. Points revenue is included with total revenues in the Company's consolidated statements of earnings (loss) and comprehensive earnings (loss).

### *Inventories*

The future realization of the carrying amount of inventory is affected by future sales demand, inventory levels, and product quality. At each balance sheet date, the Company reviews its on-hand inventory and uses historical trends and current inventory mix to determine a reserve for the impact of future markdowns which will take the net realizable value of inventory on-hand below cost. Inventory valuation also incorporates a write-down to reflect future losses on the disposition of obsolete merchandise. The Company reduces inventory for estimated shrinkage that has occurred between physical inventory counts and the end of the fiscal year based on historical experience as a percentage of sales. In addition, the Company records a vendor settlement accrual to cover any disputes between the Company and its vendors. The Company estimates this reserve based on historical experience of settlements with its vendors.

### *Share-based payments*

The cost of equity-settled transactions with counterparties is based on the Company's estimate of the fair value of share-based instruments and the number of equity instruments that will eventually vest. The Company's estimated fair value of the share-based instruments is calculated using the following variables: risk-free interest rate; expected volatility; expected time until exercise; and expected dividend yield. Risk-free interest rate is based on Government of Canada bond yields, while all other variables are estimated based on the Company's historical experience with its share-based payments.

### *Impairment*

To determine the recoverable amount of an impaired asset, the Company estimates expected future cash flows at the CGU level and determines a suitable discount rate in order to calculate the present value of those cash flows. In the process of measuring expected future cash flows, the Company makes assumptions about future sales, gross margin rates, expenses, capital expenditures, and working capital investments which are based upon past and expected future performance. Determining the applicable discount rate involves estimating appropriate adjustments to market risk and to Company-specific risk factors.

### *Property, plant and equipment and intangible assets (collectively, "capital assets")*

Capital assets are depreciated over their useful lives, taking into account residual values where appropriate. Assessments of useful lives and residual values are performed annually and take into consideration factors such as technological innovation, maintenance programs, and relevant market information. In assessing residual values, the Company considers the remaining life of the asset, its projected disposal value, and future market conditions.

## Accounting Standards Implemented in Fiscal 2014

Adoption of these amendments and standards in fiscal 2014 impacted the Company's results of operations, financial position, and disclosures as follows:

- Joint Arrangements ("IFRS 11") replaces IAS 31, "Interests in Joint Ventures" ("IAS 31") and SIC-13, "Jointly-controlled Entities – Non-monetary Contributions by Venturers," and requires that a party in a joint arrangement assess its rights and obligations to determine the type of joint arrangement and account for those rights and obligations accordingly. Previously, the Company accounted for its interest in Calendar Club under IAS 31 using proportionate consolidation. However, the Company concluded that its interest in Calendar Club does not meet the definition of a joint arrangement under IFRS 11 and needs to be accounted for under "Investments in Associates and Joint Ventures" ("IAS 28") as a significant investment using the equity method. The Company has retrospectively restated its comparative financial statements to reclassify proportionately consolidated Calendar Club operating results into a single equity investment line. These restatements have no impact to the Company's total net earnings (loss) or cash flows. The impact of reclassification on the Company's financial statements is as follows:

| (thousands of Canadian dollars) | 52-week<br>period ended<br>March 30,<br>2013 |
|---------------------------------|----------------------------------------------|
| Decrease in revenues            | (15,272)                                     |
| Decrease in expenses            | (13,957)                                     |
| Increase in equity investment   | 1,315                                        |

| (thousands of Canadian dollars) | As at<br>March 30,<br>2013 | As at<br>April 1,<br>2012 |
|---------------------------------|----------------------------|---------------------------|
| Decrease in assets              | (2,074)                    | (1,746)                   |
| Increase in equity investment   | 968                        | 961                       |
| Decrease in liabilities         | (1,106)                    | (785)                     |

- Amendments to Investments in Associates and Joint Ventures ("IAS 28") impact accounting for associates and joint ventures held for sale and changes in interests held in associates and joint ventures; and
- Disclosure of Interests in Other Entities ("IFRS 12") includes all of the disclosures that were previously in IAS 27, "Separate Financial Statements," IAS 31 and IAS 28, "Investments in Associates." These disclosures relate to an entity's interests in subsidiaries, joint arrangements, associates, and structured entities.

Adoption of the following amendments and standards in fiscal 2014 did not have an impact on the Company's results of operations, financial position, or disclosures:

- Amendments to Presentation of Financial Statements ("IAS 1") require companies to group together items within other comprehensive earnings which may be reclassified to net earnings. The amendments are effective for annual periods beginning on or after July 1, 2012 and were applied retrospectively;
- Amendments to Financial Instruments: Disclosures ("IFRS 7") regarding the offsetting of financial instruments. These amendments were applied retrospectively and are effective for annual periods beginning on or after January 1, 2013 and interim periods within those annual periods;
- Fair Value Measurement ("IFRS 13") provides guidance to improve consistency and comparability in fair value measurements and related disclosures through a fair value hierarchy. This standard was applied prospectively and is effective for annual periods beginning on or after January 1, 2013;

- Amendments to Separate Financial Statements (“IAS 27”) remove all requirements relating to consolidated financial statements. This standard was applied retrospectively and is effective for annual periods beginning on or after January 1, 2013; and
- Consolidated Financial Statements (“IFRS 10”) replaces portions of IAS 27, “Consolidated and Separate Financial Statements,” supersedes SIC-12, “Consolidation – Special Purpose Entities,” and establishes standards for the presentation and preparation of consolidated financial statements when an entity controls one or more entities. This standard was applied retrospectively and is effective for annual periods beginning on or after January 1, 2013.

## New Accounting Pronouncements

### Impairment of Assets (“IAS 36”)

In May 2013, the IASB issued amendments to IAS 36 which require disclosures about assets or CGUs for which an impairment loss was recognized or reversed during the period. The Company will apply the amendments to IAS 36 as of the first quarter of its 2015 fiscal year. Additional information will be disclosed through notes to financial statements.

### Levies (“IFRIC 21”)

The IASB has issued IFRIC 21, an interpretation which provides guidance on when to recognize a liability for a levy imposed by a government, both for levies that are accounted for in accordance with IAS 37, “Provisions, Contingent Liabilities and Contingent Assets,” and those where the timing and amount of the levy is certain. A levy is an outflow of resources embodying economic benefits that is imposed by governments on entities in accordance with legislation. This interpretation is applicable for annual periods beginning on or after January 1, 2014 and must be applied retrospectively. The Company will apply these amendments beginning in the first quarter of fiscal 2015. The Company is assessing the impact of the new interpretation on its consolidated financial statements.

### Financial Instruments: Presentation (“IAS 32”)

The IASB has issued amendments to IAS 32 that clarify its requirements for offsetting financial instruments. These amendments must be applied retrospectively and are effective for annual periods beginning on or after January 1, 2014. The Company will apply these amendments beginning in the first quarter of fiscal 2015. The Company does not expect implementation of these amendments to have a significant impact on its consolidated financial statements.

### Financial Instruments (“IFRS 9”)

The IASB has issued a new standard, IFRS 9, which will ultimately replace IAS 39, “Financial Instruments: Recognition and Measurement” (“IAS 39”). The replacement of IAS 39 is a multi-phase project with the objective of improving and simplifying the reporting for financial instruments. Issuance of IFRS 9 provides guidance on the classification and measurement of financial assets and financial liabilities. Due to the incomplete status of the project, the mandatory effective date of this standard has not been determined. The Company will evaluate the overall impact on its consolidated financial statements when the final standard, including all phases, is issued.

## Risks and Uncertainties

### Competition

The retail book selling business is highly competitive and continues to experience fundamental changes. Specialty bookstores, independents, other book superstores, regional multi-store operators, supermarkets, drug stores, warehouse clubs, mail order clubs, Internet booksellers, mass merchandisers, and other retailers continue to sell and even expand physical book offerings, often at substantially discounted prices. The Canadian retail landscape is also changing as a growing number of international retailers launch Canadian operations. This increased competition may negatively impact the Company’s revenues and margins.

The digital book industry is also highly competitive and is continuing to grow. The number of retailers selling eBooks has increased, as have the number of retailers selling eReaders. The technology continues to change, with eReader technology widely available on tablets and mobile devices and new eReading devices being released with expanded capabilities. As the digital book industry continues to expand and change, increased eBook sales continue to negatively impact physical book sales. As eBooks are priced lower than physical books, consumers may reduce their future purchases of physical books in favour of eBooks, which could reduce the Company's revenues.

Aggressive merchandising or discounting by competitors in the retail, online, or digital sectors could reduce the Company's revenues, market share, and operating margins.

### **Company Transformation**

As customers shift spending toward eBooks, the Company continues to adjust its merchandise mix to grow general merchandise categories to offset the erosion of physical book sales and margins. The general merchandise retail landscape contains a significant amount of competition from established retailers and there can be no assurances that the Company will be able to gain market share. Furthermore, the Company's expansion into new markets and general merchandise could place a significant strain on Indigo's management, operations, technical performance, financial resources, and internal financial control and reporting functions. The Company will continue to change and modify this strategy and there can be no assurances that the Company's strategy will be successful.

### **Relationships with Suppliers**

The Company relies heavily on suppliers to provide book and general merchandise at appropriate margins and in accordance with agreed-upon terms and timelines. Failure to maintain favorable terms and relationships with suppliers, the absence of key suppliers, or delays in Indigo's ability to acquire books or merchandise on time may affect the Company's ability to compete in the marketplace. This is especially true as the Company continues to source a greater portion of its products from overseas, and events causing disruptions of imports, changes in restrictions, or currency fluctuations could negatively impact revenues and margins of the Company.

### **Inventory Management**

The Company must manage its inventory levels to successfully operate the business. Inability to respond to changing customer preferences may result in excess inventory which must be sold at lower prices, or an inventory shortage. Additionally, as a result of purchasing more general merchandise, the Company has an increasing amount of non-returnable inventory. The Company monitors the impact of customer trends on inventory turnover and obsolescence, but inappropriate inventory levels could negatively impact the Company's revenues and financial performance.

### **Product Quality and Product Safety**

The Company sells products produced by third party manufacturers. Some of these products may expose the Company to potential liabilities and costs associated with defective products, product handling, and product safety. These risks could expose the Company to product liability claims, damage the Company's reputation, and lead to product recalls. The Company has policies and controls in place to manage these risks, including providing third party manufacturers with product safety guidance and maintaining liability insurance.

As part of its growth in general merchandise, the Company sells food products and is subject to risks associated with food safety. A significant outbreak of food-borne illness or other public health concerns related to food products could result in harm to the Company's customers, negative publicity, and product liability claims. The Company has processes in place to identify risks, communicate to employees and consumers, and to ensure that potentially harmful products are not available for sale. The Company also applies quality management procedures to ensure it meets all food safety and regulatory requirements.

Although the Company has policies and procedures in place to manage these risks, liabilities and costs related to product quality and product safety may have a negative impact on the Company's revenues and financial performance.

## **Leases**

The average unexpired lease term of Indigo's superstores and small format stores is approximately 3.5 years and 2.1 years, respectively. The Company attempts to renew these leases as they come due on favourable terms and conditions, but is susceptible to volatility in the market for supercentre and shopping mall space. Unforeseen increases in occupancy costs, or costs incurred as a result of unanticipated store closing and relocation could unfavourably impact the Company's performance.

## **Technology and Online**

Information management and technology are key components to the ongoing competitiveness and daily operation of the business. If the Company's investment in technology fails to support our growth initiatives or to keep pace with technological changes, Indigo's competitiveness may be compromised. The Company has also increased its investment in developing improvements to the digital customer experience but there can be no assurances that the Company will be able to recoup its investment costs. Furthermore, if systems are damaged or cease to function properly, capital investment may be required and the Company may suffer business interruptions in the interim. Such systems and controls are pervasive throughout our business and failures in their maintenance or development could have a significant adverse effect on the business.

## **Cybersecurity**

A failure in, or breach of, the Company's operational or security systems or infrastructure, or those of Indigo's third party vendors and other service providers, including as a result of cyber attacks, could disrupt the business, result in the disclosure or misuse of confidential or proprietary information, damage Indigo's reputation, increase the Company's costs, and cause losses. Although Indigo has business continuity plans and other safeguards in place, along with robust information security procedures and controls, the Company's business operations may be adversely affected by significant and widespread disruption to Indigo's physical infrastructure or operating systems that support the Company's business and customers. As cyber threats continue to evolve, the Company may be required to expend significant additional resources to continue to modify or enhance Indigo's protective measures, or to investigate and remediate any information security vulnerabilities.

## **Dependence on Key Personnel**

Indigo's continued success will depend to a significant extent upon its management group, who have developed specialized skills and an in-depth knowledge of the business. The loss of the services of key personnel, particularly Ms. Reisman, could have a material adverse effect on Indigo. To mitigate the risk of personnel loss, the Company has implemented a number of employee engagement and retention strategies.

## **Economic Environment**

Traditionally, retail businesses are highly susceptible to market conditions in the economy. A decline in consumer spending, especially over the December holiday season, could have an adverse effect on the Company's financial condition. Other variables, such as unanticipated increases in merchandise costs, higher labour costs, increases in shipping rates or interruptions in shipping service, or higher interest rates or unemployment rates, could also unfavourably impact the Company's financial performance.

## **External Events**

Weather conditions, as well as events such as political or social unrest, natural disasters, disease outbreaks, or acts of terrorism, could have a material adverse effect on the Company's financial performance. Moreover, if such events were to occur at peak times in the Company's annual business cycle, the impact of these events on operating performance could be significantly greater than they would otherwise have been. The Company has procedures in place to reduce the impact of business interruptions, crises, and potential disasters, but there can be no assurance that these procedures can fully eliminate the negative impact of such events.



## **Regulatory Environment**

The distribution and sale of products, along with communications to customers, are regulated by a number of laws and regulations. Changes to statutes, laws, regulations or regulatory policies, or changes in their interpretation, implementation or enforcement, could adversely affect the Company's operations and performance. The Company may also incur significant costs in the course of complying with any changes to applicable regulations. Failure to comply with applicable regulations could result in judgment, sanctions, or financial penalties that could adversely impact the Company's reputation and financial performance. The Company believes that it has taken reasonable measures designed to ensure compliance with applicable regulations, but there is no assurance that the Company will always be deemed to be in compliance.

Additionally, the distribution and sale of books is a regulated industry in which foreign ownership is generally not permitted under the Investment Canada Act. As well, the sourcing and importation of books is governed by the Book Importation Regulations to the Copyright Act (Canada). There is no assurance that the existing regulatory framework will not change in the future or that it will be effective in preventing foreign-owned retailers from competing in Canada. An increased number of competitors could have an adverse effect on the Company's financial performance.

