RUSSELL BREWERIES INC.
Management Discussion and Analysis
For the six months ended December 31, 2012

This Management's Discussion and Analysis ("MD&A") of Russell Breweries Inc. dated February 28, 2013 provides an analysis of Russell's results of operation and financial condition for the six months ended December 31, 2012. This MD&A should be read in conjunction with the unaudited condensed consolidated interim financial statements, and accompanying notes for the six months ended December 31, 2012 and with the audited consolidated financial statements and accompanying notes for the years ended June 30, 2012 and 2011. Additional information related to Russell Breweries Inc. is available on SEDAR at www.sedar.com and on the Company's website at www.russellbeer.com.

The unaudited condensed consolidated interim financial statements and related notes of the Company have been prepared in accordance with International Accounting Standards ("IAS") 34 *Interim Financial Reporting*. All financial amounts in this MD&A are in Canadian dollars, except as otherwise indicated.

This MD&A was approved and authorized for issuance by the Board of Directors on February 28, 2013.

FORWARD LOOKING STATEMENTS

This report contains forward-looking information that is based on the Company's plans, intentions and expectations. By definition, forward-looking information involves risks, uncertainties and assumptions and is not a guarantee of future performance. Actual results could differ significantly from those anticipated, and hence investors should use caution when considering this information and not to put undue reliance on forward-looking statements.

OVERVIEW

Through its wholly-owned subsidiaries, Russell Brewing Company Ltd. located in Surrey, BC, and Fort Garry Brewing Company Ltd. located in Winnipeg, Manitoba, Russell Breweries Inc. ("the Company") operates two craft breweries producing premium quality beers for pubs, restaurants and liquor stores. The Company acquired Fort Garry Brewing Company Ltd. ("Fort Garry") on October 22, 2007. Fort Garry is Manitoba's oldest and largest brewer and distributor of premium quality beers. The Company's operations include production facilities in Surrey, BC and Winnipeg, Manitoba, corporate offices in Surrey, BC, storage facilities, brewing equipment, and delivery and sales vehicles. Both breweries produce a variety of limited and seasonal products in addition to their main product lines including: Russell Cream Ale, Russell Pale Ale, Russell Honey Blonde Ale, Russell Extra Special Lager, Russell IP'eh! India Pale Ale, A Wee Angry Scotch Ale, Blood Alley Bitter, Russell Lemon Ale, , Rocky Mountain Pilsner, Fort Garry Dark Ale, Fort Garry Pale Ale, Fort Garry Premium Light, Fort Garry Red and Stone Cold Lager.

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BUSINESS DEVELOPMENTS AND SIGNIFICANT EVENTS

On November 4, 2011, the Company's wholly owned subsidiary Russell Brewing Company Ltd. was recognized with a 'Best Business Award' at the Surrey Board of Trade 13th Annual Surrey Business Excellence Awards.

On November 22, 2011, the Company announced financings of $500,000 in the form of equity units consisting of common shares and warrants to purchase common shares of the Company. On January 20, 2012, the Company completed the financing with gross proceeds totaling $765,000 – see Liquidity and Capital Resources: Financing.

On December 5, 2011, the Company and Storm Brewing, two of British Columbia's independent Craft Brewers, join together to release a new collaborative beer called The Big Smoke. This strong, smoky ale was jointly brewed by Storm Brewing and Russell Brewing using 10% Peat Smoked Malt and Bravo and Willamette Hops. This is a malt-forward beer with a big smoke aroma and a well-balanced hop finish. Limited edition, single-batch brew available in 650ml bottles through private liquor stores in BC. This beer is part of the new Collaboration Series which is a succession of small-batch brews created by independent brewers working together to create new beers that push the boundaries of taste.

On March 2, 2012, the Company released its new super-premium, single-batch beer - Nectar of the Gods Wheat Wine Ale. The entire batch was pre-sold and is currently available in select private retailers in Metro Vancouver. Nectar of the Gods Wheat Wine Ale is the first barrel-aged beer from the Company. The beer was carefully aged in Tennessee Whiskey barrels for over four months. The aging process provided the beer with layers of flavour complexity including a fruity-ester character and vanilla-like flavours and tannins.

On March 9, 2012, the Company granted incentive stock options to its employees, consultants, directors and officers on 3,000,000 common shares in its capital, exercisable for up to five years at a price of $0.10 per share. The options shall vest in accordance with the Company's stock option plan. The Company did not proceed with the 2,500,000 stock options announced on March 21, 2010.

On March 12, 2012, the Company launched 'Fort Garry – Kona Imperial Stout' limited relase as part of the new Fort Garry Brewmaster Series. Brewed with two ten different malts, two types of hops and over 50 pounds of rich roasted coffee beans harvested from sunny shores of Kona, Hawaii.

On March 29, 2012**,** the Company host the production of the 2012 Vancouver Craft Beer Week (VCBW) Collaboration Ale at its facility in Surrey, BC. In celebration of BC's largest craft beer festival, thirty of BC's finest breweries banded together to create a unique Cascadian Brown Ale.

On April 2, 2012, the Company issued 125,000 common shares in its capital as bonus shares to each of its two directors who provided personal guaranties for a $100,000 working capital loan from the Business Development Bank of Canada.

On April 4, 2012, Fort Garry Brewing Company Ltd., a wholly owned subsidiary of the Company, introduced a new specialty beer to the Manitoba market called Fort Garry Kona Imperial Stout. This is the newest beer from the super-premium Fort Garry Brewmaster Series which is a group of small-batch, limited-edition beers brewed for craft beer enthusiasts. Fort Garry - Kona Imperial Stout is now available in limited supply in single-serve 650ml bottles at the stores of Manitoba Liquor Control Commission (MLCC).

