



**ROCKY MOUNTAIN DEALERSHIPS INC.  
MANAGEMENT'S DISCUSSION & ANALYSIS  
FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2016**

This Management's Discussion and Analysis ("MD&A") was prepared as of November 7, 2016 and is provided to assist readers in understanding Rocky Mountain Dealerships Inc.'s financial performance for the three and nine months ended September 30, 2016. It should be read in conjunction with the unaudited condensed consolidated interim financial statements for the three and nine months ended September 30, 2016 and the audited consolidated financial statements for the years ended December 31, 2015, and 2014 together with the notes thereto and the auditor's report thereon. The results reported herein have been derived from consolidated financial statements prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board and are presented in Canadian dollars.

Unless the context otherwise requires, use in this MD&A of "Rocky", "the Company", "we", "us", or "our" means Rocky Mountain Dealerships Inc. and its wholly-owned subsidiaries including Rocky Mountain Equipment Canada Ltd. ("RME Canada") and Rocky Mountain Dealer Acquisition Corp. ("RMDAC").

Rocky's common shares trade on the Toronto Stock Exchange under the symbol 'RME' and on the OTCQX under the symbol 'RCKXF'. Additional information relating to Rocky, including the Company's Annual Information Form, dated March 15, 2016 ("AIF"), is available on the System for Electronic Document Analysis and Retrieval ("SEDAR") website at [www.sedar.com](http://www.sedar.com).

This MD&A contains forward-looking statements ("FLS"). Please see the section "Caution Regarding Forward-Looking Information and Statements" for a discussion of the risks, uncertainties and assumptions relating to those statements.

Unless otherwise indicated, changes in financial results for the three and nine months ended September 30, 2016 have been calculated using the same periods in the prior year as comparative figures, whereas changes in our financial position as at September 30, 2016 are calculated using December 31, 2015 as the comparative.

**SUMMARY OF THE QUARTER ENDED SEPTEMBER 30, 2016**

- Total revenues contracted by \$33.3 million or 13.0% to \$222.6 million
- Gross profit decreased by \$3.2 million or 7.9% to \$36.9 million (16.6% of sales, up from 15.6%)
- Inventory decreased by \$49.2 million or 9.9% to \$445.6 million, the lowest reported level since 2012
- Operating SG&A<sup>(1)</sup> declined by \$3.7 million or 14.6% to \$21.4 million (9.6% of sales, down from 9.8%)
- Adjusted Diluted Earnings per Share<sup>(1)</sup> increased by \$0.02 or 5.7% to \$0.37
- Adjusted EBITDA<sup>(1)</sup> increased by \$0.5 million or 4.3% to \$12.2 million
- Floor Plan Neutral Operating Cash Flow<sup>(1)</sup> increased by \$13.8 million or 28.3% to \$62.3 million

(1) – See further discussion in "Non-IFRS Measures" and "Reconciliation of Non-IFRS Measures to IFRS" sections below.

**COMPANY OVERVIEW**

Headquartered in Calgary, Alberta, Rocky is one of Canada's largest agriculture equipment dealers with a network of full-service equipment stores across the Canadian Prairie Provinces.

Rocky is Canada's largest retail dealer of CNH Industrial N.V. ("CNH") equipment, which includes Case IH, New Holland, and Case Construction. We are also a major independent dealer of equipment from a number of other short-line agriculture and industrial manufacturers.

We offer our customers a one-stop solution for their equipment needs through new and used equipment sales, parts sales, repairs and maintenance services and third-party equipment financing and insurance services. In addition, we provide or arrange other ancillary services such as GPS signal subscriptions and geomatics services.

The Company's operations in Alberta, Saskatchewan and Manitoba are conducted through RME Canada under the name Rocky Mountain Equipment.

**MARKET FUNDAMENTALS AND OUTLOOK**

Our agriculture equipment sales are made primarily to grain, pulse and oilseed crop farmers in Western Canada. Demand for our equipment is largely driven by equipment and agricultural commodity prices, input costs and weather. Changes in these demand drivers can cause our customers' buying patterns to shift. Equipment utilization rates, by contrast, are comparatively less volatile as agricultural equipment incurs hours in the field regardless of weather or economic conditions. Farmers are required to work their fields each year, however circumstances may exist whereby farmers opt for used equipment in lieu of new equipment, or they may elect to maintain rather than replace their fleets. Our broad range of product



and service offerings enable us to respond to these shifts in buying patterns and provide a measure of stability within our financial results.

Farmers across the Canadian Prairies have benefited from ample moisture and favourable growing conditions throughout most of the 2016 growing season. Despite relatively flat seeded and harvested acreage, Agriculture and Agri-Food Canada is calling for improved crop yields which is expected to boost overall production of principal field crops in 2016 by 6.3% as compared to last year, a level of production second only to 2013's bumper crop.

While much of the crop is already in the bin, harvest progress is behind both last year and the five-year average in many regions. Rain and early snowfalls have kept the farmers out of the fields and delayed the completion of the harvest, which has also resulted in a delay in the demand for our products and services. While it is not unreasonable to expect most of this crop to ultimately be harvested, these conditions may degrade the quality of the crop remaining in the field.

Prices for both wheat and canola, although down in response to increased levels of global supply and forecasted production, showed modest improvements of late, due in part to the uncertainty surrounding the delay in harvest completion. In the near term, agriculture commodity prices in Canada are expected to continue to be supported by the disparity between the Canadian and U.S. dollars, while sustained cost reductions in fuel and fertilizer prices are providing input cost relief to farmers.

Agriculture, as a whole, exhibits cyclical surges in demand and profitability driven by the aforementioned macroeconomic factors, as well as other factors that can impact our industry. While we remain at the low end of the equipment demand cycle, we reiterate the stability of the fundamentals underlying the agriculture industry. And while weather continues to have a significant influence on our overall demand, advances made in farming practices, seed technology and application techniques, have helped to mitigate this exposure to some extent. These factors notwithstanding, farmers' balance sheets continue to be healthy and the agriculture industry, especially in Western Canada, remains strong.

Our industrial equipment sales are balanced through residential construction and aggregate production, as well as commercial, industrial, and municipal construction throughout the Alberta market. The success of Rocky's industrial business is largely correlated to investment in residential housing as well as overall economic activity and spending in Alberta. The significant decline in the Alberta economy has tempered spending in all sectors and we continue to feel the effects on our industrial sales.

Rocky's success and growth, while predicated on the larger economic conditions and factors discussed above, are also affected by our continued ability to be a partner of choice for equipment purchasers. To that end, we continue to invest in our people, through training and employee engagement programs and in the communities that we serve. As noted, farmers' balance sheets are strong, and agriculture continues to be a healthy, stable industry in Western Canada. In the end, it is our response to these positive trends and advancements in the agriculture industry, and our ability to continually provide a compelling value proposition to our customers, that will predicate our long-term success.

The outlook for our end-markets, long-term health in agricultural commodity prices, the impact of previously acquired dealerships and trade areas and our strong original equipment manufacturer ("OEM") relationships, position us well to pursue our longer-term revenue and earnings growth initiatives.

Our underlying business fundamentals remain strong. We have distribution rights for some of the world's leading equipment brands over a vast sales territory. Furthermore, significant barriers to entry exist in this market, which help us maintain our position as an exclusive supplier of these brands. Our installed base and customer relationships create an annuity of equipment sales and product support revenue, which help drive dependable earnings and cash flow.