## **Credit, Foreign Exchange, and Interest Rate Risks**

The Company's maximum exposure to credit risk is equal to the carrying value of accounts receivable. Accounts receivable primarily consists of receivables from retail customers who pay by credit card, recoveries of credits from suppliers for returned or damaged products, and receivables from other companies for sales of products, gift cards, and other services. Credit card payments have minimal credit risk and the limited number of corporate receivables is closely monitored.

The Company's foreign exchange risk is largely limited to currency fluctuations between the Canadian and U.S. dollars. Decreases in the value of the Canadian dollar relative to the U.S. dollar could negatively impact net earnings since the purchase price of some of the Company's products are negotiated with vendors in U.S. dollars, while the retail price to Indigo's customers is set in Canadian dollars.

In June 2013, the Company cancelled its revolving line of credit. As such, the Company's interest rate risk is limited to its long-term debt, for which interest rates are fixed at the time a contract is finalized. The Company's interest income is also sensitive to fluctuations in Canadian interest rates, which affect the interest earned on the Company's cash and cash equivalents. The Company has minimal interest rate risk and does not use any interest rate swaps to manage its risk.

## **Legal Proceedings**

In the normal course of business, Indigo becomes involved in various claims and litigation. While the final outcome of such claims and litigation pending as at March 29, 2014 cannot be predicted with certainty, management believes that any such amount would not have a material impact on the Company's financial position.

## **Trademark and Brand Protection**

The Company has developed, and continues to develop, a line of proprietary products as well as various digital innovations. Infringement on the intellectual property developed by Indigo may have a negative effect on the Company's financial position. In order to protect the competitive advantage provided by these products and innovations, the Company has processes in place to secure and defend its intellectual property.

## **Workplace Health and Safety**

The failure of the Company to adhere to appropriate health and safety procedures and to ensure compliance with applicable laws and regulations could result in employee injuries, productivity loss, and liabilities to Indigo. To reduce the risk of workplace incidents, the Company has health and safety programs in place and has established policies and procedures aimed at ensuring compliance with applicable legislative requirements.



## Compliance with Privacy Laws

In Canada, the Personal Information Protection and Electronic Documents Act (“PIPEDA”) was passed into law by the federal government effective as of January 1, 2001. Currently, this law applies to all organizations that collect, use, or disclose personal information in the course of commercial activities, except to the extent that provincial privacy legislation has been enacted and declared substantially similar to the federal legislation. To date, certain provinces have enacted “substantially similar” private sector privacy legislation. The federal privacy legislation also regulates the inter-provincial collection, use and disclosure of personal information. Applicable Canadian privacy laws create certain obligations on organizations that handle personal information, including obligations relating to obtaining appropriate consent, limitations on use and disclosure of personal information, and ensuring appropriate security safeguards are in place. In the course of its business, the Company maintains records containing sensitive information identifying or relating to individual customers and employees. Although the Company has implemented systems to comply with applicable privacy laws in connection with the collection, use, and disclosure of such personal information, if a significant failure of such systems was to occur, the Company’s business and reputation could be adversely affected.

## Disclosure Controls and Procedures

Management is responsible for establishing and maintaining a system of disclosure controls and procedures to provide reasonable assurance that all material information relating to the Company is gathered and reported on a timely basis to senior management, including the Chief Executive Officer (“CEO”) and Chief Financial Officer (“CFO”), so that appropriate decisions can be made by them regarding public disclosure.

As required by National Instrument 52-109, “Certification of Disclosure in Issuers’ Annual and Interim Filings,” the CEO and CFO have evaluated, or caused to be evaluated under their supervision, the effectiveness of such disclosure controls and procedures. Based on that evaluation, they have concluded that the design and operation of the system of disclosure controls and procedures were effective as at March 29, 2014.

## Internal Controls over Financial Reporting

Management is also responsible for establishing and maintaining adequate internal controls over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements for external purposes in accordance with International Financial Reporting Standards.

All internal control systems, no matter how well designed, have inherent limitations. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to consolidated financial statement preparation and presentation. Additionally, management is necessarily required to use judgment in evaluating controls and procedures.

As required by National Instrument 52-109, “Certification of Disclosure in Issuers’ Annual and Interim Filings,” the CEO and CFO have evaluated, or caused to be evaluated under their supervision, the effectiveness of such internal controls over financial reporting using the framework established in the Internal Control – Integrated Framework (“COSO Framework”) published in 1992 by the Committee of Sponsoring Organizations of the Treadway Commission. Based on that evaluation, they have concluded that the design and operation of the Company’s internal controls over financial reporting were effective as at March 29, 2014.

## Changes in Internal Controls over Financial Reporting

Management has also evaluated whether there were changes in the Company’s internal controls over financial reporting that occurred during the period beginning on December 29, 2013 and ended on March 29, 2014 that have materially affected, or are reasonably likely to materially affect, the Company’s internal controls over financial reporting. The Company has determined that no material changes in internal controls over financial reporting have occurred in this period.

## Cautionary Statement Regarding Forward-Looking Statements

The above discussion includes forward-looking statements. All statements other than statements of historical facts included in this discussion that address activities, events or developments that the Company expects or anticipates will or may occur in the future are forward-looking statements. These statements are based on certain assumptions and analysis made by the Company in light of its experience, analysis and its perception of historical trends, current conditions and expected future developments as well as other factors it believes are appropriate in the circumstances. However, whether actual results and developments will conform to the expectations and predictions of the Company is subject to a number of risks and uncertainties, including the general economic, market or business conditions; competitive actions by other companies; changes in laws or regulations; and other factors, many of which are beyond the control of the Company. Consequently, all of the forward-looking statements made in this discussion are qualified by these cautionary statements and there can be no assurance that results or developments anticipated by the Company will be realized or, even if substantially realized, that they will have the expected consequences to, or effects on, the Company.

## Non-IFRS Financial Measures

The Company prepares its consolidated financial statements in accordance with International Financial Reporting Standards ("IFRS"). In order to provide additional insight into the business, the Company has also provided non-IFRS data, including comparable store sales and adjusted EBITDA, in the discussion and analysis section above. These measures are specific to Indigo and have no standardized meaning prescribed by IFRS. Therefore, these measures may not be comparable to similar measures presented by other companies.

Comparable stores sales and adjusted EBITDA are key indicators used by the Company to measure performance against internal targets and prior period results. Both measures are commonly used by financial analysts and investors to compare Indigo to other retailers. Comparable store sales are defined as sales generated by stores that have been open for more than 12 months on a 52-week basis. It is a key performance indicator for the Company as this measure excludes sales fluctuations due to store closings, permanent relocation, and chain expansion. Adjusted EBITDA is defined as earnings before interest, taxes, depreciation, amortization, impairment, and equity investment. The method of calculating adjusted EBITDA is consistent with that used in prior periods.

A reconciliation between comparable store sales and revenues (the most comparable IFRS measure) was included earlier in this report. A reconciliation between adjusted EBITDA and earnings (loss) before income taxes (the most comparable IFRS measure) is provided below:

| (millions of Canadian dollars)                   | 52-week<br>period ended<br>March 29,<br>2014 | 52-week<br>period ended<br>March 30,<br>2013 |
|--------------------------------------------------|----------------------------------------------|----------------------------------------------|
| Adjusted EBITDA                                  | 0.1                                          | 28.5                                         |
| Depreciation of property, plant and equipment    | (16.4)                                       | (17.6)                                       |
| Amortization of intangible assets                | (11.1)                                       | (10.2)                                       |
| Net impairment of capital assets                 | (2.6)                                        | (0.3)                                        |
| Interest on long-term debt and financing charges | (0.1)                                        | (0.1)                                        |
| Interest income on cash and cash equivalents     | 2.4                                          | 2.6                                          |
| Share of earnings from equity investment         | 0.8                                          | 1.3                                          |
| <b>Earnings (loss) before income taxes</b>       | <b>(26.9)</b>                                | 4.2                                          |

# Independent Auditors' Report

To the Shareholders of Indigo Books & Music Inc.

We have audited the accompanying consolidated financial statements of Indigo Books & Music Inc., which comprise the consolidated balance sheets as at March 29, 2014, March 30, 2013, and April 1, 2012, and the consolidated statements of earnings (loss) and comprehensive earnings (loss), changes in equity and cash flows for the 52 week periods then ended March 29, 2014 and March 30, 2013 and a summary of significant accounting policies and other explanatory information.

## **Management's responsibility for the consolidated financial statements**

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

## **Auditors' responsibility**

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

## **Opinion**

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Indigo Books & Music Inc. as at March 29, 2014, March 30, 2013 and April 1, 2012 and its financial performance and its cash flows for the 52 week periods then ended March 29, 2014 and March 30, 2013 in accordance with International Financial Reporting Standards.

The signature of Ernst & Young LLP is written in a cursive, handwritten style in black ink.

Toronto, Canada  
May 27, 2014

Chartered Accountants  
Licensed Public Accountants

# Consolidated Balance Sheets

| (thousands of Canadian dollars)                     | As at<br>March 29,<br>2014 | As at<br>March 30,<br>2013<br>restated<br>(notes 4 and 22) | As at<br>April 1,<br>2012<br>restated<br>(notes 4 and 22) |
|-----------------------------------------------------|----------------------------|------------------------------------------------------------|-----------------------------------------------------------|
| <b>ASSETS</b>                                       |                            |                                                            |                                                           |
| <b>Current</b>                                      |                            |                                                            |                                                           |
| Cash and cash equivalents (note 6)                  | 157,578                    | 210,562                                                    | 206,718                                                   |
| Accounts receivable                                 | 5,582                      | 7,126                                                      | 12,810                                                    |
| Inventories (note 7)                                | 218,979                    | 216,533                                                    | 229,199                                                   |
| Prepaid expenses                                    | 5,184                      | 4,153                                                      | 3,692                                                     |
| <b>Total current assets</b>                         | <b>387,323</b>             | <b>438,374</b>                                             | <b>452,419</b>                                            |
| Property, plant and equipment (note 8)              | 58,476                     | 58,903                                                     | 66,928                                                    |
| Intangible assets (note 9)                          | 21,587                     | 22,164                                                     | 22,810                                                    |
| Equity investment (note 20)                         | 598                        | 968                                                        | 961                                                       |
| Deferred tax assets (note 10)                       | 44,604                     | 48,731                                                     | 48,633                                                    |
| <b>Total assets</b>                                 | <b>512,588</b>             | <b>569,140</b>                                             | <b>591,751</b>                                            |
| <b>LIABILITIES AND EQUITY</b>                       |                            |                                                            |                                                           |
| <b>Current</b>                                      |                            |                                                            |                                                           |
| Accounts payable and accrued liabilities (note 19)  | 136,428                    | 150,177                                                    | 173,416                                                   |
| Unredeemed gift card liability (note 19)            | 46,827                     | 47,169                                                     | 42,711                                                    |
| Provisions (note 11)                                | 928                        | 2,168                                                      | 232                                                       |
| Deferred revenue                                    | 12,860                     | 13,733                                                     | 11,234                                                    |
| Income taxes payable                                | —                          | 11                                                         | 65                                                        |
| Current portion of long-term debt (notes 12 and 18) | 584                        | 773                                                        | 1,060                                                     |
| <b>Total current liabilities</b>                    | <b>197,627</b>             | <b>214,031</b>                                             | <b>228,718</b>                                            |
| Long-term accrued liabilities (note 19)             | 2,896                      | 4,004                                                      | 5,800                                                     |
| Long-term provisions (note 11)                      | 164                        | 78                                                         | 460                                                       |
| Long-term debt (notes 12 and 18)                    | 227                        | 705                                                        | 1,141                                                     |
| <b>Total liabilities</b>                            | <b>200,914</b>             | <b>218,818</b>                                             | <b>236,119</b>                                            |
| <b>Equity</b>                                       |                            |                                                            |                                                           |
| Share capital (note 13)                             | 203,812                    | 203,805                                                    | 203,373                                                   |
| Contributed surplus (note 14)                       | 8,820                      | 8,128                                                      | 7,039                                                     |
| Retained earnings                                   | 99,042                     | 138,389                                                    | 145,220                                                   |
| <b>Total equity</b>                                 | <b>311,674</b>             | <b>350,322</b>                                             | <b>355,632</b>                                            |
| <b>Total liabilities and equity</b>                 | <b>512,588</b>             | <b>569,140</b>                                             | <b>591,751</b>                                            |

See accompanying notes

On behalf of the Board:



Heather Reisman  
Director



Michael Kirby  
Director

# Consolidated Statements of Earnings (Loss) and Comprehensive Earnings (Loss)

| (thousands of Canadian dollars, except per share data)                      |  | 52-week<br>period ended<br>March 29,<br>2014 | 52-week<br>period ended<br>March 30,<br>2013<br>restated<br>(notes 4 and 22) |
|-----------------------------------------------------------------------------|--|----------------------------------------------|------------------------------------------------------------------------------|
| <b>Revenues</b>                                                             |  | <b>867,668</b>                               | 878,785                                                                      |
| Cost of sales                                                               |  | (493,955)                                    | (495,099)                                                                    |
| <b>Gross profit</b>                                                         |  | <b>373,713</b>                               | 383,686                                                                      |
| Operating, selling and administrative expenses (notes 8, 9 and 15)          |  | (403,693)                                    | (383,319)                                                                    |
| <b>Operating profit (loss)</b>                                              |  | <b>(29,980)</b>                              | 367                                                                          |
| Interest on long-term debt and financing charges                            |  | (95)                                         | (101)                                                                        |
| Interest income on cash and cash equivalents                                |  | 2,377                                        | 2,609                                                                        |
| Share of earnings from equity investment (note 20)                          |  | 789                                          | 1,315                                                                        |
| <b>Earnings (loss) before income taxes</b>                                  |  | <b>(26,909)</b>                              | 4,190                                                                        |
| Income tax recovery (expense) (note 10)                                     |  |                                              |                                                                              |
| Current                                                                     |  | 37                                           | —                                                                            |
| Deferred                                                                    |  | (4,127)                                      | 98                                                                           |
| <b>Net earnings (loss) and comprehensive earnings (loss) for the period</b> |  | <b>(30,999)</b>                              | 4,288                                                                        |
| <b>Net earnings (loss) per common share</b> (note 16)                       |  |                                              |                                                                              |
| Basic                                                                       |  | <b>\$(1.21)</b>                              | \$0.17                                                                       |
| Diluted                                                                     |  | <b>\$(1.21)</b>                              | \$0.17                                                                       |

