

DIAMOND ESTATES WINES & SPIRITS INC.

MANAGEMENT DISCUSSION AND ANALYSIS

THREE AND NINE MONTH PERIODS ENDED DECEMBER 31, 2014 AND 2013

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The following management discussion and analysis ("MD&A") of Diamond Estates Wines & Spirits Inc. ("Diamond" or "the Company") provides a review of corporate developments, results of operations and financial position for the three months ended December 31, 2014 ("Q3 2015") and the nine months ended December 31, 2014 ("YTD 2015") and the comparable fiscal periods ending December 31, 2013 ("Q3 2014" and "YTD 2014", respectively). This discussion is prepared as of February 18, 2015 and should be read in conjunction with the unaudited interim condensed consolidated financial statements and accompanying notes of Diamond for Q3 2015 and YTD 2015 and Q3 2014 and YTD 2014 and the audited consolidated financial statements for the fiscal years ended March 31, 2014 and 2013. Additional information regarding Diamond is available on Diamond's SEDAR profile at www.sedar.com. The results reported in this MD&A have been prepared in accordance with International Financial Reporting Standards ("IFRS") and are presented in Canadian dollars, which is the Company's functional currency.

FORWARD-LOOKING STATEMENTS

This MD&A contains forward-looking statements. Forward-looking statements can often be identified by the use of words such as "plans", "expects" or "does not expect", "is expected", "estimates", "intends", "anticipates" or "does not anticipate", or "believes", or variations of such words and phrases or state that certain actions, events or results "may", "could", "would", "might" or "will" be taken, occur or be achieved. Forward-looking statements involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of the Company to be materially different from any future results, performance or achievements expressed or implied by the forward-looking statements. Actual results and developments are likely to differ, and may differ materially, from those expressed or implied by the forward-looking statements contained in this MD&A. Such forward-looking statements are based on a number of assumptions which may prove to be incorrect, including, but not limited to, the ability of the Company to obtain necessary financing, the economy generally, the global financial crisis, conditions in the target market of the Company, consumer interest in the services and products of the Company, competition and anticipated and unanticipated costs. Such statements could also be materially affected by environmental regulation, liquor regulation, taxation policies, competition, the lack of available and qualified personnel or management, stock market volatility and the ability to access sufficient capital from internal or external sources. Actual results, performance or achievement could differ materially from those expressed herein. While the Company anticipates that subsequent events and developments may cause its views to change, the Company specifically disclaims any obligation to update these forward-looking statements, except as required by applicable law. These forward-looking statements should not be relied upon as representing the Company's views as of any date subsequent to the date of this MD&A. Although the Company has attempted to identify important factors that could cause actual actions, events or results to differ materially from those described in forward-looking statements, there may be other factors that cause actions, events or results not to be as anticipated, estimated or intended. Readers should not place undue reliance on forward-looking statements. The factors identified above are not intended to represent a complete list of the factors that could affect the Company. Additional factors are noted in this MD&A under "Risk Factors".

NON-IFRS FINANCIAL MEASURE

Management uses net loss as presented in the unaudited interim condensed consolidated statements of loss and comprehensive loss as well as "standardized EBITDA" as a measure to assess performance of the Company. Standardized EBITDA is another financial measure and is reconciled to net loss and comprehensive loss below under "Results of Operations".

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Standardized EBITDA is a supplemental financial measure to further assist readers in assessing the Company's ability to generate income from operations before taking into account the Company's financing decisions, depreciation of property, plant and equipment and amortization of intangible assets. Standardized EBITDA comprises gross profit less operating costs before financial expenses, depreciation and amortization, non-cash expenses, one-time and other unusual items, and income tax.

Standardized EBITDA does not represent the actual cash provided by the operating activities, nor is it a recognized measure of financial performance under IFRS. Readers are cautioned that this measure should not be considered as a replacement for those as per the unaudited interim condensed consolidated financial statements prepared under IFRS. The Company's definitions of this non-IFRS financial measure may differ from those used by other companies.

COMPANY OVERVIEW

The Company is a producer, marketer and distributor of wines and spirits in Canada. The Company operates two wineries in the Niagara region of Ontario producing VQA and blended wines under such well known brand names as 20 Bees, EastDell, Fresh, Lakeview Cellars, Dois Amigos, Dan Aykroyd, De Sousa, Benchmark, Seasons and Riders Valley. The Company also sells fine wines, beer, spirits and ready-to-drink beverage alcohol products from other suppliers around the world through its partnership, Kirkwood Diamond Canada, as the marketing and sales agent for these brands in various regions of the country. These brands vary from time to time and currently include, but are not limited to, Fat Bastard wines from France, Brick Brewing from Canada, Iceberg Vodka from Canada, Fireball Whiskey Shooter from Canada, Flor de Cana rum from Nicaragua, Anciano wines from Spain, Francois Lurton wines from France and Argentina and a number of top bourbons.