## SELECTED FINANCIAL INFORMATION

\$ thousands, except per share amounts

	For the three months ended September 30,				For the nine months ended September 30,			
	2016		2015		2016		2015	
<b>Sales</b>								
New equipment	69,173	31.1%	80,432	31.4%	260,946	40.5%	287,573	41.7%
Used equipment	105,815	47.5%	125,534	49.0%	267,949	41.6%	284,806	41.3%
Parts	37,737	16.9%	37,918	14.8%	88,393	13.7%	86,895	12.6%
Service	8,707	3.9%	10,711	4.2%	24,005	3.7%	27,151	3.9%
Other	1,215	0.6%	1,391	0.6%	3,393	0.5%	3,444	0.5%
	<b>222,647</b>	<b>100.0%</b>	<b>255,986</b>	<b>100.0%</b>	<b>644,686</b>	<b>100.0%</b>	<b>689,869</b>	<b>100.0%</b>
Cost of sales	185,786	83.4%	215,944	84.4%	545,395	84.6%	585,426	84.9%
Gross profit	36,861	16.6%	40,042	15.6%	99,291	15.4%	104,443	15.1%
Selling, general and administrative	23,619	10.6%	30,334	11.8%	73,543	11.4%	84,327	12.2%
Interest on short-term debt	3,262	1.5%	3,276	1.3%	9,652	1.5%	9,435	1.4%
Interest on long-term debt	438	0.2%	519	0.2%	1,345	0.2%	1,559	0.2%
<b>Earnings before income taxes</b>	<b>9,542</b>	<b>4.3%</b>	<b>5,913</b>	<b>2.3%</b>	<b>14,751</b>	<b>2.3%</b>	<b>9,122</b>	<b>1.3%</b>
Provision for income taxes	2,910	1.3%	1,561	0.6%	4,489	0.7%	2,409	0.3%
<b>Net earnings</b>	<b>6,632</b>	<b>3.0%</b>	<b>4,352</b>	<b>1.7%</b>	<b>10,262</b>	<b>1.6%</b>	<b>6,713</b>	<b>1.0%</b>
Earnings per share								
Basic	0.34		0.23		0.53		0.35	
Diluted	0.34		0.23		0.53		0.35	
Dividends per share	0.115		0.115		0.345		0.345	
Book value per share – diluted (as at September 30)					8.92		8.68	
Adjusted Diluted Earnings per Share <sup>(1)</sup>	0.37		0.35		0.61		0.47	
Adjusted EBITDA <sup>(1)</sup>	12,208	5.5%	11,707	4.6%	23,445	3.6%	19,656	2.8%
Operating SG&A <sup>(1)</sup>	21,391	9.6%	25,059	9.8%	66,194	10.3%	75,352	10.9%
Floor Plan Neutral Operating Cash Flow <sup>(1)</sup>	62,284	28.0%	48,534	19.0%	71,522	11.1%	85,349	12.4%

(1) – See further discussion of these non-IFRS measures in the “Non-IFRS Measures” and “Reconciliation of Non-IFRS Measures to IFRS” sections below.

## Revenue and Gross Profit

The Company uses the terms “acquired” versus “same store” in assessing its revenue. Each acquired store has an average historical level of sales prior to being acquired by Rocky. When the Company discusses “acquired” results, it is referring to these average historical levels. This base level of activity continues to be classified as acquired until such time as the acquired store has been included in our dealership network for twelve months after which point, all activity is classified as same store.

	For the three months ended September 30,					For the nine months ended September 30,				
	2016	2015	Change			2016	2015	Change		
			Total	Acquired	Same Store			Total	Acquired	Same Store
<b>Sales</b>										
New equipment	69,173	80,432	(11,259)	-	(11,259)	260,946	287,573	(26,627)	5,074	(31,701)
Used equipment	105,815	125,534	(19,719)	-	(19,719)	267,949	284,806	(16,857)	1,668	(18,525)
Parts	37,737	37,918	(181)	-	(181)	88,393	86,895	1,498	993	505
Service	8,707	10,711	(2,004)	-	(2,004)	24,005	27,151	(3,146)	225	(3,371)
Other	1,215	1,391	(176)	-	(176)	3,393	3,444	(51)	-	(51)
	<b>222,647</b>	<b>255,986</b>	<b>(33,339)</b>	-	<b>(33,339)</b>	<b>644,686</b>	<b>689,869</b>	<b>(45,183)</b>	<b>7,960</b>	<b>(53,143)</b>
Gross profit	36,861	40,042	(3,181)			99,291	104,443	(5,152)		
Gross margin	16.6%	15.6%	1.0%			15.4%	15.1%	0.3%		

For the three and nine months ended September 30, 2016, total sales were \$222.6 million (a decrease of \$33.3 million or 13.0%) and \$644.7 million (a decrease of \$45.2 million or 6.5%). Excluding \$8.0 million of acquired sales, same store revenues declined by \$53.1 million or 7.7%, on a year-to-date basis.

Same store equipment sales for the three and nine months ended September 30, 2016 declined by \$31.0 million and \$50.2 million, respectively (15.0% and 8.8%, respectively). Harvest has progressed at a slower rate in 2016 than has been typical in recent years. According to Alberta Agriculture and Forestry, approximately 28% of the 2016 crop remained unharvested



as of early October, as compared to 13% a year ago and a five-year average of 9%. Many farmers defer certain fleet investment decisions until such time as the crop is in the bin and there exists a greater degree of certainty with respect to overall production, grade and expected cash receipts. The reduction in equipment sales during the quarter is due, in part, to these factors.

The decline in new equipment sales during the quarter was also due, in part, to the timing of deliveries from our OEMs which deferred delivery of certain units beyond the third quarter of 2016 and the continued decline in demand for industrial equipment throughout our sales territory.

Equipment sales on a year-to-date basis also include \$6.7 million of acquired sales.

For the three and nine months ended September 30, 2016, same store product support sales were \$46.4 million (a decrease of \$2.2 million or 4.5%) and \$112.4 million (a decrease of \$2.9 million or 2.5%), respectively. While same store parts sales have remained relatively flat during both the third quarter and year-to-date, same store service revenues have experienced declines of \$2.0 million and \$3.4 million, respectively. The delayed harvest tempered third quarter service sales in certain regions. We also rationalized our technician headcount during the year in an effort to drive greater efficiencies and bottom line earnings accretion within our service departments. The revenue reduction associated therewith was most pronounced during the third quarter while demand for service work is at its peak. Spring sales promotions and price increases resulting from the weaker Canadian dollar also had a positive effect, primarily on our parts revenues, for the year-to-date.

Product support demand from the industrial sector continued to decline during the third quarter and year-to-date as key commodity prices remain depressed and industry headwinds persisted.

Product support sales on a year-to-date basis also include \$1.2 million of acquired sales.

Certain product support activity is performed for the benefit of other departments within the Company. This activity is excluded from reported parts and service revenues. Management assesses overall product support activity to ensure that the resources deployed are adequate in light of total activity. Total parts and service activity is reconciled to our reported revenues for the respective departments as follows:

\$ thousands

	For the three months ended September 30,		For the nine months ended September 30,	
	2016	2015	2016	2015
<b>Parts activity</b>				
Total activity	41,323	41,666	98,418	97,638
Internal activity eliminated	(3,586)	(3,748)	(10,025)	(10,743)
Reported revenues	37,737	37,918	88,393	86,895
<b>Service activity</b>				
Total activity	12,938	15,522	37,897	44,150
Internal activity eliminated	(4,231)	(4,811)	(13,892)	(16,999)
Reported revenues	8,707	10,711	24,005	27,151

Gross profit for the three and nine months ended September 30, 2016 decreased by \$3.2 million or 7.9% and \$5.2 million or 4.9%, respectively, largely as a result of reduced revenues. Gross margin for the three and nine months ended September 30, 2016 increased by 1.0% and 0.3%, respectively. The increases in gross margin for the third quarter and year-to-date were driven primarily by increases in manufacturer incentives recognized of \$1.3 million and \$0.7 million, respectively, as well as sales mix.

### Selling, General and Administrative

Selling, general and administrative ("SG&A") expenses include sales and marketing expenses, sales commissions, payroll and related benefit costs, insurance expenses, professional fees, rent and other facility costs and administration overhead including depreciation of property and equipment and amortization of intangible assets. Many of these costs are fixed. When we acquire new stores, these costs typically increase as we incur additional expenditures related to the direct selling, general and administrative functions. Over time, as these acquisitions are amalgamated into the business, the costs generally decrease as we incorporate their finance and other administrative functions into our centralized corporate resources. Similarly, our costs will increase as we add direct customer-related resources such as equipment specialists, but will normalize relative to sales volumes as those positions drive incremental revenue and increase our customer base.

Fixed costs are subject to price increases, driven primarily by real estate and labour demand in Western Canada. Variable costs included within SG&A expenses consist primarily of sales commissions.

The Company assesses its Operating SG&A relative to total sales in analyzing its results (see the definition and reconciliation



of Operating SG&A in the “Non-IFRS Measures” and “Reconciliation of Non-IFRS Measures to IFRS” sections below). The Company targets a sub-10% Operating SG&A as a percentage of sales on an annual basis.

For the three and nine months ended September 30, 2016, Operating SG&A decreased by \$3.7 million or 14.6% and \$9.2 million or 12.2%, respectively. These reductions are primarily the result of cost containment measures implemented throughout 2015 and 2016 to better align our resources deployed with current industry demand and the cost savings associated with the amalgamation of our distribution network. The decrease year-to-date comes despite an additional \$1.9 million of expenses associated with stores acquired during 2015.

Excluded from Operating SG&A for the three and nine months ended September 30, 2016 are \$1.3 million and \$3.6 million of non-recurring costs associated with the amalgamation of our Calgary and Red Deer industrial facilities, respectively. Included in these expenses are accruals associated with terminating the leases on these facilities. While the Company continues to negotiate these lease terminations with the landlords, one of whom is a related party (see the “Related Party Transactions” section below for additional details), challenging market conditions have caused the Company to reassess its original accrual recognized during the second quarter of 2016 of \$1.1 million (approximately 50% of the remaining contractual obligations). During the third quarter of 2016, we recognized the remaining \$1.1 million of remaining contractual obligations.