See accompanying notes

# Consolidated Statements of Changes in Equity

| (thousands of Canadian dollars)                             | Share<br>Capital | Contributed<br>Surplus | Retained<br>Earnings | Total<br>Equity |
|-------------------------------------------------------------|------------------|------------------------|----------------------|-----------------|
| Balance, March 31, 2012                                     | 203,373          | 7,039                  | 145,220              | 355,632         |
| Earnings for the 52-week period<br>ended March 30, 2013     | —                | —                      | 4,288                | 4,288           |
| Exercise of options (notes 13 and 14)                       | 417              | (85)                   | —                    | 332             |
| Directors' deferred share units converted (note 13)         | 15               | (15)                   | —                    | —               |
| Stock-based compensation (note 14)                          | —                | 743                    | —                    | 743             |
| Directors' compensation (note 14)                           | —                | 446                    | —                    | 446             |
| Dividends paid (note 13)                                    | —                | —                      | (11,119)             | (11,119)        |
| Balance, March 30, 2013                                     | 203,805          | 8,128                  | 138,389              | 350,322         |
| <b>Balance, March 30, 2013</b>                              | <b>203,805</b>   | <b>8,128</b>           | <b>138,389</b>       | <b>350,322</b>  |
| <b>Loss for the 52-week period<br/>ended March 29, 2014</b> | <b>—</b>         | <b>—</b>               | <b>(30,999)</b>      | <b>(30,999)</b> |
| <b>Exercise of options</b> (notes 13 and 14)                | <b>7</b>         | <b>—</b>               | <b>—</b>             | <b>7</b>        |
| <b>Directors' deferred share units converted</b> (note 13)  | <b>—</b>         | <b>—</b>               | <b>—</b>             | <b>—</b>        |
| <b>Stock-based compensation</b> (note 14)                   | <b>—</b>         | <b>1,242</b>           | <b>—</b>             | <b>1,242</b>    |
| <b>Directors' compensation</b> (note 14)                    | <b>—</b>         | <b>425</b>             | <b>—</b>             | <b>425</b>      |
| <b>Dividends paid</b> (note 13)                             | <b>—</b>         | <b>—</b>               | <b>(8,348)</b>       | <b>(8,348)</b>  |
| <b>Repurchase of options</b> (note 14)                      | <b>—</b>         | <b>(975)</b>           | <b>—</b>             | <b>(975)</b>    |
| <b>Balance, March 29, 2014</b>                              | <b>203,812</b>   | <b>8,820</b>           | <b>99,042</b>        | <b>311,674</b>  |

See accompanying notes

# Consolidated Statements of Cash Flows

| (thousands of Canadian dollars)                                               | 52-week<br>period ended<br>March 29,<br>2014 | 52-week<br>period ended<br>March 30,<br>2013<br>restated<br>(notes 4 and 22) |
|-------------------------------------------------------------------------------|----------------------------------------------|------------------------------------------------------------------------------|
| <b>CASH FLOWS FROM OPERATING ACTIVITIES</b>                                   |                                              |                                                                              |
| Net earnings (loss) for the period                                            | (30,999)                                     | 4,288                                                                        |
| Add (deduct) items not affecting cash                                         |                                              |                                                                              |
| Depreciation of property, plant and equipment (note 8)                        | 16,358                                       | 17,638                                                                       |
| Amortization of intangible assets (note 9)                                    | 11,123                                       | 10,245                                                                       |
| Net impairment of capital assets (note 8)                                     | 2,604                                        | 250                                                                          |
| Loss on disposal of capital assets                                            | 302                                          | 65                                                                           |
| Stock-based compensation (note 14)                                            | 1,242                                        | 743                                                                          |
| Directors' compensation (note 14)                                             | 425                                          | 446                                                                          |
| Deferred tax assets (note 10)                                                 | 4,127                                        | (98)                                                                         |
| Other                                                                         | (206)                                        | (482)                                                                        |
| Net change in non-cash working capital balances (note 17)                     | (19,196)                                     | 1,089                                                                        |
| Interest on long-term debt and financing charges                              | 95                                           | 101                                                                          |
| Interest income on cash and cash equivalents                                  | (2,377)                                      | (2,609)                                                                      |
| Income taxes received                                                         | 26                                           | 32                                                                           |
| Share of earnings from equity investment (note 20)                            | (789)                                        | (1,315)                                                                      |
| <b>Cash flows from (used in) operating activities</b>                         | <b>(17,265)</b>                              | <b>30,393</b>                                                                |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES</b>                                   |                                              |                                                                              |
| Purchase of property, plant and equipment (note 8)                            | (18,700)                                     | (9,441)                                                                      |
| Addition of intangible assets (note 9)                                        | (10,546)                                     | (9,621)                                                                      |
| Distributions from equity investment (note 20)                                | 1,159                                        | 1,308                                                                        |
| Interest received                                                             | 2,463                                        | 2,691                                                                        |
| <b>Cash flows used in investing activities</b>                                | <b>(25,624)</b>                              | <b>(15,063)</b>                                                              |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES</b>                                   |                                              |                                                                              |
| Notes payable (note 21)                                                       | –                                            | 190                                                                          |
| Repayment of long-term debt                                                   | (814)                                        | (1,200)                                                                      |
| Interest paid                                                                 | (110)                                        | (160)                                                                        |
| Proceeds from share issuances (note 13)                                       | 7                                            | 332                                                                          |
| Dividends paid (note 13)                                                      | (8,348)                                      | (11,119)                                                                     |
| Repurchase of options (note 14)                                               | (975)                                        | –                                                                            |
| <b>Cash flows used in financing activities</b>                                | <b>(10,240)</b>                              | <b>(11,957)</b>                                                              |
| Effect of foreign currency exchange rate changes on cash and cash equivalents | 145                                          | 471                                                                          |
| <b>Net increase (decrease) in cash and cash equivalents during the period</b> | <b>(52,984)</b>                              | <b>3,844</b>                                                                 |
| Cash and cash equivalents, beginning of period                                | 210,562                                      | 206,718                                                                      |
| <b>Cash and cash equivalents, end of period</b>                               | <b>157,578</b>                               | <b>210,562</b>                                                               |

See accompanying notes

# Notes to Consolidated Financial Statements

March 29, 2014

## 1. CORPORATE INFORMATION

Indigo Books & Music Inc. (the “Company” or “Indigo”) is a corporation domiciled and incorporated under the laws of the Province of Ontario in Canada. The Company’s registered office is located at 468 King Street West, Toronto, Ontario, M5V 1L8, Canada. The consolidated financial statements of the Company comprise the Company, its equity investment in Calendar Club of Canada Limited Partnership (“Calendar Club”), and its wholly-owned subsidiary, Soho Inc. The Company is the ultimate parent of the consolidated organization.

## 2. NATURE OF OPERATIONS

Indigo is Canada’s largest book, gift and specialty toy retailer and was formed as a result of an amalgamation of Chapters Inc. and Indigo Books & Music, Inc. under the laws of the Province of Ontario, pursuant to a Certificate of Amalgamation dated August 16, 2001. The Company operates a chain of retail bookstores across all ten provinces and one territory in Canada, including 95 superstores (2013 – 97) under the *Chapters*, *Indigo* and the *World’s Biggest Bookstore* names, as well as 131 small format stores (2013 – 134) under the banners *Coles*, *Indigo*, *Indigospirit*, *SmithBooks*, and *The Book Company*. Subsequent to year end, the Company closed the *World’s Biggest Bookstore*. In addition, the Company operates *indigo.ca*, an e-commerce retail destination which sells books, gifts, toys, and paper products. The Company also operates seasonal kiosks and year-round stores in shopping malls across Canada through Calendar Club.

The Company’s operations are focused on the merchandising of products and services in Canada. As such, the Company presents one operating segment in its consolidated financial statements.

Indigo also has a separate registered charity under the name Indigo Love of Reading Foundation (the “Foundation”). The Foundation provides new books and learning material to high-needs elementary schools across the country through donations from Indigo, its customers, suppliers, and employees.

## 3. BASIS OF PREPARATION

### Statement of compliance

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board (“IASB”) and using the accounting policies described herein.

These consolidated financial statements were approved by the Company’s Board of Directors on May 27, 2014.

### Use of judgment

The preparation of the consolidated financial statements in conformity with IFRS requires the Company to make judgments, apart from those involving estimation, in applying accounting policies that affect the recognition and measurement of assets, liabilities, revenues, and expenses. Actual results may differ from the judgments made by the Company. Information about judgments that have the most significant effect on recognition and measurement of assets, liabilities, revenues, and expenses are discussed below. Information about significant estimates is discussed in the following section.

### Impairment

An impairment loss is recognized for the amount by which the carrying amount of an asset or a cash-generating unit (“CGU”) exceeds its recoverable amount. The Company uses judgment when identifying CGUs and when assessing for indicators of impairment.



### Intangible assets

Initial capitalization of intangible asset costs is based on the Company's judgment that technological and economic feasibility are confirmed and the project will generate future economic benefits by way of estimated future discounted cash flows that are being generated.

### Leases

The Company uses judgment in determining whether a lease qualifies as a finance lease arrangement that transfers substantially all the risks and rewards incidental to ownership.

### Deferred tax assets

The recognition of deferred tax assets is based on the Company's judgment. The assessment of the probability of future taxable income in which deferred tax assets can be utilized is based on management's best estimate of future taxable income that the Company expects to achieve from reviewing its latest forecast. This estimate is adjusted for significant non-taxable income and expenses and for specific limits to the use of any unused tax loss or credit. Deferred tax assets are recognized to the extent that it is probable that taxable profit will be available against which the deductible temporary differences and the carryforward of unused tax credits and unused tax losses can be utilized. Any difference between the gross deferred tax asset and the amount recognized is recorded on the balance sheet as a valuation allowance. If the valuation allowance decreases as the result of subsequent events, the previously recognized valuation allowance will be reversed. The recognition of deferred tax assets that are subject to certain legal or economic limits or uncertainties are assessed individually by the Company based on the specific facts and circumstances.

### Use of estimates

The preparation of the consolidated financial statements in conformity with IFRS requires the Company to make estimates and assumptions in applying accounting policies that affect the recognition and measurement of assets, liabilities, revenues, and expenses. Actual results may differ from the estimates made by the Company, and actual results will seldom equal estimates. Information about estimates that have the most significant effect on the recognition and measurement of assets, liabilities, revenues, and expenses are discussed below.

### Revenues

The Company recognizes revenue from unredeemed gift cards ("gift card breakage") if the likelihood of gift card redemption by the customer is considered to be remote. The Company estimates its average gift card breakage rate based on historical redemption rates. The resulting revenue is recognized over the estimated period of redemption based on historical redemption patterns commencing when the gift cards are sold.

The Indigo plum rewards program ("Plum") allows customers to earn points on their purchases. The fair value of Plum points is calculated by multiplying the number of points issued by the estimated cost per point. The estimated cost per point is based on many factors, including the expected future redemption patterns and associated costs. On an ongoing basis, the Company monitors trends in redemption patterns (redemption at each reward level), historical redemption rates (points redeemed as a percentage of points issued) and net cost per point redeemed, adjusting the estimated cost per point based upon expected future activity. Points revenue is included with total revenues in the Company's consolidated statements of earnings (loss) and comprehensive earnings (loss).

### Inventories

The future realization of the carrying amount of inventory is affected by future sales demand, inventory levels, and product quality. At each balance sheet date, the Company reviews its on-hand inventory and uses historical trends and current inventory mix to determine a reserve for the impact of future markdowns which will take the net realizable value of inventory on-hand below cost. Inventory valuation also incorporates a write-down to reflect future losses on the disposition of

obsolete merchandise. The Company reduces inventory for estimated shrinkage that has occurred between physical inventory counts and the end of the fiscal year based on historical experience as a percentage of sales. In addition, the Company records a vendor settlement accrual to cover any disputes between the Company and its vendors. The Company estimates this reserve based on historical experience of settlements with its vendors.

#### Share-based payments

The cost of equity-settled transactions with counterparties is based on the Company's estimate of the fair value of share-based instruments and the number of equity instruments that will eventually vest. The Company's estimated fair value of the share-based instruments is calculated using the following variables: risk-free interest rate; expected volatility; expected time until exercise; and expected dividend yield. Risk-free interest rate is based on Government of Canada bond yields, while all other variables are estimated based on the Company's historical experience with its share-based payments.

#### Impairment

To determine the recoverable amount of an impaired asset, the Company estimates expected future cash flows at the CGU level and determines a suitable discount rate in order to calculate the present value of those cash flows. In the process of measuring expected future cash flows, the Company makes assumptions about future sales, gross margin rates, expenses, capital expenditures, and working capital investments which are based upon past and expected future performance. Determining the applicable discount rate involves estimating appropriate adjustments to market risk and to Company-specific risk factors.

#### Property, plant and equipment and intangible assets (collectively, "capital assets")

Capital assets are depreciated over their useful lives, taking into account residual values where appropriate. Assessments of useful lives and residual values are performed annually and take into consideration factors such as technological innovation, maintenance programs, and relevant market information. In assessing residual values, the Company considers the remaining life of the asset, its projected disposal value, and future market conditions.

## 4. SIGNIFICANT ACCOUNTING POLICIES

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements.

#### **Basis of measurement**

The Company's consolidated financial statements are prepared on the historical cost basis of accounting, except as disclosed in the accounting policies set out below.

#### **Basis of consolidation**

The consolidated financial statements comprise the financial statements of the Company and entities controlled by the Company. Control exists when the Company is exposed to, or has the right to, variable returns from its involvement with the controlled entity and when the Company has the current ability to affect those returns through its power over the controlled entity. When the Company does not own all of the equity in a subsidiary, the non-controlling interest is disclosed as a separate line item in the consolidated balance sheets and the earnings accruing to non-controlling interest holders is disclosed as a separate line item in the consolidated statements of earnings (loss) and comprehensive earnings (loss).

The financial statements of the subsidiary are prepared for the same reporting period as the parent company, using consistent accounting policies. Subsidiaries are fully consolidated from the date of acquisition, being the date on which the Company obtains control, and continue to be consolidated until the date that such control ceases. All intercompany balances and transactions and any unrealized gains and losses arising from intercompany transactions are eliminated in preparing these consolidated financial statements.

### **Equity investment**

The equity method of accounting is applied to investments in companies where Indigo has the ability to exert significant influence over the financial and operating policy decisions of the company but lacks control or joint control over those policies. Under the equity method, the Company's investment is initially recognized at cost and subsequently increased or decreased to recognize the Company's share of earnings and losses of the investment, and for impairment losses after the initial recognition date. The Company's share of losses that are in excess of its investment are recognized only to the extent that the Company has incurred legal or constructive obligations or made payments on behalf of the company. The Company's share of earnings and losses of its equity investment are recognized through profit or loss during the period. Cash distributions received from the investment are accounted for as a reduction in the carrying amount of the Company's equity investment.

