THIRD QUARTER REPORT

FOR THE 13 & 39-WEEK PERIODS ENDED DECEMBER 26, 2015

"Creativity has got to start with humanity"

— *Marilyn Monroe*

Indigo

Enrich your life™

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Management's Discussion and Analysis

The following Management's Discussion and Analysis ("MD&A") is prepared as at February 2, 2016 and is based primarily on the unaudited interim condensed consolidated financial statements of Indigo Books & Music Inc. (the "Company" or "Indigo") for the 13 and 39-week periods ended December 26, 2015 and December 27, 2014. The Company's unaudited interim condensed consolidated financial statements and accompanying notes are reported in Canadian dollars and have been prepared in accordance with International Accounting Standard ("IAS") 34, "Interim Financial Reporting." The same accounting policies and methods of computation as those used in the preparation of the fiscal 2015 Annual Report were followed in the preparation of these unaudited interim condensed consolidated financial statements.

These unaudited interim condensed consolidated financial statements do not contain all disclosures required by International Financial Reporting Standards ("IFRS") for annual financial statements. This MD&A should be read in conjunction with the unaudited interim condensed consolidated financial statements and notes contained in this Quarterly Report, the audited annual consolidated financial statements and accompanying notes for the 52-week period ended March 28, 2015 and the MD&A included in the Company's fiscal 2015 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*.

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 February 2, 2016, the Company operated 90 superstores under the banners *Chapters* and *Indigo* and 126 small format stores under the banners *Coles*, *Indigospirit*, *SmithBooks*, and *The Book Company*. During the third quarter of fiscal 2016, the Company had no new store openings or closures. 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 the third quarter of fiscal 2016 was 25,953,545 compared to 25,743,234 last year. As at February 2, 2016, the number of outstanding common shares was 25,676,076 with a book value of $207.9 million. The number of common shares reserved for issuance under the employee stock option plan is 3,351,411 as at February 2, 2016. As at December 26, 2015, there were 1,926,205 stock options outstanding of which 664,825 were exercisable.

Results of Operations

The following table summarizes the Company's consolidated results of operations 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.

(millions of Canadian dollars)	**13-week period ended December 26, 2015**	**% Revenue**	13-week period ended December 27, 2014	% Revenue	**39-week period ended December 26, 2015**	**% Revenue**	39-week period ended December 27, 2014	% Revenue
Revenue	**383.2**	**100.0**	339.4	100.0	**773.8**	**100.0**	709.2	100.0
Cost of sales	**(214.1)**	**55.9**	(191.7)	56.5	**(429.7)**	**55.5**	(398.3)	56.2
Cost of operations	**(85.7)**	**22.4**	(80.4)	23.7	**(219.7)**	**28.4**	(213.6)	30.1
Selling, administrative, and other expenses	**(30.9)**	**8.1**	(26.5)	7.8	**(70.3)**	**9.1**	(66.0)	9.3
Adjusted EBITDA[1]	**52.5**	**13.7**	40.8	12.0	**54.1**	**7.0**	31.3	4.4

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

Revenue Increased Significantly Despite Operating Five Fewer Stores

Total consolidated revenue for the 13-week period ended December 26, 2015 increased $43.8 million or 12.9% to $383.2 million from $339.4 million for the same period last year. The increase in revenue was driven by continued growth in all sales channels across a number of product categories and by more effective use of promotional discounting compared to last year. General merchandise sales continued to show double-digit growth, with units and average prices increasing in all categories. The toy business also benefited from the opening of two new American Girl®[1] specialty boutiques in the current quarter. Book sales continued to be strong, with high single-digit growth in the quarter due to a combination of popular titles and a growing trend for adult colouring books.

Comparable store sales for the third quarter increased 15.5% in superstores and increased 13.4% in small format stores. The increase in comparable store sales was driven by the reasons mentioned above. Comparable store sales are defined as sales generated by stores that have been open for more than 12 months

1 American Girl is a registered trademark of American Girl, LLC.

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 December 26, 2015, the Company operated one less superstore and four fewer small format stores compared to December 27, 2014.

Online sales increased by $8.2 million or 17.9% to $54.1 million for the 13-week period ended December 26, 2015 compared to $45.9 million for the same period last year. Online sales continued to experience growth in books and double-digit increases in general merchandise. This growth was driven by higher traffic and conversion rates as a result of successful promotional campaigns and a continued focus on gaining multi-channel customers.

Revenue from other sources includes revenue generated through cafés, irewards card sales, revenue from unredeemed gift cards ("gift card breakage"), revenue from unredeemed plum points ("Plum breakage"), corporate sales, and revenue-sharing with Kobo. Revenue from other sources decreased $1.2 million or 15.4% to $6.6 million for the 13-week period ended December 26, 2015 compared to $7.8 million for the same period last year primarily as a result of lower gift card breakage. The $0.6 million decrease in gift card breakage was driven by changes in historical redemption rates. Consistent with the Company's expectations, irewards card sales also decreased by $0.3 million as members moved to the free plum rewards program, and revenue sharing from Kobo decreased by $0.2 million as a result of slowing eBook growth.

On a fiscal year-to-date basis, total consolidated revenue increased by $64.6 million or 9.1% to $773.8 million compared to $709.2 million for the same period last year for the same reasons above. During the second quarter of fiscal 2016, the Company launched several new initiatives, including the ability to earn and redeem points both online and through Indigo's mobile app for members of its free plum rewards program. The Company also implemented a number of significant renovations in retail locations throughout the year. Year-to-date comparable store sales increased 12.3% for superstores and increased 9.7% in small format stores for the same reasons discussed above.

Revenue by channel is highlighted below:

(millions of Canadian dollars)	**13-week period ended December 26, 2015**	13-week period ended December 27, 2014	% increase (decrease)	Comparable store sales % increase (decrease)
Superstores	**266.1**	234.5	13.5	15.5
Small format stores	**56.4**	51.2	10.2	13.4
Online (including store kiosks)	**54.1**	45.9	17.9	N/A
Other	**6.6**	7.8	(15.4)	N/A
	383.2	339.4	12.9	15.1

Revenue by product line is as follows:

	13-week period ended December 26, 2015	13-week period ended December 27, 2014	**39-week period ended December 26, 2015**	39-week period ended December 27, 2014
Print[1]	**57.8%**	61.3%	**61.6%**	64.7%
General merchandise[2]	**39.5%**	34.8%	**34.9%**	30.8%
eReading[3]	**1.2%**	2.0%	**1.5%**	2.0%
Other[4]	**1.5%**	1.9%	**2.0%**	2.5%
Total	**100.0%**	100.0%	**100.0%**	100.0%

1 Includes books, calendars, magazines, newspapers, and shipping revenue.
2 Includes lifestyle, paper, toys, music, DVDs, electronics, and shipping revenue.
3 Includes eReaders, eReader accessories, Kobo revenue share, and shipping revenue.
4 Includes cafés, irewards, gift card breakage, Plum breakage, and corporate sales.