We also recognized gains on our derivative financial instruments of \$2.9 million and \$4.1 million, respectively, (2015 – losses of \$3.4 million and \$3.3 million, respectively) and impairment losses on redundant land classified as held for sale of \$1.4 million and \$1.4 million, respectively (2015 – \$Nil and \$Nil, respectively). The gains (losses) associated with the derivatives arose primarily as a result of fluctuations in the Company’s common share price and the associated impact on its total return swaps. The impairment losses on redundant land reflect our assessment of current market demand and valuation for those assets. These gains (losses) recognized during the third quarter and year-to-date have also been removed from SG&A expenses in deriving Operating SG&A.

### **Interest**

The Company’s short-term interest expense is attributable to the floor plan financing associated with its new and used equipment inventory as well as interest on its Operating Facility (as defined below, see discussion under the heading “Adequacy of Capital Resources – Finance Facilities”). Interest on long-term debt pertains primarily to the Company’s Term Facility (as defined below, see discussion under the heading “Adequacy of Capital Resources – Finance Facilities”) as well as its former debenture repayment, acquisition, real estate and fleet facilities for the comparable period. During the three and nine months ended September 30, 2016, total interest expense remained relatively flat.

### **Net Earnings**

Net earnings for the three and nine months ended September 30, 2016 increased by \$2.3 million (an increase of 52.4% or \$0.11 per diluted share) and \$3.5 million (an increase of 52.9% or \$0.18 per diluted share), respectively. Adjusted Diluted Earnings per Share increased by \$0.02 and \$0.14 to \$0.37 and \$0.61 for the respective three and nine month periods ended September 30, 2016, as compared to the same periods last year. See the definition and reconciliation of Adjusted Diluted Earnings per Share in the “Non-IFRS Measures” and “Reconciliation of Non-IFRS Measures to IFRS” sections below. During the year-to-date, the reduction in gross profit was more than offset by reduced Operating SG&A resulting in increased Adjusted Diluted Earnings per Share.





## SUMMARY OF QUARTERLY RESULTS

\$ thousands, except per share amounts

	Q3 2016	Q2 2016	Q1 2016	Q4 2015	Q3 2015	Q2 2015	Q1 2015	Q4 2014	Q3 2014
<b>Sales</b>									
New equipment	69,173	111,971	79,802	162,424	80,432	95,393	111,748	182,555	81,837
Used equipment	105,815	78,468	83,666	92,676	125,534	75,487	83,785	79,810	102,354
Parts	37,737	32,314	18,342	20,614	37,918	31,989	16,988	21,320	35,568
Service	8,707	8,550	6,748	8,714	10,711	9,387	7,053	9,569	10,041
Other	1,215	1,272	906	1,159	1,391	1,204	849	838	995
	<b>222,647</b>	232,575	189,464	285,587	255,986	213,460	220,423	294,092	230,795
Cost of sales	185,786	198,428	161,181	248,049	215,944	180,519	188,963	254,623	191,680
Gross profit	36,861	34,147	28,283	37,538	40,042	32,941	31,460	39,469	39,115
Gross margin	16.6%	14.7%	14.9%	13.1%	15.6%	15.4%	14.3%	13.4%	16.9%
SG&A	23,619	25,455	24,469	27,449	30,334	26,363	27,630	27,548	27,165
Interest and taxes	6,610	5,326	3,550	5,509	5,356	4,549	3,498	5,700	5,746
Net earnings	6,632	3,366	264	4,580	4,352	2,029	332	6,221	6,204
EPS – basic	0.34	0.17	0.01	0.24	0.23	0.10	0.02	0.32	0.32
EPS – diluted	0.34	0.17	0.01	0.24	0.23	0.10	0.02	0.32	0.32

Fluctuating seasonal revenue cycles are common in both the agriculture and industrial industries as a result of weather conditions, the timing of crop receipts and farming cycles and the timing of infrastructure expenditures. As a result, our financial results typically vary between quarters. The first quarter is generally the weakest due to the lack of agriculture activity and winter shutdowns, while the fourth quarter is the strongest due to the post-harvest purchases that are typical in the agriculture sector.

Seeding activity typically commences between the latter part of the first quarter and the start of the second quarter while harvest begins towards the middle of the third quarter, and continues through into the fourth quarter. Our financial results vary between quarters accordingly.

Over time, we expect second and third quarter sales activity to increase relative to the fourth quarter as our increased installed base drives more parts and service activity and our customers decide to trade their equipment earlier in the year to take advantage of advancements in technology before the harvest season.

Weather conditions, such as a late spring or harvest, excess moisture or drought conditions may also positively or negatively impact sales activity and profitability for any given period.



## BALANCE SHEET SUMMARY

\$ thousands

### Assets

	September 30, 2016	December 31, 2015	September 30, 2015
Inventory	445,613	499,760	489,690
Other current assets	45,897	63,824	83,380
Total current assets	491,510	563,584	573,070
Property and equipment	49,157	39,888	36,295
Deferred tax asset	1,827	2,367	1,685
Derivative financial assets	48	-	-
Intangible assets	548	671	712
Goodwill	18,776	18,802	18,910
<b>Total assets</b>	<b>561,866</b>	<b>625,312</b>	<b>630,672</b>

### Liabilities and equity

Floor plan payable	299,292	356,568	352,135
Other current liabilities	49,729	53,893	65,859
Total current liabilities	349,021	410,461	417,994
Long-term debt	35,159	40,080	40,050
Obligations under finance leases	632	154	-
Derivative financial liabilities	4,146	4,859	4,765
	388,958	455,554	462,809
Shareholders' equity	172,908	169,758	167,863
<b>Total liabilities and equity</b>	<b>561,866</b>	<b>625,312</b>	<b>630,672</b>

Current assets at September 30, 2016, consisted primarily of new and used equipment inventory. The Company's new and used equipment inventory is comprised predominantly of agriculture equipment. Rocky has a diverse customer base for its agriculture equipment and strives to carry an appropriate mix of both new and used equipment to best serve our customers. Typically, our agriculture customers trade in their used equipment when making equipment purchases. Industrial equipment, by contrast, is generally utilized to the end of its useful life by one owner. Trades of used industrial equipment are less common and as such, the Company carries less used industrial equipment relative to new. Recent market conditions have, however, created an environment whereby we are experiencing a modest increase in industrial equipment trades. The composition of the Company's equipment inventory is as follows:

\$ thousands

	September 30, 2016	December 31, 2015	September 30, 2015
New agriculture equipment	111,139	113,182	138,973
New industrial equipment	40,272	59,153	65,091
Total new equipment	151,411	172,335	204,064
Used agriculture equipment	241,846	282,868	233,875
Used industrial equipment	7,632	4,916	6,200
Total used equipment	249,478	287,784	240,075
<b>Total equipment inventory</b>	<b>400,889</b>	<b>460,119</b>	<b>444,139</b>

During the nine months ended September 30, 2016, the Company continued its inventory reduction efforts. As it pertains to agriculture equipment, the progress made to date in 2016 is consistent with our expectations and the seasonal nature of demand. Typically, our biggest opportunity for inventory reduction comes in the third quarter of the year, which was again the case in 2016.

On the industrial side of the business, weaker sales activity has slowed our progress, however, we remain committed to our stated inventory reduction initiative and will continue to tailor our sales and procurement efforts accordingly.

Current liabilities are comprised predominantly of floor plan payable for financed equipment inventory of approximately \$299.3 million as at September 30, 2016 (December 31, 2015 – \$356.6 million). As a percentage of equipment inventory, floor plan payable was 74.7% as at September 30, 2016, down from 77.5% at December 31, 2015.



## LIQUIDITY AND CAPITAL RESOURCES

We assess liquidity in terms of our ability to generate sufficient cash flow, along with other sources of liquidity including cash and borrowings, to fund our operations and growth in operations. Net cash flow is affected by the following items:

- Operating activities, including, the levels of accounts receivable, inventory, accounts payable and floor plan payable;
- Financing activities, including bank credit facilities, long-term debt and other capital market activities; and,
- Investing activities, including capital expenditures, dispositions of fixed assets and acquisitions of complementary businesses.

### Summary of Cash Inflows (Outflows)

\$ thousands

	For the three months ended September 30,		For the nine months ended September 30,	
	2016	2015	2016	2015
Net earnings	6,632	4,352	10,262	6,713
Non-cash items and changes in working capital	13,958	17,015	3,984	15,908
Cash flows from operating activities	20,590	21,367	14,246	22,621
Cash flows used for financing activities	(3,922)	(9,224)	(9,269)	(10,523)
Cash flows used for investing activities	(886)	(3,947)	(7,987)	(25,513)
Net change in cash	15,782	8,196	(3,010)	(13,415)
Cash, beginning of period	(2,102)	1,341	16,690	22,952
Cash (cash deficiency), end of period	13,680	9,537	13,680	9,537
Floor Plan Neutral Operating Cash Flow <sup>(1)</sup>	62,284	48,534	71,522	85,349

(1) – See further discussion in “Non-IFRS Measures” and “Reconciliation of Non-IFRS Measures to IFRS” sections below.

