

# ANDREW PELLER

— LIMITED —

## MANAGEMENT'S REPORT AND INTERIM CONSOLIDATED FINANCIAL STATEMENT FOR THE THREE AND SIX MONTHS ENDED SEPTEMBER 30, 2008 AND 2007



The following management's discussion and analysis ('MD&A') provides a review of corporate developments, results of operations and financial position for the three and six months ended September 30, 2008 in comparison with those for the three and six months ended September 30, 2007. This discussion is prepared as of November 5, 2008 and should be read in conjunction with the interim consolidated financial statements for the period ended September 30, 2008 and 2007, and the audited consolidated financial statements for the years ended March 31, 2008 and 2007 and the accompanying notes contained therein. All dollar amounts are expressed in Canadian dollars unless otherwise indicated.

### FORWARD-LOOKING INFORMATION

Certain statements in this Management's Discussion & Analysis may contain "forward-looking statements" within the meaning of applicable securities laws, including the "safe harbour provisions" of the Securities Act (Ontario) with respect to Andrew Peller Limited ('APL' or the 'Company') and its subsidiaries. Such statements include, but are not limited to, statements about the growth of the business in light of the Company's recent acquisitions; its launch of new premium wines; sales trends in foreign markets; its supply of domestically grown grapes; and current economic conditions. These statements are subject to certain risks, assumptions and uncertainties that could cause actual results to differ materially from those included in the forward-looking statements. The words "believe", "plan", "intend", "estimate", "expect" or "anticipate" and similar expressions, as well as future or conditional verbs such as "will", "should", "would" and "could" often identify forward-looking statements. We have based these forward-looking statements on our current views with respect to future events and financial performance. With respect to forward-looking statements contained in this MD&A, the Company has made assumptions and applied certain factors regarding, among other things: future grape, glass bottle and wine prices; its ability to obtain grapes, imported wine, glass and its ability to obtain other raw materials; fluctuations in the U.S./Canadian dollar exchange rates; its ability to market products successfully to its anticipated customers; the trade balance within the domestic Canadian wine market; market trends; reliance on key personnel; protection of its intellectual property rights; the economic environment; the regulatory requirements regarding producing, marketing, advertising and labeling of its products; the regulation of liquor distribution and retailing in Ontario; the application of federal and provincial environmental laws; and the impact of increasing competition.

These forward-looking statements are also subject to the risks and uncertainties discussed in the "Risk Factors" section and elsewhere in this MD&A and other risks detailed from time to time in the publicly filed disclosure documents of the Company which are available at [www.sedar.com](http://www.sedar.com). Forward-looking statements are not guarantees of future performance and involve risks, uncertainties and assumptions which could cause actual results to differ materially from those conclusions, forecasts or projections anticipated in these forward-looking statements. Because of these risks, uncertainties and assumptions, you should not place undue reliance on these forward-looking statements. The Company's forward-looking statements are made only as of the date of this MD&A, and except as required by applicable law, Andrew Peller Limited undertakes no obligation to update or revise these forward-looking statements to reflect new information, future events or circumstances.

### Overview

Andrew Peller Limited ('APL' or the 'Company') is a leading producer and marketer of quality wines in Canada. With wineries in British Columbia, Ontario and Nova Scotia, the Company markets wines produced from grapes grown in Ontario's Niagara Peninsula, British Columbia's Okanagan and Similkameen Valleys and from vineyards around the world. The Company's award-winning premium and ultra-premium brands include Peller Estates, Trius, Hillebrand, Thirty Bench, Croc Crossing, XOXO, Sandhill, Copper Moon, Calona Vineyards Artist Series VQA wines and Red Rooster. Complementing these premium brands are a number of popular priced products including Hochtaler, Domaine D'Or, Schloss Laderheim, Royal and Sommet.

With a focus on serving the needs of all wine consumers, the Company produces and markets consumer-made wine kit products through Winexpert, Vineco International Products, Wine Kitz and Heron Bay.

The Company also owns and operates Vineyards Estate Wines, Aisle 43 and WineCountry Vintners, independent wine retailers in Ontario with more than 100 well-positioned retail locations. The Company also markets craft beer under the Granville Island brand. The Company's products are sold predominantly in Canada.

The Company's stated mission is to build sales volumes of its premium and ultra-premium brands by delivering to its customers and consumers the highest quality wines at the best possible value. To meet this goal, the Company is investing in improvements in the quality of grapes and wines, its winemaking capabilities and in its quality management programs. Premium wine sales continue to grow in Canada and these products generate higher sales and increased profitability compared to lower-priced table wines.

APL is focused on initiatives to reduce costs and enhance its production efficiencies through a continual review of the Company's operations. Most recently, the Company has completed a comprehensive review of its operations in Kelowna, British Columbia which resulted in a 25% increase in productivity, while reducing overall labour costs. The Company continues to expand and strengthen its distribution through provincial liquor boards, the Company's network of more than 100 Vineyards Estate Wines, Aisle 43 and WineCountry Vintners retail locations, estate wineries, restaurants and other licensed establishments. This distribution network is supported by enhanced sales, marketing and promotional programs. In addition, the Company from time to time evaluates the potential for acquisitions and partnerships, both in Canada and internationally, to further complement its product portfolio and market presence.

On June 13, 2008 the Company acquired 50% of the shares of Rocky Ridge Vineyards Inc. ("Rocky Ridge") for cash consideration of \$4.0 million, including acquisition costs. Rocky Ridge is a premium vineyard located in the Similkameen Valley of British Columbia. The Company previously owned 50% of the shares of Rocky Ridge and as a result of this transaction Rocky Ridge became a wholly-owned subsidiary of the Company.

