



Canada's Leading
Specialty Mattress Retailer

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Management's Discussion and Analysis of Financial Condition and Results of Operation of Sleep Country Canada Holdings Inc.

The following Management's Discussion and Analysis ("MD&A") is prepared as of February 24, 2016 and is intended to assist readers in understanding the financial performance and financial condition of Sleep Country Canada Holdings Inc. ("SCC" or "Sleep Country" or the "Company") for the year ended December 31, 2015 and should be read in conjunction with the audited consolidated financial statements and the accompanying notes of SCC for the years ended December 31, 2015 and December 31, 2014.

1 Basis of Presentation

The Company's annual 2015 audited consolidated financial statements and accompanying notes have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board using the accounting policies described therein. All amounts are presented in thousands of Canadian dollars, except number of stores, per share amounts or unless otherwise indicated.

All references in this MD&A to "2015" are to SCC's year ended December 31, 2015, to "2014" are to Sleep Country Canada Inc.'s ("SCCI") year ended December 31, 2014, to "Q4 2015" are to SCC's quarter ended December 31, 2015 and to "Q4 2014" are to SCCI's quarter ended December 31, 2014. This MD&A includes financial information for periods prior to the acquisition of SCCI by SCC on July 16, 2015, including the comparative periods. This information is based on the historical financial information as previously reported by SCCI.

The audited consolidated financial statements and the accompanying notes of SCC for the year ended December 31, 2015 and this MD&A were reviewed by the Company's audit committee and were approved by its Board of Directors on February 24, 2016.

2 Forward-Looking Information

This MD&A, including, in particular, the sections below entitled "Factors Affecting our Results of Operations", "Liquidity and Capital Resources", "Outlook" and "Risk Factors", contains forward-looking information and forward-looking statements which reflect the current view of management with respect to the Company's objectives, plans, goals, strategies, outlook, results of operations, financial and operating performance, prospects and opportunities. Wherever used, the words "may", "will", "anticipate", "intend", "estimate", "expect", "plan", "believe" and similar expressions identify forward-looking information and forward-looking statements. Forward-looking information and forward-looking statements should not be read as guarantees of future events, performance or results, and will not necessarily be accurate indications of whether, or the times at which, such events, performance or results will be achieved. All of the information in this MD&A containing forward-looking information or forward-looking statements is qualified by these cautionary statements.

Forward-looking information and forward-looking statements are based on information available to management at the time they are made, underlying estimates, opinions and assumptions made by management and management's current good faith belief with respect to future strategies, prospects, events, performance and results, and are subject to inherent risks and uncertainties surrounding future expectations generally. Such risks and uncertainties include, but are not limited to, those described below under the heading "Risk Factors" and in the Company's 2015 annual information form (the "AIF") filed on February 24, 2016. A copy of the AIF can be accessed under the Company's profile on the System for Electronic Document Analysis and Retrieval ("SEDAR") at www.sedar.com. Additional risks and uncertainties not presently known to the Company or that the Company currently believes to be less significant may also adversely affect the Company.

SCC cautions that the list of risk factors and uncertainties described in this MD&A and the AIF is not exhaustive and that should certain risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual strategies, prospects, events, performance and results may vary significantly from those expected. There can be no assurance that the actual strategies, prospects, results, performance, events or activities 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. Readers are urged to consider the risks, uncertainties and assumptions carefully in evaluating the forward-looking information and forward-looking statements and are cautioned not to place undue reliance on such information and statements. SCC does not undertake to update any such forward-looking information or forward-looking statements, whether as a result of new information, future events or otherwise, except as required by applicable laws.

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3 Overview

Sleep Country is Canada's leading mattress retailer and the only specialty mattress retailer with a national footprint. Sleep Country operates under two mattress retail banners (the "**Banners**"): "*Dormez-vous?*", the largest retailer of mattresses in Québec; and "*Sleep Country Canada*" the largest mattress retailer in the rest of Canada. Sleep Country continues to expand its presence coast to coast. As at December 31, 2015, Sleep Country had 224 stores and 17 distribution centres across Canada. Sleep Country's stores average approximately 5,000 square feet and offer a large selection of mattresses and a wide assortment of complementary sleep related products and accessories, which include bed frames, pillows, mattress pads, sheets, duvets, headboards and footboards. Sleep Country's stores are all corporate-owned, enabling it to develop and maintain a strong culture of customer service, resulting in a consistent and superior in-store and home delivery customer experience. Between March 2006 and December 2014, SCCI operated in Arizona, U.S.A. under the "*Sleep America*" banner. The Sleep America business was sold on January 6, 2015 and is presented as "Discontinued Operations" in the financial statements.

SLEEP COUNTRY CANADA

Sleep Country launched its concept in the Vancouver market with four stores in 1994 and has since expanded across Canada with 174 corporately owned stores and 15 distribution centres in British Columbia, Alberta, Manitoba, Saskatchewan, Ontario, Nova Scotia and New Brunswick as at December 31, 2015. SCC's regional footprint includes the following distribution centres: Victoria, BC; Richmond, BC; Langley, BC; Kelowna, BC; Calgary, AB; Edmonton, AB; Winnipeg, MB; Regina, SK; Toronto, ON; London, ON; Ancaster, ON; Cobourg, ON; Ottawa, ON; Moncton, NB and Halifax, NS.

DORMEZ-VOUS?

In January 2006, Sleep Country acquired Dormez-vous?, a Québec based mattress retailer with five stores and one distribution centre in the Montreal area. As of December 31, 2015, the Dormez-vous? Banner has expanded to 50 stores with two distribution centres in Montreal and Québec City.

4 Corporate Highlights for Fiscal 2015

INITIAL PUBLIC OFFERING

On July 16, 2015, SCC successfully completed an initial public offering (the "**IPO**") of its common shares at a price of \$17.00 per share. SCC issued 17,650,000 shares for total gross proceeds of \$300,050,000. The shares commenced trading on July 16, 2015 on the Toronto Stock Exchange under the symbol "ZZZ".

In connection with the IPO, SCC completed the acquisition (the "**Acquisition**") of SCCI, SC Management Holdings Inc. ("**SC Management**") and Sleep Country US Holdco Canada Inc. ("**SC US Holdco**" and, together with SCCI and SC Management, the "**Acquired Entities**"). The net proceeds of the IPO were used by SCC to satisfy a portion of the purchase price, with the balance being satisfied by the issuance of common shares of SCC.

Immediately prior to closing of the IPO, SCC, certain of its subsidiaries, certain of the existing shareholders of SCC, SC US Holdco, SC Management and their respective affiliates undertook steps to simplify the share structure of the Acquired Entities (the "**Pre-Closing Transactions**"). In connection with the Pre-Closing Transactions, the Series A and B promissory notes of SCCI were settled for Class A common shares and the Class A convertible shares were converted into Class D common shares based on the relative fair values at the conversion date. Subsequent to the conversion of the foregoing instruments, SCCI declared and paid a pre-IPO capital dividend in the aggregate amount of \$13,000 on its Class A common shares, Class B common shares and Class D common shares. Upon closing of the IPO, the unvested options under SCCI's legacy stock option plan vested and the options were settled for a combination of cash and Class E special shares, with loans in the aggregate amount of approximately \$2.36 million from SCCI to satisfy the exercise price of such options. These loans were repaid as part of the Acquisition. SCCI's shares were then sold to SCC for a combination of cash, common shares of SCC and convertible notes based on the economic value of the Company's shares as determined on July 10, 2015.

SC Management and SC US Holdco were subsequently dissolved into Sleep Country Canada LP ("**SCCLP**") immediately following the completion of the IPO on July 16, 2015. On January 1, 2016, SCCLP was wound up and its general partner was dissolved, in each case into SCCI.

NEW SENIOR SECURED CREDIT FACILITY

On July 16, 2015, in connection with the IPO, SCCI negotiated a new revolving credit facility with a limit of \$175 million which matures on July 16, 2020. As at December 31, 2015, \$124 million was drawn against this new credit facility. The credit facility is guaranteed by SCC.

SECONDARY OFFERING

On December 17, 2015, Birch Hill Feather LP, Birch Hill Feather (US) Holdings LP and Panzer Limited (collectively, the “**Selling Shareholders**”) completed a secondary offering (the “**Secondary Offering**”) of common shares of SCC at a price of \$18.50 per share. The Selling Shareholders sold an aggregate of 10,000,000 common shares of SCC to a syndicate of underwriters for total gross proceeds of \$185 million. The Company did not receive any proceeds from the Secondary Offering.

DIVIDENDS

On November 3, 2015, the Board of Directors of the Company declared a dividend on the Company’s common shares in the amount of \$0.13 per share, payable on November 26, 2015 to shareholders of record at the close of business on November 16, 2015. This was the Company’s first dividend since the completion of the IPO. The dividend was designated as an “eligible dividend” for Canadian tax purposes.

On January 29, 2016, the Board of Directors of the Company declared a dividend on the Company’s common shares in the amount of \$0.13 per share, payable on February 26, 2016 to shareholders of record at the close of business on February 16, 2016. The dividend is designated as an “eligible dividend” for Canadian tax purposes.

On February 24, 2016 the Board announced the suspension of the Dividend Reinvestment Program (“DRIP”), effective after Sleep Country’s dividend payable on February 26, 2016. Shareholders who had elected to participate in the DRIP will in the future receive cash dividends on the next payment date. At such time as the Company elects to reinstate the DRIP, shareholders that were enrolled at suspension and remain enrolled at reinstatement will automatically resume participation in the DRIP.

DISCONTINUED OPERATIONS

SCCI entered into an agreement to sell the Sleep America business on November 5, 2014 for total proceeds of US\$12.4 million (net of working capital adjustment of US\$0.1 million). The assets and liabilities of Sleep America have been presented as held for sale in 2014 and its operations as “Discontinued Operations” in Q4 2015, 2015, 2014 and all comparative periods. The sale of the Sleep America business was completed on January 6, 2015.

5 Factors Affecting our Results of Operations

REVENUES

Revenues are derived primarily from the retail sales of mattress sets, accessories (including bed frames, pillows, mattress pads, sheets, duvets, headboards and footboards), third party warranty products and delivery fees. Revenue is recognized upon either delivery or customer pick-up.

SCC’s goal is to build on the market position of its Banners and to grow its revenue by driving Same Store Sales Growth (or “**SSSG**”), continuing to add stores in both new and existing markets and expanding its merchandising opportunities in accessories. SCC’s revenue is impacted by competition from other retailers that sell similar products and by seasonal patterns.

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SAME STORE SALES GROWTH

SSSG is a non-IFRS measure used in the retail industry to compare sales derived from established stores over a certain period compared to the same period in prior year. SSSG helps to explain what portion of sales growth can be attributed to growth in established stores and what portion can be attributed to the opening of the stores. SCC calculates SSSG as the percentage increase or decrease in sales of stores opened for at least 12 complete months relative to the same period in the prior year.

SSSG is primarily driven by:

- Increases in customer traffic through marketing and advertising;
- Increases in the conversion rate of turning shoppers into purchasers; and
- Increases in the average transaction size.

EXPANSION OPPORTUNITIES

SCC has the ability to add new stores in existing markets (in-fill stores), add new stores in satellite markets and pursue expansion opportunities into new markets. An existing market or in-fill opportunity is a pre-existing built out region in which SCC already has an established store presence serviced by one or more existing distribution centres. A satellite market is a new region/store which is adjacent or close to a pre-existing built out region which benefits from advertising spill and is serviced logistically from the nearby distribution centre. A new market is a brand new territory, such as the Company's recent entry into New Brunswick, requiring incremental advertising and distribution logistics.

Sleep Country has successfully expanded every year since its founding in 1994. This capability to expand depends on SCC's ability to choose new locations and new markets, to hire and train new employees for its stores and distribution centres and, in the case of expansion into new markets, create top-of-mind brand awareness of its Banners.

SCC's site selection strategy is focused on maximizing sales per store and per region throughout its store network. Prior to identifying and ultimately selecting locations for new stores, management conducts extensive analysis utilizing the following factors: (i) demographics such as population density, household income and population growth rates; (ii) store visibility and accessibility; (iii) lease and advertising economics; (iv) competitive dynamics; (v) overlap with existing stores and distribution footprint; and (vi) potential cannibalization of existing stores. In terms of regional expansion, once a target area has been determined, management focuses on ensuring that SCC can successfully incorporate its culture (vision and mission) into the new region. To help accomplish this, SCC has traditionally started by ensuring that the core of its new regional team is comprised of existing employees in leadership roles who are willing to relocate. The team is then supplemented with local hires, who received three to four weeks of training and have to spend a few weeks in existing stores and distribution centres learning SCC's service model and learning the culture.

The following table summarizes SCC's store count from continuing operations for each of the three and twelve-month periods ended December 31, 2014 and December 31, 2015:

	Q4 2015	Q4 2014	2015	2014
Number of stores, beginning of period	224	212	212	208
Stores newly opened	1	1	13	5
Stores closed	1	1	1	1
Number of stores, end of period	224	212	224	212
Stores relocated	1	3	3	3
Stores renovated	5	1	10	9

The one new store opened in Q4 2015 was an in-fill store. Of the 13 new stores opened in 2015, seven were in-fill stores, three were satellite stores and three were in the new market of New Brunswick.

ENHANCED STORE DESIGN

An enhanced store design was implemented in certain existing stores during the second half of 2014. During 2015, 10 existing stores were renovated to this design. In addition, all new stores opened during 2015 feature this enhanced store design. Over time, SCC intends to strategically select additional stores to renovate to this new design, which will continue to be featured by all new stores that it opens.

COMPETITION

The retail mattress industry is highly competitive. The seven leading retailers in the industry include Sleep Country/Dormez-vous?, Sears Canada Inc., Leon's Furniture Limited/The Brick Ltd., Hudson's Bay Company, BMTC Group Inc., IKEA and Costco Wholesale Canada Inc. Of these leading seven retailers, Sleep Country is the only specialty mattress retailer. Management believes it can maintain a leading position through its highly differentiated service model that has been unrivalled in execution over the last 21 years and serves as a significant barrier to entry.

SEASONALITY

The mattress retail industry is affected by seasonal conditions. SCC typically experiences higher sales and a greater proportion of income during the third and fourth quarters due to a concentration of summer season holidays in the third quarter and other seasonal factors. Sales have historically trended lower in the first quarter as consumers tighten their budgets after the holiday season. The cold winter weather in many parts of the country during the first quarter also tends to lower customers' desire to shop. SCC expects these trends to continue for the foreseeable future. Average quarterly share of annual sales over the last three fiscal years is as follows:

First quarter	21%
Second quarter	23%
Third quarter	31%
Fourth quarter	25%
Yearly total	100%

COST OF SALES AND GROSS PROFIT

Cost of sales includes product-related costs and the costs of SCC's sales and distribution operations net of volume rebates received from suppliers. Cost of sales is impacted by the number of stores, fluctuations in the volume of inventories sold, average unit selling prices and SCC's ability to manage store level occupancy costs.

Product gross margin is affected by changes in sales product mix, suppliers' term discount and inventory management.

The largest component of SCC's sales operational costs are the sales associates' compensation and store occupancy costs. The largest component of SCC's distribution operations are labour costs and delivery expenses.

Volume rebates are driven by the purchase volume of inventory from suppliers. Some suppliers also offer step-ups on higher volume achieved as additional incentives. The rebates are pro-rated between products sold and those still in inventory. Only rebates on products sold are recorded as a reduction to cost of sales.

6 Q4 and Full Year Operational Highlights

	Q4			Year ended		
	2015	2014	Change %	2015	2014	Change %
<small>(C\$ millions unless otherwise stated; other than store count)</small>						
Revenues	\$ 119.1	\$ 100.6	18.4%	\$ 456.2	\$ 396.1	15.2%
SSSG	12.9%	10.2%		11.3%	8.3%	
Stores opened	1	1		13	5	
Stores closed	1	1		1	1	
Stores renovated	5	1		10	9	
Gross profit margin	27.3%	26.6%		27.8%	26.1%	
Operating EBITDA	16.3	13.6	19.9%	69.1	50.6	36.6%
Operating EBITDA margin %	13.7%	13.5%		15.2%	12.8%	
Net income (loss) from continuing operations	8.6	3.3	160.6%	(51.7)	(17.1)	202.3%
Adjusted net income from continuing operations	8.5	7.2	19.4%	39.3	25.3	55.6%
Adjusted earnings per share from continuing operations	\$ 0.23	\$ 0.19	19.4%	\$ 1.05	\$ 0.67	55.5%

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HIGHLIGHTS OF RESULTS FROM CONTINUING OPERATIONS IN Q4 2015

Total revenues increased by 18.4% driven by strong same store sales growth of 12.9% on top of 10.2% in Q4 2014. The Company continued to execute on its store expansion strategy and opened one new store in Q4 2015 (Q4 2014 - one). Gross profit margins and EBITDA margins improved in Q4 2015 compared to Q4 2014 which translated into higher Adjusted Net Income of \$8.5 million (Q4 2014 - \$7.2 million) and a growth of 19.4% in Adjusted Earnings Per Share from \$0.19 in Q4 2014 to \$0.23 in Q4 2015. See "Non-IFRS Measures".

HIGHLIGHTS OF RESULTS FROM CONTINUING OPERATIONS IN 2015

Total revenues increased by 15.2% driven by strong same store sales growth of 11.3% on top of 8.3% in 2014. The Company continued to execute on its store expansion strategy and opened 13 new stores in 2015 (2014 - five).

Revenue was also positively impacted by the enhanced store design which was implemented in certain existing stores during the second half of 2014. To date, 13 of SCC's existing stores have been renovated to this enhanced design. Early results have reported that the 13 renovated stores have achieved higher SSSG than other stores in their regions since their respective reopening dates. Over time, Sleep Country intends to strategically select stores to renovate to this enhanced design and all new stores that it opens will feature this enhanced design.