The Company's mission is to build profitable beverage alcohol brands that celebrate life and achievement in a socially responsible manner. To meet this goal, the Company has made significant investments in processing, winemaking, brand marketing and sales programming. Based on its analysis of the market, the Company believes in the long-term growth prospects for the domestic and import beverage alcohol markets in Canada.

The Company is committed to delivering these results through its distribution network focused on the provincial liquor boards, licensed restaurants and bars, Diamond's three retail locations and export channels. The Company supports this focus through the enhanced efforts of its sales, marketing and brand promotional activities and through the ongoing review of its manufacturing efficiencies and costs. The Company has a total workforce of approximately 113 employees, including 54 engaged in the selling and marketing of its brands, 20 in the manufacturing and distribution of its brands, 20 involved in the retailing of its domestic products through our retail facilities and 19 in accounting and administration.

GOING CONCERN

The accompanying unaudited interim condensed consolidated financial statements have been prepared using the IFRS applicable to a going concern. Accordingly, they do not give effect to adjustments that would be necessary should the Company be unable to continue as a going concern and, therefore, be required to realize its assets and liquidate its liabilities and commitments in other than the normal course of business and at amounts different from those in the accompanying unaudited interim condensed consolidated financial statements. Such adjustments could be material.

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The Company has incurred repeated losses as net loss and comprehensive loss for YTD 2015 was \$942,715 (YTD 2014 - \$3,359,675) with an accumulated deficit as at December 31, 2014 of \$33,305,392 (March 31, 2014 - \$32,600,112). Working capital as at December 31, 2014 improved to \$(939,511) (as a result of the addition of The Kirkwood Group's agency business) compared with a deficiency \$108,319 as at March 31, 2014, but is not available for winery operations.

The Company's ongoing losses, nominal working capital for the winery division, narrow margins and tight covenant measurements with its lender indicate the existence of material uncertainties that may cast significant doubt on its ability to continue as a going concern.

REVERSE TAKEOVER

On September 24, 2013, Whiteknight Acquisitions II Inc. ("WKN"), now the Company, acquired 100% of the issued and outstanding shares of Diamond Estates Wines & Spirits Ltd. ("Diamond Ltd."), a private company. The transaction constituted the Qualifying Transaction of WKN as such term is defined in Policy 2.4 of the TSX-V. To effect the transaction, WKN issued 26,275,310 common shares and 399,973 share purchase warrants in exchange for all of the issued and outstanding securities of Diamond Ltd. (see further discussion under "Capitalization"). WKN subsequently changed its name to "Diamond Estates Wines & Spirits Inc." ("Diamond"), such that Diamond is now the parent company of Diamond Ltd., its 100% owned-subsiidiary.

Although the transaction resulted in Diamond Ltd. legally becoming a wholly-owned subsidiary of WKN, the transaction constituted a reverse takeover of WKN and was accounted for as a reverse takeover transaction in accordance with guidance provided in IFRS 2 Share Based Payments. As WKN did not qualify as a business according to the definition in IFRS 3, this reverse takeover transaction did not constitute a business combination. It was treated as an issuance of shares by Diamond Ltd. for the net monetary assets of WKN.

LAUNCH OF KIRKWOOD DIAMOND CANADA PARTNERSHIP

On October 1, 2014, the Company and The Kirkwood Group ("TKG") formed a new partnership named Kirkwood Diamond Canada ("KDC" or the "partnership") and began the process of merging their respective agency businesses. The Company has a 50.01% interest in the partnership and a tie-breaking vote on the Executive Committee of the partnership, effectively giving it strategic and directional control over the operations of the partnership. Accordingly, the partnership's financial results have been consolidated into the Company's financial statements starting at the beginning of this Q3 reporting period.

Each partner contributed intangible assets, consisting of sales agent and distribution agreements with beverage alcohol suppliers, of their respective agencies to KDC in exchange for their respective partnership interests. For Q3 2015, each partner operated their respective agency businesses independently and carved out the activity for the benefit of the partnership. Each partner therefore also retained ownership of their respective working capital during this period in order to continue to operate their own businesses independently. On a beneficial basis, each partner therefore contributed their respective inventories as at October 1, 2014 to the partnership offset by notes payable. However, accounts receivable and accounts payable balances at October 1, 2014 related to activity prior to the inception of the partnership were retained by the partners such that they did not form part of the business combination. The Company did not issue any equity or cash consideration, contingent or otherwise, to the owners of The Kirkwood Group as a result of this transaction.