On June 30, 2008 the Company acquired 100% of the common shares of World Vintners Inc. ("WVI") a producer and seller of high quality consumer-made wine kits. WVI's sales for its most recently-completed financial year ended July 31, 2007 were approximately \$12.0 million. The acquisition brings to the Company a dedicated network of 75 franchised wine-on-premise and retail outlets under the Wine Kitz brand name. WVI also produces the popular Heron Bay brand sold through independent wine-on-premise and retail outlets across Canada. WVI was acquired for cash consideration of \$11.0 million, including acquisition costs. The Company expects to generate significant synergies in its wine kit operations as a result of this acquisition. The allocation of purchase price is preliminary and is based on management's estimates of the fair value of the assets acquired and liabilities assumed. Management is currently obtaining fair market values for the net assets and intangible assets acquired.

As a result of continued strong performance, the Company increased annual common share dividends effective for shareholders of record on September 30, 2006 by 18% and a further 19% on June 8, 2007. On June 5, 2008 the Company announced that it would increase annual common share dividends for shareholders of record on June 30, 2008. The dividend on Class A shares increased 10% from \$0.300 per share to \$0.330 per share. The dividend on Class B shares increased 10% from \$0.261 per share to \$0.288 per share. This was the third consecutive annual increase in dividends in three years.

### **Financial Statements and Accounting Policies**

The Company prepared its financial statements in Canadian dollars in accordance with Canadian generally accepted accounting principles (GAAP). Changes to the Company's significant accounting policies are summarized in Note 1 to the interim consolidated financial statements. The Company also utilizes EBITA (defined as earnings before interest, income taxes, amortization, other income (losses) and unusual items) to measure its financial performance.

EBITA is not a recognized measure under GAAP; however, management believes that EBITA is a useful supplemental measure to net earnings, as it provides readers with an indication of earnings available for investment prior to debt service, capital expenditures and income taxes.

Readers are cautioned that EBITA should not be construed as an alternative to net earnings determined in accordance with GAAP as an indicator of the Company's performance or to cash flows from operating, investing and financing activities as a measure of liquidity and cash flows. The Company's method of calculating EBITA may differ from the methods by which other companies calculate EBITA and, accordingly, EBITA may not be comparable to measures used by other companies.

### **Critical Accounting Estimates**

During the year, management is required to make estimates or rely on assumptions that are inherently uncertain. These estimates can vary with respect to the level of judgment involved and ultimately the impact that these estimates may have on the Company's financial statements. Estimates are deemed to be critical when a different estimate could reasonably be used or where changes are reasonably likely to occur which would materially affect the Company's financial position, or results in operations. The Company's significant accounting policies are discussed in Note 1 of the Notes to the Consolidated Financial Statements; critical estimates inherent in these accounting policies are set out below.

### **Inventory Valuation**

Inventories are valued at the lower of cost and net realizable value. The Company determines cost on an average cost basis using separate pools for domestic and imported wines.

All inventories are counted as close as possible to year end without impacting the operations of the Company. Management has provided an allowance for slow moving and obsolete inventory which is considered to be sufficient for potential losses.

On April 1, 2008 the Company adopted the Canadian Institute of Chartered Accountants (CICA) Handbook Section 3031 "Inventories". This pronouncement provides guidance on the determination of cost and its subsequent recognition as an expense, including any write-down to net realizable value. It also provides guidance on the cost formulas that are used to assign costs to inventories and is effective for the Company's fiscal year beginning on April 1, 2008. As required, this standard has been adopted prospectively and comparative amounts have not been restated. The change in carrying value predominately relates to changes in the application of overheads in bulk and finished goods inventory. As a result, on adoption of this standard, the Company recorded an adjustment on April 1, 2008 to reduce inventories by \$1,552, reduce future income taxes by \$485, and reduce opening retained earnings by \$1,067.

### **Intangible assets**

Intangible assets primarily relate to customer contracts, brands and customer based relationships that have been acquired through recent acquisitions. Management believes that brands do not have a fixed or determinable life and consequently brands are not amortized but are subject to annual impairment tests based on a comparison of the carrying amount to the estimated fair market value of the brands. The amortization periods related to those intangible assets with finite lives are based on the expected duration of the contracts and relationships acquired. These intangible assets will be tested for impairment when events or circumstances arise that indicates impairment may exist.

### **Fair value of financial instruments**

Accounts receivable, accounts payable and accrued liabilities and bank indebtedness are reflected in the consolidated financial statements at carrying values, which approximate fair value due to the short-term maturity of these instruments.

### **Recently adopted accounting pronouncements**

On April 1, 2007 the Company adopted the following Canadian Institute of Chartered Accountants ("CICA") Handbook Sections:

CICA Handbook Section 1535 "Capital Disclosures" required disclosures in the financial statements of qualitative and quantitative information that enables users to evaluate objectives, policies and processes for managing capital expenditures.

CICA Handbook Section 3862 “Financial Instruments – Disclosures” required disclosures in the financial statements that will enable users to evaluate: the significance of financial instruments for the Company’s financial position and performance; and the nature and extent of risks arising from financial instruments to which the Company is exposed during the period and at the balance sheet date, and how the Company managed those risks.

CICA Handbook Section 3863 “Financial Instruments – Presentation” established standards for presentation of financial instruments and non-financial derivatives. This section complemented the existing CICA Handbook Section 3861 “Financial Instruments – Disclosure and Presentation”.

CICA Handbook Section 3031 “Inventories” provided guidance on the determination of cost and its subsequent recognition as an expense, including any write-down to net realizable value. It also provided guidance on the cost formulas that are used to assign costs to inventories.

### Recently issued accounting pronouncements

The CICA has issued the following accounting standards:

In February 2008, the CICA issued Section 3064, “Goodwill and Intangible Assets,” which replaces Section 3062, “Goodwill and Other Intangible Assets.” This new standard provides guidance on the recognition, measurement, presentation and disclosure of goodwill and intangible assets. This accounting standard is effective for annual and interim periods beginning on or after October 1, 2008.