Gross profit margins and EBITDA margins improved in 2015 compared to 2014 which translated into a growth in Adjusted Net Income of 55.6% from \$25.3 million in 2014 to \$39.3 million in 2015. Adjusted Earnings Per Share increased by 55.5% to \$1.05 in 2015 from \$0.67 in 2014. See "Non-IFRS Measures".

During 2015, the Company incurred a number of one-time, non-cash transactions related to the capital structure that existed prior to the IPO as well as other non-recurring items at the time of the IPO. Including these items, which are not indicative of strong core business performance achieved in the period, net loss for 2015 was \$51.7 million (\$1.90 loss per share) compared to a loss of \$17.1 million (\$1.52 loss per share) for 2014.

In January 2015, the Company also completed the sale of the Sleep America business for US\$12.4 million (net of a working capital adjustment of US\$0.1 million). The assets and liabilities of Sleep America have been presented as held for sale in 2014 and its operations as "Discontinued Operations" in Q4 2015, 2015, 2014 and all comparative periods.

OUTLOOK

Since its inception, Sleep Country has developed a leading regional market strategy, a strong brand with top-of-mind unaided brand awareness, a reputation for excellence in customer service and strong supplier relationships. Now that this platform has been established, the Company believes it has a low-risk path to growth and expansion within its existing markets.

Management believes that Sleep Country is well-positioned to continue to grow revenue, profitability and cash flows by:

- continuing to add 8 to 12 new stores per year in both existing and new markets;
- driving SSSG by continuing to invest in advertising and sales training;
- renovating 15 to 20 stores per year to feature the enhanced store design; and
- expanding its merchandising opportunities in accessories.

SELECTED FINANCIAL INFORMATION

The following table sets out selected IFRS and certain non-IFRS financial measures of SCC and should be read in conjunction with the audited consolidated financial statements for 2015.

(C\$ thousands unless otherwise stated)	Q4 2015	Q4 2014	2015	2014	2013
Consolidated Income Statement					
Revenues	\$ 119,106	\$ 100,649	\$ 456,185	\$ 396,085	\$ 353,922
Cost of sales	86,548	73,855	329,370	292,665	265,834
Gross profit	32,558	26,794	126,815	103,420	88,088
General and administrative expenses	16,487	13,846	67,805	54,898	50,226
Depreciation and amortization	2,774	2,459	10,346	9,897	9,342
Income before finance, interest and other (income) expenses and income taxes	13,297	10,489	48,664	38,625	28,520
Finance related expenses	1,226	6,400	112,316	61,502	23,215
Interest income and other (income) expenses - net	(12)	(58)	15	21	(145)
Net loss before income taxes	12,083	4,147	(63,667)	(22,898)	5,450
Income taxes	3,465	867	(11,975)	(5,762)	1,069
Net income (loss) from continuing operations	8,618	3,280	(51,692)	(17,136)	4,381
Net income (loss) from discontinued operations	(23)	4,772	5,992	2,996	(2,588)
Net income (loss)	\$ 8,595	\$ 8,052	\$ (45,700)	\$ (14,140)	\$ 1,793
Operating EBITDA⁽¹⁾	\$ 16,291	\$ 13,577	\$ 69,125	\$ 50,645	\$ 39,407
Operating EBITDA Margin⁽¹⁾	13.7%	13.5%	15.2%	12.8%	11.1%
Adjusted net income from continuing operations⁽¹⁾	8,542	7,155	39,314	25,274	20,344
Earnings per share from continuing operations - Basic	\$ 0.16	\$ (0.01)	\$ (1.90)	\$ (1.52)	\$ 0.01
Earnings per share from continuing operations - Diluted	\$ 0.16	\$ -	\$ (1.90)	\$ (1.52)	\$ 0.01
Earnings per share from discontinued operations - Basic	\$ -	\$ 0.17	\$ 0.20	\$ 0.10	\$ (0.10)
Earnings per share from discontinued operations - Diluted	\$ -	\$ 0.06	\$ 0.20	\$ 0.10	\$ (0.10)
Adjusted earnings per share from continuing operations⁽¹⁾	\$ 0.23	\$ 0.19	\$ 1.05	\$ 0.67	\$ 0.54
Dividends declared per share	\$ 0.13	\$ -	\$ 0.13	\$ -	\$ -
Total assets			31-Dec-15	31-Dec-14	31-Dec-13
			439,367	462,370	440,223
Long-term debt			124,223	257,838	220,115

Note:

⁽¹⁾ See the section below entitled "Non-IFRS Measures" for further details concerning how the Company calculates Operating EBITDA, Operating EBITDA Margin, Adjusted Net Income and Adjusted Earnings per Share (EPS) and for reconciliation to the most comparable IFRS measure.

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7 Fourth Quarter 2015 versus Fourth Quarter 2014

CONTINUING OPERATIONS

Revenues

Revenues increased by 18.4%, from \$100.6 million in Q4 2014 to \$119.1 million in Q4 2015 primarily driven by a 12.9% increase in SSSG. See "Non-IFRS Measures". Sales growth was further aided by the addition of 13 new stores in 2015 as well the one new store opened in Q4 2014.

The increase in total revenue was comprised of an increase in mattress sales and accessory sales. Mattress sales revenue increased by 15.6%, from \$81.1 million to \$93.7 million. Accessory revenue increased by 29.8%, from \$19.5 million to \$25.4 million.

Gross profit

Gross profit was \$32.6 million in Q4 2015 compared to \$26.8 million in Q4 2014, representing an increase of \$5.8 million. Gross profit margin increased by 0.7% to 27.3% for Q4 2015 from 26.6% in Q4 2014 as a result of the following factors:

- Sales and distribution compensation decreased as a percentage of sales from 17.1% in Q4 2014 to 16.2% in Q4 2015;
- Improved leverage on store occupancy costs which decreased as a percentage of sales from 10.6% to 9.7%; and
- Inventory and other directly related expenses net of volume rebates increased as a percentage of sales from 44.9% to 46.1% mainly due to increased warranty provisions taken.

General and administrative ("G&A") expenses

Total G&A expenses increased by \$2.7 million, or 19.6%, from \$13.8 million in Q4 2014 to \$16.5 million in Q4 2015; however, as a percentage of sales, G&A remained flat. The increase in G&A was driven by a:

- planned \$1.4 million increase in advertising expense to drive more traffic into SCC's stores;
- \$0.5 million increase in professional fees mostly due to public company expenses; and
- \$0.3 million increase in bank and finance charges due to an increase in sales volume.

EBITDA

EBITDA was \$16.1 million for Q4 2015 compared to \$12.9 million for Q4 2014, representing an increase of \$3.2 million (or 24.8%). See "Non-IFRS Measures". The increase was primarily due to strong revenue growth in Q4 2015 combined with improved gross profit margins partially offset by an increase in G&A expenses.

Operating EBITDA

Operating EBITDA was \$16.3 million for Q4 2015 compared to \$13.6 million for Q4 2014, representing an increase of \$2.7 million (or 19.9%). See "Non-IFRS Measures". The increase was primarily due to strong revenue growth in Q4 2015 combined with improved gross profit margins partially offset by an increase in G&A expenses.

Depreciation and amortization expenses

Depreciation and amortization increased from \$2.5 million in Q4 2014 to \$2.8 million in Q4 2015 mainly due to capital expenditure on new stores and store renovations.

Finance related expenses

Prior to the IPO, finance related expenses consisted of interest on senior credit facilities, finance leases, Series A and B promissory notes and Class A convertible shares and fair value adjustment expense on Class B common shares. Class B common shares were accounted for as liabilities. Subsequent to the completion of the IPO on July 16, 2015, finance related expenses consist of interest on senior credit facilities and finance leases.

Finance related expenses were \$1.2 million in Q4 2015 compared to \$6.4 million in Q4 2014, representing a decrease of \$5.2 million (or 81.3%). \$5,366 of the finance related expense in Q4 2014 was due to the early settlement of Series A and B promissory notes and Class A convertible shares and restructuring of Class B common shares in connection with the Pre-Closing Transactions. After the IPO, these finance related expenses were no longer incurred.

Excluding finance expenses that related to the capital structure that existed prior to the IPO, finance related expenses increased from \$1.0 million in Q4 2014 to \$1.2 million in Q4 2015, mainly due to higher average outstanding balances on the senior credit facilities in Q4 2015 compared to Q4 2014.

Income taxes (recovery)

Q4 2015 had an income tax expense of \$3.5 million versus \$0.9 million for Q4 2014.

The increase in current income tax expense of \$2.9 million was as a result of the increased taxable income, due to improved business results and operating margins and a higher allocation of partnership income of SCCLP to SCCI.

The increase in current income tax expense was offset by an increase in deferred income tax recoveries of \$0.3 million mainly due to a favorable deferred tax impact of additional finance costs associated with early repayment of the subordinated debts.

Net income

The net income for Q4 2015 was \$8.6 million (\$0.16 per share) compared to \$3.3 million (loss of \$0.01 per share) in Q4 2014 representing an increase of \$5.3 million. The increase was mainly due to an increase in EBITDA, lower finance related expenses, partially offset by an increase in income tax expense. See “Non-IFRS Measures”.

Adjusted net income

Adjusted Net Income for Q4 2015 was \$8.5 million (\$0.23 per share) compared to \$7.2 million (\$0.19 per share) for Q4 2014, which is an increase of \$1.3 million (or 19.4%). The increase was primarily due to higher Operating EBITDA partially offset by an increase in finance related expenses and income tax expense. See “Non-IFRS Measures”.

DISCONTINUED OPERATIONS

Net income (loss)

The sale of the Sleep America business for US\$12.4 million (net of working capital adjustment of US\$0.1 million) closed on January 6, 2015. Subsequently, in Q4 2015, Sleep America, LLC (the entity that operated the Sleep America business), SC US Holdco and SC Management were wound up into SCCLP. As a result, SCC realized a year-to-date gain of \$6.0 million, of which \$nil million was recognized in Q4 2015. The performance of the Sleep America business was presented in Q4 2014 as “Discontinued Operations” following the approval of the sale on November 5, 2014.

Management's Discussion and Analysis of Financial Condition and Results of Operation of Sleep Country Canada Holdings Inc.

8 Annual Financial Results 2015 versus 2014

CONTINUING OPERATIONS

Revenues

Revenues increased by 15.2%, from \$396.1 million in 2014 to \$456.2 million in 2015 primarily driven by an 11.3% increase in SSSG. See "Non-IFRS Measures". Sales growth was further aided by the addition of 13 new stores in 2015 as well as the five new stores opened in 2014.

The increase in total revenue was comprised of an increase in mattress sales and accessory sales. Mattress sales revenue increased by 13.1%, from \$323.1 million to \$365.6 million. Accessory revenue increased by 24.2%, from \$73.0 million to \$90.6 million.

Gross profit

Gross profit was \$126.8 million in 2015 compared to \$103.4 million in 2014, representing an increase of \$23.4 million. Gross profit margin increased by 1.7% to 27.8% for 2015 from 26.1% in 2014. The increase in gross profit margin was mainly due to the following factors:

- Inventory and other directly related expenses net of volume rebates decreased as a percentage of sales from 45.7% to 45.5% mainly due to a more favourable product mix;
- Sales and distribution compensation decreased as a percentage of sales from 17.0% in 2014 to 16.3% in 2015; and
- Improved leverage on store occupancy costs which decreased as a percentage of sales from 10.6% to 9.7%.

G&A expenses

Total G&A expenses increased by \$12.9 million, or 23.5%, from \$54.9 million in 2014 to \$67.8 million in 2015 mainly due to \$6.9 million in non-recurring management bonus relating to the legacy option plan that existed prior to the IPO and \$2.4 million in non-recurring professional fees related to the IPO. Excluding these non-recurring costs related to the IPO, total G&A expenses increased by \$3.6 million, or 6.7%, mainly due to an increase in advertising costs and an increase in bank and finance charges related to increased sales volumes.

EBITDA

EBITDA was \$59.0 million for 2015 compared to \$48.5 million for 2014, representing an increase of \$10.5 million (or 21.6%). See "Non-IFRS Measures". The increase was primarily due to the strong revenue growth in 2015 combined with improved gross profit margins on a more favorable product mix and operating leverage on fixed costs including G&A expenses, offset by \$6.9 million in non-recurring bonus relating to the legacy option plan that existed prior to the IPO and \$2.4 million in non-recurring professional fees related to the IPO.

Operating EBITDA

Operating EBITDA was \$69.1 million for 2015 compared to \$50.6 million for 2014, representing an increase of \$18.5 million (or 36.6%). Operating EBITDA Margin also improved from 12.8% to 15.2% in 2015 compared to 2014. The increase in Operating EBITDA was primarily due to the strong revenue growth in 2015 combined with improved gross profit margins on a more favorable product mix and operating leverage on fixed costs including G&A expenses. See "Non-IFRS Measures".

Depreciation and amortization expenses

Depreciation and amortization increased marginally from \$9.9 million in 2014 to \$10.3 million in 2015, mainly due to capital expenditure on new stores and store renovations.

Finance related expenses

Prior to the IPO, finance related expenses consisted of interest on senior credit facilities, finance leases, Series A and B promissory notes and Class A convertible shares and fair value adjustment expense on Class B common shares. Class B common shares were accounted for as liabilities. Subsequent to the completion of the IPO on July 16, 2015, finance related expenses consist of interest on senior credit facilities and finance leases.

Finance related expenses were \$112.3 million in 2015 compared to \$61.5 million in 2014, representing an increase of \$50.8 million (or 82.6%). The increase was mainly due to the non-cash accelerated interest accretion upon the early repayment of certain promissory notes, non-cash accelerated interest accretion recognized upon redemption of certain convertible shares, non-cash fair value adjustment on Class B common shares, higher interest expense on the increased senior credit facility and interest paid on Class B common shares. The contractual term for the promissory notes and convertible shares had a redemption date of 2023. As a result of their early settlement in July 2015 as part of Pre-Closing Transactions, non-cash accelerated interest expense has been recognized in the quarter. The non-cash accelerated interest expense including accretion on the promissory notes in 2015 was \$84.7 million (2014 - \$46.1 million) and the interest expense on the Class A convertible shares and Class B common shares, along with the non-cash fair value adjustment on the Class B common shares in 2015 was \$20.6 million (2014 - \$10.6 million). In addition, acceleration of amortization of debt issuance cost relating to the senior credit facility that was in place prior to the IPO was \$1.2 million (2014 - \$nil).

Excluding finance expenses that related to the capital structure that existed prior to the IPO, finance related expenses increased from \$4.8 million in 2014 to \$5.8 million in 2015, mainly due to higher average outstanding balances on the senior credit facilities in 2015 compared to 2014.

Income taxes (recovery)

2015 had an income tax recovery of \$12.0 million versus an income tax recovery of \$5.8 million for 2014.

The deferred income tax recovery increased by \$11.4 million from \$10.7 million for 2014 to \$22.1 million for 2015 mainly as a result of a favourable deferred tax impact of IPO-related costs and additional finance costs associated with early repayment of the subordinated debt. This increase was offset by an increase in current income tax expense of \$5.1 million from \$5.0 million in 2014 to \$10.1 million in 2015 as a result of the increased taxable income due to improved business results and a higher allocation of partnership income of SCCLP to SCCI.

Net loss

During 2015, the Company incurred a number of one-time, non-cash transactions related to the capital structure that existed prior to the IPO as well as other non-recurring items at the time of the IPO. Including these items, which are not indicative of strong core business performance achieved in the period, net loss for 2015 was \$51.7 million (\$1.90 loss per share) compared to a loss of \$17.1 million (\$1.52 loss per share) for 2014. The items that impacted the net loss in 2015 were:

- i) the non-cash accelerated interest accretion expense upon the early settlement of the subordinated debt and convertible shares amounting to \$105.3 million;
- ii) acceleration on the amortization of debt issuance costs relating to the senior credit facility that existed prior to the IPO amounting to \$1.2 million;
- iii) non-recurring management bonus relating to the legacy option plan that existed prior to the IPO amounting to \$6.9 million;
- iv) non-recurring professional fees related to the IPO of \$2.4 million;
- v) management compensation of \$0.7 million that has reduced since the IPO; and
- vi) share based compensation associated with the new management compensation plan of \$0.2 million.

In aggregate, these items amounted to \$91.2 million on an after-tax basis.

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Adjusted Net Income

Adjusted Net Income for 2015 was \$39.3 million compared to \$25.3 million for 2014, which is an increase of \$14.0 million (or 55.6%). The increase was primarily due to improved Operating EBITDA, offset by higher finance related expenses and higher taxation expense. See "Non-IFRS Measures".

DISCONTINUED OPERATIONS

Net income (loss)

The sale of the Sleep America business for US\$12.4 million (net of working capital adjustment of US\$0.1 million) closed on January 6, 2015. Subsequently, in Q3 2015, Sleep America, LLC (the entity that operated the Sleep America business), SC US Holdco and SC Management were wound up into SCCLP. As a result, SCC realized a gain of \$6.0 million. The performance of the Sleep America business was presented in Q4 2014 as "Discontinued Operations" following the approval of the sale on November 5, 2014.

9 Summary of Quarterly Results

Over the past two years, the Company's quarterly revenue and earnings have steadily increased with the third quarter typically generating the greatest contribution to revenues and earnings, and the first quarter the least. This is largely due to the seasonal nature of revenue and the timing of marketing programs. Accordingly, results of operations for any interim period are not necessarily indicative of the results of operations for the full fiscal year. The following table shows the financial performance of the Company by quarter for the last two years and has been prepared in accordance with IFRS.