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

	Superstores		Small format stores	
(millions of Canadian dollars)	**13-week period ended December 26, 2015**	13-week period ended December 27, 2014	**13-week period ended December 26, 2015**	13-week period ended December 27, 2014
Total revenue	**266.1**	234.5	**56.4**	51.2
Adjustments for stores not in both fiscal periods	**(8.3)**	(11.3)	**(0.7)**	(2.1)
Comparable store sales	**257.8**	223.2	**55.7**	49.1

Cost of Sales (as a Percent of Revenue) Improved Compared to Last Year
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 increased $22.4 million to $214.1 million for the 13-week period ended December 26, 2015 compared to $191.7 million for the same period last year. The increase was driven by higher sales volumes, as discussed above. Cost of sales as a percent of total revenue decreased by 0.6% to 55.9% this period compared to 56.5% for the same period last year. This percentage improvement was mainly driven by higher vendor support and improved inventory management.

On a fiscal year-to-date basis, cost of sales increased $31.4 million to $429.7 million compared to $398.3 million in the same period last year. Margin rate improvements were driven by greater sell-through of full-priced goods and more effective promotional discounting. Year-to-date cost of sales as a percent of total revenue decreased by 0.7% to 55.5% this period compared to 56.2% for the same period last year.

Cost of Operations (as a Percent of Revenue) Improved Compared to Last Year

Cost of operations includes all store, store support, online, and distribution centre costs. Cost of operations increased $5.3 million to $85.7 million for the 13-week period ended December 26, 2015 compared to $80.4 million for the same period last year. Store operating costs increased by $2.8 million, driven by higher labour costs associated with increased volumes. As a result of higher sales volumes, online costs also increased by $1.3 million and retail distribution costs were $0.7 million higher. As a percent of total revenue, cost of operations decreased by 1.3% to 22.4% this period compared to 23.7% for the same period last year.

On a fiscal year-to-date basis, cost of operations increased $6.1 million to $219.7 million compared to $213.6 million in the same period last year. Online costs, store operating costs, and retail distribution costs have all increased for the same reasons discussed above. Compared to the same period last year, online costs were $2.2 million higher, store operating costs increased by $2.0 million, and retail distribution costs were $1.4 million higher. Year-to-date cost of operations as a percent of total revenue decreased 1.7% to 28.4% compared to 30.1% in the same period last year.

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

Selling, administrative, and other expenses include marketing, head office costs, and operating expenses associated with the Company's transformation. For the 13-week period ended December 26, 2015, these expenses increased $4.4 million to $30.9 million, compared to $26.5 million for the same period last year. Head office costs increased by $2.0 million, driven by higher bonus accruals based on year-to-date performance compared to last year. Creative and marketing expenses increased by $1.3 million due to an increase in advertising campaigns compared to the same period last year. Operating expenditures related to strategic projects were higher by $0.6 million compared to the same period last year as the Company continues to implement transformational changes across its retail locations and focus on productivity initiatives. The Company also had a foreign exchange gain of $0.1 million in the third quarter of fiscal 2016 compared to a foreign exchange gain of $0.1 million last year. As a percent of total revenue, selling, administrative, and other expenses increased by 0.3% to 8.1% this period compared to 7.8% for the same period last year.

On a fiscal year-to-date basis, selling, administrative, and other expenses increased $4.3 million to $70.3 million compared to $66.0 million in the same period last year. The increase was driven by higher spending on strategic projects, marketing and creative initiatives, and increased home office costs. Compared to the same period last year, operating expenditures related to strategic projects were higher by $2.1 million, marketing expenses were $2.7 million higher, creative spending increased by $1.4 million, bonus accruals increased by $1.5 million, and severance costs increased by $0.6 million. This increase was partly offset by proceeds from the disposal of a store lease during the first quarter of fiscal 2016. As part of the disposal agreement, the Company received a one-time payment which offset its lease surrender costs. The net proceeds for exiting this lease were $4.5 million. Additionally, the Company had a foreign exchange gain of $2.5 million in the current year compared to a foreign exchange gain of $0.3 million last year. Compared to the same period last year, the increased foreign exchange gain was driven by the Company having a higher U.S. dollar cash balance in the current period and the strengthening U.S. dollar. Year-to-date selling, administrative, and other expenses as a percent of total revenue decreased 0.2% to 9.1% compared to 9.3% in the same period last year.

Adjusted EBITDA Improved Significantly Compared to Last Year

Adjusted EBITDA, defined as earnings before interest, taxes, depreciation, amortization, impairment, asset disposals, and equity investment improved by $11.7 million to $52.5 million for the 13-week period ended December 26, 2015 compared to $40.8 million for the same period last year. Adjusted EBITDA as a percent of revenue was 13.7% this period compared to 12.0% for the same period last year. As discussed above, the improvement was driven by continued growth in sales at improved margin rates.

On a fiscal year-to-date basis, adjusted EBITDA improved $22.8 million to $54.1 million compared to $31.3 million in the same period last year due to the same factors mentioned above. Year-to-date adjusted EBITDA as a percent of total revenue was 7.0% compared to 4.4% in the same period last year.

Depreciation and Amortization Decreased while Capital Asset Reversals Increased Compared to Last Year

Depreciation and amortization for the 13-week period ended December 26, 2015 decreased by $0.8 million to $5.9 million compared to $6.7 million for the same period last year. Capital expenditures in the third quarter of fiscal 2016 totalled $9.8 million compared to $5.6 million last year and included $6.5 million for store construction, renovations, and equipment, $2.1 million for intangible assets (primarily application software and internal development costs), and $1.2 million for technology equipment. None of the capital expenditures were financed through leases. Capital expenditures increased compared to the same period last year primarily due to the Company starting a number of new strategic initiatives this year to position itself for future growth. The Company had $1.6 million of net capital asset reversals in the current period compared to net capital asset reversals of $0.5 million in the comparative period last year. Impairment losses arose due to an upcoming store closure, while impairment reversals were spread across a number of cash-generating units at the store level and were driven by improved store performance.