On May 8, 2012, the Company won a silver medal at the prestigious World Beer Cup 2012 for its Russell IP'eh! India Pale Ale. This is the second time this beer has been honoured with a medal at the World Beer Cup – in 2010 it won bronze.

On May 24, 2012, the Company released the Rick August Russian Imperial Stout, Grand Prize Winner of the 2011 Golden Stag Home Brewing Contest.

On June 12, 2012, the Company was awarded a Silver Medal at the Canadian Brewing Awards for the 'Fort Garry – Kona Imperial Stout'.

BUSINESS DEVELOPMENTS AND SIGNIFICANT EVENTS (continued)

On June 13, 2012, the Company won a silver medal for Nectar of the Gods Wheat Wine Ale at the Canadian Brewing Awards in Montreal on Saturday June, 2012 in the Wood and Barrel Aged Strong Beer category. Nectar of the Gods Wheat Wine Ale is the Company's first barrel-aged beer. Fort Garry Brewing Company, a wholly owned subsidiary of the Company, was also awarded a silver medal at the Canadian Brewing Awards for their Kona Imperial Stout as part of their new Brewmaster Series.

On July 10, 2012, the Company celebrates its 17th Anniversary with a limited edition barrel aged Scotch Ale. This strong, dark ale was brewed with Scottish specialty peated malts for a slightly smoky character then skillfully aged in Bourbon barrels. A special Anniversary Ale crafted by our team of brewers to thank everyone for enjoying our unique beers throughout the years.

On July 13, 2012, the Company announced that it agreed to terms under a letter of intent for the initial non-exclusive rights to import, produce, package, use, market, sell and distribute Russell brands and branded merchandise with FVI Capital Inc. ("FVI") in China. The letter specifies the principal terms of a technology and trade mark license agreement ("Agreement") which includes an initial up-front licensing fee, to be paid by a new Company ("Licensee") being established by FVI to hold the license and ongoing royalties based on volume of beer produced up to 50,000 hectolitres . The Company will take an initial 20% equity position in Licensee. As part of the agreement, the new Company has a 48 month first matching option to acquire an exclusive license for the entire Chinese market for an additional license fee payment and ongoing per hectoliter royalty payments and the Company has an option to increase its stake in the Licensee to 25% at Fair Market Value within the same 48 month term.

On July 26, 2012, the Company released its Blood Alley Bitter in 6 pack 341ml bottles.

On July 27, 2012, the Company announced that it agreed to a one year extension (the "Extension") and amendment to a loan agreement (the "Loan Agreement") dated December 31, 2007, pursuant to which the lender ("Lender"), a shareholder of Russell, had provided to the Company a loan (the "Loan") valued at maturity in the amount of $1,239,000. (see LIQUIDITY AND CAPITAL RESOURCES)

On September 21, 2012, the Company released 'Russell Marzen', a seasonal limited release as part of the Russell Brewmaster Series.

On October 9, 2012, the Company completed a non-exclusive technology and trade mark license agreement ("Agreement") with Russell Breweries (China) Inc. to import, produce, package, use, market, sell and distribute Russell brands in China, including Hong Kong and Taiwan. The principal terms of the Agreement includes use of name for the new company, an initial up-front licensing fee and ongoing royalties based on volume of beer produced and sold. In addition, the Company will subscribe for a 20% equity position in Licensee with an option to increase its position to 25%.

On October 10, 2012, the Company released the next batch of the super-premium, single-batch beer - Nectar of the Gods Wheat Wine Ale. The entire batch was pre-sold to select private liquor stores in Metro Vancouver.

On November 15, 2012, the Company released 'Happy Jack Pumpkin Ale', a limited-edition seasonal beer as part of the Fort Garry Brewmaster Series.

On November 22, 2012, Mr. Paul Robertson has resigned as a Director of the Company. On November 26, 2012, Mr. Perpinder Singh Patrola has been appointed to the Board of Directors and Mr. Robert Murray and Mr. Richard Shier have resigned as Directors.

On November 23, 2012, the Company released 'Russell IP'eh! India Pale Ale' in 6 pack 341ml bottles.

On November 24, 2012, the Company released 'Hop Therapy Double IPA', a new single-batch brew as part of the Russell Brewmaster Series.

BUSINESS DEVELOPMENTS AND SIGNIFICANT EVENTS (continued)

On November 26th, 2012, the Company released 'Naughty & Spiced Porter', a limited-edition seasonal beer as part of the Russell Brewmaster Series. The Company also released 'St Nick's Porter', a limited-edition seasonal beer as part of the Fort Garry Brewmaster Series.

During the period ended December 31, 2012, the Company redeemed its convertible debentures maturing on November 4, 2012, December 3, 2012 and December 24, 2012. The aggregate principal amount of the convertible debentures outstanding was $740,750. On the redemption dates, the Company redeemed the whole of the principal amount of the convertible debentures by issuing a total of 4,938,333 fully paid and non-assessable common shares in the capital of the Company, at a price equal to $0.15 per common share. (see LIQUIDITY AND CAPITAL RESOURCES).