### Cash Flows from Operating Activities

The Company assesses its Floor Plan Neutral Operating Cash Flow in analyzing its cash flows from operating activities. See the definition and reconciliation of Floor Plan Neutral Operating Cash Flow in the “Non-IFRS Measures” and “Reconciliation of Non-IFRS Measures to IFRS” sections below.

Rocky is eligible to finance its equipment inventory using its various floor plan facilities. Floor plan facilities are asset-backed lending arrangements whereby each draw is associated with a specific piece of equipment. The Company is under no obligation to finance any of its equipment inventory and, as a general rule, financed units can be paid out for a period of time and refinanced at a later date. Adjusting cash flows from operating activities for changes in the balance of floor plan payable allows management to isolate and analyze cash flows from operating activities, prior to any sources or uses of cash associated with equipment financing decisions.

For the three and nine months ended September 30, 2016, Floor Plan Neutral Operating Cash Flow increased by \$13.8 million (up from \$48.5 million) and decreased by \$13.8 million (down from \$85.3 million), respectively.

During the third quarter of 2015, high sales volumes processed towards the end of the quarter resulted in an increase in cash tied up in accounts receivable, reducing Floor Plan Neutral Operating Cash Flow in the comparative quarter.

On a year-to-date basis, the reduction of inventory (excluding acquired inventory) during the first half of 2015 generated strong Floor Plan Neutral Operating Cash Flow. While we continue to reduce our inventory balance and generate cash, the amount of cash generated from inventory declined during the nine months ended September 30, 2016, yielding an overall decline in Floor Plan Neutral Operating Cash Flow for the nine months ended September 30, 2016.

Cash flows from operating activities for the three and nine months ended September 30, 2016 declined by \$0.8 million (down from \$21.4 million) and \$8.4 million (down from \$22.6 million), respectively. The decrease during the quarter is primarily the result of the aforementioned build in receivables in the comparative period, offset in part by increased floor plan repayments which consumed operating cash flows otherwise generated during the period.

On a year-to-date basis, the decrease is due primarily to decreased cash generation from inventory, net of floor plan payable.

### Cash Flows from Financing Activities

Cash flows from financing activities pertained primarily to debt and dividend payments as well as net proceeds associated with the financing of acquisitions and real estate assets. For the three and nine months ended September 30, 2016, cash outflows from financing activities declined by \$5.3 million (down from \$9.2 million) and \$1.3 million (down from \$10.5 million), respectively.





As part of an amendment to the Syndicated Facility during the third quarter of 2015, the Company repaid \$5.1 million outstanding on its former Fleet Facility with a draw on its Operating Facility. Repayments of debt during the nine months ended September 30, 2016 also reflect an interest-only period on the Company's Term Facility which expired during Q2 of 2016 when principal payments commenced. During the nine months ended September 30, 2015, the Company drew on its credit facilities to fund the purchase of, and repay debt assumed pursuant to, an acquisition as well as to fund the construction of a new facility in Neepawa, Manitoba. The net inflow of cash served to partially offset scheduled debt repayments and dividends in the comparative period.

### **Cash Flows from Investing Activities**

Cash utilized for investing activities was the result of our normal capital expenditures, investment in new facility construction and the net cash consideration paid pursuant to business combinations, offset by proceeds on the disposition of property and equipment. For the three and nine months ended September 30, 2016, cash outflows from investing activities decreased by \$3.1 million (down from \$3.9 million) and \$17.5 million (down from \$25.5 million), respectively. The decrease during the quarter pertained largely to reduced capital expenditures on branch construction. On a year-to-date basis, the decrease reflects the purchase consideration paid on the acquisition affected during the second quarter of last year.

### **ADEQUACY OF CAPITAL RESOURCES**

We use operating cash flows to finance the purchase of inventory, service our debt requirements, pay dividends, and fund our operating activities, including working capital, both operating and finance leases and floor plan payable. Our ability to service our debt and distribute dividends to shareholders will depend upon our ability to generate cash, which depends on our future operating performance, general economic conditions, availability of adequate credit facilities, compliance with debt covenants, as well as other factors, some of which are beyond our control. Based on our current operational performance, we believe that cash flows from operations, along with existing credit facilities, will provide for our capital needs.

### **Finance Facilities**

The Company has a credit facility with a syndicate of lenders (the "Syndicated Facility"). The Syndicated Facility is a revolving facility which matures on September 24, 2018, secured in favour of the syndicate by a general security agreement. Advances under the Syndicated Facility may be made based on our lenders' prime rate or the U.S. base rate plus 1.0% – 2.5% or based on the banker's acceptance ("BA") rate plus 2.0% – 3.5%. The Company pays standby fees of between 0.4% – 0.7% per annum on any undrawn portion of the Syndicated Facility. The standby fees and premiums on base interest rates within the respective ranges are determined based on the Company's ratio of debt to tangible net worth.

The Syndicated Facility consists of:

- The "Operating Facility" – which may be utilized to advance up to the lesser of the established borrowing base and \$60.0 million. The borrowing base is supported by otherwise unencumbered assets including certain accounts receivable, inventory and items of property and equipment, less priority payables. This facility may be used to finance general corporate operating requirements.
- The "Flooring Facility" – which may be utilized to finance up to 75% of the value of eligible equipment inventory to a maximum of \$125.0 million. Draws against the Flooring Facility are repayable over a term of 28 months, however they become due in full upon the sale of the associated equipment.
- The "Term Facility" – which may be utilized to finance up to 60% of the cost of acquisitions and 75% of the cost of real estate to a maximum of \$75.0 million. Draws are repayable in quarterly installments with acquisition and real estate related draws amortized over periods of 7 and 15 years, respectively. The Term Facility has a seven year repayment period which commenced in April of 2016.

Including the syndicated Flooring Facility, we have total floor plan facilities of approximately \$592.0 million (inclusive of seasonal increases) from various lending institutions for the purpose of financing equipment inventory. These facilities are made available to Rocky by the equipment manufacturers' captive finance companies or divisions (such as CNH Industrial Capital Canada Ltd.), as well as by banks and specialty lenders. The Company also has an additional \$75.0 million of floor plan availability with its OEMs, to be made available to the Company if required as a result of business combinations.



In addition to our available cash balance of \$13.7 million as at September 30, 2016, we have approximately \$385.7 million available on our various credit facilities.

\$ millions

	Facility limit	Amount drawn	Available
Operating Facility <sup>(1)</sup>	60.0	-	<b>60.0</b>
Term Facility	75.0	41.6	<b>33.4</b>
Various floor plan facilities			
OEM floor plan facilities	205.0	97.5	<b>107.5</b>
Syndicated Flooring Facility	125.0	67.3	<b>57.7</b>
Other floor plan facilities	262.0	134.9	<b>127.1</b>
	<b>727.0</b>	<b>341.3</b>	<b>385.7</b>

(1) – Availability subject to borrowing base calculation.

Having recently completed the construction of our new facility in Yorkton, Saskatchewan, the Company expects to draw on it Term Facility in the coming months. The construction of this facility was funded by operating cash flows.

### Financial Covenants

Pursuant to agreements with lenders, the Company is required to monitor and report certain financial ratios on a quarterly basis. The Company's financial covenants and applicable compliance ranges are as follows:

	September 30, 2016	December 31, 2015
Fixed charge coverage of at least	<b>1.15-1.20:1</b>	1.20-1.50:1
Debt to tangible net worth less than	<b>4.00-5.00:1</b>	4.00-5.00:1
Current ratio of at least	<b>1.15-1.20:1</b>	1.15-1.20:1

Each lender has its own definition of which account balances are to be included in these computations. Failing to meet these covenants would constitute a default event which may result in, among other restrictions and remedies, the associated debt becoming due and restrictions being placed on the Company's ability to draw on its facilities or make distributions to shareholders.

As at September 30, 2016 and December 31, 2015, the Company was in compliance with all externally imposed capital requirements.

The Company's continued compliance with its financial covenants is dependent on various factors which influence our financial results including, but not limited to, overall demand for our products and services and the timing of that demand driven by weather and other factors. As agriculture equipment demand remains at the low end of the cycle and our industrial results continue to be impacted by considerable economic headwinds in Alberta, there is a risk that the Company's financial results and/or position may weaken and that we may not comply with our financial covenants, most notably, our fixed charge coverage ratios.