On a fiscal year-to-date basis, depreciation and amortization decreased by $2.2 million to $17.7 million compared to $19.9 million in the same period last year. The decrease in amortization was driven by below average capital asset additions last year. Year-to-date, the Company has spent $19.4 million on capital expenditures compared to $14.1 million last year. Capital expenditures for the current year included $11.5 million for store renovations and equipment, $5.9 million for intangible assets (primarily application software and internal development costs), and $2.0 million for technology equipment. None of the capital expenditures were financed through leases. As discussed above, the Company had $1.6 million of net capital asset reversals in the current period compared to net capital asset reversals of $0.5 million in the comparative period last year.

Net Interest Income Decreased Compared to Last Year

The Company recognized net interest income of $0.3 million for the 13-week period ended December 26, 2015 compared to $0.4 million for the same period last year. Compared to the same period last year, the Company maintained a higher average cash balance, but this higher balance was offset by lower average interest rates in the current period. The Company nets interest income against interest expense.

On a fiscal year-to-date basis, the Company recognized net interest income of $1.0 million compared to $1.2 million in the same period last year for the same reasons discussed above.

Earnings from Equity Investment Increased Compared to Last Year

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 $2.4 million for the 13-week period ended December 26, 2015 compared to net earnings of $1.7 million for the same period last year due to improved business performance.

On a fiscal year-to-date basis, Indigo recognized net earnings from Calendar Club of $1.7 million compared to net earnings of $1.1 million in the same period last year.

Income Tax Recovery Increased Compared to Last Year

The Company recognized an income tax recovery of $2.1 million for the 13-week period ended December 26, 2015 compared to an income tax expense of $3.8 million for the same period last year. Previously, the Company recorded a valuation allowance against deferred tax assets based on management's best estimate of future taxable income that the Company expected to achieve. The Company's latest forecast has improved since the fiscal year end and, as such, the valuation allowance is no longer required and $12.4 million has been reversed in the current period. This reversal was partially offset by the Company's $10.3 million income tax expense. As a result of the reversal in valuation allowance, the Company's effective tax rate was (4.1)% this year compared to 10.4% in the same period last year.

On a year-to-date basis, the Company recognized income tax recovery of $2.1 million compared to income tax expense of $3.8 million in the same period last year, for the same reasons discussed above. The Company's effective tax rate was (5.2)% this year compared to 26.9% in the same period last year.

Net Earnings Improved Significantly Compared to Last Year

The Company recognized net earnings of $52.8 million for the 13-week period ended December 26, 2015 ($2.03 net earnings per common share), compared to net earnings of $33.0 million ($1.28 net earnings per common share) for the same period last year. As discussed above, the improvement was driven by continued revenue growth at improved margin rates and lower tax expense in the current period.

On a fiscal year-to-date basis, the Company recognized net earnings of $42.0 million ($1.62 net earnings per common share), compared to net earnings of $10.4 million ($0.41 net earnings per common share) in the same period last year. The improvement in net earnings was driven by the factors discussed above and, in addition, the Company's one-time proceeds from disposal of a lease.

Seasonality and Third 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 revenue, net earnings (loss), and basic and diluted earnings (loss) per share for the preceding eight fiscal quarters.

	Fiscal quarters							
(millions of Canadian dollars, except per share data)	**Q3 Fiscal 2016**	Q2 Fiscal 2016	Q1 Fiscal 2016	Q4 Fiscal 2015	Q3 Fiscal 2015	Q2 Fiscal 2015	Q1 Fiscal 2015	Q4 Fiscal 2014
Revenue	**383.2**	205.7	184.9	186.2	339.4	189.0	180.8	184.3
Total net earnings (loss)	**52.8**	(1.8)	(9.0)	(13.9)	33.0	(8.5)	(14.0)	(14.4)
Basic earnings (loss) per share	**$ 2.03**	$ (0.07)	$ (0.35)	$ (0.54)	$ 1.28	$ (0.33)	$ (0.55)	$ (0.56)
Diluted earnings (loss) per share	**$ 2.02**	$ (0.07)	$ (0.35)	$ (0.54)	$ 1.27	$ (0.33)	$ (0.55)	$ (0.56)

Overview of Consolidated Balance Sheets

Total Assets

As at December 26, 2015, total assets increased $28.1 million to $682.4 million compared to $654.3 million as at December 27, 2014. Compared to the same period last year, increases in cash and cash equivalents and deferred tax assets were partly offset by a reduction in inventories. The $25.0 million increase in cash and cash equivalents and $2.8 million reduction in inventories were driven by higher sales and improved inventory management in the current period compared to the same period last year. The $5.6 million increase in deferred tax assets resulted from the reversal of a previously recorded valuation allowance, as discussed above.

On a fiscal year-to-date basis, total assets increased $144.0 million to $682.4 million compared to $538.4 million as at March 28, 2015. The increase was driven by higher cash and cash equivalents, inventories, and accounts receivable. The $109.1 million increase in cash and cash equivalents and $17.5 million increase in accounts receivable were driven by sales generated during the fiscal 2016 holiday period. Consistent with the seasonal nature of the business, inventory increased by $12.1 million as the Company holds a higher amount of inventory during the holiday season.

Total Liabilities

As at December 26, 2015, total liabilities decreased $3.6 million to $326.5 million compared to $330.1 million as at December 27, 2014. The decrease was driven by a $7.1 million reduction in current and long-term accounts payable and accrued liabilities, partially offset by a $4.5 million increase in unredeemed gift card liability. The decrease in total accounts payable and accrued liabilities is consistent with the Company's lower inventory balance this year compared to the same period last year. Higher unredeemed gift card liability was driven by increased purchases of gift cards during the fiscal 2016 holiday season compared to the same period last year.

On a fiscal year-to-date basis, total liabilities increased $99.3 million to $326.5 million compared to $227.2 million as at March 28, 2015. The increase was driven by a $79.6 million increase in current and long-term accounts payable and accrued liabilities and a $20.5 million increase in unredeemed gift card liability, which are consistent with the seasonal nature of a retail business during the holiday season.

Total Equity

Total equity at December 26, 2015 increased $31.8 million to $355.9 million compared to $324.1 million as at December 27, 2014. The increase in total equity was primarily driven by an increase in net earnings to $42.0 million for the current year compared to net earnings of $10.4 million last year. Share capital increased by $2.0 million due to the exercise of stock options and Directors' deferred share units. Contributed surplus increased $0.7 million due to the expensing of employee stock options and Directors' deferred share units.