Currently, the Company's products are segmented into the following categories:

Categories	Brands
Super Premium	Russell Nectar of the Gods Wheat Wine Ale, Fort Garry Kona Imperial Stout, Russell Hop Therapy Double IPA,
Premium:	Russell IP'EH!, Black Death Porter, Russell Marzen, A Wee Angry Scotch Ale, Blood Alley Bitter, Fort Garry Munich Eisbock
Session:	Russell Cream Ale, Russell Pale Ale, Russell Honey Blonde Ale, Russell Extra Special Lager, Fort Garry Dark, Fort Garry Pale, Fort Garry Rouge, Fort Garry Light, Citrus Twist, Craft Collection
Value:	Rocky Mountain Pilsner, Stone Cold Lager, Two Rivers
Seasonal:	Russell Lemon Ale, Russell Lime Lager, Russell Naughty & Spiced Porter , Russell Rick August Russian Imperial Stout
Partnership:	Chambar Ale, Main Street Pilsner, GUUU Ale, Bayside Shark Lager, Cactus Double Down Draught, The Big Smoke

SELECTED INFORMATION

The following table summarizes certain financial information of the Company for the periods indicated below:

Selected Information	Six Months Ended December 31, 2012	Six Months Ended December 31, 2011	Six Months Ended December 31, 2010
	$	$	$
Statement of Comprehensive Loss Data			
Gross Revenue	4,309,628	4,116,726	3,894,407
Net Sales (after excise tax and provincial mark-up)	3,317,319	3,130,659	3,008,929
Earnings (loss) before interest and other income, taxes, depreciation and amortization	230,131	28,725	(211,199)
Total income (loss) from continuing operations	(151,101)	(369,321)	(600,578)
Operating income (loss) per share	(0.00)	(0.00)	(0.00)
Net income (loss) and comprehensive income (loss)	(151,101)	(369,321)	(600,578)
Basic and diluted earnings (loss) per share	(0.00)	(0.00)	(0.00)
Statement of Financial Position Data			
Total assets	6,928,056	7,257,802	8,730,830
Total long term financial liabilities	248,998	323,190	1,577,658
Cash dividends declared per share	Nil	Nil	Nil

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PERFORMANCE AND RESULTS OF OPERATIONS

Three Months Ended December 31, 2012 (“Q2 2013F”)

The Company had a net loss of $87,693 for Q2 2013F compared to the net loss of $286,193 for the period ended December 31, 2011 (“Q2 2012F”). The decrease in net loss is primarily a result of $196,951 increase in gross margin, and $19,354 decrease in other expenses, which is offset by $13,428 increase in selling, general and administrative expenses.

Gross sales for Q2 2013F were $1,984,546 up $64,404 or 3% compared to $1,920,142 for Q2 2012F. Net Sales for Q2 2013F were $1,510,530 up $36,106 or 2% compared to $1,474,424 for Q2 2012F. The increase in the sales volumes of the Company’s premium and super premium brands were key drivers for the increase in gross and net revenue, which reflects the Company’s recent marketing strategy with a focus on premium brands.

The gross margin for Q2 2013F increased $196,951 or 27% to $924,507 compared to $727,556 for Q2 2012F. The gross margin percentage of Q2 2013F was up 11% to 61% compared to 50% for Q2 2012F. The increase in gross margin is primarily a result of the continued sales growth in higher margin premium and super premium brands.

Selling, general and administration expenses for Q2 2013F were $909,712 up $13,428 or 1% compared to $896,284 for Q2 2012F.

Consulting fees decreased $4,500 to $nil from $4,500 due to termination of consulting agreement with a company controlled by a former director in August 2012.

Foreign exchange loss decreased $1,307 to $503 gain from $804 loss due to fluctuations of the exchange rate between the Canadian Dollar and the US Dollar.

Insurance decreased $4,518 to $6,501 from $11,019 due to consolidation of all subsidiary’s insurance policies under one insurance company.

Automotive decreased $16,464 to $28,534 from $44,998, repairs and maintenance decreased $4,704 to $5,582 from $10,286, and shop supplies decreased $9,638 to $5,844 from $15,482. The decreases are results of various improvements in operating efficiencies implemented since 2011.

Rent and utilities decreased $24,843 to $113,84 from $138,427 due to cost savings generated from sublease of idle space for $1,500 per month.

Advertising and promotion increased $8,176 to $200,106 from $191,930, labour increased $21,828 to $238,882 from $217,054, office expense increased $5,490 to $35,804 from $30,314, and travel increased $1,811 to $15,564 from $13,753. The increase in these expenses is a result of more promotion and tasting events held in the period for releasing 6 new products.

Bank charge increased $3,282 to $28,477 from $25,195 due to increase in credit card sales related to the 3% increase in gross sales in the period.

Director fees are maintained at $1,000 per month for each of independent directors; management fees increased $11,770 to $84,270 from $72,500, professional fees increased $5,835 to $100,682 from $94,847, telephone increased $1,686 to $18,036 from $16,350, transfer agent and filing fees increased $2,997 to $7,545 from $4,548. The increase in these expenses is a result of increased workload on production expansion, increased sales, and redemption and conversion of three tranches of convertible debentures due in November and December 2012.

Refundable container increased $6,794 to $2,072 from negative $4,722, which reflects seasonal adjustments on returning containers.

The Company also included $9,534 (Q2 2012F: $nil) share based compensation in selling, general and administration expenses, representing the estimated fair value of 3,000,000 options granted to the Company’s key employees and directors calculated at the grant date and recognized on the graded vesting method over the period during which 472,222 options vested.

PERFORMANCE AND RESULTS OF OPERATIONS (continued)
Three Months Ended December 31, 2012 ("Q2 2013F")(continued)

Other expenses for Q2 2013F were down $19,354 to $66,079 compared to $85,433 for Q2 2012F. The decrease is primarily a result of $23,757 decrease in accretion of convertible debentures which is matured and converted to common shares in November and December 2012.

Six Months Ended December 31, 2012 ("2013F YTD")

The Company had a net loss of $151,101 for Q2 2013F compared to the net loss of $369,321 for the period ended December 31, 2011 ("2012F YTD"). The decrease in net loss is primarily a result of $252,725 increase in gross margin, and $9,315 decrease in other expenses, which is offset by $38,061 increase in selling, general and administrative expenses.

Gross sales for 2013F YTD were $4,309,628 up $192,902 or 5% compared to $4,116,726 for 2012F YTD. Net Sales for 2013F YTD were $3,317,319 up $186,660 or 6% compared to $3,130,659 for 2012F YTD. The increase in the sales volumes of the Company's premium and super premium brands were key drivers for the increase in gross and net revenue, which reflects the Company's recent marketing strategy with a focus on premium brands.