					2015
(C\$ thousands unless otherwise stated)	Q4	Q3	Q2	Q1	Total
Revenues	\$ 119,106	\$ 142,946	\$ 102,520	\$ 91,613	\$ 456,185
SSSG	12.9%	13.4%	7.7%	10.5%	11.3%
EBITDA ⁽¹⁾	16,071	19,700	12,935	10,304	59,010
Operating EBITDA ⁽¹⁾	16,291	28,742	13,370	10,722	69,125
Operating EBITDA Margin ⁽¹⁾	13.7%	20.1%	13.0%	11.7%	15.2%
Net income (loss) from continuing operations	8,618	8,047	(50,666)	(17,691)	(51,692)
Net income (loss) from discontinued operations	(23)	(176)	(586)	6,777	5,992
Net income (loss)	8,595	7,871	(51,252)	(10,914)	(45,700)
Adjusted net income from continuing operations ⁽¹⁾	8,542	17,811	7,085 ⁽²⁾	5,876 ⁽²⁾	39,314
Earnings per share from					
continuing operations - Basic	\$ 0.16	\$ 0.39	\$ (2.70)	\$ (1.09)	\$ (1.90)
Earnings per share from					
discontinued operations - Basic	\$ -	\$ (0.01)	\$ (0.02)	\$ 0.20	\$ 0.20
Earnings per share from					
continuing operations - Diluted	\$ 0.16	\$ 0.39	\$ (2.70)	\$ (1.09)	\$ (1.90)
Earnings per share from					
discontinued operations - Diluted	\$ -	\$ (0.01)	\$ (0.02)	\$ 0.20	\$ 0.20
Adjusted earnings per share from					
continuing operations ⁽¹⁾	\$ 0.23	\$ 0.47	\$ 0.19	\$ 0.16	\$ 1.05

Note:

⁽¹⁾ See the section below entitled "Non-IFRS Measures" for further details concerning how the Company calculates SSSG, EBITDA, Operating EBITDA, Operating EBITDA Margin, Adjusted Net Income and Adjusted Earnings per Share (EPS) and for reconciliation to the most comparable IFRS measure.

⁽²⁾ Prior to the IPO, a certain percentage of taxable income of Sleep Country Canada LP ("SCCLP") was allocated to minority shareholders. As a result of the Pre-Closing Transactions, 100% of taxable income of SCCLP is allocated to SCCI. Adjustments have been made to reflect the change in taxation expense.

					2014
(C\$ thousands unless otherwise stated)	Q4	Q3	Q2	Q1	Total
Revenues	\$ 100,649	\$ 121,426	\$ 92,666	\$ 81,344	\$ 396,085
SSSG	10.2%	11.1%	9.1%	1.30%	8.3%
EBITDA ⁽¹⁾	12,948	22,224	7,594	5,756	48,522
Operating EBITDA ⁽¹⁾	13,577	22,727	8,782	5,559	50,645
Operating EBITDA Margin ⁽¹⁾	13.5%	18.7%	9.5%	6.8%	12.8%
Net income (loss) from continuing operations	3,280	10,531	(27,946)	(3,001)	(17,136)
Net income (loss) from discontinued operations	4,772	(527)	(688)	(561)	2,996
Net income (loss)	8,052	10,004	(28,634)	(3,562)	(14,140)
Adjusted net income from continuing operations ⁽¹⁾	7,155	13,086	3,553 ⁽²⁾	1,480 ⁽²⁾	25,274 ⁽²⁾
Earnings per share from					
continuing operations – Basic	\$ (0.01)	\$ 0.21	\$ (1.56)	\$ (0.19)	\$ (1.52)
Earnings per share from					
discontinued operations – Basic	\$ 0.17	\$ (0.02)	\$ (0.02)	\$ (0.02)	\$ 0.10
Earnings per share from					
continuing operations – Diluted	\$ -	\$ 0.07	\$ (1.56)	\$ (0.19)	\$ (1.52)
Earnings per share from					
discontinued operations – Diluted	\$ 0.06	\$ (0.01)	\$ (0.02)	\$ (0.02)	\$ 0.10
Adjusted earnings per share from					
continuing operations ⁽¹⁾	\$ 0.19	\$ 0.35	\$ 0.09	\$ 0.04	\$ 0.67

Note:

⁽¹⁾ See the section below entitled “Non-IFRS Measures” for further details concerning how the Company calculates SSSG, EBITDA, Operating EBITDA, Operating EBITDA Margin, Adjusted Net Income and Adjusted Earnings per Share (EPS) and for reconciliation to the most comparable IFRS measure.

⁽²⁾ Prior to the IPO, a certain percentage of taxable income of Sleep Country Canada LP (“SCCLP”) was allocated to minority shareholders. As a result of the Pre-Closing Transactions, 100% of taxable income of SCCLP is allocated to SCCI. Adjustments have been made to reflect the change in taxation expense.

10 Segment Performance

As at December 31, 2015, SCC manages its business on the basis of one operating segment, being Canada, which is also SCC’s only reportable segment consistent with the internal reporting provided to management.

11 Liquidity and Capital Resources

LIQUIDITY

SCC’s primary sources of cash consist of existing cash balances, operating activities, and available credit facilities. SCC’s primary uses of cash are to fund operating expenses, capital expenditures, finance costs, taxation expense, debt principal payments and dividends. Historically, SCC has experienced lower sales and EBITDA in the first quarter of the year. Management believes that cash generated from operations, together with cash and cash equivalents on hand and amounts available under SCC’s credit facilities will be sufficient to meet its future cash requirements. However, SCC’s ability to fund future cash requirements will depend on its future operating performance, which could be affected by general economic, financial and other factors including factors beyond its control despite the risk management strategies that management puts in place. See the section entitled “Risk Factors” in the AIF for a discussion of the various risks and uncertainties that may affect the Company’s ability to fund its future cash requirements.

Management reviews new store opening, acquisition and investment opportunities in the normal course of its business and may, if suitable opportunities arise, realize these opportunities to meet SCC’s business strategy. Historically, the funding for any such acquisitions or investments has come from cash flow generated from operating activities and/or additional debt.

The Company operates under a negative working capital position as a result of the difference in timing between when a customer pays for their purchased product and when the Company pays their suppliers. Typically, a customer will pay in full at the time of the sale; however, the Company has negotiated extended payment terms with the majority of its suppliers. Management believes that cash generated from operations, together with cash and cash equivalents on hand and amounts available under SCC’s credit facilities will be sufficient to sustain a negative working capital position.

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A summary of net cash flows by activities is presented below for 2015 and 2014:

(C\$ thousands unless otherwise stated)	2015	2014
Cash flows from operating activities	\$ 58,992	\$ 47,715
Cash flows from (used in) investing activities	(196,379)	(7,285)
Cash flows used in financing activities	112,688	(26,534)
Exchange rate difference on cash and cash equivalents	-	41
Net increase (decrease) in cash	(24,699)	13,937
Cash at beginning of period	41,338	27,401
Cash at end of period	\$ 16,639	\$ 41,338

Net cash flows from operating activities

Net cash flows generated from operating activities increased from \$47.7 million for 2014 to \$59.0 million for 2015. During 2015, cash generated from operating activities before changes in Working Capital was \$50.0 million and was positively impacted by cash generated of \$9.0 million from a decrease in Working Capital. The decrease in Working Capital for 2015 was primarily driven by higher trade and other payables, higher customer deposits, lower prepaid expenses and deposits and was offset by higher inventories and trade and other receivables. During 2014, cash generated from operating activities before changes in Working Capital of \$41.6 million was positively impacted by cash generated of \$6.1 million from a decrease in Working Capital. The decrease in Working Capital for 2014 was primarily driven by higher trade and other payables and customer deposits, and was offset by higher inventories, trade and other receivables and prepaid expenses and deposits.

Net cash flows used in investing activities

Net cash flows generated from investing activities consist mainly of purchase of shares in SCCI of \$196.8 million and proceeds from the sale of Sleep America for US\$12.4 million offset by investments in capital expenditure. Total capital expenditure increased from \$7.3 million for 2014 to \$14.6 million for 2015 mainly due to new store openings and store renovations.

Net cash flows used in financing activities

Net cash flows generated by financing activities were \$112.7 million for 2015, consisting primarily of cash received from the IPO (net of IPO expenses) of \$283.5 million and from the issue of Class E shares of \$2.3 million. This was partially offset by a net decrease in the senior term loan of \$2.8 million, repayment of the promissory notes, Class A convertible shares, Class B common shares and Class D common shares of SCCI of \$78.8 million, purchase of Class A common shares of \$77.6 million, dividends on shares of \$5.8 million and interest payments of \$6.6 million on the senior term loan and Class B common shares. Net cash flows used in 2014 were \$26.5 million consisting primarily of the repayment of promissory notes of \$60.5 million, interest payment of \$6.0 million on the senior term loan and Class B common shares, dividends on Class A shares of SCCI of \$7.5 million, return of capital on Class A convertible, Class B and Class D common shares of \$7.0 million, financing costs on the senior credit facility of \$1.4 million offset by additional senior term loan taken of \$56.8 million.

Contractual obligations

The Company's contractual obligations consist primarily of leases for stores and distribution centres, all of which are classified as operating leases. Minimum lease payments under long-term leases for store locations and distribution centres, excluding percentage rent, as at December 31, 2015, are listed below.

Not later than one year	\$ 33,636
Later than one year and not later than five years	89,058
Later than five years	34,301
Total	\$ 156,995

CAPITAL RESOURCES

Senior secured credit facility

On January 1, 2015, SCCI held a revolving credit facility of \$15 million and a term credit facility of \$130 million. On February 25, 2015, SCCI increased its revolving credit facility by \$15 million to \$30 million. On July 16, 2015, concurrently with the closing of the IPO, SCCI replaced its \$30 million revolving and \$130 million term credit facilities with a \$175 million revolving credit facility which matures on July 16, 2020, with full repayment due at maturity of all amounts outstanding. Net transaction costs associated with the replaced revolving and term facilities of \$1,205 were expensed in 2015.

As at December 31, 2015, the balance outstanding on the revolving credit facility was \$124 million (December 31, 2014 - \$nil and \$126.75 million outstanding on the term credit facility).

Interest on the term facility is based on the prime or bankers' acceptance rates plus applicable margins based on the achievement of certain targets, as defined by the senior secured credit agreement. As at December 31, 2015 the applicable margin for bankers' acceptances was 225 basis points and the applicable margin for prime was 125 basis points. Interest on the bankers' acceptance is payable in advance, whereas that on the prime rate is payable in arrears. Interest on the revolving facilities is payable monthly in advance at the bankers' acceptance rate or in arrears at the prime rate plus the applicable margin based on the achievement of certain targets, as defined by the senior secured credit agreement.

Under the terms of the revolving credit facilities, certain financial and non-financial covenants must be maintained. As at December 31, 2015, the Company and its subsidiaries were in compliance with all covenants under the senior secured credit facility.

Series A and Series B promissory notes

In 2015, \$61.9 million of Series A and Series B notes were repaid. Also, promissory notes held by related parties were early settled as part of the IPO in July 2015. As a result of these transactions, the cash flow assumptions related to the Series A and B promissory notes were revised and resulted in non-cash accelerated interest expense being recognized. For 2015, SCCI incurred non-cash accelerated interest expense as noted, including accretion, of \$84.7 million (2014 - \$46.1 million) on the Series A and B notes.

In connection with the closing of the IPO, the Series A and B notes were settled for Class A common shares of SCCI based on their face value of \$140,092.

Class A convertible shares and Class B common shares

On February 25, 2015, there was a repayment of \$4.0 million on the Class A convertible shares. Also, convertible shares held by related parties were early settled as part of the IPO in July 2015. This resulted in non-cash accelerated interest accretion expense being recognized on the Class A convertible shares. The non-cash interest accretion on the Class A convertible shares, along with interest expense on the Class B common shares were partially offset by a non-cash fair value adjustment, for a cumulative expense of \$20.6 million recorded for 2015 (2014 - \$10.6 million).

In connection with the closing of the IPO, the Class A convertible shares were converted into Class A common shares of SCCI based on their face value of \$33.4 million.

OFF BALANCE SHEET ARRANGEMENTS

SCC did not have any material off-balance sheet arrangements as at December 31, 2015 and December 31, 2014, nor does it have any subsequent to December 31, 2015.

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RELATED PARTY TRANSACTIONS

Funds controlled by Birch Hill Equity Partners Management Inc. ("Birch Hill") beneficially own, control or direct, directly or indirectly, approximately 14.5% of the votes attached to the Company's issued and outstanding common shares. Birch Hill also has dispositive powers, but not voting direction or control, with respect to approximately 4.4% of the common shares beneficially owned by certain co-investors. Birch Hill also maintains two nominee directors on the Company's Board of Directors. As such, Birch Hill is considered to have significant influence and is deemed to be a related party of the Company as at December 31, 2015.

The following balances are due from related parties:

	2015	2014
Short-term advances to related parties	\$ 4	\$ 16

Short-term advances due from related parties were a result of tax liability and professional fee expenses paid by the Company on behalf of the related parties.

Prior to the IPO, 28.82% of the Class A convertible shares and 97.64% of the Class B common shares of SCCI were held by key management, of which two members of the Board of Directors held an ownership interest.

12 Transactions with Key Management Personnel

Key management personnel are those individuals having authority and responsibility for planning, directing and controlling the activities of the Company, including members of the Company's Board of Directors. The Company considers key management to be the Board of Directors and its five most highly compensated executive officers. SCC incurred the following compensation expenses in relation to key management personnel:

(C\$ thousands unless otherwise stated)

	2015	2014
Salaries and short-term employee benefits	\$ 5,006	\$ 3,620
Share-based compensation	171	14
Non recurring bonus relating to the legacy option plan	5,096	-
Directors fees	150	-
	\$ 10,423	\$ 3,634

13 Risk Factors

SCC's activities expose it to a variety of financial risks: market risk (including foreign exchange risk and cash flow and fair value interest risk), credit risk and liquidity risk. SCC's overall risk management program and business practices seek to minimize any potential adverse effects on SCC's consolidated financial performance.

Risk management is carried out by the senior management team and is reviewed by SCC's Board of Directors.

MARKET RISK

Market risk is the loss that may arise from changes in factors such as interest rates, foreign exchange rates and the impact these factors may have on other counterparties.

FOREIGN EXCHANGE RISK

SCC's operating results are reported in Canadian dollars. A portion of the Company's merchandise purchases are denominated in U.S. dollars which results in foreign currency exposure related to fluctuations between the Canadian and U.S. dollars. The Company does not currently use foreign exchange option or forward contracts to hedge its foreign currency risk. A sudden increase in the U.S. dollar relative to the Canadian dollar could result in higher costs to the Company which could in turn result in increased prices and reduced sales, decreased profit margins and could negatively impact the Company's business and financial results.

CASH FLOW AND FAIR VALUE INTEREST RISK

SCC has no significant interest-bearing assets. SCC's income and operating cash flows are substantially independent of changes in market interest rates.

SCC's primary interest rate risk arises from long-term debt. SCC manages its exposure to changes in interest rates by using a combination of fixed and variable rate debt and utilizing interest rate swaps as necessary to achieve the desired proportion of variable and fixed rate debt. An increase (or decrease) in interest rates by 1% would result in a \$1.2 million increase (or decrease) on annual interest expense on the credit facility. SCC also has a small number of finance leases that carry interest at variable rates.

CREDIT RISK

Credit risk refers to the risk of losses due to failure of SCC's customers or other counterparties to meet their payment obligations. Credit risk arises from deposits with banks, as well as credit exposures from mattress suppliers for the payment of volume and co-operative advertising rebate amounts and balances owed from third-party financing companies under the various financing plans SCC offers its customers. In accordance with SCC's investment practice, all deposits are held at banks possessing a credit rating of "AA-" or better. Sales to retail customers are settled in cash, financed by third-party financing companies or by using major credit cards. SCC transfers the credit risk for financing plans to third-party financing companies. The third-party financing companies that SCC deals with carry a minimum rating of "BBB" or better.

There are no significant impaired receivables that have not been provided for in the allowance. There are no amounts considered past due or impaired.

LIQUIDITY RISK

Liquidity risk is the risk that SCC cannot meet a demand for cash or fund its obligations as they come due. Liquidity risk also includes the risk of not being able to liquidate assets in a timely manner at a reasonable price. Prudent liquidity management implies maintaining sufficient cash and cash equivalents and the availability of funding through an adequate amount of committed credit facilities.

CAPITAL RISK

SCC's objectives when managing capital are to safeguard its ability to continue as a going concern in order to provide returns for its shareholders in the form of cash dividends, benefits to other stakeholders and to maintain an optimal capital structure to minimize the cost of capital.

For an understanding of other potential risks, including non-financial risks, see the section entitled "Risk Factors" in the AIF.

14 Critical Accounting Estimates

A summary of significant accounting policies is included in Note 3 of SCC's 2015 audited consolidated financial statements. Critical accounting estimates require management to make certain judgments and estimates, which may differ from actual results. Accounting estimates are based on historical experience and other factors that management believes to be reasonable under the time frame and circumstances. Changes in management's accounting estimates can have a material impact on the financial results of the Company. The Company's critical accounting estimates are included in Note 4 of the SCC's 2015 audited consolidated financial statements and are described below.

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IMPAIRMENT OF GOODWILL AND BRANDS

Management is required to use judgment in determining the grouping of assets to identify the Company's cash generating units ("CGUs") for the purposes of testing fixed assets for impairment. Judgment is further required to determine appropriate groupings of CGUs for the level at which goodwill and intangible assets are tested for impairment. In addition, judgment is used to determine whether a triggering event has occurred requiring an impairment test to be completed.