Working Capital and Leverage

The Company's working capital position usually declines from the end of its fiscal year until the third fiscal quarter due to the seasonal nature of the business. The Company relies on cash and accounts payable to fund the business before generating a disproportionate amount of cash during the December holiday season.

The Company reported working capital of $235.9 million as at December 26, 2015, compared to $209.5 million as at December 27, 2014 and $198.7 million as at March 28, 2015. Compared to the same period last year, higher working capital in the current period was driven by the $25.0 million increase in cash and cash equivalents and by higher sales, as previously discussed.

The Company's leverage position (defined as Total Liabilities to Total Equity) was 0.9:1 as at December 26, 2015 compared to 1.0:1 at December 27, 2014 and 0.7:1 as at March 28, 2015. The decrease compared to the same period last year was driven by the reduction in current and long-term accounts payable and accrued liabilities combined with an increase in total equity, as discussed above.

Overview of Consolidated Statements of Cash Flows

Cash and cash equivalents increased $136.1 million for the 13-week period ended December 26, 2015 compared to an increase of $137.8 million in the same period last year. The increase in the current period was driven by cash flows generated by operating activities of $143.7 million, cash flows generated from financing activities of $1.2 million, and the effect of foreign currency exchange rate changes on cash and cash equivalents of $0.7 million. These cash flows were partially offset by cash used for investing activities of $9.5 million.

Cash Flows from Operating Activities

The Company generated cash flows of $143.7 million from operating activities in the 13-week period ended December 26, 2015 compared to $142.6 million last year, an improvement of $1.1 million. This improvement was driven by higher net earnings of $52.8 million this period compared to net earnings of $33.0 million in the same period last year. The improvement was partly offset by a reduction in cash generated from working capital as the Company generated $91.4 million this period compared to $101.4 million in the same period last year. In both periods, current and long-term accounts payable and accrued liabilities were a key driver for cash generated from working capital. The Company's current and long-term accounts payable and accrued liabilities were lower in the current period, driving the reduction to cash generated from working capital. The Company also recognized an income tax recovery in the current period compared to an income tax expense in the same period last year due to the previously discussed valuation allowance reversal.

On a fiscal year-to-date basis, cash flows generated from operating activities decreased by $18.6 million to $122.8 million in the current period compared to $141.4 million in the same period last year. This decrease was driven by a reduction in cash generated from working capital as the Company generated $70.7 million this period compared to $109.5 million in the same period last year. Cash generated from working capital decreased and income tax recovery increased for the same reasons discussed above. These reductions were partially offset by higher net earnings of $42.0 million this period compared to net earnings of $10.4 million in the same period last year.

Cash Flows Used for Investing Activities

The Company used cash flows of $9.5 million for investing activities for the 13-week period ended December 26, 2015 compared to using $5.4 million in the same period last year, an increase of $4.1 million. The increase was driven by the Company starting a number of new strategic initiatives this year to position itself for future growth. Total cash spent on capital projects for the 13-week period ended December 26, 2015 was $9.8 million compared to $5.6 million spent in the same period last year.

On a fiscal year-to-date basis, the Company used cash flows of $18.7 million for investing activities compared to using $13.1 million in the same period last year, an increase of $5.6 million. The Company spent $19.4 million on capital projects compared to spending $14.1 million in the same period last year. Driven by the successes of its transformational strategy, the Company is continuing to implement changes across its retail outlets and is working on a number of back-end productivity initiatives.

Cash was used for capital projects as follows:

(millions of Canadian dollars)	**13-week period ended December 26, 2015**	13-week period ended December 27, 2014	**39-week period ended December 26, 2015**	39-week period ended December 27, 2014
Store construction, renovations, and equipment	**6.5**	3.7	**11.5**	7.0
Intangible assets (primarily application software and internal development costs)	**2.1**	1.4	**5.9**	5.2
Technology equipment	**1.2**	0.5	**2.0**	1.9
	9.8	5.6	**19.4**	14.1

Cash Flows from Financing Activities

The Company generated cash flows of $1.2 million for financing activities for the 13-week period ended December 26, 2015 compared to generating $0.1 million in the same period last year. In the current period, more options were exercised compared to last year, resulting in a $0.9 million increase to proceeds from share issuances.

On a fiscal year-to-date basis, cash flows generated from financing activities increased to $1.3 million in the current period compared to $0.4 million in the same period last year. In the current year, proceeds from share issuances increased by $0.5 million due to increased option exercises while capital lease and interest payments were lower by $0.4 million as the Company had fewer capital leases compared to last year. Over the past year, the Company has not entered any new capital lease agreements so the amount of cash required to fund debt service requirements is expected to decline over the next several periods. However, the Company continues to consider long-term debt as a possible source of capital.

Liquidity and Capital Resources

The Company has a highly seasonal business which generates the majority of its revenue 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 and cash and cash equivalents.

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 2016. In addition, the Company has the ability to reduce capital spending to fund debt requirements if necessary; however, a long-term decline in capital expenditures may negatively impact revenue and profit growth.

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 unaudited interim condensed consolidated financial statements which have been prepared in accordance with IFRS and IAS 34. The preparation of these unaudited interim condensed consolidated financial statements in conformity with IFRS requires management to undertake a number of judgments and estimates about the recognition and measurement of assets, liabilities, revenues, and expenses. These judgments and estimates are based on management's historical experience and other assumptions which the Company believes to be reasonable under the circumstances. Actual results may differ from the judgments and estimates made by management, and actual results will seldom equal estimates.

Material judgments and estimates are made with respect to: revenue recognition from unredeemed gift cards and plum points; fair value of plum points; inventory shrinkage; reserves for slow-moving or damaged products and products that have been permanently marked down; vendor settlement; fair value of share-based instruments and number of equity instruments expected to vest; identification of cash generating units ("CGUs") and expected future cash flows from CGUs; depreciation and amortization periods; lease classification; and recognition and valuation of deferred tax assets.

The Company evaluates its judgments and estimates on an ongoing basis and methods used to calculate critical accounting estimates are consistent with prior periods. The significant accounting policies and significant judgments and estimates of the Company are described in notes 3 and 4 of the consolidated financial statements contained in the Company's fiscal 2015 Annual Report.