The gross margin for 2013F YTD increased $252,725 or 16% to $1,846,450 compared to $1,593,725 for 2012F YTD. The gross margin percentage of 2013F YTD was up 5% to 56% compared to 51% for 2012F YTD. The increase in gross margin is primarily a result of the continued sales growth in higher margin premium and super premium brands.

Selling, general and administration expenses for 2013F YTD were $1,764,553 up $38,061 or 2% compared to $1,726,492 for 2012F YTD.

Consulting fees decreased $7,500 to $1,500 from $9,000 due to termination of consulting agreement with a company controlled by a former director in August 2012.

Foreign exchange loss decreased $9,688 to $4,441 gain from $5,247 loss due to fluctuations of the exchange rate between the Canadian Dollar and the US Dollar.

Insurance decreased $6,150 to $14,673 from $20,823 due to consolidation of all subsidiary's insurance policies under one insurance company.

Automotive decreased $17,177 to $72,621 from $89,798, shop supplies decreased $2,254 to $19,818 from $22,072, and travel decreased $1,993 to $25,486 from $27,479. The decreases are results of various improvements in operating efficiencies implemented since 2011.

Bank charge decreased $3,859 to $39,157 from $$43,016 while gross sales increased by 5% which reflects more sales collected by cheques and direct deposits;

Rent and utilities decreased $21,274 to $250,471 from $271,745 due to cost savings generated from sublease of idle space for $1,500 per month.

Refundable container decreased $26,791 to $23,346 negative from positive $3,445, which reflects seasonal adjustments on returning containers.

Advertising and promotion increased $12,869 to $409,518 from $396,649, labour increased $17,818 to $440,909 from $423,091, office expense increased $18,383 to $83,331 from $64,948, and repairs and maintenance increased $6,530 to $20,864 from $14,334. The increase in these expenses is a result of more promotion and tasting events held in the period for releasing 9 new products.

Director fees increased $3,198 to $18,198 from $15,000, management fees are maintained at $145,000 level, professional fees increased $27,431 to $163,580 from $136,149, telephone increased $3,175 to $34,290 from $31,115, transfer agent and filing fees increased $5,547 to $13,128 from $7,581. The increase in these expenses is a result of increased workload on production expansion, increased sales, overseas licensing and redemption and conversion of three tranches of convertible debentures due in November and December 2012.

PERFORMANCE AND RESULTS OF OPERATIONS (continued)
Six Months Ended December 31, 2012 ("2013F YTD")(continued)

The Company also included $40,391 (2012F YTD: $nil) share based compensation in selling, general and administration expenses, representing the estimated fair value of 3,000,000 options granted to the Company's key employees and directors calculated at the grant date and recognized on the graded vesting method over the period during which 972,222 options vested.

Other expenses for 2013F YTD were down $9,315 to $161,232 compared to $170,547 for 2012F YTD. The decrease is primarily a result of $10,893 decrease in accretion of convertible debentures which is matured and converted to common shares in November and December 2012.

Summary of Quarterly Results

The following is selected financial information from the Company's eight most recently completed fiscal quarters:

Fiscal Year Quarter	2013F Q2	2013F Q1	2012F Q4	2012F Q3	2012F Q2	2012F Q1	2011F Q4	2011F Q3
							Restated	Restated
	$	$	$	$	$	$	$	$
Net revenues	1,510,530	1,806,789	1,812,981	1,534,355	1,474,424	1,656,235	1,369,025	1,495,918
SG&A(1)	909,712	854,841	1,255,263	860,238	841,377	785,650	1,364,002	763,743
EBITDA(2)	82,485	147,646	29,704	(25,459)	(88,925)	117,650	(352,618)	(139,666)
Net income (loss)	(87,693)	(63,408)	(498,442)	(241,403)	(286,193)	(83,128)	(614,672)	(306,261)
Net earnings (loss) per share	(0.00)	(0.00)	(0.01)	(0.00)	(0.00)	(0.00)	(0.01)	(0.01)

(1) SG&A represents Selling, General and Administrative expenses.

(2) EBITDA represents earnings before interest, income taxes, depreciation and amortization. EBITDA is a non-IFRS earnings measure, therefore it does not have any standardized meaning prescribed by International Financial Reporting Standards and may not be similar to measures presented by other companies. Management uses this measurement to evaluate the operating results of the Company.

The Company has historically experienced a seasonal pattern in its operating results, with the second and third quarters historically exhibiting lower revenues. Q2 2013F net sales were $1,510,530 down $296,259 compared to the net sales of $1,806,789 for Q1 2013F. Q2 2013F net loss were $87,693 up $24,285 compared to the net loss of $63,408 for Q1 2013F. The decrease in net sales and increase in net loss is due to seasonality. The results in any one quarter are not indicative of results in any other quarter, or for the year as a whole.

Other significant impacts on quarterly expense trends may be share-based compensation expense which is included in selling, general and administrative expenses as follows: Q2 2013F $9,534, Q1 2013F $30,857, Q4 2012F $53,959, Q3 2012F $28,885; Q2 2012F $nil, Q1 2012F $nil, Q4 2011F $14,246, and Q3 2011F $nil.

LIQUIDITY AND CAPITAL RESOURCES

Financial Condition

At December 31, 2012, the Company had a net working capital deficit of $927,733. The Company has $211,175 of cash and $100,000 of restricted cash securing $100,000 of bank indebtedness. Liabilities include $1,335,503 of accounts payable and accrued liabilities, $1,042,873 of long-term debts, and $127,890 of finance lease obligations. The Company has declared $183,600 dividends to its subsidiary's exchangeable preferred shareholders. The Company has not paid any dividends to its common share holders.