In determining the recoverable amount of a CGU, various estimates are employed. The Company determines fair value less costs of disposal using estimates such as projected future sales, earnings, capital investments and discount rates. Projected future sales and earnings are consistent with strategic plans provided to the Company's Board of Directors. Discount rates are based on an estimate of the Company's weighted average cost of capital taking into account external industry information reflecting the risk associated with the specific cash flows. As at December 31, 2015 and 2014, impairment reviews were performed by comparing the carrying value of goodwill and brands with the recoverable amount of the CGU to which goodwill and brands have been allocated. Management determined that there has been no impairment.

LONG-TERM DEBT - PROMISSORY NOTES A AND B, CLASS B COMMON SHARES AND CLASS A CONVERTIBLE SHARES

The calculation of amortized cost associated with the Series A and B promissory notes, Class B common shares and the Class A convertible shares, in each case of SCCI, required management to utilize the effective interest rate approach and make certain judgments regarding the expected cash outflows associated with the respective financial liability. Changes in the expected timing and amounts of cash outflows due to early repayments or changes in the redemption values impacted amounts recognized as interest expense. For example, if the promissory notes were repaid prior to the contractual maturity date, non-cash interest accretion would be accelerated resulting in additional charges in the consolidated statement of operations, which would be material.

15 Financial Instruments

At December 31, 2015, the financial instruments consisted of cash, accounts receivable, accounts payable and accrued liabilities and senior secured notes. Cash and cash equivalents, trade and other receivables, due from related companies, accounts payable and accrued liabilities are measured at amortized cost and their fair values approximate carrying values due to their short-term nature. The carrying values of the revolving facilities approximate their fair values as the terms and conditions of the borrowing arrangements are comparable to market terms and conditions as at December 31, 2015 and December 31, 2014. The finance leases approximate their fair values as the implicit interest rates used in determining their fair value approximate interest rates as at December 31, 2015 and December 31, 2014. The Company's financial instruments are exposed to certain financial risks, including currency risk, interest rate risk, credit risk and liquidity risk, which are discussed above under the heading "Risk Factors".

16 Disclosure Controls and Procedures

Disclosure controls and procedures are designed to provide reasonable assurance that material information relating to the Company is made known to the Chief Executive Officer and the Chief Financial Officer (the "Certifying Officers") by others on a timely basis so that appropriate decisions can be made regarding public disclosure within the time periods required by applicable securities laws. The Certifying Officers are responsible for establishing and maintaining the Company's disclosure controls and procedures.

Our system of disclosure controls and procedures includes, but is not limited to, our Disclosure Policy, our Code of Business Conduct, the effective functioning of our Disclosure Committee, procedures in place to systematically identify matters warranting consideration of disclosure by the Disclosure Committee, verification processes for individual financial and non-financial metrics and information contained in annual and interim filings, including the consolidated financial statements, MD&As, AIF, Management Information Circular and other documents and external communications.

Based on an evaluation of the Company's disclosure control and procedures, the Certifying Officers have concluded that these controls are appropriately designed and were operating effectively as of December 31, 2015. Although the Company's disclosure controls and procedures were operating effectively as of December 31, 2015, there can be no assurance that the Company's disclosure controls and procedures will detect or uncover all failures of persons within the Company to disclose material information otherwise required to be set forth in the Company's regulatory filings.

17 Internal Control over Financial Reporting

Management is also responsible for establishing and maintaining appropriate internal controls over financial reporting. Our internal controls over financial reporting include, but are not limited to, Entity Level Controls, Information Technology General Controls, Information Technology Application and Development Controls, detailed policies and procedures related to financial accounting and reporting and controls over systems that process and summarize transactions. Our procedures for financial reporting also include the active involvement of qualified financial professionals, senior management, executive management and our Audit Committee.

Internal control over financial reporting (“ICFR”) is designed to provide reasonable assurance regarding the reliability of the Company’s financial reporting and the preparation of financial statements in accordance with IFRS. The Certifying Officers are responsible for establishing and maintaining adequate ICFR for the Company. In designing ICFR, it should be recognized that due to inherent limitations, any controls, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives and may not prevent or detect misstatements. Projections of any evaluations of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate. Additionally, management is required to use judgment in evaluating ICFR.

The Company’s internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Company, (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company, and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company’s assets that could have a material effect on the financial statements.

A “material weakness” in internal control over financial reporting is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of a company’s annual or interim financial statements will not be prevented or detected in a timely basis by the company’s internal controls.

The Certifying Officers have evaluated the effectiveness of the Company’s ICFR as at December 31, 2015 using the framework established in “Internal Control – Integrated Framework (COSO Framework)” published by The Committee of Sponsoring Organizations of the Treadway Commission (COSO), 2013. Based on that evaluation, the Certifying Officers concluded that the ICFR, as defined by National Instrument 52-109 – *Certification of Disclosure on Issuers’ Annual and Interim Filings*, are appropriately designed and were operating effectively as at December 31, 2015 and that no material weaknesses were identified through their evaluation.

18 Future Accounting Standards

The IASB and International Financial Reporting Interpretation Committee (IFRIC) have issued the following standards that have not been applied in preparing these consolidated financial statements as their effective dates fall within annual periods beginning subsequent to the current reporting period. The company is evaluating the impact of these standards and whether to early adopt these standards:

AMENDMENT TO IAS 1, PRESENTATION OF FINANCIAL STATEMENTS

This standard was amended to clarify guidance on materiality and aggregation, the presentation of subtotals, the structure of financial statements, and the disclosure of accounting policies. The amendment is required for years beginning on or after January 1, 2016.

IFRS 15, REVENUE FROM CONTRACTS WITH CUSTOMERS

This standard replaces all previous revenue recognition standards, including IAS 18 - Revenue. The new standard is effective for annual periods beginning on or after January 1, 2018 with early adoption permitted. The Company is analyzing the new standard to determine its impact on the Company’s consolidated balance sheet and consolidated statement of operations.

Management's Discussion and Analysis of Financial Condition and Results of Operation of Sleep Country Canada Holdings Inc.

IFRS 9, FINANCIAL INSTRUMENTS

This standard was issued concerning classification and measurement, impairment and hedge accounting, to supersede IAS 39, Financial Instruments: Recognition and Measurement. IFRS 9 will be effective for years beginning on or after January 1, 2018 with early adoption permitted. The Company is analyzing the new standard to determine its impact on the Company's consolidated balance sheet and consolidated statement of operations.

AMENDMENT TO IFRS 7, FINANCIAL INSTRUMENTS: DISCLOSURES

This standard was amended to provide guidance on additional disclosures on transition from IAS 39 to IFRS 9. The amendments are effective on adoption of IFRS 9.

IFRS 16, LEASES

IFRS 16, Leases ("IFRS 16") sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract, the customer (lessee) and the supplier (lessor). This will replace IAS 17, Leases ("IAS 17") and related Interpretations. IFRS 16 provides revised guidance on identifying a lease and for separating lease and non-lease components of a contract. IFRS 16 introduces a single accounting model for all lessees and requires a lessee to recognize right-of-use assets and lease liabilities for leases with terms of more than 12 months, unless the underlying asset is of low value, and depreciation of lease assets separately from interest on lease liabilities in the income statement. Under IFRS 16, lessor accounting for operating and finance leases will remain substantially unchanged. IFRS 16 is effective for annual periods beginning on or after January 1, 2019, with earlier application permitted for entities that apply IFRS 15, Revenue from Contracts with Customers.

As the Company has significant contractual obligations in the form of operating leases under IAS 17, there will be a material increase to both assets and liabilities upon adoption of IFRS 16, and material changes to the timing of recognition of expenses associated with the lease arrangements. The Company is analyzing the new standard to determine its impact on the Company's consolidated balance sheet and consolidated statement of operations.

19 Outstanding Share Data

As of the date hereof, 37,578,176 common shares and no Class A common shares of the Company are issued and outstanding. As of the date hereof, 139,334 options to purchase an equivalent number of common shares and 30,495 performance share units are issued and outstanding. For further details concerning the rights, privileges and restrictions attached to the common shares and the Class A common shares, please refer to the section entitled "Description of Share Capital" in the AIF.

20 Non-IFRS Measures

The Company prepares its financial statements in accordance with IFRS. In order to provide additional insight into the business, to provide investors with supplemental measures of its operating performance and to highlight trends in its business that may not otherwise be apparent when relying solely on IFRS financial measures, the Company has also provided in this MD&A certain non-IFRS measures, including "Same Store Sales Growth" or "SSSG", "EBITDA", "Operating EBITDA", "Operating EBITDA Margin", "Adjusted Net Income", "Adjusted EPS" and "Working Capital", each as defined below. These measures are provided as additional information to complement IFRS measures by providing further understanding of the Company's results of operations from management's perspective. Management also uses non-IFRS measures in order to facilitate operating performance comparisons from period to period, to prepare annual operating budgets and forecasts and to determine components of management compensation. The Company also believes that securities analysts, investors and other interested parties frequently use non-IFRS measures in the evaluation of issuers.

Readers are cautioned that these non-IFRS measures are not recognized under IFRS and do not have a standardized meaning prescribed by IFRS. They are therefore unlikely to be comparable to similarly titled measures presented by other publicly traded companies. Accordingly, they should not be considered in isolation nor as a substitute for analysis of the Company's financial information reported under IFRS. See below for further details concerning how the Company calculates these non-IFRS measures and for reconciliations to the most comparable IFRS measures.

EBITDA AND OPERATING EBITDA FROM CONTINUING OPERATIONS

EBITDA and Operating EBITDA from continuing operations are used by SCC to assess its operating performance.

EBITDA is defined as income (loss) before interest, taxes, depreciation and amortization expenses.

Operating EBITDA is defined as income (loss) before interest, taxes, depreciation and amortization expenses adjusted for:

- Normalization of management bonuses;
- Reduction in management compensation due to a change in the senior leadership team;
- Non-recurring management bonuses;
- Certain non-recurring professional fees relating to the IPO and certain shareholder matters, and
- Share based compensation.

NET INCOME AND ADJUSTED NET INCOME FROM CONTINUING OPERATIONS

Adjusted Net Income from continuing operations is used by SCC to assess its operating performance. Adjusted Net Income from continuing operations is defined as net income (loss) from continuing operations adjusted for:

- Interest expense on Series A and B notes;
- Interest expense and non-cash fair value adjustment on Class A convertible shares and Class B common shares;
- Acceleration of amortization of debt issuance costs;
- Normalization of management bonuses;
- Non-recurring management bonuses;
- Certain non-recurring professional fees relating to the IPO and certain shareholder matters;
- Reduction in management compensation due to a change in the senior leadership team;
- Share based compensation; and
- Tax impact of the change in corporate structure.

WORKING CAPITAL

“**Working Capital**” is defined as the sum of trade and other receivables, due from related parties, inventories, prepaid expenses and deposits less trade and other payables and customer deposits.

Management's Discussion and Analysis of Financial Condition and Results of Operation of Sleep Country Canada Holdings Inc.

CALCULATION OF NON-IFRS MEASURES

(C\$ thousands unless otherwise stated, except earnings per share)

	Q4 2015	Q4 2014	2015	2014	2013
Reconciliation of net loss from continuing operations to EBITDA and Operating EBITDA:					
Net loss from continuing operations	\$ 8,618	\$ 3,280	\$ (51,692)	\$ (17,136)	\$ 4,381
Interest and other (income) expenses – net	(12)	(58)	15	21	(145)
Finance related expenses	1,226	6,400	112,316	61,502	23,215
Income taxes	3,465	867	(11,975)	(5,762)	1,069
Depreciation and amortization	2,774	2,459	10,346	9,897	9,342
EBITDA	16,071	12,948	59,010	48,522	37,862
Adjustments to EBITDA:					
Reduction in management bonuses ¹	-	120	3	389	167
Non-recurring management bonuses ²	-	-	6,898	-	-
Non recurring items ³	121	160	2,358	356	24
Reduction in management compensation ⁴	-	346	685	1,364	1,337
Share-based compensation ⁵	99	3	171	14	17
Total adjustments	220	629	10,115	2,123	1,545
Operating EBITDA	16,291	13,577	69,125	50,645	39,407
Operating EBITDA Margin	13.7%	13.5%	15.2%	12.8%	11.1%
Reconciliation of net loss from continuing operations to Adjusted Net Income:					
Net income loss	\$ 8,618	\$ 3,280	\$ (51,692)	\$ (17,136)	\$ 4,720
Adjustments:					
Interest expense on Series A and B notes ⁶	-	4,498	84,726	46,051	18,059
Interest expense and fair value adjustment on Class A convertible shares and Class B common shares ⁷	-	868	20,602	10,584	2,370
Acceleration on amortization of debt issuance cost ⁸	-	-	1,205	-	-
Total interest adjustment	-	5,366	106,533	56,635	20,429
Reduction in management bonuses ¹	-	120	3	389	167
Non-recurring management bonuses ²	-	-	6,898	-	-
Non recurring items ³	121	160	2,358	356	24
Reduction in management compensation ⁴	-	346	685	1,364	1,337
Share-based compensation ⁵	99	3	171	14	17
Total adjustments	220	5,995	116,648	58,758	21,974
Tax impact of all adjustments	(58)	(1,117)	(25,404)	(12,656)	(5,147)
Tax impact of change in corporate structure ⁹	(238)	(1,003)	(238)	(3,692)	(1,203)
Adjusted net income from continuing operations	8,542	7,155	39,314	25,274	20,344
Weighted average number of shares¹⁰	37,554	37,539	37,543	37,539	37,539
Earnings per share from continuing operations	\$ 0.16	\$ (0.01)	\$ (1.90)	\$ (1.52)	\$ 0.01
Adjusted earnings per share from continuing operations	\$ 0.23	\$ 0.19	\$ 1.05	\$ 0.67	\$ 0.54

¹ Due to the fluctuation of financial performance, the management bonus payout in certain years hit stretch targets with a higher than what would be considered to be a "normal" run-rate. Adjustments are made to bring the management bonus payout to the average percentage payout of past 6 years over the base bonus level (or 126% over base).

² Adjustment for non-recurring management bonus relating to the close out of the legacy option plan that existed prior to the IPO.

³ Non-recurring items include professional fees and internal costs relating to SCCHI's capital reorganization and IPO.

⁴ Reduction in management compensation upon internal restructuring following the IPO.

⁵ Adjustment for share-based compensation, a non-cash item.

⁶ Adjustment for interest expense on promissory notes that were restructured in connection with the Pre-Closing Transactions.

⁷ Adjustment for non-cash fair value adjustment and interest expense on convertible shares and Class B common shares that were restructured in connection with the Pre-Closing Transactions.

⁸ Adjustment for acceleration of amortization of debt issuance cost relating to the senior credit facility that was in place prior to the IPO.

⁹ Prior to the IPO, a certain percentage of taxable income of Sleep Country Canada LP ("SCCLP") was allocated to minority shareholders. As a result of the Pre-Closing Transactions, 100% of taxable income of SCCLP is allocated to SCCHI and therefore this adjustment reflects the change in taxation expense.

¹⁰ This reflects the number of common shares outstanding post-IPO under the new corporate structure. The actual number of shares outstanding in 2014 for basic earnings per share were 19,711,000 shares for the twelve-month period ended December 31, 2014 and 18,990,000 shares for the three-month period ended December 31, 2014.

21 Additional Information

Additional information relating to the Company, including the Company's annual information form, quarterly and annual reports and supplementary information is available on SEDAR at www.sedar.com. Press releases and other information are also available in the Investor Relations section of the Company's website at www.sleepcountry.ca.



Independent Auditor's Report

February 24, 2016

**To the Shareholders of
Sleep Country Canada Holdings Inc.**

We have audited the accompanying consolidated financial statements of Sleep Country Canada Holdings Inc., which comprise the consolidated statements of financial position as at December 31, 2015 and December 31, 2014 and the consolidated statements of operations, comprehensive income (loss), changes in shareholders' equity and cash flows for the years then ended, and the related notes, which comprise 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 as issued by the International Accounting Standards Board, 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.

AUDITOR'S 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 auditor's 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 auditor considers 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 Sleep Country Canada Holdings Inc. as at December 31, 2015 and December 31, 2014 and the results of its operations and its cash flows for the years then ended in accordance with International Financial Reporting Standards.

PricewaterhouseCoopers LLP

(Signed) PricewaterhouseCoopers LLP
Chartered Professional Accountants, Licensed Public Accountants

Consolidated Statements of Financial Position of Sleep Country Canada Holdings Inc.

As at December 31, 2015 and December 31, 2014

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

	2015 \$	2014 \$
Assets		
Current assets		
Cash and cash equivalents (note 5)	16,639	41,331
Trade and other receivables (note 6)	8,402	6,477
Due from related parties - non-interest bearing and due on demand (note 19)	4	16
Inventories (note 7)	32,070	26,369
Prepaid expenses and deposits	1,624	2,475
Assets of disposal group held for sale (note 22)	-	14,086
	58,739	90,754
Property and equipment (note 8)	28,987	24,948
Deferred tax assets (note 13)	4,956	-
Other assets	463	480
Intangible assets other than goodwill (note 9)	104,076	104,042
Goodwill (note 9)	242,146	242,146
	439,367	462,370
Liabilities		
Current liabilities		
Trade and other payables (note 10)	46,024	33,729
Customer deposits	15,598	12,116
Long-term debt (note 12)	725	7,367
Liabilities of disposal group held for sale (note 22)	-	5,210
	62,347	58,422
Other liabilities (note 11)	8,897	6,965
Deferred tax liabilities (note 13)	10,309	31,820
Long-term debt (note 12)	124,223	257,838
	205,776	355,045
Shareholders' Equity		
Share capital and other (note 15)	350,655	123,603
Deficit	(117,064)	(63,693)
Currency translation reserve	-	428
Non-controlling interest (note 23)	-	46,987
	233,591	107,325
	439,367	462,370

Contingent liabilities and unrecognized contractual commitments (note 17)

Approved by the Board of Directors



Andrew Moor
Director



David Shaw
Director

The accompanying notes are an integral part of these consolidated financial statements.