Accounting Standards Implemented in the Third Quarter of Fiscal 2016

There were no new accounting standards implemented in the period.

New Accounting Pronouncements

Revenue from Contracts with Customers ("IFRS 15")

In May 2014, the IASB issued IFRS 15, a new standard that specifies how and when to recognize revenue as well as requiring entities to provide users of financial statements with more informative, relevant disclosures. IFRS 15 supersedes IAS 18, "Revenue," IAS 11, "Construction Contracts," and a number of revenue-related interpretations. Application of IFRS 15 is mandatory for all IFRS reporters and it applies to nearly all contracts with customers: the main exceptions are leases, financial instruments, and insurance contracts. IFRS 15 must be applied for reporting periods beginning on or after January 1, 2018 and early adoption is permitted. The Company is assessing the impact of adopting this standard on its results of operations, financial position, and disclosures. The Company plans to apply this standard for reporting periods beginning on or after January 1, 2018.

Financial Instruments ("IFRS 9")

In July 2014, the IASB issued the final version of IFRS 9, which reflects all phases of the financial instruments project and replaces IAS 39, "Financial Instruments: Recognition and Measurement," and all previous versions of IFRS 9. The standard introduces new requirements for classification and measurement, impairment, and hedge accounting. IFRS 9 is effective for annual periods beginning on or after January 1, 2018, with early application permitted. The Company is assessing the impact of the new standard on its results of operations, financial position, and disclosures. The Company plans to apply this standard for reporting periods beginning on or after January 1, 2018.

Leases ("IFRS 16")

On January 13, 2016, the IASB issued IFRS 16 which supersedes existing standards and interpretations under IAS 17, "Leases." IFRS 16 requires all leases to be reported on a Company's balance sheet and will provide greater transparency on companies' lease assets and liabilities. The new standard will apply for annual periods beginning on or after January 1, 2019. Earlier application is permitted provided the Company has also adopted IFRS 15. The Company is assessing the impact of adopting this standard on its results of operations, financial position, and disclosures. The Company plans to apply this standard for reporting periods beginning on or after January 1, 2019.

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.

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 IFRS.

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 2013 by the Committee of Sponsoring Organizations of the Treadway Commission.

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 September 27, 2015 and ended on December 26, 2015 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 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, asset disposals, and equity investment. The method of calculating adjusted EBITDA is consistent with that used in prior periods.

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

(millions of Canadian dollars)	**13-week period ended December 26, 2015**	13-week period ended December 27, 2014	**39-week period ended December 26, 2015**	39-week period ended December 27, 2014
Adjusted EBITDA	**52.5**	40.8	**54.1**	31.3
Depreciation of property, plant, and equipment	**(3.7)**	(3.7)	**(10.8)**	(11.0)
Amortization of intangible assets	**(2.2)**	(3.0)	**(6.9)**	(8.9)
Net reversal of capital assets	**1.6**	0.5	**1.6**	0.5
Loss on disposal of capital assets	**(0.2)**	–	**(0.9)**	–
Interest on long-term debt and financing charges	**0.0**	0.0	**0.0**	0.0
Interest income on cash and cash equivalents	**0.3**	0.5	**1.1**	1.3
Share of earnings from equity investment	**2.4**	1.7	**1.7**	1.1
Earnings before income taxes	**50.7**	36.8	**39.9**	14.3

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NOTICE OF NO AUDITOR REVIEW OF INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Under National Instrument 51-102, Part 4, subsection 4.3(3)(a), if an auditor has not performed a review of the interim condensed consolidated financial statements, they must be accompanied by a notice indicating that the financial statements have not been reviewed by an auditor.

The accompanying unaudited interim condensed consolidated financial statements of the Company have been prepared by and are the responsibility of the Company's management.

The Company's independent auditor has not performed a review of these interim condensed consolidated financial statements.

Heather Reisman
Chair & Chief Executive Officer

Laura Carr
Chief Financial Officer

Dated as of the 2nd day of February, 2016.

Consolidated Balance Sheets

(Unaudited)

(thousands of Canadian dollars)	**As at December 26, 2015**	As at December 27, 2014	As at March 28, 2015
ASSETS			
Current			
Cash and cash equivalents (note 5)	**312,254**	287,227	203,162
Accounts receivable	**22,354**	20,784	4,896
Inventories (note 6)	**220,507**	223,260	208,395
Income taxes recoverable	**–**	–	25
Prepaid expenses	**4,576**	5,864	5,477
Total current assets	**559,691**	537,135	421,955
Property, plant, and equipment (note 9)	**58,340**	56,771	54,886
Intangible assets	**15,593**	17,902	16,587
Equity investment	**2,426**	1,684	726
Deferred tax assets	**46,332**	40,766	44,241
Total assets	**682,382**	654,258	538,395
LIABILITIES AND EQUITY			
Current			
Accounts payable and accrued liabilities	**241,539**	248,881	160,645
Unredeemed gift card liability	**68,735**	64,232	48,211
Provisions	**43**	885	913
Deferred revenue	**13,414**	13,380	13,298
Income taxes payable	**25**	26	–
Current portion of long-term debt (note 12)	**84**	187	172
Total current liabilities	**323,840**	327,591	223,239
Long-term accrued liabilities	**2,596**	2,335	3,841
Long-term provisions	**83**	99	110
Long-term debt (note 12)	**9**	94	56
Total liabilities	**326,528**	330,119	227,246
Equity			
Share capital (note 7)	**207,897**	204,970	205,871
Contributed surplus (note 8)	**10,455**	9,715	9,770
Retained earnings	**137,502**	109,454	95,508
Total equity	**355,854**	324,139	311,149
Total liabilities and equity	**682,382**	654,258	538,395

See accompanying notes

On behalf of the Board:

Heather Reisman, Director

Michael Kirby, Director

Consolidated Statements of Earnings and Comprehensive Earnings

(Unaudited)