### Derivative Financial Instruments

The Company utilizes derivative financial instruments to hedge its exposure to changes in interest rates and fluctuations in the valuation of its common shares. We do not use derivatives to speculate, but rather as a risk management tool. The Company's portfolio of derivative financial instruments consists of interest rate and total return swaps.

Losses (gains) recognized on derivative financial instruments are as follows:

\$ thousands

	For the three months ended September 30,		For the nine months ended September 30,	
	2016	2015	2016	2015
(Gain) loss recognized in net earnings	<b>(2,929)</b>	3,438	<b>(4,146)</b>	3,274
(Gain) loss recognized in other comprehensive income				
(loss) – net of tax	<b>(207)</b>	175	<b>542</b>	976
Tax on (gain) loss recognized in other comprehensive income (loss)	<b>(76)</b>	62	<b>200</b>	348



### Interest Rate Swaps

The Company has several interest rate swaps related to portions of its Term Facility and various floor plan facilities (collectively, the “Hedged Facilities”).

The Hedged Facilities each bear interest at a floating rate based on the prevailing BA rate. The interest rate swaps hedge our exposure to fluctuations in the BA rate. The Company’s hedged and at risk positions are summarized as follows:

			September 30, 2016		December 31, 2015	
	Maturity	Type	Effective rate	Amount (\$ thousands)	Effective Rate	Amount (\$ thousands)
Hedged position						
Current debt						
Floor plan facility #1	August, 2018	Non-amortizing	4.2%	25,000	4.2%	25,000
Floor plan facility #2	September, 2020	Non-amortizing	5.1%	35,000	5.1%	35,000
Floor plan facility #3	September, 2022	Non-amortizing	5.4%	50,000	5.4%	50,000
			5.0%	110,000	5.0%	110,000
Long-term debt						
Term Facility #1 <sup>(1)</sup>	May, 2016	Amortizing	-	-	3.5%	1,365
Term Facility #2 <sup>(2)</sup>	April, 2017	Amortizing	4.1%	20,125	4.1%	22,750
			4.1%	20,125	4.0%	24,115
			4.9%	130,125	4.8%	134,115
Position at risk						
Floating-rate debt				255,031		299,694
Position hedged						
				51.0%		44.8%

(1) – Formerly the Acquisition Facility.

(2) – Formerly the Debenture Repayment Facility.

At inception, these instruments were designated as hedges and were accounted for using hedge accounting. Subsequently, the interest rate swaps on the Term Facility failed their effectiveness testing and as such, hedge accounting was discontinued. The \$36 thousand accumulated loss associated with the Term Facility #2 swap which has been recognized within accumulated other comprehensive loss will be reversed into net earnings over the remainder of the term of the derivative. Future changes in the fair value of this derivative will be recognized within net earnings in the period in which they arise.

The interest rate swaps on the various floor plan facilities continue to remain effective and as such, we continue to account for these cash flow hedges using hedge accounting. If we sell or terminate a hedged item, or it matures before the related hedging instrument is terminated, we recognize in income any realized or unrealized gain or loss on the derivative instrument. In accounting for these cash flow hedges, changes in fair value of the swaps are included in the consolidated statement of other comprehensive income to the extent the hedge continues to be effective. The related other comprehensive amounts are allocated to net earnings in the same period in which the hedged item affects net earnings. To the extent that changes in the fair value of these derivatives are not completely offset by changes in the fair value of the hedged items, the ineffective portions of the hedging relationships are recorded immediately in net earnings.

For the respective three and nine month periods ended September 30, 2016, we recognized in net earnings, mark-to-market gains of \$0.1 million and \$0.2 million on our interest rate swaps (2015 – gain of \$43 thousand and loss of \$0.1 million).

### Total Return Swaps

The Company has several total return swap arrangements to hedge the exposure associated with increases in its share price on its outstanding Director Share Units (“DSUs”) and Share Appreciation Rights (“SARs”). If not renewed by the Company, these arrangements mature between April 2017 and July 2018. It is the Company’s intention to maintain a hedged position which matches the terms associated with the DSUs and SARs. The hedging relationship with the SARs is ineffective to the extent that the Company’s share price falls below the strike price of the SARs.

During the vesting period, the accounting treatment of the SARs creates an inherent discrepancy from the total return swaps in terms of the timing of the impact on net earnings. Changes in the Company’s share price are factored into the Black-Scholes option pricing model to determine the fair value of the SARs at each reporting date. This fair value will then be expensed over the remainder of the vesting period. The derivative financial instruments, by contrast, are marked-to-market at each reporting date. Once vested, the SARs will also be marked-to-market at each reporting date, eliminating the timing discrepancy.



The Company does not apply hedge accounting to these relationships and as such, gains and losses arising from marking these derivatives to market are recognized in net earnings in the period in which they arise. For the respective three and nine month periods ended September 30, 2016, the Company recognized mark-to-market gains of \$2.9 million and \$3.9 million (2015 – losses of \$3.5 million and \$3.2 million).

The Company's hedged and at risk positions are summarized as follows:

In thousands of shares/units except per share amounts		September 30, 2016		December 31, 2015	
		Weighted average price/share \$	Shares/units	Weighted average price/share \$	Shares/units
Hedged position					
DSUs		10.54	100	10.54	100
SARs		9.21	1,170	9.21	1,170
		9.31	1,270	9.31	1,270
Position at risk					
DSUs			64		75
SARs			1,062		1,146
			1,126		1,221
Position hedged			112.8%		104.0%

### Dividends

On November 7, 2016, Rocky's Board of Directors (the "Board") approved a quarterly dividend of \$0.115 per common share on its outstanding common shares. The common share dividend is payable on December 30, 2016, to shareholders of record at the close of business on November 30, 2016.

This dividend is designated by Rocky to be an "eligible dividend" for the purposes of the Income Tax Act (Canada) and any similar provincial or territorial legislation. An enhanced dividend tax credit applies to "eligible dividends" paid to Canadian residents. Please consult with your own tax advisor for advice with respect to the income tax consequences to you from Rocky designating its dividends as "eligible dividends." Investors are cautioned that quarterly dividends remain subject to approval by Rocky's Board, and that the Board may, at any time, increase, decrease or suspend payment of the dividend.

### SHARE CAPITAL – OUTSTANDING SHARES

During the nine months ended September 30, 2016 and 2015, there were no changes in the issued and outstanding common shares of the Company. As at September 30, 2016 and 2015 as well as November 7, 2016, there were 19,384,086 shares outstanding.

The options outstanding at September 30, 2016 are as follows:

Grant date	Options outstanding (thousands)	Options exercisable (thousands)	Weighted average exercise price (\$)	Weighted average contractual life (years)
March 28, 2012	214	214	11.96	0.5
March 13, 2013	339	339	12.89	1.4
March 13, 2014	367	245	11.52	2.4
	920	798	12.13	1.6

As at November 7, 2016, there were 914,166 options outstanding.

### CONTRACTUAL OBLIGATIONS

The Company's contractual obligations consist primarily of its floor plan payable used to finance the purchase of new, and to a lesser extent, used equipment. The Company has classified its floor plan payable as current as the corresponding inventory to which it relates has also been classified as current.

Floor plan payable as well as trade payables, accruals and other form the majority of the Company's contractual obligations which will be discharged within the next 12 months.



Other significant contractual obligations outstanding as at September 30, 2016 include long-term debt consisting predominantly of the Term Facility and operating lease commitments which relate primarily to the Company's facilities. Lease terms are between one and eleven years and most building leases contain renewal options for periods ranging from three to five years.

The Company assesses its liquidity based on the period in which cash flows are expected to occur. The following table summarizes the Company's expected undiscounted cash flows as at September 30, 2016 assuming the Syndicated Facility is renewed prior to maturity on September 24, 2018. The analysis is based on foreign exchange rates and interest rates in effect at the consolidated balance sheet date, and includes both principal and interest cash flows.

\$ thousands	Total	2016	2017-2018	2019-2020	Thereafter
Trade payables, accruals and other	39,636	39,636	-	-	-
Floor plan payable	309,963	77,491	232,472	-	-
Long-term debt	45,431	1,892	14,720	13,970	14,849
Obligations under finance leases	1,102	115	911	76	-
Operating lease obligations	35,349	2,216	14,769	9,139	9,225
Derivative financial liabilities	6,159	443	3,042	2,098	576
Total contractual obligations	437,640	121,793	265,914	25,283	24,650

In the event that the Syndicated Facility is not renewed prior to its maturity, the cash outflow for long-term debt outstanding as at September 30, 2016 would be \$41.7 million in 2017-2018 and \$Nil thereafter.