Consolidated Statements of Operations of Sleep Country Canada Holdings Inc.

For the years ended December 31, 2015 and December 31, 2014

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

	2015	2014
	\$	\$
Revenues	456,185	396,085
Cost of sales (notes 7 and 14)	329,370	292,665
Gross profit	126,815	103,420
General and administrative expenses (note 14)	67,805	54,898
Depreciation and amortization	10,346	9,897
Income before finance, interest and other (income) expenses and income taxes	48,664	38,625
Finance related expenses (note 12)	112,316	61,502
Interest and other (income) expenses - net	15	21
	112,331	61,523
Loss before income tax recovery	(63,667)	(22,898)
Provision for income taxes (recovery) (note 13)		
Current	10,112	4,959
Deferred	(22,087)	(10,721)
	(11,975)	(5,762)
Net loss from continuing operations	(51,692)	(17,136)
Net income from discontinued operations (note 22)	5,992	2,996
Net loss for the year	(45,700)	(14,140)
Total net income (loss) attributable to		
Owners of the parent	(46,879)	(28,002)
Non-controlling interest	1,179	13,862
	(45,700)	(14,140)
Earnings (loss) per share attributed to the common shareholders of the Company (note 16)		
Basic and diluted earnings (loss) per share (in dollars)		
Continuing operations	\$ (1.90)	\$ (1.52)
Discontinued operations	0.20	0.10
Earnings (loss) per share	\$ (1.70)	\$ (1.42)

The accompanying notes are an integral part of these consolidated financial statements.

Consolidated Statements of Comprehensive Income (Loss) of Sleep Country Canada Holdings Inc.

For the years ended December 31, 2015 and December 31, 2014

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

	2015 \$	2014 \$
Net loss for the year	(45,700)	(14,140)
Other comprehensive income (loss) to be reclassified to consolidated statement of operations		
Cumulative translation differences related to discontinued operations	(428)	348
Total comprehensive loss for the year	(46,128)	(13,792)
Total comprehensive income (loss) attributable to		
Owners of the parent	(47,307)	(27,654)
Non-controlling interest	1,179	13,862
	(46,128)	(13,792)

The accompanying notes are an integral part of these consolidated financial statements.

Consolidated Statements of Changes in Shareholders' Equity of Sleep Country Canada Holdings Inc.

For the years ended December 31, 2015 and December 31, 2014

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

	Share capital and other			Total			
	Sleep Country Canada Holdings \$	Sleep Country Canada Inc. \$	Currency translation reserve \$	Deficit \$	Controlling interest \$	Non- controlling interest \$	Total equity \$
Balance – January 1, 2014	-	123,994	80	(28,234)	95,840	33,125	128,965
Net income (loss) for the year	-	-	-	(28,002)	(28,002)	13,862	(14,140)
Other comprehensive income	-	-	348	-	348	-	348
Comprehensive income (loss) for the year	-	-	348	(28,002)	(27,654)	13,862	(13,792)
Share-based compensation	-	14	-	-	14	-	14
Repurchase of shares and other	-	(405)	-	-	(405)	-	(405)
Pre-Offering dividends	-	-	-	(7,457)	(7,457)	-	(7,457)
Balance – December 31, 2014	-	123,603	428	(63,693)	60,338	46,987	107,325
Balance – January 1, 2015	-	123,603	428	(63,693)	60,338	46,987	107,325
Net income (loss) for the year	-	-	-	(46,879)	(46,879)	1,179	(45,700)
Other comprehensive loss	-	-	(428)	-	(428)	-	(428)
Comprehensive income (loss) for the year	-	-	(428)	(46,879)	(47,307)	1,179	(46,128)
Pre-Offering dividend declared	-	-	-	(1,612)	(1,612)	-	(1,612)
Post-Offering dividend declared	-	-	-	(4,880)	(4,880)	-	(4,880)
Issuance of common shares (note 15)	626,647	-	-	-	626,647	-	626,647
Reorganization (notes 15 and 23)	(276,159)	(123,603)	-	-	(399,762)	(48,166)	(447,928)
Share-based compensation (note 20)	167	-	-	-	167	-	167
Balance – December 31, 2015	350,655	-	-	(117,064)	233,591	-	233,591

The accompanying notes are an integral part of these consolidated financial statements.

Consolidated Statements of Cash Flows of Sleep Country Canada Holdings Inc.

For the years ended December 31, 2015 and December 31, 2014

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

	2015 \$	2014 \$
Cash provided by (used in)		
Operating activities		
Net loss for the year	(45,700)	(14,140)
Items not affecting cash		
Depreciation of property and equipment (note 8)	9,004	9,003
Amortization of intangible assets (note 9)	1,341	1,629
Reversal of brand intangible asset impairment (note 9)	-	(5,981)
Share-based compensation	171	14
Gain on sale of Sleep America (note 22)	(6,016)	-
Finance related expenses	112,316	61,502
Other non-cash expenses	887	330
Deferred income taxes	(22,087)	(10,721)
	49,916	41,636
Changes in non-cash items relating to operating activities (note 18)	9,076	6,079
	58,992	47,715
Investing activities		
Purchase of property and equipment	(13,200)	(6,533)
Purchase of intangible assets (note 9)	(1,375)	(752)
Proceeds on sale of Sleep America (note 22)	14,984	-
Purchase of Sleep Country Canada Inc.'s shares (note 23)	(196,788)	-
	(196,379)	(7,285)
Financing activities		
Issuance of common shares (note 23)	283,428	-
Purchase of Class A common shares for cancellation (note 23)	(77,621)	-
Issuance of Class E special shares (note 23)	2,337	-
Additional term loan taken on senior secured credit facility (note 12)	-	60,000
Repayment of senior secured credit facility	(2,750)	(3,250)
Financing costs on senior secured credit facility	(721)	(1,409)
Repayment of Series A and B promissory notes (note 12)	(61,855)	(60,502)
Repayment on Class A convertible shares, Class B and Class D common shares	(16,987)	(7,035)
Dividends paid on Class A common shares	(5,769)	(7,457)
Interest paid	(6,636)	(5,971)
Decrease in other long-term debt	(738)	(910)
	112,688	(26,534)
Exchange rate difference on cash and cash equivalents	-	41
Increase (decrease) in cash and cash equivalents during the year	(24,699)	13,937
Cash and cash equivalents – Beginning of year	41,338	27,401
Cash and cash equivalents – End of year	16,639	41,338
Non-cash investing and financing activities		
Series B promissory notes issued – interest in kind (note 12)	17,684	20,841
Acquisition of property and equipment under finance lease	1	398

The accompanying notes are an integral part of these consolidated financial statements.

Notes to Consolidated Financial Statements of Sleep Country Canada Holdings Inc.

December 31, 2015 and December 31, 2014

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

1 Organization

Sleep Country Canada Holdings Inc. (the Company or SCC) was incorporated by articles of incorporation under the Canada Business Corporations Act on May 27, 2015. The Company is authorized to issue an unlimited number of common shares without par value. The common shares are voting and entitled to dividends if, as and when declared by the Board of Directors. On May 27, 2015, the Company issued one common share to Birch Hill Feather (US) Holdings LP for cash consideration of \$1.

On July 16, 2015, in connection with the closing of its initial public offering of common shares (the Offering or the IPO), the Company completed the acquisition (the Acquisition) of all of the issued and outstanding shares of Sleep Country Canada Inc. (SCCI), Sleep Country US Holdco Canada Inc. (SC US Holdco) and SC Management Holding Inc. (SC Management, and together with SCCI and SC US Holdco, the Acquired Entities) not already owned by the Company pursuant to the terms and conditions of a share purchase agreement dated July 10, 2015 (the Purchase Agreement) entered into between the Company, the Acquired Entities and the former shareholders of the Acquired Entities. The Company and the Acquired Entities were controlled by funds managed by Birch Hill Equity Partners Management Inc. (Birch Hill). Prior to the Offering, Birch Hill held 84.6% of Class A common shares, 81.62% of Series A and B promissory notes and 71.18% of Class A convertible shares of SCCI. Upon completion of the Offering and the Acquisition, Birch Hill, and certain co-investors had voting direction and control over approximately 45.6% of the Company's common shares. On December 11, 2015, Birch Hill and its co-investors completed a secondary offering of 10,000,000 common shares of the Company (the Secondary Offering), following which Birch Hill and its co-investors had voting direction and control over approximately 18.9% of the Company's common shares.

Following completion of the Acquisition, on July 16, 2015, SC US Holdco and SC Management were dissolved into SCCI, leaving SCCI as the sole limited partner of Sleep Country Canada LP (SCCLP). On completion of the Acquisition, the general partner of SCCLP was Sleep Country Canada GP ULC, a newly formed Alberta unlimited liability Company (SCCGP). On January 1, 2016, SCCGP and SCCLP were dissolved and all the assets of SCCLP were transferred to SCCI.

The Company and its subsidiaries operate in the retail market place, offering mattresses and bedding related products. As at December 31, 2015, the main subsidiaries of the Company were SCCI, SCC GP and SCCLP.

The address of its registered office is 140 - Unit 1, Wendell Avenue, Toronto, Ontario.

2 Basis of Presentation

The consolidated financial statements of the Company are 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.

As the Company is a newly formed entity incorporated in 2015 and Birch Hill retained control over the Company and SCCI prior to the Offering and the Acquisition, the Acquisition is accounted for as a reorganization and recapitalization using the continuity of interests method. Financial information for the pre-Acquisition period, including the comparative period, is presented based on the historical financial information of SCCI.

The consolidated financial statements of the Company include the financial results of Sleep Country Canada Holdings Inc. and its subsidiaries.

The Company's operations can be affected by seasonal fluctuations due to changes in customer buying habits throughout the year.

The consolidated financial statements were reviewed by the Company's Audit Committee and approved and authorized for issuance by the Board of Directors on February 24, 2016.

Notes to Consolidated Financial Statements of Sleep Country Canada Holdings Inc.

December 31, 2015 and December 31, 2014

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

3 Significant Accounting Policies

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

BASIS OF CONSOLIDATION

The consolidated financial statements include the accounts of the Company and other entities that the Company controls. Control exists when the Company is exposed to or has rights to variable returns from its involvement in the entity and has the ability to direct the activities that significantly affect the entities' returns through its power over the entity. All intercompany transactions and balances are eliminated on consolidation.

NON-CONTROLLING INTERESTS

Non-controlling interest represents equity interests in subsidiaries owned by outside parties. The share of net assets of subsidiaries attributable to non-controlling interests is presented as a component of equity. Their share of net earnings is recognized directly in equity. Changes in the parent company's ownership interest in subsidiaries that do not result in a loss of control are accounted for as transactions within equity. When the Company ceases to have control or significant influence, any retained interest in the entity is re-measured to its fair value, with the change in the carrying amount recognized in net income (loss). The fair value is the initial carrying amount for the purposes of subsequently accounting for the retained interest as an associate, joint venture or financial asset.

As at December 31, 2015, the Company held through its subsidiaries the general partner unit and all of the preferred and common units of SCCLP. As at December 31, 2015, all commercial operations of the Company were undertaken by SCCLP and its registered address is 140 - Unit 1, Wendell Avenue, Toronto, Ontario.

As at December 31, 2014, SCCI held the general partner unit and the preferred units in Sleep Country LP, representing 98% of the partners' capital as at December 31, 2014, with common units being held by third party investors.

The allocation of the profit or loss of SCCLP is specified in the limited partnership agreement whereby on an annual basis specific allocations are made to the general partner and the remaining profit or loss is allocated to the third party investors on a pro rata basis based on the percentage of common units held. On July 16, 2015, subsequent to Acquisition, the Company effectively controlled the general partner unit, preferred units and 100% of the common units of SCCLP. For the year ended December 31, 2015, the allocation of profit or loss to the Company was 94.6% until July 16, 2015 and 100% thereafter (December 31, 2014 - 67%).

FINANCIAL ASSETS AND LIABILITIES

Financial assets and liabilities are recognized when the Company becomes a party to the contractual provision of the financial instrument. Financial assets are derecognized when the contractual rights to receive cash flows from the financial asset expire and financial liabilities are derecognized when obligations under the contract expire, are discharged or cancelled. Financial instruments upon initial recognition are measured at fair value and classified as financial assets or liabilities at fair value through the consolidated statements of operations, loans and receivables or other financial liabilities. Loans and receivables and other financial liabilities are measured at amortized cost. The following classifications have been applied:

- cash and cash equivalents, trade and other receivables and due from related parties are classified as loans and receivables; and
- trade and other payables, customer deposits and long-term debt have been classified as other financial liabilities. The Class B common shares of SCCI meet the definition of a financial liability under IFRS as the redemption feature (puttable on the death of the employee or certain other circumstances) creates an unavoidable contractual obligation to pay cash. The Class B common shares of SCCI are presented as a liability, measured at amortized cost based on the calculated redemption amount at each reporting period.

Long-term debt is recognized initially at fair value, net of recognized transaction costs, and is subsequently measured at amortized cost, being the carrying value. Any difference between the carrying value and the redemption value is recognized in the consolidated statements of operations and comprehensive income (loss) using the effective interest rate method.

Fees paid on the establishment of senior credit facilities are capitalized as a prepayment for liquidity services and amortized over the period of the facility to which it relates.

OFFSETTING FINANCIAL INSTRUMENTS

Financial assets and financial liabilities are offset and the net amount is reported in the consolidated statements of financial position when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis or to realize the asset and settle the liability simultaneously.

FOREIGN CURRENCY TRANSLATION

- Functional and presentation currency

Items included in the consolidated financial statements of each of the Company's entities are measured using the currency of the primary economic environment in which the entity operates (the functional currency). The functional currencies of the subsidiaries are Canadian dollars and, prior to January 6, 2015, United States dollars. The consolidated financial statements are presented in Canadian dollars, which is the Company's functional currency. The Company translates its foreign operations, whereby assets and liabilities are translated at the exchange rate in effect at the consolidated statements of financial position dates, while revenues and expenses are translated at an appropriate weighted average rate. Any resulting translation gains or losses are included in other comprehensive income (loss) and the currency translation reserve.

- Transactions and balances

Transactions denominated in a foreign currency are translated into the functional currencies at the rate in effect at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into the functional currencies at the exchange rates in effect at the year-end date and revenues and expenses are translated at the average rate during the year. Foreign exchange gains and losses are included in the consolidated statements of operations.

SEGMENT INFORMATION

As at December 31, 2015, the Company manages its business on the basis of one operating segment, which is also the Company's only reportable segment, which is consistent with the internal reporting provided to the chief operating decision-maker, the Chief Executive Officer. The Company operates in Canada, which is its country of domicile.

CASH AND CASH EQUIVALENTS

Cash and cash equivalents include cash on hand, deposits held with banks and other short-term highly liquid investments with original maturities of three months or less.

INVENTORIES

Inventories are stated at the lower of their carrying value determined on a specific item basis and estimated net realizable value. Net realizable value is the estimated selling price less applicable selling expenses. Trade discounts and volume rebates earned are deducted in determining the carrying value of inventory purchases.

TRADE AND OTHER RECEIVABLES

Receivable balances are recognized initially at fair value and a provision for impairment is established when there is evidence that the Company will not be able to collect all the amounts due according to the original terms of the receivable balance.

Notes to Consolidated Financial Statements of Sleep Country Canada Holdings Inc.

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

PROPERTY AND EQUIPMENT

Property and equipment are recorded at cost less accumulated depreciation, net of any impairment loss. Depreciation is computed on a straight-line basis at annual rates based on the estimated useful lives of the related assets as follows:

Computer hardware	36 months
Furniture, fixtures and other	48 to 60 months
Leasehold improvements	over the term of the lease
Assets under finance lease	over the term of the lease

Included in furniture, fixtures and other are office equipment depreciated over 60 months and certain vehicles depreciated over 48 months. Assets under finance lease primarily represent the delivery truck fleet.

The Company recognizes in the carrying amount of property and equipment the full purchase price of assets acquired/constructed as well as the costs incurred that are directly incremental as a result of the construction of a specific asset, when they relate to bringing the asset into working condition.

Estimates of useful lives, residual values and methods of depreciation are reviewed annually. Any changes are accounted for prospectively as a change in accounting estimate.

GOODWILL AND INTANGIBLE ASSETS

Intangible assets are assets acquired that lack physical substance and that meet the specified criteria for separate recognition from goodwill.

- Computer software
Computer software is recorded at cost less accumulated amortization, net of any impairment loss. Amortization is computed on a straight-line basis at annual rates based on the estimated useful life of 36 months.
- Non-compete contracts
Non-compete contracts are amortized over an estimated life of ten years.
- Brands
Brands are recorded at cost and are not subject to amortization, having an indefinite life. They are tested for impairment annually, as of the consolidated statements of financial position dates, or more frequently if events or circumstances indicate that they may be impaired.
- Goodwill
Goodwill is the residual amount that results when the purchase price of an acquired business exceeds the sum of the amounts allocated to the assets acquired, less liabilities assumed. Goodwill is not amortized and management tests goodwill for impairment annually or more frequently if events or changes in circumstances indicate that the asset might be impaired.

IMPAIRMENT OF NON-FINANCIAL ASSETS

Impairment of goodwill and indefinite life intangibles

Management tests goodwill and brands for impairment annually or more frequently if events or changes in circumstances indicate that the asset might be impaired. The asset will be written down if the carrying amount of the asset exceeds the higher of its fair value less costs to sell and its value in use.

For the purpose of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows. Goodwill is allocated to cash generating units (CGUs) or groups of CGUs for the purpose of impairment testing. The allocation is made to those CGUs or groups of CGUs that are expected to benefit from the synergies of the business combination from which the goodwill arose. The impairment tests are performed by comparing the carrying value of the assets (or asset groups) of these CGUs with their recoverable amount, which is the higher of their fair value less costs to sell and their value in use (which is the present value of the expected future cash flows of the relevant asset or CGU), as determined by management.