(thousands of Canadian dollars, except per share data)	**13-week period ended December 26, 2015**	13-week period ended December 27, 2014	**39-week period ended December 26, 2015**	39-week period ended December 27, 2014
Revenue (note 9)	**383,171**	339,389	**773,787**	709,221
Cost of sales	**(214,057)**	(191,709)	**(429,669)**	(398,265)
Gross profit	**169,114**	147,680	**344,118**	310,956
Operating, selling, and administrative expenses (note 9)	**(121,162)**	(113,012)	**(306,963)**	(298,997)
Operating profit	**47,952**	34,668	**37,155**	11,959
Interest on long-term debt and financing charges	**(4)**	(19)	**(9)**	(48)
Interest income on cash and cash equivalents	**330**	465	**1,057**	1,253
Share of earnings from equity investment	**2,426**	1,684	**1,700**	1,086
Earnings before income taxes	**50,704**	36,798	**39,903**	14,250
Income tax recovery (expense)	**2,091**	(3,838)	**2,091**	(3,838)
Net earnings and comprehensive earnings for the period	**52,795**	32,960	**41,994**	10,412
Net earnings per common share (note 10)				
Basic	**$ 2.03**	$ 1.28	**$ 1.62**	$ 0.41
Diluted	**$ 2.02**	$ 1.27	**$ 1.61**	$ 0.40

See accompanying notes

Consolidated Statements of Changes in Equity

(Unaudited)

(thousands of Canadian dollars)	Share Capital	Contributed Surplus	Retained Earnings	Total Equity
Balance, March 29, 2014	203,812	8,820	99,042	311,674
Net earnings for the 39-week period ended December 27, 2014	–	–	10,412	10,412
Exercise of options (notes 7 and 8)	1,158	(170)	–	988
Share-based compensation (note 8)	–	813	–	813
Directors' compensation (note 8)	–	252	–	252
Balance, December 27, 2014	204,970	9,715	109,454	324,139
Balance, March 28, 2015	**205,871**	**9,770**	**95,508**	**311,149**
Net earnings for the 39-week period ended December 26, 2015	**–**	**–**	**41,994**	**41,994**
Exercise of options (notes 7 and 8)	**1,735**	**(269)**	**–**	**1,466**
Directors' deferred share units converted (note 7)	**291**	**(291)**	**–**	**–**
Share-based compensation (note 8)	**–**	**951**	**–**	**951**
Directors' compensation (note 8)	**–**	**294**	**–**	**294**
Balance, December 26, 2015	**207,897**	**10,455**	**137,502**	**355,854**

See accompanying notes

Consolidated Statements of Cash Flows

(Unaudited)

(thousands of Canadian dollars)	**13-week period ended December 26, 2015**	13-week period ended December 27, 2014	**39-week period ended December 26, 2015**	39-week period ended December 27, 2014
CASH FLOWS FROM OPERATING ACTIVITIES				
Net earnings for the period	**52,795**	32,960	**41,994**	10,412
Add (deduct) items not affecting cash				
Depreciation of property, plant, and equipment	**3,666**	3,703	**10,830**	11,036
Amortization of intangible assets	**2,210**	3,032	**6,870**	8,881
Net reversal of capital assets (note 9)	**(1,619)**	(458)	**(1,619)**	(458)
Loss on disposal of capital assets (note 9)	**236**	25	**896**	34
Share-based compensation (note 8)	**341**	315	**951**	813
Directors' compensation (note 8)	**98**	86	**294**	252
Deferred tax assets	**(2,091)**	3,838	**(2,091)**	3,838
Other	**(665)**	(175)	**(3,316)**	(716)
Net change in non-cash working capital balances (note 11)	**91,397**	101,386	**70,723**	109,546
Interest on long-term debt and financing charges	**4**	19	**9**	48
Interest income on cash and cash equivalents	**(330)**	(465)	**(1,057)**	(1,253)
Income taxes received	**50**	26	**50**	26
Share of earnings from equity investment	**(2,426)**	(1,684)	**(1,700)**	(1,086)
Cash flows from operating activities	**143,666**	142,608	**122,834**	141,373
CASH FLOWS FROM INVESTING ACTIVITIES				
Purchase of property, plant, and equipment	**(7,665)**	(4,196)	**(13,562)**	(8,907)
Addition of intangible assets	**(2,106)**	(1,384)	**(5,880)**	(5,196)
Proceeds from disposal of capital assets	**–**	–	**5**	–
Interest received	**284**	207	**770**	995
Cash flows used in investing activities	**(9,487)**	(5,373)	**(18,667)**	(13,108)
CASH FLOWS FROM FINANCING ACTIVITIES				
Repayment of long-term debt	**(40)**	(170)	**(135)**	(536)
Interest paid	**(17)**	(19)	**(51)**	(50)
Proceeds from share issuances (note 7)	**1,209**	317	**1,466**	988
Cash flows from financing activities	**1,152**	128	**1,280**	402
Effect of foreign currency exchange rate changes on cash and cash equivalents	**724**	435	**3,645**	982
Net increase in cash and cash equivalents during the period	**136,055**	137,798	**109,092**	129,649
Cash and cash equivalents, beginning of period	**176,199**	149,429	**203,162**	157,578
Cash and cash equivalents, end of period	**312,254**	287,227	**312,254**	287,227

See accompanying notes

Notes to the Interim Condensed Consolidated Financial Statements

December 26, 2015
(Unaudited)

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 unaudited interim condensed 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. BASIS OF PREPARATION

Statement of Compliance

These unaudited interim condensed consolidated financial statements have been prepared using accounting policies consistent with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") and in accordance with International Accounting Standard ("IAS") 34, "Interim Financial Reporting." The same accounting policies and methods of computation as those used in the preparation of the fiscal 2015 Annual Report were followed in the preparation of these unaudited interim condensed consolidated financial statements. These unaudited interim condensed consolidated financial statements should be read in conjunction with the Company's fiscal 2015 Annual Report.

The unaudited interim condensed consolidated financial statements for the 13 and 39-week periods ended December 26, 2015 (including comparatives) were approved by the Board of Directors on February 2, 2016.

Significant Judgments and Estimates

The preparation of these unaudited interim condensed consolidated financial statements in conformity with IFRS requires management to undertake a number of judgments and estimates about the recognition and measurement of assets, liabilities, revenues, and expenses. These judgments and estimates are based on management's historical experience and other assumptions which the Company believes to be reasonable under the circumstances. Actual results may differ from the judgments and estimates made by management, and actual results will seldom equal estimates.

Material judgments and estimates are made with respect to: revenue recognition from unredeemed gift cards and plum rewards program ("Plum") points; fair value of Plum points; inventory shrinkage; reserves for slow-moving or damaged products and products that have been permanently marked down; vendor settlement; fair value of share-based instruments and number of equity instruments expected to vest; identification of cash generating units ("CGUs") and expected future cash flows from CGUs; depreciation and amortization periods; lease classification; and recognition and valuation of deferred tax assets.

3. CHANGES IN ACCOUNTING POLICIES

There were no new accounting standards implemented in the period.