The Company has an operating line of credit, six finance leases, six operating leases, two term loans, and one discount loan. As at December 31, 2012 and the date of this MD&A, the Company is in compliance with all of these covenants.

LIQUIDITY AND CAPITAL RESOURCES (continued)
Financial Condition (continued)

Funds on hand are low due to seasonality, continued losses from operations and need for additional financing. The Company will need additional capital to fund its short term operating losses and planned non-discretionary capital expenditures for the next twelve months. The Company is seeking additional cash in the equity and/or debt markets. There is no guarantee that the Company will be able to raise additional equity or debt financing on favorable terms if at all or generate cash flow from operations in the future.

Cash Flow

Six Months Ended December 31, 2012 ("2013F YTD")

Net cash provided in operating activities in 2013F YTD was $283,756 compared to $322,330 cash provided in 2012F YTD, an increase in use of $38,574 due to $255,385 cash used in accounts receivable, prepaid expenses and deposits, due to related parties and accounts payable and accrued liabilities which is offset by an decrease in net loss adjusted for non-cash items by $216,811.

Cash used in 2013F YTD for investing activities was $27,085 for purchasing equipment compared to $22,520 used in purchasing equipments in 2011F YTD.

During 2013F YTD, the Company received $22,436 cash from bank indebtedness, repaid $69,001 of long-term debts and $28,130 of finance lease obligations compared to $20,000 received for share subscription, $100,000 received from a demand loan, repayment of $144,875 for bank indebtedness, repayments of $69,000 for long-term debts, repayments of $31,674 for finance lease obligations, and payment of $18,519 for interest on convertible debentures in 2012F YTD.

Outstanding Share Data

As at December 31, 2012, the Company had 67,168,895 common shares issued and outstanding. In addition, the Company had the following outstanding share data at the date of this MD&A:

Outstanding Share Data	Number of Common Shares	Exercise Price per Common Share	Expiry Dates
Issued and outstanding as at February 28, 2013	67,168,895	N/A	N/A
Stock options	3,437,500	$0.10	June 19, 2013 – March 9, 2017
Conversion of preferred shares(1)	1,405,560	$0.60	March 31, 2013
Penalty on preferred shares allotted but unissued(1)	68,000	N/A	N/A
Fully Diluted as at February 28, 2013	72,079,955	N/A	N/A

(1) After five years (the "Exchange Date") the 68,000 preferred shares will automatically be exchanged into 16.67 common shares of the Company or earlier if certain events occur, including a change in control of the Company or an insolvency event in Russell. Russell will incur a penalty if it has not paid all cumulative dividends due and payable as of March 31, 2011 and for any unpaid dividends calculated each six months thereafter until the Exchange Date. The maximum penalty would result in one additional common share of the Company being exchanged for each Exchangeable Share. At the Exchange Date, the exchange ratio will also increase to account for any unpaid dividends at the Exchange Date such that the additional number of the Company's common shares to be issued is equal to the unpaid dividend amount divided by $0.60. As at December 31, 2012, the unpaid dividend amount was $183,600. The Company did not pay the dividend due and payable as of March 31, 2011. The maximum penalty may result in an aggregate of 68,000 additional common shares of the Company being issued at the Exchange Date.

LIQUIDITY AND CAPITAL RESOURCES (continued)

Financing

(a) On October 5, 2010, the Company's subsidiary Fort Garry Brewing Company Ltd. accepted an offer of $100,000 pre-authorized working capital loan from Business Development Bank of Canada ("BDC"). The BDC Loan, bearing interest at floating base rate plus a variance of 1%, repayable in monthly installments of $1,750, maturing August 15, 2015, is secured by the assets of Fort Garry and supported by a guarantee made by two directors of the Company. In return for the guarantee, the Company is allowed to issue 250,000 common shares of the Company as bonus shares for a deemed value of $0.08 per share for a total value of $20,000, which was recorded as a discount against the value allocated to the loan. During the six months ended December 31, 2012, the Company repaid $10,500 plus interest of $2,014. The Company also recorded interest expense of $2,499 (2011 - $3,201) related to the accretion of the discounted value of the loan, which has been recorded as interest on long-term debt in the statement of operations. As at December 31, 2012, the outstanding balance of the loan is $49,248.

The Company also has a term bank loan with BDC, bearing interest at a floating base rate plus a variance of 1%, repayable in monthly installments of $9,750 plus interest maturing November 15, 2014, secured by the assets of Fort Garry. During the six month ended December 31, 2012, the Company repaid $58,500 plus interest of $8,052. As at December 31, 2012, the outstanding balance of the loan is $224,250.

(b) On December 31, 2010, the Company entered into an amendment and extension loan agreement to the loan agreement described in the June 30, 2011 financial statement note 10(c), pursuant to which the lender extended the maturity date to July 31, 2012 and reduced the loan amount to $738,600 from $1,239,000, provided that the Company repay the loan in the amount of $619,000 on January 1, 2011 (paid). Pursuant to the amended loan agreement, the lender provides to the Company a new loan valued at maturity in the amount of $738,600. A discounted value or loan advance amount of $620,000 is calculated based on a 10% per annum interest rate, calculated semi-annually, with interest payable on maturity resulting in a total loan value at maturity of $738,600. In consideration of the lender agreeing to amend and extend the loan, the lender will also earn a bonus of $22,500 to be included in the loan amount. The term of the loan is nineteen months. The Company may repay the loan at any time without penalty by paying the discounted loan advance amount of $620,000 together with accumulated interest. The loan is guaranteed by Russell Brewing Company Ltd. and Fort Garry Brewing Company Ltd., both wholly-owned subsidiaries of the Company.