Impairment of definite life intangibles and property and equipment

Assets that are subject to amortization are periodically reviewed for indicators of impairment. Whenever events or changes in circumstances indicate that the carrying amount may not be recoverable, the asset or CGU is tested for impairment. To the extent that the asset or CGU's carrying amount exceeds its recoverable amount, an impairment loss is recognized in the consolidated statement of operations. The recoverable amount of an asset or a CGU is the higher of its fair value less costs of disposal and its value in use. Value in use is the present value of the future cash flows expected to be derived from an asset or CGU. The fair value is the price that could be received for an asset or CGU in an orderly transaction between market participants at the measurement date, less costs of disposal. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows.

Impairment reversals

If, in a subsequent period, the amount of recognized impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, a reversal of the previously recognized impairment, except for goodwill, is recognized in the consolidated statement of operations.

TRADE AND OTHER PAYABLES

Trade and other payables are obligations to pay for goods or services that have been acquired or rendered in the ordinary course of business from suppliers and employees. Trade and other payables are classified as current liabilities if payment is due or expected within one year or less. Otherwise, they are presented as non-current liabilities. Trade and other payables are recognized initially at fair value and subsequently measured at amortized cost.

CUSTOMER DEPOSITS

Customer deposits represent amounts paid by customers in advance of delivery of product (i.e. mattresses). These deposits can be for all or a portion of the total purchase price of the product. The amounts received representing the customer deposit is unencumbered and can be used for general corporate purposes. Once the product is delivered to the customer the liability is relieved and is recorded in sales. Over time, some portion of the customer deposits are not redeemed (breakage). Breakage income on customer deposits is determined based on historical patterns when it can be determined that the likelihood of usage is remote.

DECOMMISSIONING PROVISIONS

These provisions represent the cost of the Company's obligation to rehabilitate its stores and is estimated based on the present value of expected future rehabilitation costs and is recognized in the period in which the obligation is incurred. The present value of these costs is added to the cost of the associated asset and amortized over its useful life, while the corresponding liability will accrete to its future value over the same period.

Notes to Consolidated Financial Statements of Sleep Country Canada Holdings Inc.

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

SHARE-BASED COMPENSATION

The Company has a share-based compensation plan (the stock option plan) and a performance share unit plan (PSU plan), which are equity-settled share-based arrangements.

Equity-settled share-based payments to employees are measured at the fair value of the equity instrument granted. An option valuation model (Black-Scholes) is used to fair value stock options issued to employees on the date of grant. The market value of the Company's common shares on the date of the grant is used to determine the fair value of the equity-based share units issued to participants.

The Company grants stock options to certain employees, key management and the directors of the Company, while PSUs are granted only to key management. Stock options cliff vest after four years and PSUs cliff vest after three years. The initial fair value of equity-settled share-based arrangements is recognized as compensation expense with a corresponding increase in equity reserves over the related service period provided to the Company. Compensation expense is recognized over the applicable vesting period by increasing contributed surplus based on the number of awards expected to vest. This number is reviewed at least annually, with any change in estimate recognized immediately in compensation expense with a corresponding adjustment to contributed surplus.

REVENUE RECOGNITION

Revenue is recognized either on the customer picking up the product or on delivery of the product to the customer's home. Provisions for returns relating to the Company's various customer satisfaction programs are accrued based on historical experience.

LEASES

Assets, primarily delivery trucks, held under leases which result in the Company receiving substantially all the risks and rewards of ownership of the asset (finance leases) are capitalized at the lower of the fair value of the property and equipment or the estimated present value of the minimum lease payments. The corresponding finance lease obligation is included within long-term debt. The interest element is amortized using the effective interest rate method.

The Company leases stores and distribution centres. Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. The Company recognizes rental expense incurred and inducements received from landlords on a straight-line basis over the term of the lease. Any difference between the calculated expense and the amounts actually paid is reflected as deferred lease inducements in other liabilities in the Company's consolidated statements of financial position.

INCOME TAXES

Income taxes comprise current and deferred income taxes. Income taxes are recognized in the consolidated statements of operations, except to the extent that they relate to items recognized directly in other comprehensive income (loss) or directly in equity, in which case the income tax is recognized directly in other comprehensive income (loss) or equity, respectively.

Current income tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the end of the reporting period, and any adjustment to tax payable in respect of previous years.

Income taxes provided for by the Company and its corporate subsidiaries are accounted for using the liability method. Deferred income taxes arise due to the temporary differences in the financial reporting and tax bases of assets and liabilities. Changes in these temporary differences are reflected in the provision for deferred income taxes using substantively enacted income tax rates and regulations. Deferred taxes are recognized for all temporary differences except where they arise on goodwill that is not tax deductible, on the initial recognition of an asset or liability that is not a business combination and at the time of the transaction affects neither accounting nor taxable income, and in respect of differences associated with investments in subsidiaries where the group is able to control the timing of their reversal and it is probable that the temporary differences will not reverse in the foreseeable future. Deferred income tax assets are recognized to the extent that the recoverability of deferred income tax assets is considered more likely than not.

ASSETS HELD FOR SALE AND DISCONTINUED OPERATIONS

Assets are classified as assets held for sale when their carrying amount is to be recovered principally through a sale transaction and a sale is considered highly probable. They are stated at the lower of the carrying amount and fair value less costs to sell. There were no impairment losses recognized on the initial classification of these assets. Reversals of impairments are not recognized in excess of any cumulative impairment loss.

A discontinued operation is a component of the Company's business that represents a separate major line of business or geographical area of operations that has been disposed of or is held for sale. Classification as a discontinued operation including related impairment charges occurs upon disposal or when the operation meets the criteria to be classified as held for sale, if earlier. When an operation is classified as a discontinued operation, the comparative consolidated statement of operations is presented as if the operation had been discontinued from the start of the comparative period.

ACCOUNTING STANDARDS AND AMENDMENTS ISSUED BUT NOT YET ADOPTED

The IASB and International Financial Reporting Interpretation Committee (IFRIC) have issued the following standards that have not been applied in preparing these consolidated financial statements as their effective dates fall within annual periods beginning subsequent to the current reporting period. The Company is evaluating the impact of these standards and whether to early adopt these standards:

Amendment to IAS 1, Presentation of Financial Statements

This standard was amended to clarify guidance on materiality and aggregation, the presentation of subtotals, the structure of financial statements, and the disclosure of accounting policies. The amendment is required for years beginning on or after January 1, 2016.

IFRS 15, Revenue from Contracts with Customers

This standard replaces all previous revenue recognition standards, including IAS 18 - Revenue. The new standard is effective for annual periods beginning on or after January 1, 2018 with early adoption permitted. The Company is analyzing the new standard to determine its impact on the Company's consolidated statements of financial position and consolidated statements of operations.

IFRS 9, Financial Instruments

This standard was issued concerning classification and measurement, impairment and hedge accounting, to supersede IAS 39, Financial Instruments: Recognition and Measurement. IFRS 9 will be effective for years beginning on or after January 1, 2018 with early adoption permitted. The Company is analyzing the new standard to determine its impact on the Company's consolidated statements of financial position and consolidated statements of operations.

Amendment to IFRS 7, Financial Instruments: Disclosures

This standard was amended to provide guidance on additional disclosures on transition from IAS 39 to IFRS 9. The amendments are effective on adoption of IFRS 9.

IFRS 16, Leases

IFRS 16, Leases (IFRS 16) sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract, the customer (lessee) and the supplier (lessor). This will replace IAS 17, Leases (IAS 17) and related Interpretations. IFRS 16 provides revised guidance on identifying a lease and for separating lease and non-lease components of a contract. IFRS 16 introduces a single accounting model for all lessees and requires a lessee to recognize right-of-use assets and lease liabilities for leases with terms of more than 12 months, unless the underlying asset is of low value, and depreciation of lease assets separately from interest on lease liabilities in the income statement. Under IFRS 16, lessor accounting for operating and finance leases will remain substantially unchanged. IFRS 16 is effective for annual periods beginning on or after January 1, 2019, with earlier application permitted for entities that apply IFRS 15, Revenue from Contracts with Customers.

Notes to Consolidated Financial Statements of Sleep Country Canada Holdings Inc.

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

As the Company has significant contractual obligations in the form of operating leases under IAS 17, there will be a material increase to both assets and liabilities upon adoption of IFRS 16, and material changes to the timing of recognition of expenses associated with the lease arrangements. The Company is analyzing the new standard to determine its impact on the Company's consolidated statements of financial position and consolidated statements of operations.

4 Critical Accounting Estimates and Judgments

The preparation of financial statements requires management to make estimates and assumptions using judgments that affect the application of accounting policies and the reported amounts of assets and liabilities, income and expense during the reporting period. Estimates and other judgments are continually evaluated and are based on management's experience and other factors, including expectations about future events that are believed to be reasonable under the circumstances. Actual results may differ from those estimates.

The following discusses the most significant accounting judgments and estimates that the Company has made in the preparation of the consolidated financial statements.

IMPAIRMENT OF GOODWILL AND BRANDS

Management is required to use judgment in determining the grouping of assets to identify their CGUs for the purposes of testing fixed assets for impairment. Judgment is further required to determine appropriate groupings of CGUs in order to determine the level at which goodwill and intangible assets are tested for impairment. In addition, judgment is used to determine whether a triggering event has occurred requiring an impairment test to be completed.

In determining the recoverable amount of a CGU, various estimates are employed. The Company determines fair value less costs of disposal using estimates such as projected future sales, earnings, capital investments and discount rates. Projected future sales and earnings are consistent with strategic plans provided to the Company's Board of Directors. Discount rates are based on an estimate of the Company's weighted average cost of capital taking into account external industry information reflecting the risk associated with the specific cash flows. As at December 31, 2015 and December 31, 2014, impairment reviews were performed by comparing the carrying value of goodwill and brands with the recoverable amount of the CGU to which goodwill and brands have been allocated. Management determined that there had been no impairment as at both of those dates (note 9).

Long-term debt - Series A and B promissory notes, Class B common shares and Class A convertible shares

The calculation of amortized cost associated with the Series A and B promissory notes, Class B common shares and the Class A convertible shares, in each case of SCCI, required management to utilize the effective interest rate approach and make certain judgments regarding the expected cash outflows associated with the respective financial liability. Changes in the expected timing and amounts of cash outflows due to early repayments or changes in the redemption values impacted amounts recognized as interest expense. For example, if the promissory notes were repaid prior to the contractual maturity date, non-cash interest accretion would be accelerated resulting in additional charges in the consolidated statements of operations, which would be material.

5 Cash and Cash Equivalents

	2015	2014
	\$	\$
Cash at bank	16,639	41,331

6 Trade and Other Receivables

The Company's trade and other receivables consist of balances due from vendors related to volume and co-operative advertising rebates and balances due from the third party financing companies. As at December 31, 2015, no receivable balances were considered impaired (2014 - \$nil). The carrying amounts of the Company's trade and other receivables, which approximate their fair values, are denominated in Canadian dollars.

The maximum exposure to credit risk at the reporting date is the carrying value of the trade and other receivables.

7 Inventories

	2015	2014
	\$	\$
Merchandise	32,070	26,369
Inventory and directly related costs recognized as an expense	205,324	178,932
Write-downs of inventory due to net realizable value lower than cost	155	855
Write-offs due to damage or shrinkage	874	760

There have been no reversals of previously taken write-downs in 2015 or 2014.

Notes to Consolidated Financial Statements of Sleep Country Canada Holdings Inc.

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

8 Property and Equipment

	Computer hardware \$	Furniture, fixtures and other \$	Leasehold improvements \$	Assets under finance lease \$	Total \$
Year ended December 31, 2014					
At January 1, 2014	1,206	3,369	23,204	2,676	30,455
Additions	448	496	5,589	398	6,931
Depreciation	(697)	(1,050)	(6,539)	(717)	(9,003)
Disposal	-	(2)	(77)	(95)	(174)
Exchange differences	8	50	258	-	316
Transferred to disposal group classified as held for sale	(82)	(539)	(2,956)	-	(3,577)
At December 31, 2014	883	2,324	19,479	2,262	24,948
At December 31, 2014					
Cost	3,148	4,852	43,540	4,794	56,334
Accumulated depreciation	(2,265)	(2,528)	(24,061)	(2,532)	(31,386)
Net book value	883	2,324	19,479	2,262	24,948
Year ended December 31, 2015					
At January 1, 2015	883	2,324	19,479	2,262	24,948
Additions	713	1,673	10,813	1	13,200
Depreciation	(677)	(987)	(6,601)	(739)	(9,004)
Disposal	-	(12)	(145)	-	(157)
At December 31, 2015	919	2,998	23,546	1,524	28,987
At December 31, 2015					
Cost	2,305	6,075	53,064	4,440	65,884
Accumulated depreciation	(1,386)	(3,077)	(29,518)	(2,916)	(36,897)
Net book value	919	2,998	23,546	1,524	28,987

9 Intangible Assets

	Brands \$	Non-compete contracts \$	Computer software \$	Total \$
Year ended December 31, 2014				
At January 1, 2014	101,540	1,333	2,133	105,006
Additions	-	-	752	752
Amortization for the year	-	(280)	(1,349)	(1,629)
Disposal during the year	-	-	(80)	(80)
Exchange differences	-	-	4	4
Reversal of impairment loss	5,981	-	-	5,981
Transferred to disposal group classified as held for sale	(5,981)	-	(11)	(5,992)
At December 31, 2014	101,540	1,053	1,449	104,042
At December 31, 2014				
Cost	101,540	2,804	8,035	112,379
Accumulated amortization and impairments	-	(1,751)	(6,586)	(8,337)
Net book value	101,540	1,053	1,449	104,042
Year ended December 31, 2015				
At January 1, 2015	101,540	1,053	1,449	104,042
Additions	-	-	1,375	1,375
Amortization for the year	-	(282)	(1,059)	(1,341)
Exchange differences	-	-	-	-
At December 31, 2015	101,540	771	1,765	104,076
At December 31, 2015				
Cost	101,540	2,804	9,191	113,535
Accumulated amortization and impairments	-	(2,033)	(7,426)	(9,459)
Net book value	101,540	771	1,765	104,076

Amortization of \$1,341 (2014 - \$1,572) from the Canadian operating segment is included in the consolidated statements of operations. Amortization of \$nil (2014 - \$57) from the United States operating segment is reported in the net result of discontinued operations in the consolidated statements of operations.

In 2009, due to continued weakness in the business environment in which Sleep America operated, management determined that the value of the corporate brand had been impaired and a write-down of \$5,981 was recorded in the same year. As a result of entering into a sale agreement for the Sleep America assets on November 5, 2014, the impairment taken in 2009 was reversed, as discussed below (note 22).

Goodwill of \$242,146 (2014 - \$242,146) and the Sleep Country and Dormez-vous? corporate brands of \$101,540 (2014 - \$101,540) have been allocated to the overall Canadian operating segment: mattress retailer (Canadian Goodwill CGU). Goodwill of \$490, updated annually for foreign exchange translation, was allocated to the United States operating segment (US Goodwill CGU), and included as assets of disposal group held for sale as at December 31, 2014. Management has determined, using appropriate valuation methodologies, that there was no impairment of its goodwill or brands as at December 31, 2015 or December 31, 2014. In assessing goodwill and brands for impairment as at December 31, 2015, the Company compared the aggregate recoverable amount of the assets included in the CGUs to their respective carrying amounts. The recoverable amount has been determined based on the fair value less cost of disposal (discounted cash flows) of the CGUs using the 2016 budgets approved by management that made maximum use of observable markets for inputs and outputs. The fair value less cost of disposal is categorized as Level 3 in the fair value hierarchy. For periods beyond the budget period, cash flows were extrapolated using revenue growth rates of 6.2% - 6.5% (2014 - 4.5% - 5.3%) and a terminal growth rate of 2.5% (2014 - 2.5%) that do not exceed the long-term average for the mattress retailer segment. A discount rate of 10.3% (2014 - 12.5%) was used in the model. As at December 31, 2015 and December 31, 2014, any reasonable changes to the model assumptions would not result in an impairment.

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In January 2015, the Sleep America business was sold in excess of its carrying amount, which led to the reversal of a previously taken impairment on the Sleep America brand intangible in the amount of \$5,981. The recoverable amount was determined by the fair value less costs to sell and is categorized as Level 2 in the fair value hierarchy. The recoverable amount does not exceed the initial carrying value. The intangible asset was subsequently classified as an asset held for sale (note 22).

10 Accounts Payable and Accrued Liabilities

	2015	2014
	\$	\$
Trade payables	19,291	12,174
Income taxes payable	3,234	4,081
Accrued expenses	23,499	17,474
	46,024	33,729

Under certain agreements, the Company has the right to set off financial assets with financial liabilities with respect to vendor rebates owed and purchases. At December 31, 2015, the Company had gross financial assets of \$241 offset against gross financial liabilities of \$19,532. The net amount of \$19,291 owing has been recorded in trade payables as at December 31, 2015. The total gross financial assets of \$1,043 and gross financial liabilities of \$13,217 were netted to \$12,174 as trade payables owing at December 31, 2014.

11 Other Liabilities

	2015	2014
	\$	\$
Rent escalation	1,928	2,104
Decommissioning provisions	847	822
Deferred lease inducements	4,593	3,515
Warranty liability	1,529	524
	8,897	6,965

12 Long-Term Debt

	2015	2014
	\$	\$
Senior secured credit facility (i)	123,424	125,483
Series A and Series B promissory notes of SCCI	-	117,436
Class B common shares (2014 - 1,033,229) of SCCI	-	2,494
Class A convertible shares (2014 - 31,509,702) of SCCI	-	17,530
Finance lease obligation	1,524	2,262
	124,948	265,205
Less: Current portion of long-term debt	725	7,367
	124,223	257,838

(i) Represented net of transaction costs of \$576 as at December 31, 2015 (2014 - \$1,267).