### **Cash and cash equivalents**

Cash and cash equivalents consist of cash on hand, balances with banks, and highly liquid investments that are readily convertible to known amounts of cash with maturities of three months or less at the date of acquisition. Cash is considered to be restricted when it is subject to contingent rights of a third-party customer, vendor, or government agency.

### **Inventories**

Inventories are valued at the lower of cost, determined on a moving average cost basis, and market, being net realizable value. Costs include all direct and reasonable expenditures that are incurred in bringing inventories to their present location and condition. Net realizable value is the estimated selling price in the ordinary course of business. When the Company permanently reduces the retail price of an item and the markdown incurred brings the retail price below the cost of the item, there is a corresponding reduction in inventory recognized in the period. Vendor rebates are recorded as a reduction in the price of the products, and corresponding inventories are recorded net of vendor rebates.

### **Prepaid expenses**

Prepaid expenses include store supplies, rent, license fees, maintenance contracts, and insurance. Store supplies are expensed as they are used while other costs are amortized over the term of the contract.

### **Income taxes**

Current income taxes are the expected taxes payable or receivable on the taxable earnings or loss for the period. Current income taxes are payable on taxable earnings for the period as calculated under Canadian taxation guidelines, which differs from taxable earnings under IFRS. Calculation of current income taxes is based on tax rates and tax laws that have been enacted, or substantively enacted, by the end of the reporting period. Current income taxes relating to items recognized directly in equity are recognized in equity and not in the consolidated statements of earnings (loss) and comprehensive earnings (loss).

Deferred income taxes are calculated at the reporting date using the liability method based on temporary differences between the carrying amounts of assets and liabilities and their tax bases. However, deferred tax assets and liabilities on temporary differences arising from the initial recognition of goodwill, or of an asset or liability in a transaction that is not a business combination, will not be recognized when neither accounting nor taxable profit or loss are affected at the time of the transaction.

Deferred tax assets arising from temporary differences associated with investments in subsidiaries are provided for if it is probable that the differences will reverse in the foreseeable future and taxable profit will be available against which the tax assets may be utilized. Deferred tax assets on temporary differences associated with investments in subsidiaries are not provided for if the timing of the reversal of these temporary differences can be controlled by the Company and it is probable that reversal will not occur in the foreseeable future.

Deferred tax assets and liabilities are calculated, without discounting, at tax rates that are expected to apply to their respective periods of realization, provided they are enacted or substantively enacted by the end of the reporting period. Deferred tax assets and liabilities are offset only when the Company has the right and intention to set off current tax assets and liabilities from the same taxable entity and the same taxation authority.

Deferred tax assets are recognized to the extent that it is probable that taxable profit will be available against which the deductible temporary differences and the carryforward of unused tax credits and unused tax losses can be utilized. Any difference between the gross deferred tax asset and the amount recognized is recorded on the balance sheet as a valuation allowance. If the valuation allowance decreases as the result of subsequent events, the previously recognized valuation allowance will be reversed.

### **Property, plant and equipment**

All items of property, plant and equipment are initially recognized at cost, which includes any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by the Company. Subsequent to initial recognition, property, plant and equipment assets are shown at cost less accumulated depreciation and any accumulated impairment losses.

Depreciation of an asset begins once it becomes available for use. The depreciable amount of an asset, being the cost of an asset less the residual value, is allocated on a straight-line basis over the estimated useful life of the asset. Residual value is estimated to be zero unless the Company expects to dispose of the asset at a value that exceeds the estimated disposal costs. The residual values, useful lives, and depreciation methods applied to assets are reviewed annually based on relevant market information and management considerations.

The following useful lives are applied:

|                                   |                                                                           |
|-----------------------------------|---------------------------------------------------------------------------|
| Furniture, fixtures and equipment | 5 – 10 years                                                              |
| Computer equipment                | 3 – 5 years                                                               |
| Equipment under finance leases    | 3 – 5 years                                                               |
| Leasehold improvements            | over the lease term and probable renewal periods to a maximum of 10 years |

Items of property, plant and equipment are assessed for impairment as detailed in the accounting policy note on impairment and are derecognized either upon disposal or when no future economic benefits are expected from their use. Any gain or loss arising on derecognition is included in earnings when the asset is derecognized.

### **Leased assets**

Leases are classified as finance leases when the terms of the lease transfer substantially all the risks and rewards related to ownership of the leased asset to the Company. At lease inception, the related asset is recognized at the lower of the fair value of the leased asset or the present value of the lease payments. The corresponding liability amount is recognized as long-term debt.

Depreciation methods and useful lives for assets held under finance lease agreements correspond to those applied to comparable assets which are legally owned by the Company. If there is no reasonable certainty that the Company will obtain ownership of the financed asset at the end of the lease term, the asset is depreciated over the shorter of its estimated useful life or the lease term. The corresponding long-term debt is reduced by lease payments less interest paid. Interest payments are expensed as part of interest on long-term debt and financing charges on the consolidated statements of earnings (loss) and comprehensive earnings (loss) over the period of the lease. As at March 29, 2014, computer equipment assets are the only type of asset leased under finance lease arrangements.

All other leases are treated as operating leases. Payments on operating lease agreements are recognized as an expense on a straight-line basis over the lease term. Associated costs, such as maintenance and insurance, are expensed as incurred.

The Company performs quarterly assessments of contracts which do not take the legal form of a lease to determine whether they convey the right to use an asset in return for a payment or series of payments and therefore need to be accounted for as leases. As at March 29, 2014, the Company had no such contracts.

## Leased premises

The Company conducts all of its business from leased premises. Leasehold improvements are depreciated over the lesser of their economic life or the initial lease term plus renewal periods where renewal has been determined to be reasonably assured ("lease term"). Leasehold improvements are assessed for impairment as detailed in the accounting policy note on impairment. Leasehold improvement allowances are depreciated over the lease term. Other inducements, such as rent-free periods, are amortized into earnings over the lease term, with the unamortized portion recorded in current and long-term accounts payable and accrued liabilities. As at March 29, 2014, all of the Company's leases on premises were accounted for as operating leases. Expenses incurred for leased premises include base rent, taxes, and contingent rent based upon a percentage of sales.

## Intangible assets

Intangible assets are initially recognized at cost, if acquired separately, or at fair value, if acquired as part of a business combination. After initial recognition, intangible assets are carried at cost less accumulated amortization and any accumulated impairment losses.

Amortization commences when the intangible assets are available for their intended use. The useful lives of intangible assets are assessed as either finite or indefinite. Intangible assets with finite lives are amortized over their useful economic life. Intangible assets with indefinite lives are not amortized but are reviewed at each reporting date to determine whether the indefinite life continues to be supportable. If not, the change in useful life from indefinite to finite is made on a prospective basis. Residual value is estimated to be zero unless the Company expects to dispose of the asset at a value that exceeds the estimated disposal costs. The residual values, useful lives and amortization methods applied to assets are reviewed annually based on relevant market information and management considerations.

The following useful lives are applied:

|                               |             |
|-------------------------------|-------------|
| Computer application software | 3 – 5 years |
| Internal development costs    | 3 years     |

Intangible assets are assessed for impairment as detailed in the accounting policy note on impairment. An intangible asset is derecognized either upon disposal or when no future economic benefit is expected from its use. Any gain or loss arising on derecognition is included in earnings when the asset is derecognized.

### Computer application software

When computer application software is not an integral part of a related item of computer hardware, the software is treated as an intangible asset. Computer application software that is integral to the use of related computer hardware is recorded as property, plant and equipment.

### Internal development costs

Costs that are directly attributable to internal development are recognized as intangible assets provided they meet the definition of an intangible asset. Development costs not meeting these criteria are expensed as incurred. Capitalized development costs include external direct costs of materials and services and the payroll and payroll-related costs for employees who are directly associated with the projects.

## Impairment testing

### Capital assets

For the purposes of assessing impairment, capital assets are grouped at the lowest levels for which there are largely independent cash inflows and for which a reasonable and consistent allocation basis can be identified. For capital assets which can be reasonably and consistently allocated to individual stores, the store level is used as the CGU for impairment testing. For

all other capital assets, the corporate level is used as the group of CGUs. Capital assets and related CGUs or groups of CGUs are tested for impairment at each reporting date and whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Events or changes in circumstances which may indicate impairment include a significant change to the Company's operations, a significant decline in performance, or a change in market conditions which adversely affects the Company.

An impairment loss is recognized for the amount by which the carrying amount of a CGU or group of CGUs exceeds its recoverable amount. To determine the recoverable amount, management uses a value in use calculation to determine the present value of the expected future cash flows from each CGU or group of CGUs based on the CGU's estimated growth rate. The Company's growth rate and future cash flows are based on historical data and management's expectations. Impairment losses are charged pro rata to the capital assets in the CGU or group of CGUs. Capital assets and CGUs or groups of CGUs are subsequently reassessed for indicators that a previously recognized impairment loss may no longer exist. An impairment loss is reversed if the recoverable amount of the capital asset, CGU, or group of CGUs exceeds its carrying amount, but only to the extent that the carrying amount of the asset does not exceed the carrying amount that would have been determined, net of depreciation or amortization, if no impairment loss had been recognized.

#### **Financial assets**

Individually significant financial assets are tested for impairment on an individual basis. The remaining financial assets are assessed collectively in groups that share similar credit risk characteristics. Financial assets are tested for impairment at each reporting date and whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Evidence of impairment may include indications that a debtor or a group of debtors are experiencing significant financial difficulty, default or delinquency in interest or principal payments, and observable data indicating that there is a measurable decrease in the estimated future cash flows.

A financial asset is deemed to be impaired if there is objective evidence that one or more loss events having a negative effect on future cash flows of the financial asset occurs after initial recognition and the loss can be reliably measured. The impairment loss is measured as the difference between the carrying amount of the financial asset and the present value of the estimated future cash flows, discounted at the original effective interest rate. The impairment loss is recorded as an allowance and recognized in net earnings. If the impairment loss decreases as the result of subsequent events, the previously recognized impairment loss is reversed.

#### **Provisions**

Provisions are recognized when the Company has a present legal or constructive obligation as a result of past events, for which it is probable that the Company will be required to settle the obligation and a reliable estimate of the settlement can be made. The amount recognized as a provision is the best estimate of the consideration required to settle the present obligation at the end of the reporting period, taking into account risks and uncertainties of cash flow. Where the effect of discounting to present value is material, provisions are adjusted to reflect the time value of money. Examples of provisions include legal claims, onerous leases, and decommissioning liabilities.

#### **Borrowing costs**

Borrowing costs are primarily comprised of interest on the Company's long-term debt. Borrowing costs are capitalized using the effective interest rate method to the extent that they are directly attributable to the acquisition, production, or construction of qualifying assets that require a substantial period of time to get ready for their intended use or sale. All other borrowing costs are expensed as incurred and reported in the consolidated statements of earnings (loss) and comprehensive earnings (loss) as part of interest on long-term debt and finance charges.

## **Total equity**

Share capital represents the nominal value of shares that have been issued. Retained earnings include all current and prior period retained profits. Dividend distributions payable to equity shareholders are recorded as dividends payable when the dividends have been approved by the Board of Directors prior to the reporting date.

## **Share-based awards**

The Company has established an employee stock option plan for key employees. The fair value of each tranche of options granted is estimated on grant date using the Black-Scholes option pricing model. The Black-Scholes option pricing model is based on variables such as: risk-free interest rate; expected volatility; expected time until exercise; and expected dividend yield. Expected stock price volatility is based on the historical volatility of the Company's stock for a period approximating the expected life. The grant date fair value, net of estimated forfeitures, is recognized as an expense with a corresponding increase to contributed surplus over the vesting period. Estimates are subsequently revised if there is an indication that the number of stock options expected to vest differs from previous estimates. Any consideration paid by employees on exercise of stock options is credited to share capital with a corresponding reduction to contributed surplus.

## **Revenues**

The Company recognizes revenue when the substantial risks and rewards of ownership pass to the customer. Revenue is measured at the fair value of consideration received or receivable by the Company for goods supplied, inclusive of amounts invoiced for shipping, and net of sales discounts, returns and amounts deferred related to the issuance of Plum points. Return allowances are estimated using historical experience. Revenue is recognized when the amount can be measured reliably, it is probable that economic benefits associated with the transaction will flow to the Company, the costs incurred or to be incurred can be measured reliably, and the criteria for each of the Company's activities (as described below) have been met.

### **Retail sales**

Revenue for retail customers is recognized at the time of purchase.

### **Online sales**

Revenue for online customers is recognized when the product is shipped.

### **Commission revenue**

The Company earns commission revenue through partnerships with other companies and recognizes revenue once services have been rendered and the amount of revenue can be measured reliably.

### **Gift cards**

The Company sells gift cards to its customers and recognizes the revenue as gift cards are redeemed. The Company also recognizes gift card breakage if the likelihood of gift card redemption by the customer is considered to be remote. The Company determines its average gift card breakage rate based on historical redemption rates. Once the breakage rate is determined, the resulting revenue is recognized over the estimated period of redemption based on historical redemption patterns, commencing when the gift cards are sold. Gift card breakage is included in revenues in the Company's consolidated statements of earnings (loss) and comprehensive earnings (loss).

### **Indigo irewards loyalty program**

For an annual fee, the Company offers loyalty cards to customers that entitle the cardholder to receive discounts on purchases. Each card is issued with a 12-month expiry period. The fee revenue related to the issuance of a card is deferred and amortized into earnings over the expiry period, based upon historical sales volumes.



#### Indigo plum rewards program

Plum is a free program that allows members to earn points on their purchases in the Company's stores and enjoy member pricing at the Company's online website. Members can then redeem points for discounts on future purchases of store merchandise.

When a Plum member purchases merchandise, the Company allocates the payment received between the merchandise and the points. The payment is allocated based on the residual method, where the amount allocated to the merchandise is the total payment less the fair value of the points. The portion of revenue attributed to the merchandise is recognized at the time of purchase. Revenue attributed to the points is recorded as deferred revenue and recognized when points are redeemed.

The fair value of the points is calculated by multiplying the number of points issued by the estimated cost per point. The estimated cost per point is determined based on a number of factors, including the expected future redemption patterns and associated costs. On an ongoing basis, the Company monitors trends in redemption patterns (redemption at each reward level), historical redemption rates (points redeemed as a percentage of points issued) and net cost per point redeemed, adjusting the estimated cost per point based upon expected future activity. Points revenue is included with total revenues in the Company's consolidated statements of earnings (loss) and comprehensive earnings (loss).

#### Interest income

Interest income is reported on an accrual basis using the effective interest method.