New Accounting Pronouncements

Revenue from Contracts with Customers ("IFRS 15")

In May 2014, the IASB issued IFRS 15, a new standard that specifies how and when to recognize revenue as well as requiring entities to provide users of financial statements with more informative, relevant disclosures. IFRS 15 supersedes IAS 18, "Revenue," IAS 11, "Construction Contracts," and a number of revenue-related interpretations. Application of IFRS 15 is mandatory for all IFRS reporters and it applies to nearly all contracts with customers: the main exceptions are leases, financial instruments, and insurance contracts. IFRS 15 must be applied for reporting periods beginning on or after January 1, 2018 and early adoption is permitted. The Company is assessing the impact of adopting this standard on its results of operations, financial position, and disclosures. The Company plans to apply this standard for reporting periods beginning on or after January 1, 2018.

Financial Instruments ("IFRS 9")

In July 2014, the IASB issued the final version of IFRS 9, which reflects all phases of the financial instruments project and replaces IAS 39, "Financial Instruments: Recognition and Measurement," and all previous versions of IFRS 9. The standard introduces new requirements for classification and measurement, impairment, and hedge accounting. IFRS 9 is effective for annual periods beginning on or after January 1, 2018, with early application permitted. The Company is assessing the impact of the new standard on its results of operations, financial position, and disclosures. The Company plans to apply this standard for reporting periods beginning on or after January 1, 2018.

Leases ("IFRS 16")

On January 13, 2016, the IASB issued IFRS 16 which supersedes existing standards and interpretations under IAS 17, "Leases." IFRS 16 requires all leases to be reported on a Company's balance sheet and will provide greater transparency on companies' lease assets and liabilities. The new standard will apply for annual periods beginning on or after January 1, 2019. Earlier application is permitted provided the Company has also adopted IFRS 15. The Company is assessing the impact of adopting this standard on its results of operations, financial position, and disclosures. The Company plans to apply this standard for reporting periods beginning on or after January 1, 2019.

4. SEASONALITY OF OPERATIONS

The business of Indigo follows a seasonal pattern, with sales of merchandise being highest in the third fiscal quarter due to consumer holiday buying patterns. As a result, a disproportionate portion of total annual revenue is typically earned in the third fiscal quarter. Therefore, the results of operations for the 13 and 39-week periods ended December 26, 2015 and December 27, 2014 are not indicative of the results of other periods.

5. CASH AND CASH EQUIVALENTS

Cash and cash equivalents consist of the following:

(thousands of Canadian dollars)	**December 26, 2015**	December 27, 2014	March 28, 2015
Cash	**228,206**	172,722	139,658
Restricted cash	**3,550**	3,138	3,138
Cash equivalents	**80,498**	111,367	60,366
Cash and cash equivalents	**312,254**	287,227	203,162

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

6. INVENTORIES

The cost of inventories recognized as an expense during the 13 and 39-week periods ended December 26, 2015 were $217.2 million and $436.8 million, respectively (2014: 13 weeks – $192.0 million; 39 weeks – $400.2 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 during the 13 and 39-week periods ended December 26, 2015 were $2.6 million and $6.4 million, respectively (2014: 13 weeks – $3.2 million; 39 weeks – $8.0 million), and there were no reversals of inventory write-downs that were recognized in prior periods (2014: 13 weeks – nil; 39 weeks – nil). The amount of inventory with net realizable value equal to cost was $3.1 million as at December 26, 2015 (2014 – $1.7 million).

7. SHARE CAPITAL

Share capital consists of the following:

	39-week period ended December 26, 2015		39-week period ended December 27, 2014		52-week period ended March 28, 2015	
	Number of shares	**Amount C$ (thousands)**	Number of shares	Amount C$ (thousands)	Number of shares	Amount C$ (thousands)
Balance, beginning of period	**25,495,289**	**205,871**	25,298,239	203,812	25,298,239	203,812
Issued during the period						
Directors' deferred share units converted	**29,142**	**291**	–	–	–	–
Options exercised	**151,645**	**1,735**	125,050	1,158	197,050	2,059
Balance, end of period	**25,676,076**	**207,897**	25,423,289	204,970	25,495,289	205,871

8. SHARE-BASED COMPENSATION

As at December 26, 2015, 1,926,205 stock options were outstanding with exercise prices ranging from $8.00 to $15.21. Of these outstanding stock options, 664,825 were exercisable. As at December 27, 2014, there were 1,811,100 stock options outstanding of which 432,290 were exercisable.

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 the 13 and 39-week periods ended December 26, 2015, the pre-forfeiture rate fair values of options granted were less than $0.1 million and $1.3 million, respectively (2014: 13 weeks – $0.1 million; 39 weeks – $1.5 million).

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 in the comparative prior year period:

	13-week period ended December 26, 2015	13-week period ended December 27, 2014
Black-Scholes option pricing assumptions		
Risk-free interest rate	**0.5%**	1.1%
Expected volatility	**33.0%**	32.9%
Expected time until exercise	**3.0 years**	3.0 years
Expected dividend yield	**–**	–
Other assumptions		
Forfeiture rate	**28.4%**	28.0%

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. During the 13 and 39-week periods ended December 26, 2015, the Company issued 7,197 DSUs with a value of $0.1 million and 26,211 DSUs with a value of $0.3 million, respectively (2014: 13 weeks – 7,360 DSUs with a value of $0.1 million; 39 weeks – 22,561 DSUs with a value of $0.3 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 December 26, 2015 was $3.7 million (December 27, 2014 – $3.6 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 the grant date.

9. SUPPLEMENTARY OPERATING INFORMATION

Supplemental product line revenue information:

(thousands of Canadian dollars)	**13-week period ended December 26, 2015**	13-week period ended December 27, 2014	**39-week period ended December 26, 2015**	39-week period ended December 27, 2014
Print[1]	**221,532**	208,152	**476,992**	459,175
General merchandise[2]	**151,327**	118,002	**270,273**	218,447
eReading[3]	**4,762**	6,667	**11,441**	14,353
Other[4]	**5,550**	6,568	**15,081**	17,246
Total	**383,171**	339,389	**773,787**	709,221

1 Includes books, calendars, magazines, newspapers, and shipping revenue.

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

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

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

Supplemental operating and administrative expenses information:

(thousands of Canadian dollars)	**13-week period ended December 26, 2015**	13-week period ended December 27, 2014	**39-week period ended December 26, 2015**	39-week period ended December 27, 2014
Wages, salaries, and bonuses	**52,283**	46,682	**132,782**	125,015
Short-term benefits expense	**4,758**	4,423	**13,987**	13,453
Termination benefits expense	**1,305**	504	**2,189**	1,322
Retirement benefits expense	**380**	331	**1,070**	1,010
Share-based compensation	**341**	315	**951**	813
Total employee benefits expense	**59,067**	52,255	**150,979**	141,613

Termination benefits arise when the Company terminates certain employment agreements.