International Financial Reporting Standards (“IFRS”). In February 2008, the Canadian Accounting Standards Board confirmed that the use of IFRS will be required for Canadian publicly accountable enterprises for years beginning on or after January 1, 2011. The Company will be required to report under IFRS beginning April 1, 2011.

The Company is currently evaluating the impact of adopting the above accounting and reporting standards.

### Results of Operations (unaudited)

FOR THE SIX MONTHS ENDED SEPTEMBER 30, (in thousands of dollars except per share amounts)	2008 \$	2007 \$	2006 \$
Sales	\$ 128,974	\$ 118,376	114,548
Gross profit	54,038	50,662	47,874
Gross profit (% of sales)	41.9%	42.8%	41.8%
Selling general and administrative expenses	\$ 38,560	\$ 35,466	33,744
Earnings before interest, taxes, amortization, other income (loss) and unusual items	15,478	15,196	14,130
Other loss and unusual items	(1,292)	(80)	(198)
Net and comprehensive earnings	5,097	5,566	4,932
Net earnings excluding other loss and unusual items	5,993	5,618	5,062
Earnings per share – basic and fully diluted - Class A	\$ 0.350	\$ 0.380	\$ 0.340
Earnings per share – basic and fully diluted - Class B	\$ 0.310	\$ 0.330	\$ 0.300
Dividend per share – Class A (annual)	\$ 0.330	\$0.300	\$0.253
Dividend per share – Class B (annual)	\$ 0.288	\$0.261	\$0.220

Sales increased 9.0% for the six months ended September 30, 2008 due to higher sales of the Company's blended, premium and ultra-premium wines sold through all of the Company's trade channels, the acquisition of WVI and to the benefit of new product launches which occurred during 2008 and 2007. The acquisition of WVI contributed sales of \$2.7 million during the period. The increase is also the result of higher sales of premium wines due to the return to normal grape supply conditions in Ontario following a short crop in 2007 and improved supply of wine and beer in Western Canadian markets.

During 2007 and 2008 the Company launched a number of new products through provincial liquor stores and the Company's network of retail stores. Sales of VQA wines in fiscal 2007 were negatively impacted by the short crop of VQA grapes in Ontario, which returned to more normal supply in fiscal 2008. The Company has continued to invest in its sales and marketing efforts with the aim to grow sales volumes of its products through new and increased advertising and promotional initiatives in all trade channels, increased sales staff focused on the licensee channel, investment in the new Aisle 43 retail stores, training of retail staff, and additional investments to increase tourism at its estate wineries.

Gross profit as a percentage of sales was 41.9% in the first six months of fiscal 2009 compared to 42.8% and 41.8% in the prior year periods, respectively. The decrease in gross profit in fiscal 2009 was due to increases in both domestic grape costs and wine purchased on international market in the period and higher packaging costs. Gross profit in fiscal 2006 was impacted by accounting adjustments required to value purchased inventory from Cascadia at fair market value.

Selling and administrative expenses have increased over the last three years due primarily to costs related to acquisitions including WVI and enhanced sales and marketing efforts in all of the Company's trade channels to drive higher sales. As a percentage of sales, selling and administrative expenses were 29.9% for the six months ended September 30, 2008 and 30.0% for the six months ended September 30, 2007 and 29.5% in the first six months of fiscal 2007.

As a result of the higher sales, partially offset by lower gross profit margins and higher costs, earnings before interest, taxes, amortization, other income (loss) and unusual items ("EBITA") rose 1.9% to \$15.5 million in the first six months of fiscal 2009 compared to \$15.2 million and \$14.1 million in the comparative periods in fiscal 2008 and 2007, respectively.

Amortization expenses increased 3.1% in the first six months of fiscal 2009 compared with the same period in the last fiscal year while interest expense increased slightly primarily due to higher debt levels used to finance acquisitions and higher inventory levels which were partially offset by lower rates of interest.

The Company incurred a loss in fiscal 2009 of approximately \$1.2 million related to the mark-to-market adjustments on interest rate swaps and foreign exchange contracts. Under CICA accounting standards, these financial instruments must be reflected in the Company's financial statements at fair value each period. In the comparative period in fiscal 2008 a gain of approximately \$0.04 million was recognized. In addition, unusual charges to earnings of \$0.1 million were recorded in fiscal 2009 and 2008 resulting from carrying charges for the Company's Port Moody facility. The Company closed its Port Moody B.C. winery effective December 31, 2005 and expects to sell the facility during 2010.

The Company's effective income tax rate was lower during the first quarter of fiscal 2009 compared to the prior year due to a lower federal income tax rate.

Net and comprehensive earnings, not including the impact of the other losses and unusual items, were \$6.0 million for the first six months of fiscal 2009 compared to \$5.6 million in fiscal 2008 and \$5.1 million in fiscal 2007. Including the impact of the other losses and unusual items, net earnings and comprehensive earnings for the six months ended September 30, 2008 was \$5.1 million or \$0.35 per Class A share compared to \$5.6 million or \$0.38 per Class A share last year.

## Quarterly Performance (unaudited)

(\$000) except per share amounts	Q2 09	Q1 09	Q4 08	Q3 08	Q2 08	Q1 08	Q4 07	Q3 07
	\$	\$	\$	\$	\$	\$	\$	\$
Sales	<b>69,356</b>	59,618	52,702	66,052	61,236	57,140	50,419	63,225
Gross profit	<b>29,102</b>	24,936	23,325	28,740	26,196	24,466	20,894	26,340
Gross profit (% of sales)	<b>42.0%</b>	41.8%	44.3%	43.5%	42.8%	42.8%	41.4%	41.7%
EBITA	<b>8,294</b>	7,184	4,689	9,823	7,765	7,431	4,249	9,286
Other income (loss) and unusual items	<b>(1,073)</b>	(219)	(417)	(221)	(394)	314	7	(15)
Net and comprehensive earnings	<b>2,444</b>	2,653	802	5,013	2,652	2,914	398	4,142
EPS – Class A basic & diluted	<b>\$0.17</b>	\$0.18	\$0.05	\$0.35	\$0.18	\$0.20	0.02	0.29
EPS – Class B basic & diluted	<b>\$0.15</b>	\$0.16	\$0.05	\$0.30	\$0.16	\$0.17	0.02	0.25

The third quarter of each year is historically the strongest in terms of sales, gross profit and net and comprehensive earnings due to increased consumer purchasing of the Company's products during the holiday season.