SENIOR SECURED CREDIT FACILITY

On June 30, 2014, SCCI replaced an existing \$70,000 term credit facility with a five-year senior credit agreement with a term credit facility of \$130,000, which was fully drawn upon the agreement date, and a revolving credit facility of \$15,000, with an accordion feature of \$15,000, subject to a standby fee. The terms of this credit facility included quarterly principal repayments payable in arrears commencing September 30, 2014.

On February 25, 2015, SCCI increased its revolving credit facility by \$15,000 to \$30,000. On July 16, 2015, SCCI replaced its \$30,000 revolving and \$130,000 term credit facilities with a \$175,000 revolving credit facility which matures on July 16, 2020, with full repayment due at maturity of all amounts outstanding. Net transaction costs associated with the replaced revolving and term facilities of \$1,205 were expensed. The Company has guaranteed all of SCCI's obligations under the new credit facilities.

As at December 31, 2015, the balance outstanding on the revolving credit facility was \$124,000 (December 31, 2014 - \$nil on the revolving credit facility and \$126,750 outstanding on the term credit facility).

Interest on the term facility is based on the prime or bankers' acceptance rates plus applicable margins based on the achievement of certain targets, as defined by the senior secured credit agreement. As at December 31, 2015, the applicable margin for bankers' acceptances was 225 basis points and the applicable margin for prime was 125 basis points. Interest on the bankers' acceptance is payable in advance, whereas that on the prime rate is payable in arrears. Interest on the revolving facilities is payable monthly in advance at the bankers' acceptance rate or in arrears at the prime rate plus the applicable margin based on the achievement of certain targets, as defined by the senior secured credit agreement. The weighted average interest rate on the facility was 4.6% (2014 - 4.9%).

Under the terms of the new credit facilities, certain financial (which includes leverage and interest coverage ratios) and non-financial covenants must be maintained. As at December 31, 2015, SCCI was in compliance with all covenants.

The new credit facilities are secured by a first ranking charge on the assets of SCCI and SCC, except for specified permitted encumbrances.

SERIES A AND SERIES B PROMISSORY NOTES OF SCCI

The Series A promissory notes of SCCI (Series A notes) were recorded at their amortized cost, representing the present value of future interest and principal repayments to maturity, at a discount rate of 15%, being the estimated fair value rate of interest. Interest expense was accreting monthly such that on maturity the carrying amount would be equal to the principal of the Series A notes plus the issued Series B promissory notes of SCCI (Series B notes) that are issued in lieu of cash interest payments.

The Series A notes bore interest at a fixed rate of 12% per annum and interest was due on December 31 of each year. The Series A notes, including all accrued but unpaid interest, were due and payable on September 23, 2023. The Series A note holders were subordinated to the credit facility. Each Series A note ranked pari passu with all other notes.

SCCI had the option to pay the annual interest payment in cash or to issue to the note holder a Series B note for the amount of interest due. The Series B notes were non-interest bearing. An amount of \$17,684, net of withholding tax, in non-interest bearing Series B notes in lieu of the cash interest payment due on December 31, 2014 was issued in January 2015 (2014 - \$20,841). As at December 31, 2014, 82.36% of the Series A and Series B notes were held by related parties (note 19).

In 2015, \$61,855 of Series A and Series B notes were repaid. In July 2015, SCCI was acquired by the Company, prior to which, the outstanding Series A and B promissory notes were settled in shares of SCCI at their face value of \$140,092 (note 23). As a result of these transactions, the cash flow assumptions related to the Series A and Series B promissory notes were revised and resulted in accelerated interest expense being recognized. For the twelve-month period ended December 31, 2015, SCCI incurred accelerated interest expense as noted, including accretion, of \$84,726 (twelve-month period ended December 31, 2014 - \$46,051) on Series A and B notes.

CLASS B COMMON SHARES OF SCCI

As at December 31, 2014, the majority of the Class B common shares of SCCI were held by management. Under the terms of the investor agreement, management employees had the ability, upon death or disability, to put these shares back to SCCI for cash equal to the then fair market value of the shares. Due to this put option, Class B common shares of SCCI were accounted for as a liability and recorded at their amortized cost, determined in reference to the redemption amount. As a part of the acquisition of SCCI by the Company on July 16, 2015, the Class B common shares were settled for shares of the Company.

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CLASS A CONVERTIBLE SHARES OF SCCI (CONVERTIBLE SHARES)

The convertible shares were mandatorily redeemable, paid a fixed rate of return of 12% and as such were presented as debt in the consolidated financial statements. The convertible shares could not be repaid either in full or in part unless a concurrent pro rata payment was made on the Series A and Series B notes. There could also be no payment in respect of the interest on any of the Series A notes unless there was a concurrent pro rata dividend payment in cash in respect of the convertible shares. Each convertible share was to be converted into the number of Class D common shares equal to the notional value of the convertible share divided by the fair value of the Class D common share, which includes accrued dividends at 12%. Legal waivers were obtained from each of the convertible shareholders in respect of the non-payment of dividends that would otherwise be required during the year.

The convertible shares are recorded at amortized cost representing the present value of future dividends and redemption amounts, using the same term to maturity as the Series A notes, and at a discount rate of 15%, being the estimated fair value rate of interest and was accreting monthly such that on redemption the carrying amount will be equal to the redemption amount plus the accrued and unpaid dividends.

On February 25, 2015, there was a repayment of \$3,987 on the Class A convertible shares (2014 - \$7,035). In July 2015, SCCI was acquired by the Company. As part of the acquisition, the convertible shares were converted into Class D common shares of SCCI based on their face value of \$33,444 and ultimately exchanged for shares in the Company (note 23).

As a result of these transactions, the cash flow assumptions on the convertible shares have been revised and resulted in accelerated interest accretion. Due to the interest accretion, an expense of \$19,901 has been recorded for the twelve-month period ended December 31, 2015 (twelve-month period ended December 31, 2014 - \$8,810).

Finance related expenses included in the consolidated statements of operations include the following:

	2015	2014
	\$	\$
Interest on finance lease obligations	154	193
Revolver commitment fees	93	81
Interest expense on senior credit facility	6,741	4,593
Interest expense on Series A and Series B notes	84,726	46,051
Interest expense and fair value adjustment on Class A convertible and Class B common shares	20,602	10,584
	112,316	61,502

13 Income Tax

COMPONENTS OF INCOME TAX PROVISION (RECOVERY)

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

	2015	2014
	\$	\$
Current income tax expense	10,112	4,959
Deferred income tax expense (recovery) relating to		
Temporary differences	(22,300)	(10,721)
Deferred income tax rate changes	213	-
	(22,087)	(10,721)
Recovery of income taxes	(11,975)	(5,762)

RECONCILIATION TO EFFECTIVE TAX RATE

The overall income tax provision differs from the amount that would be obtained by applying the combined statutory income tax rate to income (loss) due to the following:

	2015	2014
	\$	\$
Loss of continuing operations before income taxes (recovery)	(63,667)	(22,898)
Weighted average Canadian income tax rate	26.50%	26.28%
Income tax expense (recovery) based on statutory income tax rate	(16,872)	(6,017)
Effect of income tax allocated to non-controlling interest	(238)	(3,692)
Effect of non-deductible expenses and other items	4,922	3,947
Deferred tax rate changes	213	-
	(11,975)	(5,762)
Effective income tax rate	18.80%	25.16%

DEFERRED INCOME TAX LIABILITY

Significant components of the net deferred income tax liability are as follows:

	2015	2014
	\$	\$
Excess of carrying value of intangible assets over tax values	(13,636)	(13,620)
Benefit of share issuance costs and financing fees deductible in future years	4,581	219
Loss carry-forwards - net of unrecognized deferred tax assets	789	-
Other temporary differences	2,913	2,001
Deferred income tax liability on Series A and B notes	-	(20,420)
	(5,353)	(31,820)

SCC has recognized a deferred tax asset of \$4,956, which is dependent on future taxable income. The Company has tax planning strategies available to ensure the realization of the deferred tax asset in the future.

Reconciliation of deferred income tax movement:

	2015	2014
	\$	\$
Deferred tax recovery in the consolidated statement of operations	(22,088)	(10,721)
Deferred tax expense (recovery) recorded in equity relating to share issuance costs	(4,378)	-
	(26,466)	(10,721)

The US operations were wound up in 2015 with the sale of the Sleep America business. The unrecognized deferred tax assets of US\$14,903 as at December 31, 2014 are no longer available. The deferred income tax assets were not included in the sale of Sleep America's assets and liabilities as described in note 22.

The Company has a refundable tax on hand balance of \$1,038 at the end of the 2014 taxation year.

As at December 31, 2015, the Company has unused capital losses of \$20,644 (2014 - \$nil) with no expiry date.

Capital losses may only be used to offset capital gains. No deferred tax benefit has been set up for these losses as the Company does not expect to realize capital gains in the foreseeable future.

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14 Expenses by Nature

	Cost of sales	
	2015	2014
	\$	\$
Inventory and directly related costs recognized as an expense, including write-downs and write-offs	207,701	180,821
Salaries, wages and benefits	74,349	67,307
Rent and other occupancy charges	44,317	42,001
Other	3,003	2,536
	329,370	292,665
	General and administrative	
	2015	2014
	\$	\$
Media and advertising expenses	20,499	18,814
Telecommunication and information technology	3,093	2,954
Salaries, wages and benefits	20,407	13,036
Credit card and finance charges	9,800	8,941
Rent and other occupancy charges	6,640	6,645
Professional fees	3,443	1,084
Other	3,923	3,424
	67,805	54,898

15 Share Capital and Other

Authorized share capital - SCC

Unlimited common shares

Unlimited Class A common shares

Issued and outstanding, no par value

	2015	2014
	\$	\$
37,578,176 common shares (2014 - nil)	626,647	-
Reorganization adjustment and other	(276,159)	-
Contributed surplus	167	-
	350,655	-

	Number of shares	Common shares \$	Reorganization adjustment \$	Contributed surplus \$	Total \$
On incorporation May 27, 2015	1	-	-	-	-
Shares issued for cash	17,650,000	300,050	-	-	300,050
Less: Issuance costs*	-	(12,242)	-	-	(12,242)
Shares issued on capital reorg	19,889,134	338,115	(276,159)	-	61,956
Share-based compensation	-	-	-	167	167
Dividend re-investment	39,041	724	-	-	724
As at December 31, 2015	37,578,176	626,647	(276,159)	167	350,655

* Issuance costs are net of deferred tax of \$4,956, which is recorded on the statement of financial position as at December 31, 2015.

COMMON SHARES AND CLASS A COMMON SHARES - SCC

The holders of common shares are entitled to receive notice of any meetings of shareholders, to attend and to cast one vote per common share at all such meetings. Holders of common shares do not have cumulative voting rights with respect to the election of directors and, accordingly, holders of a majority of the common shares entitled to vote in any election of directors may elect all directors standing for election. Holders of common shares are entitled to receive on a pro rata basis such dividends, if any, as and when declared by the Board of Directors at its discretion from funds legally available therefor and upon liquidation, dissolution or winding-up of the Company are entitled to receive on a pro rata basis the net assets of the Company after payment of debts and other liabilities, in each case subject to the rights, privileges, restrictions and conditions attaching to any other series or class of shares ranking senior in priority to or on a pro rata basis with the common shares with respect to dividends or liquidation. The common shares do not carry any pre-emptive, subscription, redemption or conversion rights, nor do they contain any sinking or purchase fund provisions.

Holders of Class A common shares will be entitled to the same rights and privileges as holders of common shares described above and will rank equally with the holders of common shares upon liquidation, dissolution or winding-up of the Company. The Class A common shares will not carry any pre-emptive or subscription rights, nor will they contain any sinking or purchase fund provisions. Class A common shares are redeemable at the option of the Company upon written notice to the holders of the Class A common shares, with the redemption price being equal to the price per common share in the initial public offering. In the event that the Company did not redeem Class A common shares within 45 days of initial public offering of the common shares, the Class A common shares were to automatically convert, on a one-for-one basis, into common shares. 4,565,962 Class A common shares were issued on July 16, 2015, all of which were redeemed on the same date with the net proceeds of \$77,621 from the initial public offering. As at December 31, 2015, there are no outstanding Class A common shares.

Authorized share capital - SCCI

Unlimited common shares

Unlimited Class A, B, C and D common shares

Issued and outstanding - SCCI

	2015 \$	2014 \$
Class A common shares (2014 - 18,989,868)	-	18,989
Contributed surplus	-	104,614
	-	123,603

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CLASS A, B, C AND D COMMON SHARES (COMMON SHARES) OF SCCI

The holders of the common shares of SCCI were entitled to receive, equally on a per share basis with the common shareholders, dividends as and when declared by the Board of Directors of SCCI. However, the holders of Class B common shares were entitled to receive, as and when declared by the Board of Directors of SCCI, dividends without dividends being declared to the Class A, C and D common shareholders.

The holders of Class A, B and C common shares are entitled to receive notice of and to attend all meetings of the shareholders of SCCI and are entitled to receive one vote per share on all matters to be voted on at all meetings of shareholders. The holders of Class D common shares are not entitled to receive notice of and to attend all meetings of the shareholders of SCCI and are not entitled to vote. The holders of common shares are not entitled to vote separately as a class or series or to dissent on certain proposals specified in the Articles of Incorporation.

Upon the voluntary or involuntary liquidation, dissolution or windup of SCCI, the holders of the common shares are entitled to share in the remaining assets available for distribution after payment of liabilities.

CLASS E SPECIAL SHARES (SPECIAL SHARES) OF SCCI

The holders of the special shares shall be entitled, at their option, to have the special shares converted into Class D common shares of SCCI. Each special share shall be converted into the number of Class D common shares having an aggregate value equal to the value of the special units of SCCLP then held by SCCI less the aggregate amount of dividends paid on the special shares.

Upon the voluntary or involuntary liquidation, dissolution or windup of SCCI, the holders of the special shares are entitled to receive, concurrent with any distribution of any amount of any part of the assets of SCCI among any of the other classes of shares, for each special share, an amount determined by the Board of Directors of SCCI.

16 Earnings (Loss) per Share (EPS)

Basic earnings (loss) per share amounts are calculated by dividing the net earnings (loss) attributable to common shareholders of the Company by the weighted average number of shares issued and outstanding during the year.

Diluted earnings (loss) per share amounts are calculated by dividing the net earnings (loss) attributable to common shareholders of the Company by the weighted average number of shares issued and outstanding during the year, adjusted for the effects of potentially dilutive stock options and PSUs.

The following table sets forth the calculation of basic and diluted EPS:

Attributable to common shareholders			
			2015
	Net earnings (loss) \$	Weighted average number of shares (in thousands of shares)	EPS \$
Basic and diluted			
Continuing operations	(52,508)	27,582	(1.90)
Discontinued operations	5,629	27,582	0.20
	(46,879)	27,582	(1.70)
Attributable to common shareholders			
			2014
	Net earnings (loss) \$	Weighted average number of shares (in thousands of shares)	EPS \$
Basic and diluted			
Continuing operations	(30,009)	19,711	(1.52)
Discontinued operations	2,007	19,711	0.10
	(28,002)	19,711	(1.42)

The effects of stock options were anti-dilutive for the three and twelve-month periods ended December 31, 2015 and for the twelve-month period ended December 31, 2014. The effects of performance share units (PSUs) were dilutive for the three and twelve-month periods ended December 31, 2015. The effects of convertible shares of SCCI were anti-dilutive for the twelve-month period ended December 31, 2014.

17 Contingent Liabilities and Unrecognized Contractual Commitments

OPERATING LEASES

The Company and its subsidiaries conduct all of their operations from leased stores and distribution centres. The Company has entered into operating lease arrangements for leased premises, delivery trucks, passenger vehicles and office equipment with terms varying from three to 15 years. For the year ended December 31, 2015, the total amount paid under these operating leases was \$33,057 (2014 - \$37,084).

Non-cancellable operating lease rentals are payable as follows:

	2015 \$	2014 \$
Less than 1 year	33,636	32,260
Between 1 and 5 years	89,058	85,179
More than 5 years	34,301	34,175
	156,995	151,614

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18 Changes in Non-Cash Items Relating to Operating Activities

	2015	2014
	\$	\$
Trade and other receivables	(1,925)	(951)
Due from related companies	12	(5)
Inventories	(5,701)	(2,608)
Prepaid expenses and deposits	851	(60)
Trade and other payables	12,295	6,730
Customer deposits	3,482	2,389
Other	62	584
	9,076	6,079

19 Related Party Transactions and Balances

As at December 31, 2014, SCCI was controlled by funds controlled by Birch Hill, which owned approximately 80.36% of SCCI's common shares, 82.36% of Class A and B promissory notes and 71.18% of Class A convertible shares. As at December 31, 2014, 28.82% of SCCI's Class A convertible shares and 97.64% of the Class B common shares were held by management. In connection with the Offering, all of the Class A convertible shares and Class B common shares of SCCI were disposed of by management and Birch Hill. SCCI is now a direct wholly-owned subsidiary of the Company.

Following completion of the Offering and the Secondary Offering, as at December 31, 2015, funds controlled by Birch Hill beneficially own, control or direct, directly or indirectly, approximately 14.5% of the votes attached to the Company's issued and outstanding common shares. Birch Hill also has dispositive powers, but not voting direction or control, with respect to approximately 4.4% of the common shares beneficially owned by certain co-investors. Birch Hill also maintains two nominee directors on the Company's Board of Directors. As such, Birch Hill is considered to have significant influence and is deemed to be a related party of the Company as at December 31, 2015.