On July 27, 2012, the Company agreed to an one year extension (the "Extension") and amendment to a loan agreement (the "Loan Agreement") dated December 31, 2007, pursuant to which the lender ("Lender"), a shareholder of the Company, had provided to the Company a loan (the "Loan") valued at maturity in the amount of $1,239,000.

The Extension is for one year, with $812,460 due on maturity on July 31, 2013. The Company has negotiated a discounted value or loan advance amount (the "Loan Advance Amount") of $738,600, that is calculated based on a 10% per annum interest rate, calculated semi-annually, with interest payable on maturity, resulting in a total loan value of $812,460 at maturity. In consideration of the Lender's agreement to amend and extend the Loan, the Lender will earn a bonus (the "Bonus") of $24,374 to be included in the Loan amount. Russell may repay the Loan at any time without penalty by paying the Loan Advance Amount together with accumulated interest and prorated Bonus.

The Loan is guaranteed by Russell Brewing Company Ltd. and Fort Garry Brewing Company Ltd. both wholly-owned subsidiaries of the Company. As security for the Loan, the Company will grant to the Lender a subordinated security agreement creating a security interest and charge over all of their respective property and assets subordinate to senior debt and senior security of up to $2.5 million plus capital lease obligations incurred for future acquisitions of equipment and other capital assets.

During the six months ended December 31, 2012, the Company recorded interest expense of $37,656 (2011 - $37,527) related to the accretion of the discounted value of the loan, which has been recorded as interest on long-term debt in the statement of operations.

LIQUIDITY AND CAPITAL RESOURCES (continued)

Financing (continued)

(c) On December 19, 2011, the Company entered into a loan facility agreement with a primary lender in the amount of $100,000, repayable at any time prior to January 31, 2012. An additional financing placement fee of $10,000 was charged to the Company to secure this loan. Interest on the unpaid balance of the loan would accrue at an interest rate of 2.5% commencing 29 days following the due date of January 31, 2012, compounded monthly, not in advance. Before January 31, 2012, the Company repaid $100,000 plus $10,000 financing placement fee. There was no interest paid.

(d) During the year ended June 30, 2011, the Company completed, in three tranches, a private placement of units (the “Unit Offering”) and a private placement of convertible debentures (the “Debenture Offering”) (together, the “Offerings”). Under the Unit Offering, the Company issued 12,730,000 units (the “Units”), at a price of $0.08 per Unit, for aggregate gross proceeds of $1,018,400. Each Unit is comprised of one common share and one common share purchase warrant (a “Warrant”). Each Warrant is exercisable for two years after the issuance of the Units to acquire one common share at an exercise price of $0.15 per common share. Under the Debenture Offering, the Company issued convertible debentures (the “Convertible Debentures”) in the aggregate principal amount of $740,750. The Convertible Debentures are convertible into common shares at a price of $0.15 per common share for a two-year period from the date of issue. The Convertible Debentures bear interest at 10% per annum, payable quarterly in arrears.

Canaccord Genuity Corp. (“Canaccord”) acted as agent for the Offerings and as consideration for its services received a cash commission equal to 10% of the gross proceeds from the Offerings and 2,120,200 warrants (the “Agent’s Warrants”) equal to 12% of the number of Units and 12% of the number of common shares underlying the Convertible Debentures sold pursuant to the Offerings. Each Agent’s Warrant entitles the holder, on exercise, to acquire one unit on the same terms as the Units for a price of $0.08 per unit for a period of 24 months from date of issue. The Company also issued 625,000 common shares with a fair value of $56,250 to the Agent as a corporate finance fee. Other share issue costs were $96,607.

During the six months ended December 31, 2012, the Company redeemed its convertible debentures maturing on November 4, 2012, December 3, 2012 and December 24, 2012. The aggregate principal amount of the convertible debentures outstanding was $740,750. On the redemption dates, the Company redeemed the whole of the principal amount of the convertible debentures by issuing a total of 4,938,333 fully paid and non-assessable common shares in the capital of the Company, at a price equal to $0.15 per common share.

The securities issued pursuant to the Redemption will be subject to a hold period of four months and one day from the date of issue in compliance with applicable securities laws and the rules of the TSX Venture Exchange.

(e) On January 20, 2012, the Company closed a non-brokered private placement (the “Private Placement”). Under the Private Placement, the Company issued 15,300,000 units (the “Units”) at a purchase price of $0.05 per Unit, for aggregate gross proceeds of $765,000. Each Unit is comprised of one common share (“Common Share”) in the capital of the Company, and one half of one non-transferable share purchase warrant (“Warrant”). Each whole Warrant entitles the holder to purchase one additional Common Share at a price of $0.10 for a period of one year from closing the Private Placement. The term of the Warrants is subject to an acceleration right at the option of the Company, provided that the daily volume-weighted average trading price of the Common Shares is $0.15 or higher for at least 10 consecutive trading days and the Company has provided Warrant holders with 30 days prior written notice of the accelerated exercise date. The Company has paid finder’s fees totaling $35,000 and share issue cost totaling $14,140 in connection with the Private Placement in accordance with the policies of the TSX Venture Exchange.

LIQUIDITY AND CAPITAL RESOURCES (continued)

Contractual Obligations, Commitments

The Company utilizes several operating leases to finance manufacturing equipment and vehicles. The Company also leases the building in Surrey, BC and Winnipeg, Manitoba where it has its warehousing and packaging operations. By entering into operating leases, the Company is able to update its equipment more frequently, not utilize its cash to invest in these assets and in so doing lower its overall average cost compared with purchasing the assets. All leases are evaluated at inception for appropriate accounting treatment.