## RELATED PARTY TRANSACTIONS

The Company entered into the following transactions with related parties:

\$ thousands	For the three months ended September 30,		For the nine months ended September 30,	
	2016	2015	2016	2015
Equipment and product support sales	40	446	192	1,315
Expenditures				
Rental payments on Company facilities	1,463	1,442	4,358	4,192
Equipment purchases	146	93	195	662
Flight costs	30	16	46	72
Contributions <sup>(1)</sup>	107	-	107	-
Other expenses	-	-	33	92

(1) – Contributions include payments to Ag for Life and Alberta Prosperity Fund.

All related parties are either directly or indirectly owned by a member of senior management or director of the Company and/or a close family member thereof. These transactions were made on terms equivalent to those that prevail in arm's length transactions and are made only if such terms can be substantiated.

Amounts due from (to) related parties are included in the consolidated balance sheet under trade receivables and other (trade payables, accruals and other) and are as follows:

\$ thousands	September 30, 2016	December 31, 2015
Due from related parties	33	111
Due to related parties	(988)	(13)

The amounts due from related parties are not secured and are to be settled in cash. As at September 30, 2016 and December 31, 2015, the amounts due from related parties are considered collectible and therefore have not been provided for in the allowance for doubtful accounts. During the respective three and nine month periods ended September 30, 2016, \$Nil and \$Nil has been recognized in bad debt expenses with respect to related party transactions (2015 – \$Nil and \$Nil).

The amount due to related parties reflects the estimated net costs associated with vacating one of the industrial facilities which is currently leased from a related party. While the Company continues to negotiate this lease termination with the landlord, challenging market conditions have caused the Company to reassess its original accrual recognized during the second quarter of 2016 of \$0.5 million (approximately 50% of the remaining contractual obligation). During the third quarter of 2016, we recognized the remaining \$0.5 million contractual obligation.





The Company has contractual obligations to related parties in the form of facility leases. As at September 30, 2016, these contractual obligations and due dates, inclusive of the aforementioned vacated facility which is presented at its gross amount, are as follows:

\$ thousands	Total	2016	2017-2018	2019-2020	Thereafter
Operating lease obligations	28,158	1,473	9,927	7,533	9,225

## OFF-BALANCE SHEET ARRANGEMENTS

We use off-balance sheet financing in connection with numerous operating leases. These leases relate to the Company's buildings and certain vehicles with lease terms of between one and eleven years. Most building leases contain renewal options for periods of three to five years. We have paid monthly amounts under these operating leases of up to \$64.2 thousand. In some instances, the counterparty to the Company's operating lease obligations is a related party. Refer to the "Related Party Transactions" section of this MD&A for a discussion of the terms and amounts of such arrangements. The range of expiry dates on the current operating leases extend until August 2026.

## CRITICAL ACCOUNTING ESTIMATES

The preparation of the consolidated financial statements requires that certain estimates and judgments be made with respect to the reported amounts of sales and expenses and the carrying amounts of assets and liabilities. These estimates are based on historical experience and management's judgment. Anticipating future events involves uncertainty and consequently, the estimates used by management in the preparation of the consolidated financial statements may change as future events unfold, additional information is acquired or the Company's operating environment changes. Management considers the following to be the most significant of these estimates.

### Allowance for Doubtful Accounts

The allowance for doubtful accounts is reviewed by management on a monthly basis. Accounts receivable are considered for impairment on a case-by-case basis when they are past due or when objective evidence is received that a customer will default. The Company takes into consideration the customer's payment history, their creditworthiness and the current economic environment in which the customer operates to assess impairment. The Company's historical bad debt expenses have not been significant and are usually limited to specific customer circumstances.

### Net Realizable Value of Inventory

Equipment is valued at the lower of cost and net realizable value, with cost being determined on a specific item, actual cost basis, and net realizable value being determined by the recent sales of the same or similar equipment inventory or market values as established by industry publications, less the costs to sell. Parts inventory is recorded at the lower of cost and net realizable value, with cost being determined on an average cost basis and net realizable value being determined by recent sales of the same or similar parts inventory, less the costs to sell. Work-in-progress is valued on a specific item, actual cost basis.

### Manufacturer Incentives

Certain manufacturers offer annual performance incentives which are linked to the Company's market share achievement and annual sales and settlement volumes. The Company uses estimated annual market share statistics derived from historical results which have been adjusted for any anticipated changes in the current year, as well as eligible sales and settlement volumes to date to accrue the proportion of these annual manufacturer incentives earned during the period.

### Derivative Financial Instruments

The Company utilizes floating-to-fixed interest rate swaps to manage its interest rate exposure. These derivatives are initially recognized on the date the contract is entered into and are subsequently re-measured at their fair values. The fair values of the interest rate swaps are calculated as the net present value of the estimated future cash flows expected to arise on the variable and fixed legs, determined using applicable yield curves at each measurement date. Swap curves, which incorporate credit spreads applicable to large commercial banks, are typically used to calculate expected future cash flows and the present values thereof. Adjustments are also made to reflect the Company's own credit risk and the credit risk of the counterparty, if different from the spread implicit in the swap curve.

The Company also has several total return swap arrangements to hedge the exposure associated with increases in its share price on its outstanding DSUs and SARs. These derivatives accrue to the Company, any gains (losses) associated with changes in the value of its common shares as well as dividends paid on its hedged position, net of interest costs charged by



the bank to build and hold their positions. These derivatives are initially recognized on the date the contract is entered into and are subsequently re-measured at their fair values. The fair values are calculated as the net present value of estimated future cash flows.

### **Business Combinations**

Assets acquired and liabilities assumed pursuant to business combinations are measured at their acquisition date fair values. Where appropriate, management bases its fair value estimates on observable third party data as reported by sources deemed both reputable and qualified. In the case of inventory acquired, management estimates the value in the manner discussed within the "Net Realizable Value of Inventory" section above.

Goodwill is measured as the excess of the fair value of consideration transferred over the acquisition-date fair value of the net identifiable assets acquired.

The purchase price allocation is subject to change throughout the duration of the measurement period. The measurement period is the period from the date of acquisition, to the date the Company obtains complete information about facts and circumstances that existed as of the acquisition date and is subject to a maximum of one year.

### **RISKS AND UNCERTAINTIES**

Risk factors faced by Rocky are listed in the Company's AIF, which can be found on SEDAR. These risk factors include industry risks associated with agriculture and industrial equipment dealerships and others, including but not limited to: economic conditions; weather and climate conditions; commodity prices; inventory risk; industry oversupply; the seasonality and cyclicity of the industries we service; foreign exchange exposure; our reliance on key manufacturers; our continued ability to pay our dividend; the nature of our dealership agreements; interest rate changes; changes in the value of our common shares; government regulations in the areas we operate; competition within our industry; credit facilities; consolidation within the equipment manufacturing industry; the non-exclusive nature of key geographic markets; customer credit risks; our information systems; the availability of floor plan financing and other forms of credit to the Company; unfavorable conditions (economic, weather or otherwise) in key geographic markets; import restrictions and foreign trade risks; insurance matters; branch leases; the retention of key personnel; labour relations; labour costs and shortages; freight costs; future warranty claims; product liability risks; restrictions and impediments on acquisitions; aviation risks; growth risks; and our ability to successfully integrate our acquisitions.

Our success largely depends on the abilities and experience of our senior management team and other key personnel. These employees carry a significant amount of the management responsibility of our business and are important for setting strategic direction and dealing with certain significant customers.

Our future performance will also depend on our ability to attract, develop, and retain highly qualified employees in all areas of our business. We face significant competition for individuals with the skills required to develop, market and support our products and services. If we fail to recruit and retain sufficient numbers of these highly skilled employees, we may not be able to achieve our growth objectives and our business may be adversely affected.

### **RISKS RELATED TO FINANCIAL INSTRUMENTS**

Through its financial instruments, the Company has exposure to the following risks: credit risk, market risk (consisting of foreign currency exchange risk, interest rate risk and equity price risk), and liquidity risk.

#### **Credit Risk**

Credit risk refers to the risk that a counterparty will default on its contractual obligations resulting in a financial loss to the Company. The Company has a policy of only dealing with creditworthy counterparties and obtaining sufficient collateral, where appropriate, as a means of mitigating the risk of financial loss from defaults. The creditworthiness of counterparties is determined using information supplied by independent rating agencies where available and, if not available, the Company uses other publicly available financial information and its own trading records to rate its major customers. The Company's exposure and the credit ratings of its counterparties are continuously monitored and the aggregate value of transactions concluded is spread amongst approved counterparties. Credit exposure is controlled by counterparty limits that are reviewed regularly.

The Company's exposure to credit risk on its cash balance is mitigated as these financial assets are held with major financial institutions with strong credit ratings.

For the respective three and nine month periods ended September 30, 2016, the Company recognized recoveries of \$0.1 million and \$0.3 million associated with bad debts (2015 – expenses of \$0.1 million and \$0.3 million). Bad debt expense (recovery) is recognized in SG&A expenses.