## Liquidity and Capital Resources (unaudited)

As at (\$000)	September 30, 2008	March 31, 2008
	\$	\$
Current Assets	<b>132,285</b>	121,954
Property Plant & Equipment	<b>101,354</b>	94,480
Goodwill	<b>44,515</b>	36,171
Other Assets	<b>7,383</b>	7,139
Total Assets	<b>285,537</b>	259,744
Current Liabilities	<b>92,699</b>	95,345
Long-Term Debt	<b>74,767</b>	46,946
Employee Future Benefits	<b>2,964</b>	3,167
Future Income Taxes	<b>10,791</b>	11,606
Shareholders' Equity	<b>104,316</b>	102,680
Total Liabilities & Shareholders' Equity	<b>285,537</b>	259,744

The changes to the Company's balance sheet at September 30, 2008 compared to March 31, 2008 are primarily due to the acquisitions of Rocky Ridge Vineyards Inc. ("Rocky Ridge") and World Vintners Inc. ("WVI"), the adoption of CICA Handbook Section 3031 "Inventories", and a refinancing of the Company's debt. The Company invested approximately \$11.0 million in the acquisition of WVI and \$4.0 million in the purchase of the remaining 50% interest in Rocky Ridge during the first six months of fiscal 2009.

As at September 30, 2008 total bank indebtedness increased to \$132.0 million compared to \$111.5 million at the end of fiscal 2008. The increase was due primarily to the acquisitions of WVI and Rocky Ridge during June 2008, increased levels of accounts receivable and by investments in property, plant and equipment during the period.

On May 15, 2008 the Company refinanced its borrowings from the Bank of Montreal. The Company's term credit facilities were combined into a seven year term bank loan in the amount of \$80.0 million. The facility requires monthly principal payments of \$0.4 million plus interest and matures on April 30, 2015. The proceeds of the loan were used to repay operating facilities and provide additional capital for acquisitions.

Inventory increased by \$0.9 million during the period due to the start of the grape harvest during September in the amount of \$4.1 million resulting in a corresponding increase in accounts payable and accrued liabilities, by purchases of wine on international markets partially offset by higher sales levels. Inventory also increased by \$1.3 million for the six months ended September 30, 2008 due to the impact of the WVI acquisition. Inventory is dependent on the increased use of domestically grown grapes which are used in the sale of premium and ultra-premiums wines which are aged for a longer period than imported wine. These grapes are typically aged for one to three years before they are sold. The cost of domestically grown grapes is also significantly higher than wine purchased on international markets.

Accounts receivable are predominantly with provincial liquor boards and to a lesser extent licensed establishments and independent retailers of consumer made wine kits. Accounts receivable increased during the period by \$6.6 million due to the acquisition of WVI and due to higher sales through all trade channels. The Company has \$15.7 million dollars of accounts receivable with provincial liquor boards all of which is all deemed to be collectable. The balance of \$14.0 million represents amounts due from licensees, export customers and independent retailers of consumer made wine kits. The amount of the accounts receivable that is beyond 60 days is \$2.4 million. Against these amounts, an allowance for doubtful accounts of \$0.5 million has been provided which the Company has determined to represent a reasonable estimate of amounts that would subsequently be determined to be uncollectible.

The following table outlines the Company's contractual obligations, including long-term debt, operating leases, and commitments on short-term forward foreign exchange contracts used to hedge the currency risk on US dollar purchases.

As at September. 30, 2008 (\$000)	Total	<1 year	1-3 years	4-5 years	>5 years
Long-Term Bank Loan	80,678	6,158	11,492	10,667	52,361
Operating Leases	19,061	4,439	5,728	1,749	7,145
Pension Obligations	5,707	847	2,541	1,694	625
Long-Term Grape Contracts	357,461	25,845	51,637	51,179	228,800
Total Contractual Obligations	462,907	37,289	71,398	65,289	288,931

The ratio of debt to equity increased to 1.27:1 at September 30, 2008 compared to 1.01:1 at September 30, 2007 and 1.09:1 at March 31, 2008. At September 30, 2008, the Company had unused debt available in the amount of \$9.0 million on its demand loan facility.

While credit markets have tightened in recent months, management has successfully refinanced its long-term debt with the Bank of Montreal during May 2008 to April 30, 2015. The Company's operating facility is on a demand basis with the Royal Bank of Canada. The Royal Bank of Canada has indicated that it is prepared to make the operating facility a one year committed facility at a higher interest rate. The Company is currently reviewing its options.

Management expects to generate sufficient cash flow from operations to meet its debt servicing, principal payment and working capital requirements over both the short and the long term through increased profitability and strong management of working capital and capital expenditures. In addition, as stated above, the Company closed its Port Moody B.C. winery effective December 31, 2005 and expects to sell or re-develop the facility. The proceeds from the sale will be used to reduce bank indebtedness. The Company continually reviews what other assets could be sold if sufficient credit is not available.

During the first six months of fiscal 2009, the Company generated cash from operating activities, after changes in non-cash working capital items, of \$2.7 million compared to \$10.9 million in the same period last year. Cash flow from operating activities decreased due to negative changes in non-cash working capital items, specifically to increases in accounts receivable and inventories as well as a smaller increase in accounts payable. These issues were discussed above.

Investing activities of approximately \$20.4 million were made in the first six months of fiscal 2009 compared to \$8.2 million in the prior year. The increase during the first six months of fiscal 2009 is primarily related to the \$11.0 million acquisition of WVI and a \$4.0 million investment in acquiring the remaining 50% of Rocky Ridge, both in June 2008. Excluding these items, capital spending was \$5.4 million for the six months ended September 30, 2008 compared to \$8.2 million last year.