A summary of the Company's contractual obligations for the next five years is as follows:

	Less Than 1 Year $	Years 2 and 3 $	Years 4 and 5 $	More Than 5 Years $	Total $
Bank indebtedness	**58,229**	–	–	–	58,229
Accounts payable and accrued liabilities	**1,335,504**	–	–	–	1,335,504
Dividend payable	**193,800**	–	–	–	193,800
Long-term debt	**69,000**	946,350	3,250	–	1,018,600
Finance lease obligations	**21,142**	108,781	27,483	–	157,406
	1,677,675	1,055,131	30,733	–	2,763,539

RELATED PARTIES

The Company has identified its directors and certain senior officers as its key management personnel and the compensation costs for key management personnel and companies related to them were recorded at their exchange amounts as agreed upon by transacting parties and on terms and conditions similar to non-related parties as follows:

The Company entered into related party contracts as follows: with Marketing Services International, a company controlled by Brian Harris for management fees in his capacity as CEO of Company; with Wicked Consulting Inc., a company controlled by Andrew Harris for management fees in his capacity as COO of the Company; with Mt. Pacific Financial Corp. a company controlled by Gary Liu for accounting services in his capacity as CFO of the Company. According to the contracts, the Company incurred management fees for $13,000 per month to a company controlled by the CEO of the Company and $13,000 per month to a company controlled by the COO of the Company, and incurred accounting fees for $11,333 per months to a company controlled by the CFO of the Company. The Company also accrued director fees for $1,000 per month to each of three independent directors.

The compensation costs for key management personnel and companies related to them were recorded as follows:

	Six Months Ended December 31, 2012	Six Months Ended December 31, 2011
Management fees (a) and (b)	**$ 144,000**	$ 143,000
Directors fees (c)	**15,000**	15,000
Accounting fees (e)	**62,000**	68,537
Share-based payments (c)	**40,391**	-
	$ 261,391	$ 158,000

RELATED PARTIES (continued)

(a) During the period ended December 31, 2012, the Company incurred management fees of $nil to the CEO of the Company (2011 – $32,500) and $72,000 to a company controlled by the CEO (2011 – $40,000). As at December 31, 2012, the Company owed $57,417 to the CEO and a company controlled by the CEO (2011 – $5,727), which is non-interest bearing, unsecured and due on demand.

(b) During the period ended December 31, 2012, the Company incurred management fees of $nil to the COO of the Company (2011 – $42,500) and $72,000 to a company controlled by the COO (2011 – $30,000). As at December 31, 2012, the Company owed $68,754 to the COO and a company controlled by the COO (2011 – $44,580), which is non-interest bearing, unsecured and due on demand.

(c) During the period ended December 31, 2012, the Company granted nil and vested 972,222 stock options to directors and officers and key employees (2011 – nil) and incurred director fees of $15,000 to the independent directors of the Company (2011 – $15,000). As at December 31, 2012, the Company owed $42,110 to the independent directors (2011 – $98,000), which is non-interest bearing, unsecured and due on demand.

(d) During the period ended December 31, 2012, the Company paid consulting fees of $1,500 to a company controlled by an independent director of the Company (2011 – $9,000).

(e) During the period ended December 31, 2012, the Company incurred accounting fees of $62,000 to a company controlled by the CFO of the Company (2011 – $68,537). As at December 31, 2012, the Company owed $66,200 to this company (2011 - $46,100), which is non-interest bearing, unsecured and due on demand.

(f) During the period ended December 31, 2012, the Company incurred salaries and wages expense of $65,000 relatives of directors and officers of the Company (2011 – $68,333). As at December 31, 2012, the Company owed $nil to relatives of directors of the Company (2011 - $7,333), which is non-interest bearing, unsecured and due on demand.

These transactions were in the normal course of operations and have been recorded at their exchange amounts, which is the consideration agreed upon by the related parties.

CRITICAL ACCOUNTING ESTIMATES

The preparation of consolidated financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of revenues and expenses for the reporting period. Significant areas requiring the use of management estimates may include recovery of accounts receivable, inventory valuation, the estimated useful life of long-lived assets, the recoverability of amounts recorded for long-lived assets, estimates used in impairment analysis of long-lived assets, container liabilities, valuation of deferred tax assets and liabilities and estimates used in calculating share-based compensation. By their nature, these estimates are subject to measurement uncertainty and the effect on the financial statements of changes in such estimates in future periods could be significant. Actual results could differ from management's best estimates as additional information becomes available.

Property, Plant and Equipment

The accounting for property, plant and equipment requires that management make estimates involving the life of the assets, the selection of an appropriate method of depreciation and determining whether an impairment of assets exists.

The Company reviews the residual values, useful lives of depreciable assets and depreciation method on an annual basis and where revisions are made, the Company applies such changes in estimates on a prospective basis.

The net carrying amounts of property, plant and equipment are reviewed for impairment either individually or at the cash generating unit level at the end of each reporting period. If there are indicators of impairment, an evaluation is undertaken to determine whether the carrying amounts are in excess of their recoverable amounts. An asset's recoverable amount is determined as the higher of its fair value less cost to sell and its value-in-use. To the extent that an asset's carrying amount exceeds its recoverable amount, the excess is fully provided for in the period in which it is determined to be impaired. Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset in prior periods. There is uncertainty in these estimates as the related recoverable amounts are projected for future years based on underlying assumptions such as volume growth, inflation factors and industry trends which may not materialize. Management uses its best estimates to forecast these amounts, but the actual amounts may vary from estimates. Should future results differ from management's estimates, an impairment of these assets and a related write-down may result. As at the date of this report, the Company believes that its estimates are materially correct.

Intangible Assets

Indefinite life intangible assets consist of brands and trademarks. These assets are recorded at cost and are not amortized but instead are reviewed for impairment at the end of each reporting period. If there are indicators of impairment, an evaluation is undertaken to determine whether the carrying amounts are in excess of their recoverable amounts. An asset's recoverable amount is determined as the higher of its fair value less cost to sell and its value-in-use. There is uncertainty in these estimates as the related recoverable amounts are projected for future years based on underlying assumptions such as volume growth, inflation factors and industry trends which may not materialize. Management uses its best estimates to forecast these amounts, but the actual amounts may vary from estimates. Should future results differ from management's estimates, an impairment of these assets and a related write-down may result. As at the date of this report, the Company believes that its estimates are materially correct.