## Market Risk

Market risk is the risk from changes in market prices, such as changes in foreign currency exchange rates, interest rates and the market price of the Company's common shares, which will affect the Company's earnings or the value of the financial instruments held.

### Foreign Currency Exchange Risk

The OEMs we do business with are geographically diversified, requiring us to conduct business in two currencies: U.S. dollars and Canadian dollars. As a result, we have foreign currency exposure with respect to purchases of U.S. dollar denominated products (inventory) and we experience foreign currency gains and losses thereon. The nature of exposure to foreign exchange fluctuations differs between equipment manufacturers and the various dealer agreements with them.

A weakening of the U.S. dollar in comparison to the Canadian dollar will generally have a positive effect on our performance by lowering our cost of goods sold. However, as the markets in which we operate are highly competitive, a declining U.S. dollar also has the effect of reducing sales prices in Canadian dollars and, as a consequence, we cannot capture the entire potential benefit of a declining U.S. dollar environment. By contrast, a strengthening U.S. dollar will increase the cost of equipment purchases. If we are unable to fully offset the increase in cost of goods through price increases, our financial results will be negatively affected. We mitigate some of this risk by occasionally purchasing forward contracts for U.S. dollars on large transactions to cover the period from the time the equipment is ordered from the manufacturer to the payment date.

For the respective three and nine month periods ended September 30, 2016, the Company recognized a foreign exchange loss of \$0.1 million and a foreign exchange gain of \$0.6 million (2015 – losses of \$0.6 million and \$0.6 million). These gains (losses) are included in selling, general and administrative expenses.

### Interest Rate Risk

We also finance our equipment inventory, certain capital expenditures, business acquisitions and occasionally, our other general working capital requirements, by way of various financing facilities under which we are charged interest at floating rates. As a result, rising interest rates have the effect of increasing our overall costs. To the extent that we cannot pass on such increased costs to our customers, our net earnings or cash flow may decrease. In addition, some of our customers finance the equipment they purchase from us. A customer's decision to purchase may be affected by interest rates available to finance the purchase.

The Company manages its interest rate risk by using floating-to-fixed interest rate swaps when appropriate. Generally, the Company will obtain floor plan financing and long-term debt at floating rates. When the Company enters into a floating-to-fixed interest rate swap, it agrees with a third party to exchange the difference between the fixed and floating contract rates based on agreed notional amounts.

Refer to the "Derivative Financial Instruments" section of this MD&A for additional information and gains (losses) on derivative financial instruments.

### Equity Price Risk

As part of its overall compensation of directors, officers and employees, the Company has issued cash-settled share-based payments in the form of DSUs and SARs. The DSUs are valued on a per DSU basis at an amount equal to the volume weighted average trading price of the Company's common shares over the immediately preceding 20 day trading period. The SARs are revalued at each reporting date using the Black-Scholes option pricing model. Increases in the Company's share value result in additional compensation expense to the Company related to these two programs. As cash-settled share-based payments, the DSUs and SARs are not accounted for as financial instruments.

The Company has entered into several total return swaps to hedge the exposure associated with increases in its share value on its outstanding DSUs and SARs. The total return swaps are classified as derivative financial instruments. The intent of these derivatives is to offset the incremental cost to the Company associated with increases in its common share price on its cash-settled share-based payments.

Refer to the "Derivative Financial Instruments" section of this MD&A for additional information and gains (losses) on derivative financial instruments.



## Liquidity Risk

The Company's objective is to have sufficient liquidity to meet its liabilities when due. The Company monitors its cash balance and cash flows generated from operations as well as available credit facilities to meet its requirements.

Refer to the "Adequacy of Capital Resources" section of this MD&A for a discussion of the liquidity risks faced by the Company as well as the Company's various credit facilities.

## NON-IFRS MEASURES

Throughout this MD&A, we use terms which do not have standardized meanings under IFRS. As these non-IFRS financial measures do not have standardized meanings prescribed by IFRS, they are unlikely to be comparable to similar measures presented by other issuers. Our definition for each term is as follows:

- **"Adjusted Diluted Earnings per Share"** is calculated by eliminating from net earnings, the after-tax impact of the losses (gains) arising from the Company's derivative financial instruments and DSUs, as well as the expense (recovery) associated with its SARs. These items arise from changes in the Company's share price as well as fluctuations in interest rates and are not reflective of the Company's core operations.

The Company also adjusts for any non-recurring charges (recoveries) recognized in net earnings. Management deems non-recurring charges (recoveries) to be unusual or infrequent items that the Company incurs outside of its common day-to-day operations. Adjusting for these items allows management to isolate and analyze diluted earnings per share from core business operations. For the periods presented, costs associated with amalgamating the industrial operations and impairment losses recognized on redundant land classified held for sale have been classified as non-recurring charges. The impairment losses are not expected to give rise to a reduction in our tax provision.

- **"EBITDA"** is a commonly used metric in the dealership industry. EBITDA is calculated by adding interest on long-term debt, income taxes and depreciation and amortization to net earnings. Adding back non-operating expenses allows management to consistently compare periods by removing changes in tax rates, long-term assets and financing costs related to the Company's capital structure.
- **"Adjusted EBITDA"** is calculated by eliminating from EBITDA, the impact of the losses (gains) arising from the Company's derivative financial instruments and DSUs, as well as the expense (recovery) associated with its SARs. These items arise from changes in the Company's share price as well as fluctuations in interest rates and are not reflective of the Company's core operations.

The Company also adjusts for any non-recurring charges (recoveries) recognized in EBITDA. Management deems non-recurring charges (recoveries) to be unusual or infrequent items that the Company incurs outside of its common day-to-day operations. Adjusting for these items allows management to isolate and analyze EBITDA from core business operations. For the periods presented, costs associated with amalgamating the industrial operations and impairment losses recognized on redundant land classified held for sale have been classified as non-recurring charges.

- **"Operating SG&A"** is calculated by eliminating from SG&A, the impact of the losses (gains) arising from the Company's derivative financial instruments and DSUs, as well as the expense (recovery) associated with its SARs. These items arise from changes in the Company's share price as well as fluctuations in interest rates and are not reflective of the Company's core operations.

The Company also adjusts for depreciation and amortization as well as any non-recurring charges (recoveries) recognized in SG&A. Management deems non-recurring charges (recoveries) to be unusual or infrequent items that the Company incurs outside of its common day-to-day operations. Adjusting for these items allows management to assess discretionary expenses from ongoing operations. For the periods presented, costs associated with amalgamating the industrial operations and impairment losses recognized on redundant land classified held for sale have been classified as non-recurring charges. We target a sub-10% Operating SG&A as a percentage of total sales on an annual basis.

- **"Floor Plan Neutral Operating Cash Flow"** is calculated by eliminating the impact of the change in floor plan payable (excluding floor plan assumed pursuant to business combinations) from cash flows from operating activities. Adjusting cash flows from operating activities for changes in the balance of floor plan payable allows management to isolate and analyze operating cash flows during a period, prior to any sources or uses of cash associated with equipment financing decisions.



## RECONCILIATION OF NON-IFRS MEASURES TO IFRS

### Adjusted Diluted Earnings per Share

\$ thousands

	For the three months ended September 30,		For the nine months ended September 30,	
	2016	2015	2016	2015
Earnings used in the calculation of diluted earnings per share	6,632	4,352	10,262	6,713
(Gain) loss on derivative financial instruments	(2,929)	3,438	(4,146)	3,274
Loss (gain) on DSUs	134	(155)	204	(158)
SAR expense (recovery)	443	(92)	527	18
Non-recurring industrial amalgamation charges	1,333	-	3,564	-
Impairment loss on redundant land – not tax deductible	1,360	-	1,360	-
Tax effect of adjustments (27%)	275	(862)	(40)	(846)
Earnings used in the calculation of Adjusted Diluted Earnings per Share	7,248	6,681	11,731	9,001
Weighted average diluted shares used in the calculation of diluted earnings per share (in thousands)	19,384	19,299	19,384	19,334
Adjusted Diluted Earnings per Share	0.37	0.35	0.61	0.47

### EBITDA and Adjusted EBITDA

\$ thousands

	For the three months ended September 30,		For the nine months ended September 30,	
	2016	2015	2016	2015
Net earnings	6,632	4,352	10,262	6,713
Interest on long-term debt	438	519	1,345	1,559
Depreciation and amortization expense	1,887	2,084	5,840	5,841
Income taxes	2,910	1,561	4,489	2,409
EBITDA	11,867	8,516	21,936	16,522
(Gain) loss on derivative financial instruments	(2,929)	3,438	(4,146)	3,274
Loss (gain) on DSUs	134	(155)	204	(158)
SAR expense (recovery)	443	(92)	527	18
Non-recurring industrial amalgamation charges	1,333	-	3,564	-
Impairment loss on redundant land	1,360	-	1,360	-
Adjusted EBITDA	12,208	11,707	23,445	19,656