Working capital as at September 30, 2008 was \$39.6 million compared to \$23.9 million as at September 30, 2007 and \$26.6 million at March 31, 2008. Shareholders' equity as at September 30, 2008 was \$104.3 million or \$7.00 per common share compared to \$102.7 million or \$6.89 per common share at March 31, 2008 and \$99.0 million or \$6.65 per share as at September 30, 2007.

The dividend on Class A shares increased 10% from \$0.300 per share to \$0.330 per share effective June 30, 2008. The dividend on Class B shares increased 10% from \$0.261 per share to \$0.288 per share. This was the third consecutive annual increase in dividends in three years.

### Common Shares Outstanding

The Company is authorized to issue an unlimited number of Class A and Class B common shares. Class A shares are non-voting and are entitled to a dividend in an amount equal to 115% of any dividend paid or declared on Class B shares. Class B shares are voting and convertible into Class A shares on a one-for-one basis.

Shares outstanding	November 5, 2008	September 30, 2008	March 31, 2008
Class A shares	11,888,241	11,888,241	11,888,241
Class B shares	3,004,041	3,004,041	3,004,041
Total	14,892,282	14,892,282	14,892,282

### Strategic Outlook and Direction

Andrew Peller Limited is committed to a strategy of growth that focuses on the expansion of its core business as a producer and marketer of quality wines and craft beer through the development of leading brands that meet the needs of our consumers and customers.

The Canadian wine market has grown over the past three years due primarily to positive demographic trends and the shift in consumer preference to premium wines. However, the share of the market held by domestic producers has declined moderately. Imports of premium and ultra-premium wines have increased as consumers favoured higher-priced varietal wines over lower-priced blended table wines. Andrew Peller Limited has increased its product development and sales and marketing initiatives aimed at capitalizing on this growing trend.

The Company expects to continue to launch new premium and ultra-premium brands in 2009. The acquisitions of Thirty Bench, Cascadia and Red Rooster are expected to continue to contribute to increased sales in 2009 as well as to an enhanced presence in the sale of ultra-premium wines in Canada.

Marketing and sales support will be focused on key brands sold across the country, and management expects sales and marketing expenses for 2009 to rise moderately. The Company expects to invest in capital expenditures to support its ongoing commitment to producing the highest-quality wines.

Investments made over the past few years are expected to continue to result in increased sales and improved profitability going forward. In addition, recent initiatives have led to an increase in export sales of the Company's premium and ultra-premium wines, particularly icewine.

Following the acquisition of Cascadia, management began the process of rationalizing and integrating its two British Columbia facilities to capture production and overhead synergies. Management expects the integration to be completed during 2009.

From time to time the Company evaluates investment opportunities, including acquisitions, which could support its strategic direction.

Despite the recent economic slowdown in Canada, the Company expects it will maintain or modestly grow its sales while gross margins will remain stable at current levels. The Company's product portfolio covers the complete spectrum of price levels within the Canadian market and expects that while there may be a modest reduction in purchases of premium and ultra-premium wine; this will be mitigated by an increase in sales of non-VQA wine, sustaining the Company's overall sales at similar gross profit margins. In addition, the Company will be accelerating its efforts to generate production efficiencies and reducing overhead costs to enhance its overall profitability.

### **Risks and Uncertainties**

The Company is subject to a number of risks and uncertainties outlined in the Company's 2008 Annual Report and other securities filings.

## **Evaluation of Disclosure Controls and Procedures and Internal Control over Financial Reporting**

### **Disclosure Controls and Procedures**

Disclosure controls and procedures are designed to provide reasonable assurance that all relevant information relating to the operation of the Company and its consolidated subsidiaries is gathered and provided to senior management, including the President and Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO"), on a timely basis so that decisions can be made regarding the Company's disclosure to the public. As at November 5, 2008, the CEO and the CFO of the Company have evaluated the system of disclosure controls and procedures in the Company and its consolidated subsidiaries as set out by Canadian Securities Laws. Based on that evaluation, the CEO and CFO have concluded that the disclosure controls and procedures were effective in providing reasonable assurance that information required to be disclosed in the Company's annual and interim filings and other reports filed or submitted under Canadian securities laws is recorded, processed, summarized and reported within the time frames specified by those laws and that material information is accumulated and communicated to management of the Company, including the CEO and CFO, as appropriate to ensure the timely disclosure of that information.

### **Internal Controls over Financial Reporting**

Internal controls over financial reporting are procedures designed to provide reasonable assurance that transactions are properly authorized, assets are safeguarded against unauthorized or improper use, and transactions are properly recorded and reported. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance with respect to reliability of financial reporting and financial statement preparation.

The Company's CEO and CFO have concluded that internal controls over financial reporting are designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of the financial statements in accordance with Canadian generally accepted accounting principles as of September 30, 2008.

During the six months ended September 30, 2008, there have been no material changes in the Company's internal control over financial reporting that materially affected or were likely to affect, the Company's internal control systems.