For the 39-week period ended December 26, 2015, operating, selling, and administrative expenses also included incentives received for the disposal of a store lease. These incentives offset costs incurred as part of surrendering the lease. The Company recorded one-time net proceeds of $4.5 million and had a $0.7 million disposal of capital assets related to the lease surrender.

Capital Assets

During the 13 and 39-week periods ended December 26, 2015, the Company recognized capital asset impairments of $0.6 million and $0.6 million, respectively (2014: 13 weeks – $2.0 million; 39 weeks – $2.0 million). During the 13 and 39-week periods ended December 26, 2015, the Company recognized capital asset reversals of $2.3 million and $2.3 million, respectively (2014: 13 weeks – $2.4 million; 39 weeks – $2.4 million). All impairments and reversals were recorded as part of operating, selling, and administrative expenses in the Consolidated Statements of Earnings and Comprehensive Earnings.

Impairment losses arose due to an upcoming store closure, while impairment reversals were spread across a number of CGUs and were driven by improved store performance. The key assumptions from the value in use calculation used for impairment testing are those regarding growth rates and discount rates. The cash flow projections are based on both past and forecasted performance and are extrapolated using growth rates which are calculated separately for each CGU being tested. Average long-term growth rates used to extrapolate cash flow projections beyond the period covered by the most recent forecasts ranged from 0.0% to 3.0% (2014 – 0.0% to 3.0%). Cash flows for stores expected to operate beyond the current lease term and renewal options were projected using a terminal value calculation. 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 discount rate used to calculate value in use was 19.7% (2014 – 19.0%).

10. EARNINGS PER SHARE

Earnings per share is calculated based on the weighted average number of 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 adjustment to net earnings. The reconciliation of the denominator in calculating diluted earnings per share amounts for the 13 and 39-week periods ended December 26, 2015 and December 27, 2014 is as follows:

(thousands of shares)	**13-week period ended December 26, 2015**	13-week period ended December 27, 2014	**39-week period ended December 26, 2015**	39-week period ended December 27, 2014
Weighted average number of common shares outstanding, basic	**25,954**	25,743	**25,902**	25,693
Effect of dilutive securities – stock options	**168**	169	**142**	104
Weighted average number of common shares outstanding, diluted	**26,122**	25,912	**26,044**	25,797

For the 13 and 39-week periods ended December 26, 2015, 712,500 and 1,057,900 anti-dilutive stock options, respectively (2014: 13 weeks – 570,000 options; 39 weeks – 1,308,500 options) were excluded from the computation of diluted net earnings per common share.

11. STATEMENTS OF CASH FLOWS

Supplemental cash flow information:

(thousands of Canadian dollars)	**13-week period ended December 26, 2015**	13-week period ended December 27, 2014	**39-week period ended December 26, 2015**	39-week period ended December 27, 2014
Net change in non-cash working capital balances:				
Accounts receivable	**(3,738)**	(8,006)	**(17,458)**	(15,202)
Inventories	**36,445**	11,793	**(12,112)**	(4,281)
Prepaid expenses	**267**	542	**901**	(680)
Accounts payable and accrued liabilities (current and long-term)	**32,712**	73,422	**79,649**	111,892
Unredeemed gift card liability	**26,486**	23,459	**20,524**	17,405
Provisions (current and long-term)	**(17)**	(26)	**(897)**	(108)
Deferred revenue	**(758)**	202	**116**	520
	91,397	101,386	**70,723**	109,546

12. CAPITAL MANAGEMENT

The Company's main objectives when managing capital are:

- Ensuring sufficient liquidity to support financial obligations and to execute operating and strategic objectives;
- Maintaining financial capacity and flexibility through access to capital to support future development of the business;
- Minimizing the cost of capital while taking into consideration current and future industry, market, and economic risks and conditions; and
- Utilizing short-term funding sources to manage working capital requirements and long-term funding sources to manage the long-term capital expenditures of the business.

There were no changes to these objectives for the 13 and 39-week periods ended December 26, 2015. The primary activities engaged by the Company to generate attractive returns for shareholders 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 Company's sales networks. The Company's main sources of capital are its current cash position and cash flows generated from operations. Cash flow is used to fund working capital needs, capital expenditures, and debt service requirements. The Company manages its capital structure in accordance with changes in economic conditions.

The following table summarizes the Company's capital structure:

(thousands of Canadian dollars)	**December 26, 2015**	December 27, 2014	March 28, 2015
Current portion of long-term debt	**84**	187	172
Long-term debt	**9**	94	56
Total debt	**93**	281	228
Total equity	**355,854**	324,139	311,149
Total capital under management	**355,947**	324,420	311,377

13. 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 Executive Officers of the Company. Key management personnel remuneration includes the following expenses:

(thousands of Canadian dollars)	**13-week period ended December 26, 2015**	13-week period ended December 27, 2014	**39-week period ended December 26, 2015**	39-week period ended December 27, 2014
Wages, salaries, and bonus	**1,168**	1,214	**3,648**	3,561
Short-term benefits expense	**53**	54	**153**	154
Termination benefits expense	**454**	–	**454**	–
Retirement benefits expense	**19**	11	**54**	34
Share-based compensation	**185**	192	**540**	463
Directors' compensation	**98**	86	**294**	252
Total remuneration	**1,977**	1,557	**5,143**	4,464

Transactions with Shareholders

During the third quarter of fiscal 2016, 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. During the 13 and 39-week periods ended December 26, 2015, Indigo paid $1.8 million and $3.0 million, respectively, for these transactions (2014: 13 weeks – $2.4 million; 39 weeks – $2.7 million). As at December 26, 2015, 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 (December 27, 2014 – $0.1 million payable and $2.8 million 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 9. 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 revenue. 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 the 13 and 39-week periods ended December 26, 2015 were $9.9 million and nil, respectively, received by Indigo (2014: 13 weeks – $5.5 million received by Indigo; 39 weeks – nil).

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