#### Vendor rebates

The Company records cash consideration received from vendors as a reduction to the price of vendors' products. This is reflected as a reduction in cost of goods sold and related inventories when recognized in the consolidated financial statements. Certain exceptions apply where the cash consideration received is a reimbursement of incremental selling costs incurred by the Company, in which case the cash received is reflected as a reduction in operating and administrative expenses.

#### Earnings per share

Basic earnings per share is determined by dividing the net earnings attributable to common shareholders by the weighted average number of common shares outstanding during the period. Diluted earnings per share are calculated in accordance with the treasury stock method and are based on the weighted average number of common shares and dilutive common share equivalents outstanding during the period. The weighted average number of shares used in the computation of both basic and fully diluted earnings per share may be the same due to the anti-dilutive effect of securities.

#### Financial instruments

Financial assets and financial liabilities are recognized when the Company becomes a party to the contractual provisions of the financial instrument. Financial assets are derecognized when the contractual rights to the cash flows from the financial asset expire, or when the financial asset and all substantial risks and rewards are transferred. A financial liability is derecognized when it is extinguished, discharged, cancelled, or expires. Where a legally enforceable right to offset exists for recognized financial assets and financial liabilities and there is an intention to settle the liability and realize the asset simultaneously, or to settle on a net basis, such related financial assets and financial liabilities are offset.

For the purposes of ongoing measurement, financial assets and liabilities are classified according to their characteristics and management's intent. All financial instruments are initially recognized at fair value. The following methods and assumptions were used to estimate the initial fair value of each type of financial instrument by reference to market data and other valuation techniques, as appropriate:

- (i) The fair values of cash and cash equivalents, accounts receivable, and accounts payable and accrued liabilities approximate their carrying values given their short-term maturities; and



- (ii) The fair value of long-term debt is estimated based on the discounted cash payments of the debt at the Company's estimated incremental borrowing rates for debt of the same remaining maturities. The fair value of long-term debt approximates its carrying value.

Embedded derivatives are separated and measured at fair value if certain criteria are met. Management has reviewed all material contracts and has determined that the Company does not currently have any significant embedded derivatives that require separate accounting and disclosure.

After initial recognition, financial instruments are subsequently measured as follows:

#### Financial assets

- (i) Loans and receivables – These are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. These assets are measured at amortized cost, less impairment charges, using the effective interest method. Gains and losses are recognized in earnings through the amortization process or when the assets are derecognized.
- (ii) Financial assets at fair value through profit or loss – These assets are held for trading if acquired for the purpose of selling in the near term or are designated to this category upon initial recognition. These assets are measured at fair value, with gains or losses recognized in earnings.
- (iii) Held-to-maturity investments – These are non-derivative financial assets with fixed or determinable payments and fixed maturities which the Company intends, and is able, to hold until maturity. These assets are measured at amortized cost, less impairment charges, using the effective interest method. Gains and losses are recognized in earnings through the amortization process or when the assets are derecognized.
- (iv) Available-for-sale financial assets – These are non-derivative financial assets that are either designated to this category upon initial recognition or do not qualify for inclusion in any of the other categories. These assets are measured at fair value, with unrealized gains and losses recognized in Other Comprehensive Income until the asset is derecognized or determined to be impaired. If the asset is derecognized or determined to be impaired, the cumulative gain or loss previously reported in Accumulated Other Comprehensive Income is included in earnings.

#### Financial liabilities

- (i) Other liabilities – These liabilities are measured at amortized cost using the effective interest rate method. Gains and losses are recognized in earnings through the amortization process or when the liabilities are derecognized.
- (ii) Financial liabilities at fair value through profit or loss – These liabilities are held for trading if acquired for the purpose of selling in the near term or are designated to this category upon initial recognition. These liabilities are measured at fair value, with gains or losses recognized in earnings.

The Company's financial assets and financial liabilities are generally classified and measured as follows:

| Financial Asset/Liability                | Category              | Measurement    |
|------------------------------------------|-----------------------|----------------|
| Cash and cash equivalents                | Loans and receivables | Amortized cost |
| Accounts receivable                      | Loans and receivables | Amortized cost |
| Accounts payable and accrued liabilities | Other liabilities     | Amortized cost |
| Long-term debt                           | Other liabilities     | Amortized cost |

All other balance sheet accounts are not considered financial instruments.

All financial instruments measured at fair value after initial recognition are categorized into one of three hierarchy levels for disclosure purposes. Each level reflects the significance of the inputs used in making the fair value measurements.

Level 1: Fair value is determined by reference to quoted prices in active markets.

Level 2: Valuations use inputs based on observable market data, either directly or indirectly, other than the quoted prices.

Level 3: Valuations are based on inputs that are not based on observable market data.

As at March 29, 2014, there are no financial instruments classified into these levels. The Company measures all financial instruments at amortized cost.

### Retirement benefits

The Company provides retirement benefits through a defined contribution retirement plan. Under the defined contribution retirement plan, the Company pays fixed contributions to an independent entity. The Company has no legal or constructive obligations to pay further contributions after its payment of the fixed contribution. The costs of benefits under the defined contribution retirement plan are expensed as contributions are due and are reversed if employees leave before the vesting period.

### Foreign currency translation

The consolidated financial statements are presented in Canadian dollars, which is the functional currency of the Company. Sales transacted in foreign currencies are aggregated monthly and translated using the average exchange rate. Transactions in foreign currencies are translated at rates of exchange at the time of the transaction. Monetary assets and liabilities denominated in foreign currencies which are held at the reporting date are translated at the closing consolidated balance sheet rate. Non-monetary items are measured at historical cost and are translated using the exchange rates at the date of the transaction. Non-monetary items measured at fair value are translated using exchange rates at the date when fair value was determined. The resulting exchange gains or losses are included in earnings.

### Accounting Standards Implemented in Fiscal 2014

Adoption of these amendments and standards in fiscal 2014 impacted the Company's results of operations, financial position, and disclosures as follows:

- Joint Arrangements ("IFRS 11") replaces IAS 31, "Interests in Joint Ventures" ("IAS 31") and SIC-13, "Jointly-controlled Entities – Non-monetary Contributions by Venturers," and requires that a party in a joint arrangement assess its rights and obligations to determine the type of joint arrangement and account for those rights and obligations accordingly. Previously, the Company accounted for its interest in Calendar Club under IAS 31 using proportionate consolidation. However, the Company concluded that its interest in Calendar Club does not meet the definition of a joint arrangement under IFRS 11 and needs to be accounted for under "Investments in Associates and Joint Ventures" ("IAS 28") as a significant investment using the equity method. The Company has retrospectively restated its comparative financial statements to reclassify proportionately consolidated Calendar Club operating results into a single equity investment line. These restatements have no impact to the Company's total net earnings (loss) or cash flows. The impact of reclassification on the Company's financial statements is as follows:

|                                 | 52-week<br>period ended<br>March 30,<br>2013 |
|---------------------------------|----------------------------------------------|
| (thousands of Canadian dollars) |                                              |
| Decrease in revenues            | (15,272)                                     |
| Decrease in expenses            | (13,957)                                     |
| Increase in equity investment   | 1,315                                        |

| (thousands of Canadian dollars) | As at<br>March 30,<br>2013 | As at<br>April 1,<br>2012 |
|---------------------------------|----------------------------|---------------------------|
| Decrease in assets              | (2,074)                    | (1,746)                   |
| Increase in equity investment   | 968                        | 961                       |
| Decrease in liabilities         | (1,106)                    | (785)                     |

- Amendments to Investments in Associates and Joint Ventures (“IAS 28”) impact accounting for associates and joint ventures held for sale and changes in interests held in associates and joint ventures; and
- Disclosure of Interests in Other Entities (“IFRS 12”) includes all of the disclosures that were previously in IAS 27, “Separate Financial Statements,” IAS 31 and IAS 28, “Investments in Associates.” These disclosures relate to an entity’s interests in subsidiaries, joint arrangements, associates, and structured entities.

Adoption of the following amendments and standards in fiscal 2014 did not have an impact on the Company’s results of operations, financial position, or disclosures:

- Amendments to Presentation of Financial Statements (“IAS 1”) require companies to group together items within other comprehensive earnings which may be reclassified to net earnings. The amendments are effective for annual periods beginning on or after July 1, 2012 and were applied retrospectively;
- Amendments to Financial Instruments: Disclosures (“IFRS 7”) regarding the offsetting of financial instruments. These amendments were applied retrospectively and are effective for annual periods beginning on or after January 1, 2013 and interim periods within those annual periods;
- Fair Value Measurement (“IFRS 13”) provides guidance to improve consistency and comparability in fair value measurements and related disclosures through a fair value hierarchy. This standard was applied prospectively and is effective for annual periods beginning on or after January 1, 2013;
- Amendments to Separate Financial Statements (“IAS 27”) remove all requirements relating to consolidated financial statements. This standard was applied retrospectively and is effective for annual periods beginning on or after January 1, 2013; and
- Consolidated Financial Statements (“IFRS 10”) replaces portions of IAS 27, “Consolidated and Separate Financial Statements,” supersedes SIC-12, “Consolidation – Special Purpose Entities,” and establishes standards for the presentation and preparation of consolidated financial statements when an entity controls one or more entities. This standard was applied retrospectively and is effective for annual periods beginning on or after January 1, 2013.

## 5. NEW ACCOUNTING PRONOUNCEMENTS

### Impairment of Assets (“IAS 36”)

In May 2013, the IASB issued amendments to IAS 36 which require disclosures about assets or CGUs for which an impairment loss was recognized or reversed during the period. The Company will apply the amendments to IAS 36 as of the first quarter of its 2015 fiscal year. Additional information will be disclosed through notes to financial statements.

### Levies (“IFRIC 21”)

The IASB has issued IFRIC 21, an interpretation which provides guidance on when to recognize a liability for a levy imposed by a government, both for levies that are accounted for in accordance with IAS 37, “Provisions, Contingent Liabilities and Contingent Assets,” and those where the timing and amount of the levy is certain. A levy is an outflow of resources embodying economic benefits that is imposed by governments on entities in accordance with legislation. This interpretation is applicable for annual periods beginning on or after January 1, 2014 and must be applied retrospectively. The Company will apply these amendments beginning in the first quarter of fiscal 2015. The Company is assessing the impact of the new interpretation on its consolidated financial statements.

### Financial Instruments: Presentation (“IAS 32”)

The IASB has issued amendments to IAS 32 that clarify its requirements for offsetting financial instruments. These amendments must be applied retrospectively and are effective for annual periods beginning on or after January 1, 2014. The Company will apply these amendments beginning in the first quarter of fiscal 2015. The Company does not expect implementation of these amendments to have a significant impact on its consolidated financial statements.

### Financial Instruments (“IFRS 9”)

The IASB has issued a new standard, IFRS 9, which will ultimately replace IAS 39, “Financial Instruments: Recognition and Measurement” (“IAS 39”). The replacement of IAS 39 is a multi-phase project with the objective of improving and simplifying the reporting for financial instruments. Issuance of IFRS 9 provides guidance on the classification and measurement of financial assets and financial liabilities. Due to the incomplete status of the project, the mandatory effective date of this standard has not been determined. The Company will evaluate the overall impact on its consolidated financial statements when the final standard, including all phases, is issued.

## 6. CASH AND CASH EQUIVALENTS

Cash and cash equivalents consist of the following:

| (thousands of Canadian dollars)  | March 29,<br>2014 | March 30,<br>2013 | April 1,<br>2012 |
|----------------------------------|-------------------|-------------------|------------------|
| Cash                             | 57,098            | 88,268            | 86,199           |
| Restricted cash                  | 3,369             | 470               | 487              |
| Cash equivalents                 | 97,111            | 121,824           | 120,032          |
| <b>Cash and cash equivalents</b> | <b>157,578</b>    | <b>210,562</b>    | <b>206,718</b>   |

Restricted cash represents cash pledged as collateral for letter of credit obligations issued to support the Company’s purchases of offshore merchandise.

## 7. INVENTORIES

The cost of inventories recognized as an expense was \$495.1 million in fiscal 2014 (2013 – \$499.5 million). Inventories consist of the landed cost of goods sold and exclude online shipping costs, inventory shrink and damage reserve, and all vendor support programs. The amount of inventory write-downs as a result of net realizable value lower than cost was \$8.6 million in fiscal 2014 (2013 – \$3.9 million), and there were no reversals of inventory write-downs that were recognized in fiscal 2014 (2013 – nil). The amount of inventory with net realizable value equal to cost was \$1.8 million as at March 29, 2014 (March 30, 2013 – \$1.4 million; April 1, 2012 – \$1.7 million).

## 8. PROPERTY, PLANT AND EQUIPMENT

| (thousands of Canadian dollars)                | Furniture,<br>fixtures and<br>equipment | Computer<br>equipment | Leasehold<br>improvements | Equipment<br>under<br>finance leases | Total          |
|------------------------------------------------|-----------------------------------------|-----------------------|---------------------------|--------------------------------------|----------------|
| <b>Gross carrying amount</b>                   |                                         |                       |                           |                                      |                |
| Balance, March 31, 2012                        | 56,273                                  | 15,756                | 58,773                    | 6,146                                | 136,948        |
| Additions                                      | 4,296                                   | 2,439                 | 2,706                     | 465                                  | 9,906          |
| Transfers/reclassifications                    | (4)                                     | (411)                 | 415                       | –                                    | –              |
| Disposals                                      | (161)                                   | (20)                  | (110)                     | (2,976)                              | (3,267)        |
| Assets with zero net book value                | (5,113)                                 | (3,279)               | (5,015)                   | –                                    | (13,407)       |
| Balance, March 30, 2013                        | 55,291                                  | 14,485                | 56,769                    | 3,635                                | 130,180        |
| Additions                                      | 10,008                                  | 3,451                 | 5,241                     | 137                                  | 18,837         |
| Transfers / reclassifications                  | 16                                      | (465)                 | 449                       | –                                    | –              |
| Disposals                                      | (478)                                   | (217)                 | (208)                     | (948)                                | (1,851)        |
| Assets with zero net book value                | (2,719)                                 | (6,174)               | (7,922)                   | –                                    | (16,815)       |
| <b>Balance, March 29, 2014</b>                 | <b>62,118</b>                           | <b>11,080</b>         | <b>54,329</b>             | <b>2,824</b>                         | <b>130,351</b> |
| <b>Accumulated depreciation and impairment</b> |                                         |                       |                           |                                      |                |
| Balance, March 31, 2012                        | 25,953                                  | 8,895                 | 31,240                    | 3,932                                | 70,020         |
| Depreciation                                   | 5,208                                   | 3,092                 | 8,129                     | 1,209                                | 17,638         |
| Transfers/reclassifications                    | –                                       | 5                     | (5)                       | –                                    | –              |
| Disposals                                      | (130)                                   | (9)                   | (109)                     | (2,976)                              | (3,224)        |
| Net impairment losses and reversals            | –                                       | –                     | 250                       | –                                    | 250            |
| Assets with zero net book value                | (5,113)                                 | (3,279)               | (5,015)                   | –                                    | (13,407)       |
| Balance, March 30, 2013                        | 25,918                                  | 8,704                 | 34,490                    | 2,165                                | 71,277         |
| Depreciation                                   | 5,422                                   | 2,631                 | 7,495                     | 810                                  | 16,358         |
| Transfers / reclassifications                  | –                                       | 5                     | (5)                       | –                                    | –              |
| Disposals                                      | (216)                                   | (197)                 | (188)                     | (948)                                | (1,549)        |
| Net impairment losses and reversals            | 1,007                                   | 60                    | 1,537                     | –                                    | 2,604          |
| Assets with zero net book value                | (2,719)                                 | (6,174)               | (7,922)                   | –                                    | (16,815)       |
| <b>Balance, March 29, 2014</b>                 | <b>29,412</b>                           | <b>5,029</b>          | <b>35,407</b>             | <b>2,027</b>                         | <b>71,875</b>  |
| <b>Net carrying amount</b>                     |                                         |                       |                           |                                      |                |
| April 1, 2012                                  | 30,320                                  | 6,861                 | 27,533                    | 2,214                                | 66,928         |
| March 30, 2013                                 | 29,373                                  | 5,781                 | 22,279                    | 1,470                                | 58,903         |
| <b>March 29, 2014</b>                          | <b>32,706</b>                           | <b>6,051</b>          | <b>18,922</b>             | <b>797</b>                           | <b>58,476</b>  |

Capital assets are assessed for impairment at the CGU level, except for those capital assets which are considered to be corporate assets. As certain corporate assets cannot be allocated on a reasonable and consistent basis to individual CGUs, they are tested for impairment at the corporate level.