# ANDREW PELLER LIMITED

## CONSOLIDATED BALANCE SHEETS

These financial statements have not been reviewed  
by our auditors

	September 30	March 31
	2008	2008
(expressed in thousands of Canadian dollars)	\$	\$
<b>Assets</b>		
<b>Current Assets</b>		
Accounts receivable	29,721	23,072
Inventories	94,715	93,817
Prepaid expenses and other assets	5,617	4,242
Income taxes recoverable	2,232	823
	132,285	121,954
<b>Property, plant and equipment</b>	<b>101,354</b>	<b>94,480</b>
<b>Goodwill (note 3)</b>	<b>44,515</b>	<b>36,171</b>
<b>Other assets</b>	<b>7,383</b>	<b>7,139</b>
	<b>285,537</b>	<b>259,744</b>
<b>Liabilities</b>		
<b>Current Liabilities</b>		
Bank indebtedness	51,046	57,722
Accounts payable and accrued liabilities	34,298	29,705
Dividends payable	1,197	1,088
Current portion of long - term debt (note 4)	6,158	6,830
	92,699	95,345
<b>Long-term debt (note 4)</b>	<b>74,767</b>	<b>46,946</b>
<b>Employee future benefits</b>	<b>2,964</b>	<b>3,167</b>
<b>Future income taxes</b>	<b>10,791</b>	<b>11,606</b>
	<b>181,221</b>	<b>157,064</b>
<b>Shareholders' Equity</b>		
<b>Capital Stock</b>	<b>7,375</b>	<b>7,375</b>
<b>Retained Earnings</b>	<b>96,941</b>	<b>95,305</b>
	<b>104,316</b>	<b>102,680</b>
	<b>285,537</b>	<b>259,744</b>

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

## ANDREW PELLER LIMITED

### Consolidated Statements of Earnings, Comprehensive Earnings and Retained Earnings

These financial statements have not been reviewed by our auditors  
(expressed in thousands of Canadian dollars)

	For the Three Months Ended		For the Six Months Ended	
	September 30		September 30	
	2008	2007	2008	2007
	\$	\$	\$	\$
<b>Sales</b>	<b>69,356</b>	61,236	<b>128,974</b>	118,376
Cost of goods sold, excluding amortization	<u>40,254</u>	<u>35,040</u>	<u>74,936</u>	<u>67,714</u>
<b>Gross profit</b>	<b>29,102</b>	26,196	<b>54,038</b>	50,662
Selling and administration	<u>20,808</u>	<u>18,431</u>	<u>38,560</u>	<u>35,466</u>
<b>Earnings before interest and amortization</b>	<b>8,294</b>	7,765	<b>15,478</b>	15,196
Interest	<u>1,505</u>	<u>1,439</u>	<u>2,907</u>	<u>2,864</u>
Amortization of plant, equipment and intangibles	<u>2,126</u>	<u>1,918</u>	<u>3,936</u>	<u>3,818</u>
<b>Earnings before other items</b>	<b>4,663</b>	4,408	<b>8,635</b>	8,514
<b>Other (loss) income</b>	<b>(1,017)</b>	(325)	<b>(1,178)</b>	44
<b>Unusual items</b>	<b>(56)</b>	(69)	<b>(114)</b>	(124)
<b>Earnings before income taxes</b>	<b>3,590</b>	4,014	<b>7,343</b>	8,434
<b>Provision for income taxes</b>				
Current	<u>1,480</u>	<u>1,409</u>	<u>2,575</u>	<u>2,725</u>
Future	<u>(334)</u>	<u>(47)</u>	<u>(329)</u>	<u>143</u>
	<u>1,146</u>	<u>1,362</u>	<u>2,246</u>	<u>2,868</u>
<b>Net and comprehensive earnings for the period</b>	<b>2,444</b>	2,652	<b>5,097</b>	5,566
<b>Retained earnings- Beginning of period</b>	<b>95,694</b>	90,101	<b>95,305</b>	88,147
<b>Impact of adopting accounting pronouncements on April 1, 2007</b>	-	-	-	128
<b>Impact of adopting accounting pronouncement on April 1, 2008</b>	-	-	<b>(1,067)</b>	-
<b>Retained earnings- Beginning of period as restated</b>	<b>95,694</b>	<u>90,101</u>	<b>94,238</b>	<u>88,275</u>
Dividends:				
Class A and Class B	<u>(1,197)</u>	<u>(1,087)</u>	<u>(2,394)</u>	<u>(2,175)</u>
<b>Retained earnings - End of period</b>	<b>96,941</b>	<u>91,666</u>	<b>96,941</b>	<u>91,666</u>
<b>Net earnings per share</b>				
Basic and diluted				
Class A shares	<u>0.17</u>	<u>0.18</u>	<u>0.35</u>	<u>0.38</u>
Class B shares	<u>0.15</u>	<u>0.16</u>	<u>0.31</u>	<u>0.33</u>

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

## ANDREW PELLER LIMITED

### Consolidated Statements of Cash Flows

These financial statements have not been reviewed by our auditors  
(expressed in thousands of Canadian dollars)

	For the Three Months Ended September 30		For the Six Months Ended September 30	
	2008 \$	2007 \$	2008 \$	2007 \$
<b>Cash provided by (used in)</b>				
<b>Operating activities</b>				
Net earnings for the period	2,444	2,652	5,097	5,566
Items not affecting cash:				
Amortization of plant, equipment and intangibles	2,126	1,918	3,936	3,818
Employee future benefits	(154)	(162)	(203)	(187)
Net unrealized loss (gain) on foreign exchange contracts and interest rate swaps	1,017	325	1,178	(44)
Future income taxes	(334)	(47)	(329)	143
Amortization of deferred financing costs	55	37	93	73
	<u>5,154</u>	<u>4,723</u>	<u>9,772</u>	<u>9,369</u>
Changes in non-cash working capital items related to operations (note 5)	<u>(3,903)</u>	<u>8,088</u>	<u>(7,077)</u>	<u>1,541</u>
	<u>1,251</u>	<u>12,811</u>	<u>2,695</u>	<u>10,910</u>
<b>Investing activities</b>				
Acquisition of World Vintners Inc. (note 3)	(16)	-	(10,956)	-
Acquisition of Rocky Ridge Vineyards Inc. (note 3)	-	-	(4,016)	-
Purchase of property and equipment	<u>(2,933)</u>	<u>(4,396)</u>	<u>(5,431)</u>	<u>(8,212)</u>
	<u>(2,949)</u>	<u>(4,396)</u>	<u>(20,403)</u>	<u>(8,212)</u>
<b>Financing activities</b>				
Increase in deferred financing costs	(73)	-	(287)	-
Increase (decrease) in bank indebtedness	3,882	(9,321)	(6,676)	(1,212)
Increase in long-term debt (note 4)	-	3,470	29,036	3,470
Repayment of long-term debt	(914)	(1,476)	(2,080)	(2,951)
Dividends paid	<u>(1,197)</u>	<u>(1,088)</u>	<u>(2,285)</u>	<u>(2,005)</u>
	<u>1,698</u>	<u>(8,415)</u>	<u>17,708</u>	<u>(2,698)</u>
<b>Cash at beginning and end of period</b>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
<b>Supplemental disclosure of cash flow information</b>				
Cash paid during the period for				
Interest	1,594	1,372	2,656	2,687
Income taxes	1,532	2,235	2,359	3,294