### Operating SG&A

\$ thousands

	For the three months ended September 30,		For the nine months ended September 30,	
	2016	2015	2016	2015
SG&A	23,619	30,334	73,543	84,327
Depreciation and amortization expense	(1,887)	(2,084)	(5,840)	(5,841)
Gain (loss) on derivative financial instruments	2,929	(3,438)	4,146	(3,274)
(Loss) gain on DSUs	(134)	155	(204)	158
SAR (expense) recovery	(443)	92	(527)	(18)
Non-recurring industrial amalgamation charges	(1,333)	-	(3,564)	-
Impairment loss on redundant land	(1,360)	-	(1,360)	-
Operating SG&A	21,391	25,059	66,194	75,352
Operating SG&A as a % of revenue	9.6%	9.8%	10.3%	10.9%





## Floor Plan Neutral Operating Cash Flow

\$ thousands

	For the three months ended September 30,		For the nine months ended September 30,	
	2016	2015	2016	2015
Cash flow from operating activities	20,590	21,367	14,246	22,621
Net decrease in floor plan payable	41,694	27,167	57,276	29,946
Floor plan assumed pursuant to business combinations	-	-	-	32,782
Floor Plan Neutral Operating Cash Flow	62,284	48,534	71,522	85,349

## INTERNAL CONTROLS OVER FINANCIAL REPORTING AND DISCLOSURE CONTROLS AND PROCEDURES

The Chief Executive Officer (“CEO”) and the Chief Financial Officer (“CFO”) are responsible for establishing and maintaining the Company’s disclosure controls and procedures, (“DC&P”), to provide reasonable assurance that material information related to the Company is made known. In addition, internal controls over financial reporting (“ICFR”) have been designed by or have been caused to be designed under the supervision of the CEO and CFO to provide reasonable assurance regarding the reliability of financial reporting and preparation of financial statements for external purposes in accordance with IFRS.

The CEO and CFO have evaluated the effectiveness of our DC&P and assessed the design of our ICFR, as of September 30, 2016, pursuant to the requirements of National Instrument 52-109, and have concluded that:

- (i) The DC&P are effective to provide reasonable assurance that all material or potentially material information about activities of the Company are made known to them; and
- (ii) Information required to be disclosed by the Company in its annual filings, interim filings or other reports filed or submitted by it under securities legislation is recorded, processed, summarized and reported within the time periods specified in securities legislation.

Management has concluded that, as of September 30, 2016, the Company has sufficiently documented and tested the effectiveness of the ICFR for the Company and can conclude that these controls are working effectively. It should be noted that while the Company’s management believes that the Company’s ICFR and DC&P provide a reasonable level of assurance that they are effective, they do not expect these controls will prevent all errors or fraud. A control system, no matter how well conceived or operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met.

## CAUTION REGARDING FORWARD-LOOKING INFORMATION AND STATEMENTS

This MD&A contains FLS within the meaning of applicable securities legislation which involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of Rocky or industry results, to be materially different from any future results, events, expectations, performance or achievements expressed or implied by such FLS. FLS typically contain words or phrases such as “may”, “outlook”, “objective”, “intend”, “estimate”, “anticipate”, “should”, “could”, “would”, “will”, “expect”, “believe”, “plan”, “predict” and other similar terminology suggesting future outcomes or events. FLS involve numerous assumptions and should not be read as guarantees of future performance or results. Such statements will not necessarily be accurate indications of whether or not such future performance or results will be achieved. Readers of this MD&A should not unduly rely on FLS as a number of factors, many of which are beyond the control of Rocky, could cause actual performance or results to differ materially from the performance or results discussed in the FLS.

In particular, FLS in this MD&A include, but are not limited to, the following: (i) disclosure under the heading “Market Fundamentals and Outlook”; (ii) continuing demand for Rocky’s products and services, and the cyclical nature of agriculture equipment demand and any revenue or inventory statements or forecasts attributed thereto; (iii) statements pertaining to the growth of Rocky’s business and operations, including through acquisitions; (iv) statements pertaining to arid weather conditions and the anticipated effect of such conditions on crop quality and yield; (v) statements that the decline in investment in Alberta’s infrastructure and residential housing markets will likely negatively impact the Company’s industrial sales or results; (vi) statements that the disparity between the Canadian and U.S. dollars are expected to support agriculture commodity prices, while sustained cost reductions in fuel and fertilizer prices provide input cost relief to farmers; (vii) any discussion of the anticipated mix of new and used equipment sales for the remainder of 2016; (viii) discussion on the fundamentals of Rocky’s business, including discussion regarding growth in GDP, farmers’ crop receipts, and the future demand for agriculture equipment and commodities; (ix) statements regarding customer buying patterns, including the extent to which we are able to convert new equipment customers to used equipment customers and attract U.S. customers looking to capitalize on favorable U.S.-Canadian foreign exchange rates; (x) statements pertaining to Rocky’s ability to negotiate early termination or to sublet its redundant facilities and to realize the cost savings associated with the 20



restructuring of its industrial segment; (xi) any statements or discussions regarding Rocky's inventory management and any expected increases or decreases in Rocky's inventory levels, and the timing thereof; (xii) discussions that the impact of previously acquired dealerships and trade areas, coupled with our OEM relationships, make us well-positioned to pursue our longer-term revenue and earnings growth initiatives; (xiii) statements that we believe cash flow from operations, along with existing credit facilities, will provide for our capital needs; (xiv) discussion around SG&A expenses including the seasonal variances and expectations in operating SG&A; (xv) discussion that our first quarter is generally the weakest financial quarter due to lack of agricultural activity and winter shutdowns, that the fourth quarter is generally our strongest quarter financially, and discussion that we expect our second and third quarter sales activity to increase as our installed equipment- and customer-base increases; (xvi) statements that as acquisitions are integrated into the business, the associated SG&A costs for Rocky will generally decrease; (xvii) statements related to our per-location revenue expectations and any assessment of the economies of scale associated with any facility; (xviii) statements that our installed base and customer relationships create an annuity of equipment sales and product support revenue, which help drive dependable earnings and cash flow; (xix) statements that weather conditions may impact sales activity for any given period; (xx) statements concerning the Company's ongoing compliance with, or potential breaches of, its covenants under its credit facilities, including the Syndicated Facility; (xxi) statements concerning the Company's expected undiscounted cash flows as at September 30, 2016; and, (xxii) statements regarding the ongoing quantitative significance of our industrial segment.

With respect to the FLS listed above and contained in this MD&A, Rocky has made assumptions regarding, among other things: (i) expectations that commodity prices will continue to remain above historical levels; (ii) increasing food demand, as well as increasing crop land dedicated to bio-fuel production, will cause producers to improve their productivity, and as a result invest in new equipment, (iii) expectations that increases in farmer liquidity would generally correlate to farmers making capital re-investments in their business, so as to increase their productivity and lower their input costs, which investments may include Rocky's products and services, (iv) inventory levels will fluctuate during a year, both positively and negatively, based on timing of equipment deliveries, and volume of whole-good sales involving a unit taken in on trade, (v) the general GDP growth and/or relative economic stability in the markets we operate in, (vi) the trend towards larger farms in the agriculture sector will continue to benefit further farm equipment sales as larger farm operations tend to replace their equipment more frequently, (vii) the Company's cash flow will remain sufficient to, in connection with its credit facilities, adequately finance its capital needs, (viii) as stores are consolidated, certain functions can be centralized thereby reducing SG&A costs as a result, (ix) the anticipated improvement in ongoing revenue and cash-flow, including parts and service revenue, as our installed base increases, (x) expectations that no material change will happen to our OEM relationships; (xi) expectations that customers who purchase their equipment from the Company will, generally, return to the Company for their product support needs; and, (xii) the renewal of its Syndicated Facility prior to maturity on September 24, 2018.

Rocky's actual results could differ materially from those anticipated in the FLS in this MD&A as a result of the risk factors set forth herein under the heading "Risks and Uncertainties" and the risk factors set forth in Rocky's AIF. Although the FLS contained in this MD&A are based upon what management of Rocky believes are reasonable assumptions, Rocky cannot assure investors that actual performance or results will be consistent with these FLS. These statements reflect current expectations regarding future events and operating performance and are based on information currently available to Rocky's management. There can be no assurance that the plans, intentions or expectations upon which these FLS are based will occur. All FLS in this MD&A are qualified in their entirety by the cautionary statements herein and those set forth in Rocky's AIF available on SEDAR at [www.sedar.com](http://www.sedar.com). These FLS and outlook are made as of the date of this document and, except as required by applicable law, Rocky assumes no obligation to update or revise them to reflect new events or circumstances.