A CGU has been defined as an individual retail store, as each store generates cash flows that are largely independent from the cash flows of other stores. CGUs and groups of CGUs are tested for impairment if impairment indicators exist at the reporting date. Recoverable amounts for CGUs being tested are based on value in use, which is calculated from discounted cash flow projections over the remaining lease terms, plus any renewal options where renewal is likely. Corporate asset testing calculates discounted cash flow projections over a five-year period plus a terminal value.

The key assumptions from the value in use calculations are those regarding growth rates and discount rates. The cash flow projections are based on both past and forecasted performance and are extrapolated using long-term growth rates which are calculated separately for each CGU being tested. Average long-term growth rates for impairment testing ranged from 0.0% to 3.0% (2013 – 0.0% to 3.0%). Management's estimate of the discount rate reflects the current market assessment of the time value of money and the risks specific to the Company. The pre-tax and post-tax discount rates used to calculate value in use for store assets were 20.3% and 12.0%, respectively (2013 – 21.9% and 14.0%, respectively).

Impairment indicators were identified during fiscal 2014 for Indigo's retail stores and corporate assets. Accordingly, the Company performed impairment testing, which resulted in the recognition and reversal of impairment losses for Indigo's retail stores only. Impairment losses recognized were \$2.6 million in fiscal 2014 (2013 – \$1.3 million) and are spread across a number of CGUs. The impairment losses relate to CGUs whose carrying amounts exceed their recoverable amounts. In all cases, impairment losses arose due to stores performing at lower-than-expected profitability. There were no capital asset impairment reversals recognized in fiscal 2014 (2013 – \$1.0 million). Impairment reversals arose due to improved store performance and the likelihood of lease term renewals.

## 9. INTANGIBLE ASSETS

| (thousands of Canadian dollars)                | Computer<br>application<br>software | Internal<br>development<br>costs | Total         |
|------------------------------------------------|-------------------------------------|----------------------------------|---------------|
| <b>Gross carrying amount</b>                   |                                     |                                  |               |
| Balance, March 31, 2012                        | 23,929                              | 12,078                           | 36,007        |
| Additions                                      | 5,936                               | 3,685                            | 9,621         |
| Transfers / reclassifications                  | 266                                 | (266)                            | –             |
| Disposals                                      | (5)                                 | (21)                             | (26)          |
| Assets with zero net book value                | (4,890)                             | (2,999)                          | (7,889)       |
| Balance, March 30, 2013                        | 25,236                              | 12,477                           | 37,713        |
| Additions                                      | 6,609                               | 3,937                            | 10,546        |
| Transfers / reclassifications                  | (203)                               | 203                              | –             |
| Disposals                                      | –                                   | –                                | –             |
| Assets with zero net book value                | (4,361)                             | (3,471)                          | (7,832)       |
| <b>Balance, March 29, 2014</b>                 | <b>27,281</b>                       | <b>13,146</b>                    | <b>40,427</b> |
| <b>Accumulated amortization and impairment</b> |                                     |                                  |               |
| Balance, March 31, 2012                        | 8,408                               | 4,789                            | 13,197        |
| Amortization                                   | 6,567                               | 3,678                            | 10,245        |
| Disposals                                      | (2)                                 | (2)                              | (4)           |
| Assets with zero net book value                | (4,890)                             | (2,999)                          | (7,889)       |
| Balance, March 30, 2013                        | 10,083                              | 5,466                            | 15,549        |
| Amortization                                   | 7,071                               | 4,052                            | 11,123        |
| Disposals                                      | –                                   | –                                | –             |
| Assets with zero net book value                | (4,361)                             | (3,471)                          | (7,832)       |
| <b>Balance, March 29, 2014</b>                 | <b>12,793</b>                       | <b>6,047</b>                     | <b>18,840</b> |
| <b>Net carrying amount</b>                     |                                     |                                  |               |
| April 1, 2012                                  | 15,521                              | 7,289                            | 22,810        |
| March 30, 2013                                 | 15,153                              | 7,011                            | 22,164        |
| <b>March 29, 2014</b>                          | <b>14,488</b>                       | <b>7,099</b>                     | <b>21,587</b> |

Impairment testing for intangible assets is performed using the same methodology, CGUs, and groups of CGUs as those used for property, plant and equipment. The key assumptions from the value in use calculations for intangible asset impairment testing are also identical to the key assumptions used for property, plant and equipment testing. Impairment and reversal indicators were identified during fiscal 2014 for Indigo's retail stores. Accordingly, the Company performed impairment and reversal testing but there were no intangible asset impairment losses or reversals in fiscal 2014 (2013 – no impairment losses or reversals).

## 10. INCOME TAXES

Deferred tax assets are recognized to the extent that it is probable that taxable profit will be available against which the deductible temporary differences and the carryforward of unused tax credits and unused tax losses can be utilized. As at March 29, 2014, the Company has recorded \$56.2 million in gross value of deferred tax assets with a valuation allowance of \$11.6 million based on management's best estimate of future taxable income that the Company expects to achieve from reviewing its latest forecast. If the valuation allowance decreases as the result of subsequent events, the previously recognized valuation allowance will be reversed.

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of the Company's deferred tax assets are as follows:

| (thousands of Canadian dollars)                                      | March 29,<br>2014 | March 30,<br>2013 | April 1,<br>2012 |
|----------------------------------------------------------------------|-------------------|-------------------|------------------|
| <b>Deferred tax assets</b>                                           |                   |                   |                  |
| Reserves and allowances                                              | 2,032             | 2,990             | 3,343            |
| Tax loss carryforwards                                               | 23,562            | 22,648            | 25,620           |
| Corporate minimum tax                                                | 1,354             | 1,354             | 1,354            |
| Book amortization in excess of cumulative eligible capital deduction | 249               | 267               | 285              |
| Book amortization in excess of capital cost allowance                | 29,002            | 21,472            | 18,031           |
| <b>Deferred tax assets before valuation allowance</b>                | <b>56,199</b>     | 48,731            | 48,633           |
| Valuation allowance                                                  | (11,595)          | –                 | –                |
| <b>Net deferred tax assets</b>                                       | <b>44,604</b>     | 48,731            | 48,633           |

The Company has recorded deferred tax assets of \$44.6 million pertaining to tax loss carryforwards and other deductible temporary differences based on the probable use of the deferred tax assets.

Significant components of income tax expense (recovery) are as follows:

| (thousands of Canadian dollars)                                                                | 52-week<br>period ended<br>March 29,<br>2014 | 52-week<br>period ended<br>March 30,<br>2013 |
|------------------------------------------------------------------------------------------------|----------------------------------------------|----------------------------------------------|
| Current income tax recovery                                                                    |                                              |                                              |
| Adjustment for prior periods                                                                   | (37)                                         | —                                            |
|                                                                                                | (37)                                         | —                                            |
| Deferred income tax expense (recovery)                                                         |                                              |                                              |
| Origination and reversal of temporary differences                                              | (7,164)                                      | (6,174)                                      |
| Increase in valuation allowance                                                                | 11,595                                       | —                                            |
| Deferred income tax expense relating to utilization of loss carryforwards                      | —                                            | 7,745                                        |
| Adjustment to deferred tax assets resulting from increase<br>in substantively enacted tax rate | (261)                                        | (1,636)                                      |
| Change in tax rates due to change in expected pattern of reversal                              | (44)                                         | (32)                                         |
| Other, net                                                                                     | 1                                            | (1)                                          |
|                                                                                                | 4,127                                        | (98)                                         |
| <b>Total income tax expense (recovery)</b>                                                     | <b>4,090</b>                                 | <b>(98)</b>                                  |

The reconciliation of income taxes computed at statutory income tax rates to the effective income tax rates is as follows:

| (thousands of Canadian dollars)                                                                   | 52-week<br>period ended<br>March 29,<br>2014 | %       | 52-week<br>period ended<br>March 30,<br>2013 | %       |
|---------------------------------------------------------------------------------------------------|----------------------------------------------|---------|----------------------------------------------|---------|
| Earnings (loss) before income taxes                                                               | (26,909)                                     |         | 4,190                                        |         |
| Tax at combined federal and provincial tax rates                                                  | (7,110)                                      | 26.4%   | 1,102                                        | 26.3%   |
| Tax effect of expenses not deductible<br>for income tax purposes                                  | 246                                          | (0.9%)  | 388                                          | 9.3%    |
| Increase in valuation allowance                                                                   | 11,595                                       | (43.1%) | —                                            | —       |
| Adjustment to deferred tax assets<br>resulting from increase in substantively<br>enacted tax rate | (261)                                        | 1.0%    | (1,636)                                      | (39.0%) |
| Change in tax rates due to change<br>in expected pattern of reversal                              | (44)                                         | 0.2%    | (32)                                         | (0.8%)  |
| Other, net                                                                                        | (336)                                        | 1.2%    | 80                                           | 1.9%    |
|                                                                                                   | 4,090                                        | (15.2%) | (98)                                         | (2.3%)  |

The combined federal and provincial income tax rate used for fiscal 2014 is 26.4% (2013 – 26.3%). The rate has increased due to higher provincial income tax rates.

As at March 29, 2014, the Company has combined non-capital loss carryforwards of approximately \$89.1 million for income tax purposes that expire in 2031 if not utilized.



## 11. PROVISIONS

Provisions consist primarily of amounts recorded in respect of decommissioning liabilities, onerous lease arrangements, and legal claims. Activity related to the Company's provisions is as follows:

| (thousands of Canadian dollars) | 52-week<br>period ended<br>March 29,<br>2014 | 52-week<br>period ended<br>March 30,<br>2013 |
|---------------------------------|----------------------------------------------|----------------------------------------------|
| Balance, beginning of period    | 2,246                                        | 692                                          |
| Charged                         | 230                                          | 1,814                                        |
| Utilized / released             | (1,384)                                      | (260)                                        |
| <b>Balance, end of period</b>   | <b>1,092</b>                                 | <b>2,246</b>                                 |

## 12. COMMITMENTS AND CONTINGENCIES

### (a) Commitments

As at March 9, 2014, the Company had the following commitments:

#### (i) Operating lease obligations

The Company had operating lease commitments in respect of its stores, support office premises and certain equipment. The leases expire at various dates between 2014 and 2022, and may be subject to renewal options. Annual store rent consists of a base amount plus, in some cases, additional payments based on store sales. The Company expects to generate \$10.9 million of revenues from subleases related to these operating leases over the next seven fiscal years.

#### (ii) Finance lease obligations

The Company entered into finance lease agreements for certain equipment. The obligations under these finance leases is \$0.8 million as at March 29, 2014 (March 30, 2013 – \$1.5 million; April 1, 2012 – \$2.2 million), of which \$0.6 million (March 30, 2013 – \$0.8 million; April 1, 2012 – \$1.1 million) is included in the current portion of long-term debt. The remainder of the finance lease obligations have been included in the non-current portion of long-term debt.

The Company's minimum contractual obligations due over the next five fiscal years and thereafter are summarized below:

| (millions of Canadian dollars) | Operating leases | Finance leases | Total        |
|--------------------------------|------------------|----------------|--------------|
| 2015                           | 57.6             | 0.6            | 58.2         |
| 2016                           | 49.6             | 0.2            | 49.8         |
| 2017                           | 40.1             | –              | 40.1         |
| 2018                           | 31.8             | –              | 31.8         |
| 2019                           | 19.8             | –              | 19.8         |
| Thereafter                     | 6.9              | –              | 6.9          |
| <b>Total obligations</b>       | <b>205.8</b>     | <b>0.8</b>     | <b>206.6</b> |

### (b) Legal claims

In the normal course of business, the Company becomes involved in various claims and litigation. While the final outcome of such claims and litigation pending as at March 29, 2014 cannot be predicted with certainty, management believes that any such amount would not have a material impact on the Company's financial position or financial performance, except for those amounts which have been recorded as provisions on the Company's consolidated balance sheets.

### 13. SHARE CAPITAL

Share capital consists of the following:

#### Authorized

Unlimited Class A preference shares with no par value, voting, convertible into common shares on a one-for-one basis at the option of the shareholder

Unlimited common shares, voting

|                                           | 52-week period ended<br>March 29, 2014 |                           | 52-week period ended<br>March 30, 2013 |                           |
|-------------------------------------------|----------------------------------------|---------------------------|----------------------------------------|---------------------------|
|                                           | Number of<br>shares                    | Amount<br>C\$ (thousands) | Number of<br>shares                    | Amount<br>C\$ (thousands) |
| Balance, beginning of period              | 25,297,389                             | 203,805                   | 25,238,414                             | 203,373                   |
| Issued during the period                  |                                        |                           |                                        |                           |
| Directors' deferred share units converted | –                                      | –                         | 1,075                                  | 15                        |
| Options exercised                         | 850                                    | 7                         | 57,900                                 | 417                       |
| <b>Balance, end of period</b>             | <b>25,298,239</b>                      | <b>203,812</b>            | <b>25,297,389</b>                      | <b>203,805</b>            |

During fiscal 2014, the Company did not issue any common shares (2013 – 1,075 common shares) in exchange for Directors' deferred share units ("DSUs").