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

## Notes to the Interim Consolidated Financial Statements September 30, 2008 and 2007

(in thousands of dollars, except per share amounts)

### UNAUDITED

#### 1. Summary of Significant Accounting Policies

The interim consolidated financial statements have been prepared in accordance with accounting principles generally accepted in Canada. The note disclosure for these interim consolidated financial statements only presents material changes to the disclosure found in the Company's audited consolidated financial statements for the years ended March 31, 2008 and 2007. These interim consolidated financial statements should be read in conjunction with those consolidated financial statements and follow the same accounting policies as the audited consolidated financial statements except as disclosed below. In the opinion of management, the accompanying unaudited interim consolidated financial statements contain all adjustments necessary to present fairly, in all material respects the financial position of the Company as at September 30, 2008 and for the three and six-month period then ended.

## Recently adopted accounting pronouncements

On April 1, 2008 the Company adopted the Canadian Institute of Chartered Accountants (CICA) handbook sections 3031 “Inventories,” section 3862 “Financial Instruments - Disclosures,” section 3863 “Financial Instruments – Presentation” and section 1535 “Capital Disclosures.”

### a) Inventories

On April 1, 2008 the Company adopted the Canadian Institute of Chartered Accountants (CICA) Handbook Section 3031 “Inventories”. This pronouncement provides guidance on the determination of cost and its subsequent recognition as an expense, including any write-down to net realizable value. It also provides guidance on the cost formulas that are used to assign costs to inventories and is effective for the Company’s fiscal years beginning on April 1, 2008. As required, this standard has been adopted prospectively and comparative amounts have not been restated. The change predominately relates to changes in the application of overhead cost allocations to bulk and finished goods inventory. As a result, on adoption of this standard, the Company recorded an adjustment on April 1, 2008 to reduce inventories by \$1,552, reduce future income taxes by \$485, and reduce opening retained earnings by \$1,067.

### b) Financial Instruments Presentation and Disclosures, and Capital Disclosures

On April 1, 2008 the Company adopted CICA handbook Section 3862 “Financial Instruments - Disclosures,” section 3863 “Financial Instruments – Presentation” and section 1535 “Capital Disclosures.” These sections require additional disclosures surrounding the Company’s financial instruments and capital. The following disclosures are required under the new pronouncement:

#### *Interest rate risk*

The Company’s interest rate risk arises mainly from the interest rate impact on our cash, floating rate debt and interest rate swaps. Our interest rate management policy is to borrow at fixed rates to match the duration of long lived assets. Floating rate funding is used for short term borrowing.

The Company has fixed interest on long-term debt at 5.64% until April 30, 2015 by entering into an interest rate swap. The Company’s short-term borrowings are funded using a floating interest rate and as such are sensitive to interest rate movements. As at September 30, 2008, with other variables unchanged, a 1% change in interest rates would impact the Company’s net earnings by approximately \$350.

#### *Credit Risk*

The Company’s exposure to credit risk is very limited. Credit risk for trade receivables is monitored through established credit monitoring activities. Over 51% of the Company’s accounts receivable balance relates to amounts owing from Canadian provincial liquor boards. Excluding accounts receivable from Canadian provincial liquor board amounts, the Company does not have a significant concentration of credit risk with any single counterparty or group of counterparties. The maximum exposure to credit risk is equal to the carrying value of the financial assets.

Amounts owing from Canadian provincial liquor boards represent \$15,690 of the \$29,721 in total accounts receivables all of which has been deemed to be collectible. Of the remaining non provincial liquor board balances, \$2,447 had aged over sixty days as of September 30, 2008. An allowance for doubtful accounts of \$503 has been provided against these accounts receivable amounts which the Company has determined to represent a reasonable estimate of amounts that may be uncollectible.

#### *Liquidity Risk*

The Company manages liquidity risk by maintaining adequate cash and cash equivalent balances and by appropriately utilizing its line of credit. Company management continuously monitors and reviews both actual and forecasted cash flows and matches the maturity profile of financial assets and financial liabilities. Accounts payable are generally due within 30 days and long-term debt payment requirements are disclosed in note 4.

The following table outlines the Company's contractual obligations, including long-term debt, operating leases, and commitments on short-term forward foreign exchange contracts used to hedge the currency risk on US dollar purchases as at September 30, 2008.

	<b>Total</b>	<b>&lt; 1 Year</b>	<b>1 – 3 Years</b>	<b>4 – 5 Years</b>	<b>&gt; 5 Years</b>
Long-term debt	80,678	6,158	11,492	10,667	52,361
Operating leases	19,061	4,439	5,728	1,749	7,145
Pension obligations	5,707	847	2,541	1,694	625
Long-term grape contracts	<u>357,461</u>	<u>25,845</u>	<u>51,637</u>	<u>51,179</u>	<u>228,800</u>
Total contractual obligations	<u>462,907</u>	<u>37,289</u>	<u>71,398</u>	<u>65,289</u>	<u>288,931</u>

#### *Foreign exchange risk*

The Company's foreign exchange risk arises on the purchase of bulk wine and concentrate which are made in U.S. dollars and Euros. The Company's strategy is to hedge approximately 50% - 80% of its foreign exchange requirements prior to the beginning of each fiscal year. The Company has entered into a series of foreign exchange contracts as a hedge against movements in U.S. dollar and Euro exchange rates. These contracts are reviewed regularly. A one percent change in the value of the U.S. dollar and Euro would impact the Company's net earnings by approximately \$100 and \$30 respectively.