The following balances are due from related parties:

	2015	2014
	\$	\$
Short-term advances to related parties	4	16

Short-term advances due from related parties were a result of tax liability and professional fee expenses paid by the Company on behalf of the related parties.

Compensation awarded to key management included:

	2015	2014
	\$	\$
Salaries and short-term employee benefits	5,006	3,620
Share-based compensation	171	14
Bonus related to Pre-IPO stock option plan	5,096	-
Directors fees	150	-
	10,423	3,634

The Company considers key management to be the Board of Directors and its executive team.

20 Share-Based Compensation

On July 16, 2015, in connection with the completion of the Offering, the Company established new share-based compensation arrangements consisting of a stock option plan and a performance share unit plan (PSU). The impact of share-based compensation is summarized as follows:

	Number outstanding	Expense \$
Stock options (a)	139,334	88
Performance share unit plan (b)	30,495	79
		167

Both the stock options and PSUs are to be equity settled. As such, the expense associated with these instruments is recorded as share-based compensation expense through the consolidated statements of operations with a corresponding entry made to contributed surplus on the consolidated statements of financial position.

The maximum number of common shares that may be issued under all security-based compensation arrangements implemented by the Company, including the stock option plan and the PSU plan, may not exceed 10% of the total number of common shares issued and outstanding from time to time. The maximum number of common shares that may be issued under the PSU plan is 4% of the total number of common shares issued and outstanding from time to time.

(a) Stock options

The Company has established a stock option plan under which options to purchase common shares may be granted to directors, officers and employees of the Company. Options granted under the plan have an exercise price of not less than the weighted average trading price of the common shares on the Toronto Stock Exchange for the five trading days prior to the date of the grant. Options granted vest on the fourth anniversary of the grant date. All issued options expire after ten years from the date granted.

The Company's stock options transactions during the year were as follows:

	Number of options	Weighted average exercise price per share \$
Balance - July 16, 2015	-	-
Granted	139,334	17.00
Balance - December 31, 2015	139,334	17.00

The Black-Scholes model was used to estimate the fair value of stock options. Key assumptions include a risk free interest rate of 1.39%, which is based on a Government of Canada 5 to 10-year benchmark bond yield at the date of grant, expected volatility of 43%, which is based on certain industry comparables, an estimated dividend yield of 3% and a 7-year expected life of the options. The options expire 10 years from the date of grant and vest on the fourth anniversary of the grant date.

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(b) PSU plan

The Company has established a PSU plan for full-time employees of the Company. A PSU represents the right to receive a common share of the Company, subject to adjustment as described below. PSUs granted will vest as to 100% on the third anniversary of the grant date and will generally be settled by the issuance of treasury shares or with shares purchased on the open market. The number of common shares to be issued on the settlement of a PSU will depend on an adjustment factor that ranges from 0.5 to 1.5 based on the Company's achievement of certain performance targets established by the Board of Directors at the time of grant. Therefore, the number of common shares that will be issued to settle outstanding PSUs may be higher or lower than the number of outstanding PSUs set out below.

The Company's PSU plan transactions during 2015 were as follows:

	Number
Balance - July 16, 2015	-
Granted - July 16, 2015	30,291
Granted - November 26, 2015	204
Balance - December 31, 2015	30,495

The grant date fair value of the units was \$17.00 per unit.

The vested number of units outstanding as at December 31, 2015 was nil (December 31, 2014 - nil).

At December 31, 2015, the total number of units outstanding (vested and unvested) was 30,495.

(c) Pre-IPO stock options

SCCI had established a share-based compensation plan on November 1, 2008 (the Pre-IPO Option Plan) to provide long-term incentives to certain key officers and employees of SCCI and its subsidiaries. Under the Pre-IPO Option Plan, 960,000 options were granted to purchase Class E special shares of SCCI at a strike price of \$2.80 per share and 140,000 options were granted at a strike price of \$3.04 per share. These options were not exercisable until the occurrence of a liquidity event. In July 2015, as a result of the Offering, a liquidity event was triggered and as such, the options under the Pre-IPO Option Plan became exercisable. At the discretion of SCCI, the options were exercised for Class E Special shares and cash reflecting the growth value of certain options (note 23).

21 Financial Instruments and Risk Management

The Company's activities expose it to a variety of financial risks: market risk (including foreign exchange risk and cash flow and fair value interest risk), credit risk and liquidity risk. The Company's overall risk management program and business practices seek to minimize any potential adverse effects on the Company's consolidated financial performance.

Risk management is carried out by the senior management team and overseen by the Board of Directors.

MARKET RISK

Market risk is the loss that may arise from changes in factors such as interest rate, foreign exchange and the impact these factors may have on other counterparties.

- Foreign exchange risk

The Company operates in Canada. The exposure related to foreign exchange is limited to United States dollar payments to suppliers which is not significant.

- Cash flow and fair value interest risk

The Company has no significant interest-bearing assets. The Company's income and operating cash flows are substantially independent of changes in market interest rates.

The Company's primary interest rate risk arises from long-term debt. The Company manages its exposure to changes in interest rates by using a combination of fixed and variable rate debt and utilizing interest rate swaps as necessary to achieve the desired proportion of variable and fixed rate debt. An increase or decrease in interest rates by 1% would result in an increase/decrease of \$1,268 on interest expense on the credit facilities. There are also a small number of finance leases at variable interest rates.

CREDIT RISK

Credit risk refers to the risk of losses due to failure of the Company's customers or other counterparties to meet their payment obligations. Credit risk arises from deposits with banks, as well as credit exposures from mattress vendors for the payment of volume and co-operative advertising rebate amounts and balances owed from third party financing companies under the various financing plans the Company offers its customers. In accordance with SCC's investment practice, all deposits are held at banks possessing a credit rating of AA- or better. Sales to retail customers are settled in cash, financed by third party financing companies or by using major credit cards. The Company transfers the credit risk for financing plans to third party financing companies. The third party financing companies that SCC deals with carry a minimum rating of BBB or better.

There are no significant impaired receivables that have not been provided for in the allowance. There are no amounts considered past due or impaired.

LIQUIDITY RISK

Liquidity risk is the risk that the Company cannot meet a demand for cash or fund its obligations as they come due. Liquidity risk also includes the risk of not being able to liquidate assets in a timely manner at a reasonable price. Prudent liquidity management implies maintaining sufficient cash and cash equivalents and the availability of funding through an adequate amount of committed credit facilities.

The table below analyzes the Company's financial liabilities into relevant maturity groupings based on the remaining period from the consolidated statement of financial position date to the contractual maturity date. The amounts discussed in the table are contractual undiscounted cash flows.

	Within 1 year \$	Between 1 and 5 years \$	Over 5 years \$
At December 31, 2015			
Trade and other payables	46,023	-	-
Long-term debt	4,702	141,139	17
	50,725	141,139	17
At December 31, 2014			
Trade and other payables	33,729	-	-
Long-term debt	12,245	135,898	350,789
Class A convertible and Class B common shares of SCCI	-	-	58,643
	45,974	135,898	409,432

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FAIR VALUE OF FINANCIAL INSTRUMENTS

The different levels used to determine fair values have been defined as follows:

- Level 1 – inputs use quoted prices (unadjusted) in active markets for identical financial assets or financial liabilities that the Company has the ability to access.
- Level 2 – inputs other than quoted prices included in Level 1 that are observable for the financial asset or financial liability, either directly or indirectly. Level 2 inputs include quoted prices for similar financial assets and financial liabilities in active markets, and inputs other than quoted prices that are observable for the financial liabilities.
- Level 3 – inputs are unobservable inputs for the financial asset or financial liability and include situations where there is little, if any, market activity for the financial asset or financial liabilities.

The following describes the fair value determinations of financial instruments:

The carrying values of cash and cash equivalents, trade and other receivables, due from related companies, trade and other payables, other assets and liabilities and customer deposits approximate their fair values due to the relatively short periods to maturity of these financial instruments. The carrying values of the revolving and term facilities approximate their fair values as the terms and conditions of the borrowing arrangements are comparable to market terms and conditions as at December 31, 2015 and December 31, 2014. The finance leases approximate their fair values as the implicit interest rates used in determining their fair value approximate interest rates as at December 31, 2015 and December 31, 2014. The Class B common shares of SCCI approximate their fair value as the implicit interest rates used in determining their fair value approximate interest rates as at December 31, 2014.

The fair value of the Series A and Series B promissory notes of SCCI is estimated to be \$nil (2014 – \$200,483) and is within Level 3 of the fair value hierarchy. The fair value of the Class A convertible shares of SCCI is estimated to be \$nil (2014 – \$37,310) and is within Level 3 of the fair value hierarchy. The valuation techniques used to estimate the fair value of the Series A and Series B promissory notes and Class A convertible shares incorporate discounted contractual obligations using assumptions such as interest rate curves and an estimated credit spread.

CAPITAL RISK MANAGEMENT

The Company's objectives when managing capital are to safeguard its ability to continue as a going concern in order to provide returns for its common shareholders in the form of cash dividends, benefits to other stakeholders and to maintain an optimal capital structure to minimize the cost of capital.

In order to maintain or adjust the capital structure, the Company may issue new shares or sell assets to reduce long-term debt.

22 Assets Held for Sale and Discontinued Operations

As at December 31, 2014, the assets and liabilities for the Sleep America business were presented as held for sale following the approval of the sale on November 5, 2014 for US\$12,500. The completion of this transaction occurred on January 6, 2015. As part of this agreement, US\$1,250 is held in escrow with 50% released on January 6, 2016 and the remainder 50% to be released on July 6, 2016.

ASSETS OF DISPOSAL GROUP HELD FOR SALE

	2015	2014
	\$	\$
Current assets		
Cash	-	7
Trade and other receivables	-	335
Inventories	-	3,621
Prepaid expenses and deposits	-	64
Property and equipment	-	3,577
Intangible assets other than goodwill	-	5,992
Goodwill	-	490
	-	14,086

LIABILITIES OF DISPOSAL GROUP HELD FOR SALE

	2015	2014
	\$	\$
Current liabilities		
Trade and other payables	-	3,985
Customer deposits	-	402
Other liabilities	-	823
	-	5,210

ANALYSIS OF THE RESULT OF DISCONTINUED OPERATIONS

	2015	2014
	\$	\$
Revenue	-	40,710
Cost of sales	-	35,809
Gross profit	-	4,901
General and administrative expenses	-	6,963
Depreciation and amortization	-	735
Loss before interest and impairment reversal	-	(2,797)
Impairment reversal on intangible asset (note 9)	-	5,981
Interest income and other expenses - net	5,992	(188)
Net income from discontinued operations	5,992	2,996

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CASH FLOWS

	2015	2014
	\$	\$
Net cash flows from operating activities	(5,992)	189
Net cash flows from investing activities	14,984	(128)
Net cash flows from financing activities	(8,992)	-
Exchange rate difference on cash	-	41
	-	102

23 Issuance of Shares and Reorganization

Pursuant to a final prospectus filed on July 10, 2015 with various Canadian provincial security commissions, the Company made an initial public offering and listed its common shares on the Toronto Stock Exchange. The offering of 17,650,000 common shares at \$17 per common share raised gross proceeds of \$300,050. The net proceeds from the transaction after deducting transaction and underwriter expenses was \$283,428. The Company also issued \$338,115 of common shares in exchange for shares of SCCI, SC US Holdco and SC Management (see below). The total net issuance of 37,539,135 common shares was for \$621,543.

In connection with the Offering, the Series A and B promissory notes of SCCI were converted into 95,549,701 Class A common shares of SCCI and the Class A convertible shares of SCCI were converted into 22,810,379 Class D common shares of SCCI based on the relative fair values at the conversion date. Subsequent to the conversion of the above instruments, SCCI declared and paid a capital dividend in the aggregate amount of \$12,903 on its Class A common shares, Class B common shares and Class D common shares. On closing of the Offering, the unvested options under SCCI's Pre-IPO Option Plan vested and the options were settled for a combination of cash and 594,761 Class E special shares of SCCI. SCCI's shares were then sold to the Company for a combination of cash, common shares of the Company and acquisition notes based on the economic value of the Company's shares as determined on July 10, 2015.

Prior to the Offering, SCCI paid \$6,898 of bonuses relating to key management and, along with the Company, also incurred \$2,358 in professional services fees associated with the Offering. These expenses are recognized as general and administrative expenses on the consolidated statement of operations for the year ended December 31, 2015.

The following table reflects the adjustments to shareholders' equity as a result of the reorganization:

	Reorganization adjustment \$	Share capital and other - SCCI \$	Non- controlling interest \$
Balance as at January 1, 2015	-	123,603	46,987
Allocation to non-controlling interest for the period January 1, 2015 to July 16, 2015	-	-	1,179
Conversion of Series A and B promissory notes (i)	-	140,092	-
Conversion of Class A convertible shares (ii)	-	33,444	-
Exercise of SCCI Pre-IPO options (iii)	-	2,337	-
Exercise of SCCI Pre-IPO options for growth value (iv)	-	(9,843)	-
Capital distribution (v)	-	(12,903)	-
Issuance of shares (vi)	-	59,635	(48,166)
SCCI Pre-IPO share-based compensation expense	-	12	-
Acquisition of SCCI, SC US Holdco and SC Management through cash and share issuance (vii)	(276,159)	(336,377)	-
Balance as at December 31, 2015	(276,159)	-	-

(i) Conversion of Series A and B notes

On July 16, 2015, the SCCI promissory series notes A and B (see note 12) were converted into 95,549,701 Class A common shares of SCCI at their carrying value of \$140,092.

(ii) Conversion of Class A convertible shares

On July 16, 2015, the SCCI Class A convertible shares (see note 12) were converted into 22,810,379 Class A common shares of SCCI at their carrying value of \$33,444.

(iii) Exercise of SCCI Pre-IPO options

On July 16, 2015, members and former members of key management of SCCI and its subsidiaries exercised their stock options under the SCCI Pre-IPO Option Plan. These options were only exercisable upon the occurrence of a liquidity event, which included the Offering. 824,750 options were exercised at a strike price of \$2.80 per share to acquire Class E special shares of SCCI.

(iv) Issuance of shares under the Offering

July 16, 2015, SCCI elected to settle certain outstanding stock options under the Pre-IPO Option Plan by way of a cash payment equal to the difference between the aggregate value of the SCCI shares that would have been issued upon the exercise of these options and the aggregate exercise price of the options. These options, which had an exercise price of \$2.80 and \$3.04, were accounted for as equity settled, and the payment of \$9,843 was charged to equity.

(v) Capital distribution

On July 16, 2015, SCCI made a capital dividend to its existing owners (prior to the Offering) of \$12,903.

(vi) Issuance of shares

Prior to the Offering, SCCI issued \$25,504 in value of Class A common shares of SCCI to a fund indirectly controlled by Birch Hill in exchange for units of SCCLP having an equivalent value. SCCI also issued \$34,131 in value of Class A common shares to the Company in exchange for an increased investment in SCCI and for shares in SC US Holdco and SC Management.

(vii) Acquisition of SCCI, SC US Holdco and SC Management through cash and share issuance

As part of the Offering, the Company acquired all of the issued and outstanding shares of the Acquired Entities for consideration consisting of cash and common shares of the Company. The common shares of the Company issued to the former shareholders of the Acquired Entities were valued at the Offering price of \$17.00 per share. The total cash and share consideration paid by the Company to acquire the Acquired Entities was \$612,524 and the book value of the shares of the Acquired Entities purchased by the Company was \$336,365. The difference between these two figures of \$276,159 was recorded as a reserve which is presented as a contra-share capital amount. Upon completion of the Acquisition, the Company acquired a 100% interest in each of the Acquired Entities (indirectly a 100% ownership interest in SCCLP) and the minority interest was therefore eliminated.

Notes to Consolidated Financial Statements of Sleep Country Canada Holdings Inc.

December 31, 2015 and December 31, 2014

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

Subsequent to the Offering, the Company owned 100% of the shares of SCCI and 100% interest in SCCLP. All earnings of SCCLP subsequent to the Offering are allocated to the Company and there is no longer a non-controlling interest.

24 Subsequent Events

On January 1, 2016, SCCLP was wound up and SCCGP was dissolved, in each case into SCCI.

On January 29, 2016, the Board of Directors of the Company declared a dividend on the Company's common shares in the amount of \$0.13 per share, payable on February 26, 2016 to shareholders of record at the close of business on February 16, 2016.

Shareholder Information

EXCHANGE LISTING

The Toronto Stock Exchange
Common Shares
Ticker Symbol: ZZZ

AUDITOR

PricewaterhouseCoopers LLP
PwC Tower
18 York Street, Suite 2600
Toronto, ON M5J 0B2

BANKER

TD Securities
TD West Tower, 30th Floor
100 Wellington Street West
Toronto, ON M5K 1A2

REGISTRAR AND TRANSFER AGENT

Computershare
100 University Avenue, 8th Floor
Toronto, ON M5J 2Y1
www.computershare.com

SHAREHOLDER CONTACT

Robert Masson
CFO, Sleep Country Canada
robert.masson@sleepcountry.ca

ANNUAL MEETING OF SHAREHOLDERS

Date: Wednesday, May 11, 2016
Time: 10:30am (EST)
Davies Ward Phillips & Vineberg
155 Wellington Street West
Toronto, ON M5V 3J7
Reception on 40th Floor

BOARD OF DIRECTORS

Stephen Gunn
Executive Co-Chair

Christine Magee
Executive Co-Chair

David Friesema

Stephen Dent

Thecla Sweeney

Andrew Moor

David Shaw

John Cassaday

Douglas Bradley

OFFICERS

David Friesema
Chief Executive Officer

Robert Masson
Chief Financial Officer

Stewart Schaefer
*Chief Business Development Officer & President,
Dormez-vous?*

CAPITAL STOCK

As at December 31, 2015, there were 37,578,176
common shares outstanding.

SleepCountry

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