During fiscal 2014, the Company distributed dividends per share of \$0.33 (2013 – \$0.44).

### 14. SHARE-BASED COMPENSATION

The Company has established an employee stock option plan (the "Plan") for key employees. The number of common shares reserved for issuance under the Plan is 3,294,736. Most options granted between May 21, 2002 and March 31, 2012 have a ten-year term and have one fifth of the options granted exercisable one year after the date of issue with the remainder exercisable in equal instalments on the anniversary date over the next four years. Subsequently, most options granted after April 1, 2012 have a five-year term and have one third of the options granted exercisable one year after the date of issue with the remainder exercisable in equal instalments on the anniversary date over the next two years. A small number of options have special vesting schedules that were approved by the Board. Each option is exercisable into one common share of the Company at the price specified in the terms of the option agreement.

During the first quarter of fiscal 2014, the Company offered a one-time cash repurchase to holders of stock options above a specified value. The repurchase was approved by the Board of Directors and by the Company's shareholders; repurchased options were subsequently cancelled by the Company. As part of this transaction, the Company immediately recorded the remaining unamortized expense of \$0.5 million for repurchased options. The Company repurchased and cancelled 870,500 options and made a cash payment to option holders of \$1.0 million.

The Company uses the fair value method of accounting for stock options, which estimates the fair value of the stock options granted on the date of grant, net of estimated forfeitures, and expenses this value over the vesting period. During fiscal 2014, the pre-forfeiture fair value of options granted was \$2.8 million (2013 – \$0.7 million). The weighted average fair value of options issued in fiscal 2014 was \$1.97 per option (2013 – \$1.54 per option).

The fair value of the employee stock options is estimated at the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions during the periods presented:

|                                                 | 52-week<br>period ended<br>March 29,<br>2014 | 52-week<br>period ended<br>March 30,<br>2013 |
|-------------------------------------------------|----------------------------------------------|----------------------------------------------|
| <b>Black-Scholes option pricing assumptions</b> |                                              |                                              |
| Risk-free interest rate                         | 1.3%                                         | 1.2%                                         |
| Expected volatility                             | 35.4%                                        | 37.1%                                        |
| Expected time until exercise                    | 3.0 years                                    | 3.0 years                                    |
| Expected dividend yield                         | 3.4%                                         | 5.0%                                         |
| <b>Other assumptions</b>                        |                                              |                                              |
| Forfeiture rate                                 | 26.7%                                        | 24.9%                                        |

A summary of the status of the Plan and changes during both periods is presented below:

|                                           | 52-week period ended<br>March 29, 2014 |                                              | 52-week period ended<br>March 30, 2013 |                                              |
|-------------------------------------------|----------------------------------------|----------------------------------------------|----------------------------------------|----------------------------------------------|
|                                           | Number<br>#                            | Weighted<br>average<br>exercise price<br>C\$ | Number<br>#                            | Weighted<br>average<br>exercise price<br>C\$ |
| Outstanding options, beginning of period  | 1,627,000                              | 12.64                                        | 1,372,400                              | 13.64                                        |
| Granted                                   | 1,401,000                              | 10.25                                        | 430,000                                | 8.63                                         |
| Forfeited / repurchased                   | (1,347,000)                            | 13.77                                        | (117,500)                              | 12.97                                        |
| Expired                                   | (4,000)                                | 4.45                                         | —                                      | —                                            |
| Exercised                                 | (850)                                  | 8.00                                         | (57,900)                               | 5.74                                         |
| <b>Outstanding options, end of period</b> | <b>1,676,150</b>                       | <b>9.75</b>                                  | <b>1,627,000</b>                       | <b>12.64</b>                                 |
| <b>Options exercisable, end of period</b> | <b>245,900</b>                         | <b>8.88</b>                                  | <b>722,500</b>                         | <b>14.52</b>                                 |

#### Options outstanding and exercisable

|                                    | March 29, 2014 |                                              |                                                                    |             |                                              |
|------------------------------------|----------------|----------------------------------------------|--------------------------------------------------------------------|-------------|----------------------------------------------|
|                                    | Outstanding    |                                              |                                                                    | Exercisable |                                              |
| Range of<br>exercise prices<br>C\$ | Number<br>#    | Weighted<br>average<br>exercise price<br>C\$ | Weighted<br>average<br>remaining<br>contractual life<br>(in years) | Number<br># | Weighted<br>average<br>exercise price<br>C\$ |
| 7.20 – 8.06                        | 313,650        | 7.74                                         | 3.1                                                                | 143,700     | 7.61                                         |
| 8.07 – 9.72                        | 366,500        | 8.36                                         | 4.3                                                                | 43,900      | 8.66                                         |
| 9.73 – 10.80                       | 910,000        | 10.70                                        | 4.3                                                                | 23,800      | 10.70                                        |
| 10.81 – 14.05                      | 78,500         | 12.79                                        | 6.9                                                                | 30,000      | 12.88                                        |
| 14.06 – 15.21                      | 7,500          | 15.21                                        | 6.6                                                                | 4,500       | 15.21                                        |
| 7.20 – 15.21                       | 1,676,150      | 9.75                                         | 4.2                                                                | 245,900     | 8.88                                         |

## Directors' compensation

The Company has established a Directors' Deferred Share Unit Plan ("DSU Plan"). Under the DSU Plan, Directors receive their annual retainer fees and other Board-related compensation in the form of deferred share units ("DSUs"). The number of shares reserved for issuance under this plan is 500,000. The Company issued 43,757 DSUs with a value of \$0.4 million during fiscal 2014 (2013 – 46,409 DSUs with a value of \$0.4 million). The number of DSUs to be issued to each Director is based on a set fee schedule. The grant date fair value of the outstanding DSUs as at March 29, 2014 was \$3.3 million (March 30, 2013 – \$2.9 million; April 1, 2012 – \$2.5 million) and was recorded in contributed surplus. The fair value of DSUs is equal to the traded price of the Company's common shares on grant date.

## 15. SUPPLEMENTARY OPERATING INFORMATION

Supplemental product line revenue information:

|                                  | 52-week<br>period ended<br>March 29,<br>2014 | 52-week<br>period ended<br>March 30,<br>2013 |
|----------------------------------|----------------------------------------------|----------------------------------------------|
| Print <sup>1</sup>               | 585,239                                      | 613,626                                      |
| General merchandise <sup>2</sup> | 240,237                                      | 207,520                                      |
| eReading <sup>3</sup>            | 24,743                                       | 35,898                                       |
| Other <sup>4</sup>               | 17,449                                       | 21,741                                       |
| <b>Total</b>                     | <b>867,668</b>                               | <b>878,785</b>                               |

1 Includes books, calendars, magazines, and newspapers.

2 Includes lifestyle, paper, toys, music, DVDs, and electronics.

3 Includes eReaders, eReader accessories, and Kobo revenue share.

4 Includes cafés, irewards, gift card breakage, and Plum breakage.

Supplemental operating and administrative expenses information:

| (thousands of Canadian dollars)        | 52-week<br>period ended<br>March 29,<br>2014 | 52-week<br>period ended<br>March 30,<br>2013 |
|----------------------------------------|----------------------------------------------|----------------------------------------------|
| Wages, salaries and bonuses            | 157,904                                      | 150,469                                      |
| Short-term benefits expense            | 18,321                                       | 17,598                                       |
| Termination benefits expense           | 4,945                                        | 3,482                                        |
| Retirement benefits expense            | 1,286                                        | 1,224                                        |
| Stock-based compensation               | 1,242                                        | 743                                          |
| <b>Total employee benefits expense</b> | <b>183,698</b>                               | <b>173,516</b>                               |

Termination benefits arise when the Company terminates certain employment agreements.

Minimum lease payments recognized as an expense during fiscal 2014 were \$63.5 million (2013 – \$62.7 million). Contingent rents recognized as an expense during fiscal 2014 were \$1.0 million (2013 – \$1.3 million).

## 16. EARNINGS PER SHARE

Earnings per share is calculated based on the weighted average number of common shares outstanding during the period. In calculating diluted earnings per share amounts under the treasury stock method, the numerator remains unchanged from the basic earnings per share calculations as the assumed exercise of the Company's stock options do not result in an adjustment to net earnings. The reconciliation of the denominator in calculating diluted earnings per share amounts for the periods presented is as follows:

| (thousands of shares)                                         | 52-week<br>period ended<br>March 29,<br>2014 | 52-week<br>period ended<br>March 30,<br>2013 |
|---------------------------------------------------------------|----------------------------------------------|----------------------------------------------|
| Weighted average number of common shares outstanding, basic   | 25,601                                       | 25,529                                       |
| Effect of dilutive securities                                 |                                              |                                              |
| Stock options                                                 | 47                                           | 34                                           |
| Weighted average number of common shares outstanding, diluted | 25,648                                       | 25,563                                       |

As at March 29, 2014, 1,246,000 (March 30, 2013 – 1,505,500; April 1, 2012 – 1,293,000) options could potentially dilute basic earnings per share in the future, but were excluded from the computation of diluted net earnings per common share in the current period as they were anti-dilutive.

## 17. STATEMENTS OF CASH FLOWS

Supplemental cash flow information:

| (thousands of Canadian dollars)                  | 52-week<br>period ended<br>March 29,<br>2014 | 52-week<br>period ended<br>March 30,<br>2013 |
|--------------------------------------------------|----------------------------------------------|----------------------------------------------|
| Net change in non-cash working capital balances: |                                              |                                              |
| Accounts receivable                              | 1,544                                        | 5,494                                        |
| Inventories                                      | (2,446)                                      | 12,666                                       |
| Income taxes recoverable                         | (37)                                         | (86)                                         |
| Prepaid expenses                                 | (1,031)                                      | (461)                                        |
| Accounts payable and accrued liabilities         | (14,857)                                     | (25,035)                                     |
| Unredeemed gift card liability                   | (342)                                        | 4,458                                        |
| Provisions                                       | (1,154)                                      | 1,554                                        |
| Deferred revenue                                 | (873)                                        | 2,499                                        |
|                                                  | (19,196)                                     | 1,089                                        |
| Assets acquired under finance leases             | 137                                          | 465                                          |

## 18. CAPITAL MANAGEMENT

The Company's main objectives when managing capital are to safeguard its ability to continue as a going concern while maintaining adequate financial flexibility to invest in new business opportunities that will provide attractive returns to shareholders. The primary activities engaged by the Company to generate attractive returns include construction and related leasehold improvements of stores, the development of new business concepts, and investment in information technology and distribution capacity to support the online and retail networks. The Company's main sources of capital are its current cash position, cash flows generated from operations, and long-term debt. On June 12, 2013, the Company cancelled its revolving line of credit. Cash flow is used to fund working capital needs, capital expenditures and debt service requirements.

In order to maintain sufficient capital resources to fund the Company's transformation, management and the Company's Board of Directors decided to suspend quarterly dividend payments beyond December 3, 2013. The Company primarily manages its capital by monitoring its available cash balance to ensure that sufficient funds are available for long-term debt and interest payments over the next year.

The following table summarizes selected capital structure information for the Company:

| (thousands of Canadian dollars)       | March 29,<br>2014 | March 30,<br>2013 | April 1,<br>2012 |
|---------------------------------------|-------------------|-------------------|------------------|
| Current portion of long-term debt     | 584               | 773               | 1,060            |
| Long-term debt                        | 227               | 705               | 1,141            |
| Total debt                            | 811               | 1,478             | 2,201            |
| Total equity                          | 311,674           | 350,322           | 355,632          |
| <b>Total capital under management</b> | <b>312,485</b>    | <b>351,800</b>    | <b>357,833</b>   |

## 19. FINANCIAL RISK MANAGEMENT

The Company's activities expose it to a variety of financial risks, including risks related to foreign exchange, interest rate, credit, and liquidity.

### Foreign exchange risk

The Company's foreign exchange risk is largely limited to currency fluctuations between the Canadian and U.S. dollars. Decreases in the value of the Canadian dollar relative to the U.S. dollar could negatively impact net earnings since the purchase price of some of the Company's products are negotiated with vendors in U.S. dollars, while the retail price to customers is set in Canadian dollars. The Company did not use any forward contracts to manage foreign exchange risk in fiscal 2014 (2013 – no forward contracts).

As the Company expands its product selection to include a greater number of non-book items, foreign exchange risk has increased due to more purchases being denominated in U.S. dollars. A 10% appreciation or depreciation in the U.S. and Canadian dollar exchange rates during fiscal 2014 would have had an impact of \$3.9 million (2013 – \$3.9 million) on net earnings (loss) and comprehensive earnings (loss).

In fiscal 2014, the effect of foreign currency translation on net earnings (loss) and comprehensive earnings (loss) was a loss of \$0.4 million (2013 – gain of \$0.2 million).

### Interest rate risk

On June 12, 2013, the Company cancelled its revolving line of credit. As such, the Company's interest rate risk is largely limited to its long-term debt, for which interest rates are fixed at the time a contract is finalized. The Company's interest income is also sensitive to fluctuations in Canadian interest rates, which affect the interest earned on the Company's cash and cash equivalents. The Company has minimal interest rate risk and does not use any interest rate swaps to manage its risk.

### Credit risk

The Company is exposed to credit risk resulting from the possibility that counterparties may default on their financial obligations to the Company. The Company's maximum exposure to credit risk at the reporting date is equal to the carrying value of accounts receivable. Accounts receivable primarily consists of receivables from retail customers who pay by credit card, recoveries of credits from suppliers for returned or damaged products, and receivables from other companies for sales of products, gift cards and other services. Credit card payments have minimal credit risk and the limited number of corporate receivables is closely monitored.

## Liquidity risk

Liquidity risk is the risk that the Company will be unable to meet its obligations relating to its financial liabilities. The Company manages liquidity risk by preparing and monitoring cash flow budgets and forecasts to ensure that the Company has sufficient funds to meet its financial obligations and fund new business opportunities or other unanticipated requirements as they arise.