RISKS AND UNCERTAINTIES

Credit Risk

The Company grants credit to its customers in the normal course of business. However as the major portion of the accounts receivable are held by the BCLDB, the MLCC, and AGLC, management believes exposure to credit risk is limited.

Competition

The Company considers its main competitors to be other participants in the Canadian brewing industry, which includes imported beer and specialty and value priced brands brewed by both small regional brewers and the national brewers. Existing regional breweries are increasing their production capacities and marketing programs. National brewers are aggressively promoting their own specialty and value brands as well as premium brands. The Company also anticipates increasing competition as new brewers enter markets in which the Company currently operates.

The principal competitive factors affecting the market for the Company's products include quality and taste, packaging, advertising and promotional support, brand recognition and price. There can be no assurance that the Company will be able to compete successfully in this category against current and future competitors based on these and other factors. The Company competes with a variety of domestic and international brewers, many of whom have substantially greater financial, production, distribution and marketing resources. The Company anticipates increased competition in the premium beer category from the major domestic brewers, each of whom has introduced and is marketing premium-priced products. The large domestic brewers dominate the domestic beer market and the Company expects that certain of these companies may seek further participation in the premium beer market through the acquisition of equity positions in, or the formation of, distribution alliances with other brewers.

Increased competition could result in price reductions, reduced profit margins and loss of market share, all of which could have a material adverse effect on the Company's operations. The Company's products also compete generally with other alcoholic beverages.

Government Regulation

The Company's business is regulated by federal, provincial and municipal laws and regulations regarding such matters as licensing requirements, trade and pricing practices, permitted and required labeling, advertising, promotion and marketing practices, relationships with distributors and related matters. Failure on the part of the Company to comply with federal, provincial or municipal laws and regulations could result in the loss, revocation or suspension of the Company's licenses, permits or approvals and could have a material adverse effect on the Company's business. The Company believes that it has obtained all regulatory permits and licences necessary to operate its business where the Company's products are currently being produced and distributed. In addition, changes to taxes, environmental regulations or any other laws or regulations which affect the Company's products or their production, handling or distribution could have a material adverse effect on the Company's operations.

Trends in Consumer Preferences and Attitudes

The domestic premium beer market has grown dramatically over the past decade. The Company believes that one factor in such growth has been consumer demand. No assurance can be given however that consumer demand for these products will continue in the future. The Company's success also depends upon a number of factors related to the level of discretionary consumer spending, such as the general state of the economy, tax laws and consumer confidence in future economic conditions.

RISKS AND UNCERTAINTIES (continued)

Protection of Intellectual Property Rights; Risk of Third Party Claims of Infringement

The Company considers its trademarks, particularly certain brand names and product packaging, advertising and promotion design and artwork, to be of considerable value and critical to its business. The Company relies on trademark laws and other arrangements to protect its proprietary rights. There can be no assurance that the steps taken by the Company to protect its intellectual property rights will preclude competitors from developing similar brand names or promotional materials. While the Company believes that its proprietary rights do not infringe upon those third parties, it possesses no assurances of such a situation. The Company has applied for registration of the following trademarks: Russell, Fort Garry and Rock Mountain.

Dependence on Key Personnel

The Company's success depends to a significant degree upon the continuing contributions of key personnel, and on its ability to attract and retain qualified management, sales, production and marketing personnel. The loss of any of such persons or the failure to recruit additional key personnel in a timely manner, could adversely affect the Company. The Company does not maintain any key man life insurance on any of its personnel.

Operating Hazards

The Company's operations are subject to certain hazards and liability risks faced by all brewers, such as the potential contamination of ingredients or products and equipment defects. While the Company has not experienced a contamination problem in its products, the occurrence of such a problem could result in a costly product recall and serious damage to the Company's reputation for product quality. Although the Company maintains insurance against certain risks under various general liability and product liability insurance policies, there can be no assurance that the Company's insurance will be adequate or that claims resulting from such incidents will be accepted as filed.

Trade Regulations

The 1994 North America Free Trade Agreement ("NAFTA") among Canada, Mexico and the United States expanded the 1989 Free Trade Agreement between Canada and the United States. To date, NAFTA has had no material effect on the Company's business or operations. However, the adoption of new trade regulations or future trade disputes that result in retaliatory practices or increased tariffs between the United States and Canada could adversely affect the Company's business.

Proprietary Rights

Although the formulas for the Company's beers are proprietary trade secrets of the Company, there can be no assurance that others will not develop beers of the same or similar tastes and qualities as the Company's beers.

Seasonal Nature of Business

The alcoholic beverage industry in Canada is seasonal in nature. Accordingly, the Company has historically experienced a seasonal pattern in its operating results, with the second and third quarters historically exhibiting lower revenues. Therefore, the results in any one quarter are not indicative of results in any other quarter, or for the year as a whole.

RISKS AND UNCERTAINTIES (continued)

Uncertainty of Additional Capital

In the past, the Company relied on the issuance of equity and debt securities to meet its capital requirements. The ability of the Company to arrange additional financing in the future will depend, in part, on the prevailing capital market conditions as well as the business performance of the Company. There can be no assurance that additional capital or other types of financing will be available if needed or that, if available, the terms of such financing will be favourable to the Company. If additional financing is raised by the Company through the issuance of securities from treasury, control of the Control may change and security holders may suffer significant dilution. The Company also requires continued support from its lenders to maintain its financial condition. The loss of this support could limit expansion opportunities and put strain on the Company's continuing operations.