#### *Capital Disclosures*

The Company's objective when managing capital is to safeguard the Company's ability as a going concern, to provide an adequate return to shareholders and to meet external capital requirements on our debt and credit facilities. Unfunded capital expenditures are limited to \$10,000 on an annual basis and this is reviewed quarterly.

As part of the existing debt agreement, three key financial covenants are monitored on an ongoing basis by management to ensure compliance with the agreement as follows:

- Funded debt to a rolling twelve month EBITDA
- Working capital ratio
- Fixed charge coverage ratio

In order to facilitate management of its capital requirements, the Company prepares annual budgets that are updated as necessary depending on various factors including general industry conditions. The annual budget is approved by the Board of Directors. As at September 30, 2008, the Company has remained in compliance with all external lending agreement covenants.

#### **Recently issued accounting pronouncements**

##### *International Financial Reporting Standards*

In February 2008, the Canadian Accounting Standards Board confirmed that the use of International Financial Reporting Standards ("IFRS") will be required for Canadian publicly accountable companies for fiscal years beginning on or after January 1, 2011. The Company is currently evaluating the impact of adopting IFRS.

##### *Goodwill and intangible assets*

In February 2008, The Canadian Institute of Chartered Accountants issued Section 3064, "Goodwill and Intangible Assets" which replaces Section 3062, "Goodwill and Other Intangible Assets". The new standard provides guidance on the recognition, measurement and disclosure of goodwill and intangible assets and is effective for annual periods beginning on or after October 1, 2008. The Company is currently evaluating the impact of adopting this standard.

## **2. Seasonality**

The third quarter of each year is historically the strongest in terms of sales, gross profit and net earnings due to increased consumer purchasing of the Company's products during the holiday season.

### 3. Acquisitions

On June 30, 2008 the Company's wholly-owned subsidiary, 1773008 Ontario Inc. acquired 100% of the common shares of World Vintners Inc. ("WVI") for consideration of \$10,956, including acquisition costs. WVI is a producer and marketer of high quality consumer-made wine kits with a network of 75 franchised wine-on-premise and retail outlets under the Wine Kitz brand name. The allocation of purchase price is preliminary and is based on management's estimates of the fair value of the assets acquired and liabilities assumed. Management is currently obtaining fair market values for the net assets and intangible assets acquired, including the estimated remaining useful lives. Details of net assets acquired based on preliminary allocations are as follows: accounts receivable - \$1,170; inventories - \$1,269; income taxes recoverable - \$1,625; property, plant and equipment - \$844; intangible assets - \$380; goodwill - \$8,125; other assets - \$72; accounts payable and accrued liabilities - (\$2,529). This transaction was accounted for using the purchase method. The results of operations have been included in the consolidated financial statements of the Company, effective July 1, 2008.

On June 13, 2008 the Company acquired 50% of the shares of Rocky Ridge Vineyards Inc. ("Rocky Ridge") for consideration of \$4,016, including acquisition costs. The Company previously owned 50% of the shares of Rocky Ridge and as a result of this transaction Rocky Ridge became a wholly-owned subsidiary of the Company. Rocky Ridge is a premium vineyard located in the Similkameen Valley of British Columbia. The allocation of purchase price is preliminary and is based on management's estimates of the fair value of the assets acquired and liabilities assumed. Management is currently obtaining fair market values for the net assets acquired, including the estimated remaining useful lives. Details of net assets acquired are as follows: vineyards - \$4,400; goodwill - \$219; bank indebtedness - (\$603). This transaction was accounted for using the purchase method. The results of operations have been fully consolidated with those of the Company's effective June 14, 2008.

The value assigned to goodwill in both acquisitions is not deductible for tax purposes.

The Company is in the process of closing an agreement to purchase 100% of the outstanding shares of Small Winemakers Collection Inc., a premium wine agency based in Ontario. The agreement is expected to close during the third quarter.

### 4. Long-term debt

On May 15, 2008, the Company's four existing term loans were replaced with one seven year variable rate term facility in the amount of \$80,000. The new term loan is repayable in monthly principal payments of \$444 plus interest and matures on April 30, 2015. Subsequent to the repayment of the old term loans, the Company unwound the three interest rate swaps related to the term loans. The Company entered into a new interest rate swap which effectively fixes the interest rate on the \$80,000 term loan at 5.64% for the term of the debt effective July 2, 2008.

As part of the acquisition of Rocky Ridge, on June 13, 2008 the Company issued a promissory note to the seller of Rocky Ridge in the amount of \$1,650. The note incurs interest at 6% compounded annually and is to be paid in two equal annual installments of principal and interest on June 13, 2009 and June 13, 2010.

### 5. Changes in non-cash working capital items

The change in non-cash working capital items is comprised of the change in the following items:

	For the Three Months Ended September 30,		For the Six Months Ended September 30,	
	<u>2008</u>	<u>2007</u>	<u>2008</u>	<u>2007</u>
	\$	\$	\$	\$
Accounts receivable	(5,509)	(2,164)	(5,479)	(2,607)
Inventories	(1,382)	(1,523)	(1,181)	(31)
Prepaid expenses and other assets	(1,123)	(754)	(1,781)	(1,786)
Accounts payable and accrued liabilities	4,163	13,355	1,148	6,534
Income taxes recoverable	<u>(52)</u>	<u>(826)</u>	<u>216</u>	<u>(569)</u>
	<u>(3,903)</u>	<u>8,088</u>	<u>(7,077)</u>	<u>1,541</u>

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" Joseph A. Peller"

Joseph A. Peller  
Chairman  
November 5, 2008