The contractual maturities of the Company's current and long-term liabilities as at March 29, 2014 are as follows:

| (thousands of Canadian dollars)          | Payments due in the next 90 days | Payments due between 90 days and less than a year | Payments due after 1 year | Total          |
|------------------------------------------|----------------------------------|---------------------------------------------------|---------------------------|----------------|
| Accounts payable and accrued liabilities | 109,671                          | 26,757                                            | —                         | 136,428        |
| Unredeemed gift card liability           | 46,827                           | —                                                 | —                         | 46,827         |
| Provisions                               | —                                | 928                                               | —                         | 928            |
| Current portion of long-term debt        | —                                | 584                                               | —                         | 584            |
| Long-term accrued liabilities            | —                                | —                                                 | 2,896                     | 2,896          |
| Long-term provisions                     | —                                | —                                                 | 164                       | 164            |
| Long-term debt                           | —                                | —                                                 | 227                       | 227            |
| <b>Total</b>                             | <b>156,498</b>                   | <b>28,269</b>                                     | <b>3,287</b>              | <b>188,054</b> |

## 20. EQUITY INVESTMENT

The Company holds a 50% equity ownership in its associate, Calendar Club, to sell calendars, games, and gifts through seasonal kiosks and year-round stores in Canada. The Company uses the equity method of accounting to record Calendar Club results. In fiscal 2014, the Company received \$1.2 million (2013 – \$1.3 million) of distributions from Calendar Club.

The following tables represent financial information for Calendar Club along with the Company's share therein:

| (thousands of Canadian dollars) | Total          |                |               | Company's share |                |               |
|---------------------------------|----------------|----------------|---------------|-----------------|----------------|---------------|
|                                 | March 29, 2014 | March 30, 2013 | April 1, 2012 | March 29, 2014  | March 30, 2013 | April 1, 2012 |
| Cash and cash equivalents       | 1,185          | 2,278          | 1,766         | 593             | 1,139          | 883           |
| Total current assets            | 2,565          | 3,316          | 2,798         | 1,283           | 1,658          | 1,399         |
| Total long-term assets          | 658            | 831            | 1,071         | 329             | 416            | 536           |
| Total current liabilities       | 2,027          | 2,212          | 1,948         | 1,014           | 1,106          | 974           |

| (thousands of Canadian dollars) | Total                               |                                     | Company's share                     |                                     |
|---------------------------------|-------------------------------------|-------------------------------------|-------------------------------------|-------------------------------------|
|                                 | 52-week period ended March 29, 2014 | 52-week period ended March 30, 2013 | 52-week period ended March 29, 2014 | 52-week period ended March 30, 2013 |
| Revenue                         | 31,003                              | 30,543                              | 15,502                              | 15,272                              |
| Expenses                        | (29,425)                            | (27,914)                            | (14,713)                            | (13,957)                            |
| <b>Net earnings</b>             | <b>1,578</b>                        | <b>2,629</b>                        | <b>789</b>                          | <b>1,315</b>                        |

Changes in the carrying amount of the investment were as follows:

| (thousands of Canadian dollars)  | Carrying value |
|----------------------------------|----------------|
| Balance, March 31, 2012          | 961            |
| Equity income from Calendar Club | 1,315          |
| Distributions from Calendar Club | (1,308)        |
| Balance, March 30, 2013          | 968            |
| Equity income from Calendar Club | 789            |
| Distributions from Calendar Club | (1,159)        |
| <b>Balance, March 29, 2014</b>   | <b>598</b>     |

## 21. RELATED PARTY TRANSACTIONS

The Company's related parties include its key management personnel, shareholders, defined contribution retirement plan, equity investment in Calendar Club, and subsidiary. Unless otherwise stated, none of the transactions incorporate special terms and conditions and no guarantees were given or received. Outstanding balances are usually settled in cash.

### Transactions with key management personnel

Key management of the Company includes members of the Board of Directors as well as members of the Executive Committee. Key management personnel remuneration includes the following expenses:

| (thousands of Canadian dollars)       | 52-week<br>period ended<br>March 29,<br>2014 | 52-week<br>period ended<br>March 30,<br>2013 |
|---------------------------------------|----------------------------------------------|----------------------------------------------|
| Wages, salaries, bonus and consulting | 4,654                                        | 4,085                                        |
| Short-term benefits expense           | 242                                          | 246                                          |
| Termination benefits expense          | 457                                          | 450                                          |
| Retirement benefits expense           | 60                                           | 66                                           |
| Stock-based compensation              | 789                                          | 443                                          |
| Directors' compensation               | 425                                          | 446                                          |
| <b>Total remuneration</b>             | <b>6,627</b>                                 | <b>5,736</b>                                 |

### Transactions with shareholders

During fiscal 2014, Indigo purchased goods and services from companies in which Mr. Gerald W. Schwartz, who is the controlling shareholder of Indigo, holds a controlling or significant interest. In fiscal 2014, Indigo paid \$5.3 million for these goods and services (2013 – \$0.2 million). As at March 29, 2014, Indigo had less than \$0.1 million payable to these companies under standard payment terms and \$2.8 million of restricted cash pledged as collateral for letter of credit obligations issued to support the Company's purchases of merchandise from these companies (March 30, 2013 and April 1, 2012 – no amounts payable and no restricted cash). All transactions were in the normal course of business for both Indigo and the related companies.

### Transactions with defined contribution retirement plan

The Company's transactions with the defined contribution retirement plan include contributions paid to the retirement plan as disclosed in note 15. The Company has not entered into other transactions with the retirement plan.



**Transactions with associate**

The Company's associate, Calendar Club, is a seasonal operation which is dependent on the December holiday sales season to generate revenues. During the year, the Company loans cash to Calendar Club for working capital requirements and Calendar Club repays the loans once profits are generated in the third quarter. The net amount of these transactions for fiscal 2014 was nil (2013 – nil), as Calendar Club has repaid all loans as at March 29, 2014. In fiscal 2013, Calendar Club repaid an outstanding \$0.2 million note payable to Indigo.

**22. COMPARATIVE CONSOLIDATED FINANCIAL STATEMENTS**

The comparative consolidated financial statements have been reclassified from statements previously presented to conform to the presentation of the current year audited consolidated financial statements.

# Corporate Governance Policies

A presentation of Indigo's corporate governance policies is included in the Management Information Circular which is mailed to all shareholders. If you would like to receive a copy of this information, please contact Investor Relations at Indigo.

# Executive Management and Board of Directors

## EXECUTIVE MANAGEMENT

Heather Reisman  
*Chair & Chief Executive Officer*

Kay Brekken  
*Chief Financial Officer*

Kirsten Chapman  
*Chief Marketing Officer &  
Executive Vice President E-Commerce*

Laura Dunne  
*Senior Vice President, Human Resources &  
Organizational Development*

Kathleen Flynn  
*General Counsel & Corporate Secretary*

Joyce Gray  
*Chief Operating Officer*

Tod Morehead  
*Executive Vice President &  
Group General Merchandise Manager*

Mike Mortson  
*Executive Vice President, Supply Chain*

Sumit Oberai  
*Executive Vice President, Technology,  
Loyalty & Strategy*

## BOARD OF DIRECTORS

Frank Clegg  
*Volunteer Chairman & Chief Executive Officer*  
C4ST (Canadians for Safe Technology)

Jonathan Deitcher  
*Investment Advisor*  
RBC Dominion Securities Inc.

Mitchell Goldhar  
*President & Chief Executive Officer*  
SmartCentres

James Hall  
*Vice President*  
Callidus Capital Corporation  
and  
*President & Chief Executive Officer*  
James Hall Advisors Inc.

Michael Kirby  
*Corporate Director*  
Chair of Partners for Mental Health

Anne Marie O'Donovan  
*Executive Vice President & Chief Administration Officer,*  
*Global Banking & Markets*  
Scotiabank

Heather Reisman  
*Chair & Chief Executive Officer*  
Indigo Books & Music Inc.

Joel Silver  
*Managing Partner*  
Trilogy Growth

Gerald Schwartz  
*Chairman & Chief Executive Officer*  
Onex Corporation

# Five Year Summary of Financial Information

| For the years ended<br>(millions of Canadian dollars, except share and per share data) | IFRS              |                   |                   |                  | Canadian GAAP    |
|----------------------------------------------------------------------------------------|-------------------|-------------------|-------------------|------------------|------------------|
|                                                                                        | March 29,<br>2014 | March 30,<br>2013 | March 31,<br>2012 | April 2,<br>2011 | April 3,<br>2010 |
| <b>SELECTED STATEMENTS OF EARNINGS INFORMATION</b>                                     |                   |                   |                   |                  |                  |
| Revenues                                                                               |                   |                   |                   |                  |                  |
| Superstores                                                                            | 617.8             | 626.6             | 656.5             | 667.6            | 670.5            |
| Small format stores                                                                    | 127.4             | 137.6             | 145.2             | 149.4            | 159.3            |
| Online                                                                                 | 102.0             | 91.9              | 91.3              | 90.6             | 92.2             |
| Other                                                                                  | 20.5              | 22.7              | 27.2              | 33.9             | 46.1             |
| Total revenues                                                                         | 867.7             | 878.8             | 920.2             | 941.5            | 968.1            |
| Adjusted EBITDA <sup>1</sup>                                                           | 0.1               | 28.5              | 25.0              | 54.8             | 76.1             |
| Earnings (loss) before income taxes                                                    | (26.9)            | 4.2               | (29.3)            | 25.8             | 49.8             |
| Net earnings (loss) and comprehensive earnings (loss)                                  | (31.0)            | 4.3               | 66.2              | (19.4)           | 34.9             |
| Dividends per share                                                                    | \$0.33            | \$0.44            | \$0.44            | \$0.44           | \$0.40           |
| Net earnings (loss) per common share                                                   | \$(1.21)          | \$0.17            | \$3.68            | \$(0.23)         | \$1.42           |
| <b>SELECTED BALANCE SHEET INFORMATION</b>                                              |                   |                   |                   |                  |                  |
| Working capital                                                                        | 189.7             | 224.3             | 223.7             | 101.1            | 106.4            |
| Total assets                                                                           | 512.6             | 569.1             | 591.8             | 510.3            | 519.8            |
| Long-term debt (including current portion)                                             | 0.8               | 1.5               | 2.2               | 3.3              | 3.0              |
| Total equity                                                                           | 311.7             | 350.3             | 355.6             | 267.4            | 259.0            |
| Weighted average number of shares outstanding                                          | 25,601,260        | 25,529,035        | 25,201,127        | 24,874,199       | 24,549,622       |
| Common shares outstanding at end of period                                             | 25,298,239        | 25,297,389        | 25,238,414        | 25,140,540       | 24,742,915       |
| <b>STORE OPERATING STATISTICS</b>                                                      |                   |                   |                   |                  |                  |
| <b>Number of stores at end of period</b>                                               |                   |                   |                   |                  |                  |
| Superstores                                                                            | 95                | 97                | 97                | 97               | 96               |
| Small format stores                                                                    | 131               | 134               | 143               | 150              | 151              |
| <b>Selling square footage at end of period</b><br>(in thousands)                       |                   |                   |                   |                  |                  |
| Superstores                                                                            | 2,200             | 2,235             | 2,235             | 2,235            | 2,217            |
| Small format stores                                                                    | 370               | 379               | 400               | 413              | 417              |
| <b>Comparable store sales</b>                                                          |                   |                   |                   |                  |                  |
| Superstores                                                                            | (0.9%)            | (4.6%)            | (1.9%)            | (0.3%)           | 0.6%             |
| Small format stores                                                                    | (5.0%)            | (2.4%)            | (0.8%)            | (3.2%)           | (2.2%)           |
| <b>Sales per selling square foot</b>                                                   |                   |                   |                   |                  |                  |
| Superstores                                                                            | 281               | 280               | 294               | 299              | 302              |
| Small format stores                                                                    | 344               | 362               | 363               | 362              | 382              |

1 Earnings before interest, taxes, depreciation, amortization, impairment, and equity investment. Also see "Non-IFRS Financial Measures".

# Investor Information

## SUPPORT OFFICE

468 King Street West  
Suite 500  
Toronto, Ontario  
Canada M5V 1L8  
Telephone (416) 364-4499  
Fax (416) 364-0355  
[www.chapters.indigo.ca/investor-relations/](http://www.chapters.indigo.ca/investor-relations/)

## INVESTOR CONTACT

Kay Brekken  
*Chief Financial Officer*  
Telephone (416) 646-8945

## MEDIA CONTACT

Janet Eger  
*Vice President, Public Affairs*  
Telephone (416) 342-8561

## STOCK LISTING

Toronto Stock Exchange

## TRADING SYMBOL

IDG

## TRANSFER AGENT AND REGISTRAR

CIBC Mellon Trust Company  
P.O. Box 700, Station B  
Montreal, Quebec  
Canada H3B 3K3  
Telephone (Toll Free) 1-800-387-0825  
(Toronto) (416) 682-3860

## AUDITORS

Ernst & Young LLP  
Ernst & Young Tower  
Toronto-Dominion Centre  
Toronto, Ontario  
Canada M5K 1J7

## ANNUAL MEETING

The Annual Meeting represents an opportunity for shareholders to review and participate in the management of the Company as well as meet with its directors and officers.

Indigo's Annual Meeting will be held on  
June 26, 2014 at 10:00 a.m. at  
Torys LLP  
79 Wellington Street West, 33<sup>rd</sup> Floor  
Toronto, Ontario  
Canada M5K 1N2

Shareholders are encouraged to attend and guests are welcome.

Une traduction française de ce document est disponible sur demande.

# Indigo's Commitment to Communities Across Canada

Since 2004, Indigo has enriched the lives of thousands of Canadian children by investing over \$15.5 million in more than 1,500 schools through the Indigo Love of Reading Foundation. This year, the Foundation's annual Literacy Fund committed another \$1.5 million to 20 schools, raising its total investment to \$13.5 million in 130 elementary schools across Canada. The Foundation's grassroots Adopt a School program invested over \$500,000 into more than 190 schools this year, bringing Adopt a School's fundraising support to \$2.0 million for over 1,400 schools in just five years.

In addition to the Foundation's work, Indigo hosts FUNdraiser programs which support schools and other community groups in raising money for educational and extracurricular activities. Through both in-store events and online campaigns, Indigo has helped more than 265 not-for-profit organizations raise over \$145,000.

Expanding on this financial support, our Visual Merchandising and Retail Construction teams used their expertise to give Ogden Junior Public School, Home Office's adopted school, a library makeover. Thanks to vendor support and the experience of these teams, the library was transformed in one day with new tables, chairs and decorations to make it a welcoming and happy space for students.

For more information on Indigo's commitment to community visit [chapters.indigo.ca/fundraising](http://chapters.indigo.ca/fundraising).

## Our Beliefs

- We exist to add joy to customers' lives – when they interact with us and, when they interact with our products.
- Each and every person in the company should understand how his or her work contributes to the creation of joyful customer moments.
- We owe to each other, irrespective of role or position, the same level of respect and caring as we would show to a valued friend.
- We have a responsibility to create an environment where each individual is inspired to perform to the best of his or her ability.
- Passion, creativity and innovation are the keys to sustainable growth and profitability. Each individual working at Indigo should reflect this in his or her work. Our role, as a company, is to encourage and reward the demonstration of these attributes.
- We have a responsibility to give back to the communities in which we operate.