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The following summarizes the consideration transferred to the partnership by the Company and the partnership assets acquired and liabilities assumed at the acquisition date:

Consideration transferred to KDC by the Company		
Inventories	\$ 1,597,708	
Accounts payable and accrued liabilities	(1,597,708)	
Intangible assets	<u>3,700,000</u>	
		<u>\$ 3,700,000</u>
Fair value of KDC assets acquired and liabilities assumed		
Inventories	5,161,228	
Accounts payable and accrued liabilities	(5,161,228)	
Intangible assets	<u>7,200,000</u>	
Net assets acquired before non-controlling interest		7,200,000
Net assets attributable to Company's interest eliminated on consolidation		<u>3,700,000</u>
		<u>\$ 3,500,000</u>

The fair values of all acquired assets (including intangible) and assumed liabilities have been determined on a provisional basis and are subject to adjustment. These adjustments may include, but are not limited to, post-acquisition review of the fair value of the acquired net assets, deferred tax balance adjustments on the filing of tax returns and final working capital adjustments on the respective balances acquired.

The non-controlling interest in the partnership is 49.99%. It has been measured at fair value, primarily based on the proportionate relative value of each partner's intangible assets as described above. The primary input for that valuation was the use of each partner's fiscal 2014 gross margin, normalized for variable selling costs and client relationships retained. None of the intangible assets recognized are expected to be deductible for income tax purposes. No value has been attributed to the Company's own intangible assets transferred to the partnership as there can be no gain on disposition within the consolidated entity.

Summarized financial data for KDC as at December 31, 2014, before consolidation eliminations, are as follows:

	\$
Accounts receivable	2,827,000
Inventories	4,508,000
Intangible assets	7,200,000
Accounts payables	(4,264,000)
Notes payable - partner companies	(3,370,000)
Revenues	4,665,000
Net loss	(475,000)

The Company has recognized \$2.8 million of revenue and \$125,000 of net loss in the three month period ended December 31, 2014 that would not have otherwise have been recorded in absence of this acquisition. Included in this amount are acquisition-related expenses of \$100,000. The Company cannot reasonably determine the total revenue and net income amount that the partnership would have generated had the merger taken effect on April 1, 2014 as not all of the activities of The Kirkwood Group during that period related to the business that became part of the new partnership on October 1, 2014.

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Restructuring costs of \$488,528 were provided for in the three and nine month period periods ended December 31, 2014 to cover employee severance and lease termination costs.

DE SOUSA WINE CELLARS CORP. SALE AND LEASEBACK

On November 10, 2014, the Company completed the sale and leaseback of its De Sousa Estates Winery in Beamsville, Ontario to Oakwest Corporation Limited ("Oakwest"). This was done through the sale of the common shares in De Sousa Wine Cellars Corporation, the entity that owns the winery property. The details of the sale and leaseback, both done at fair value, are as follows:

- (a) The share sale was for cash proceeds of \$1,800,000 and resulted in the effective disposition of the winery property, previously classified under assets held for sale, resulting in a loss on disposition of \$80,916.
- (b) Approximately \$780,000 of the proceeds were used to retire the outstanding mortgage on the property, while the remaining proceeds used for working capital requirements
- (c) The Company will lease the winery from Oakwest for a period of five years with the option to extend for another five years. Minimum lease payments due over the first five year term total \$500,000. Operating lease payments expensed during the three month period ended December 31, 2014 total \$9,780.
- (d) The Company will continue to operate the winery under a profit-sharing arrangement with Oakwest under which profits greater than \$25,000 in any given year are to be split two thirds in favour of the Company and one third for Oakwest. To date, profits under the profit-sharing arrangement are below the threshold level.
- (e) The Company has maintained ownership and all rights to these brands, and funds all working capital requirements.
- (f) If Oakwest sells the property during the initial lease term, it will transfer to the Company's benefit all net proceeds in excess of \$1,800,000.

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RESULTS OF OPERATIONS (UNAUDITED)

	Q3 2015	YTD 2015	Q3 2014	YTD 2014
Revenue	\$ 7,877,312	\$ 18,907,188	\$ 5,412,780	\$ 16,637,566
Change in inventories of finished goods and raw materials consumed	4,152,591	9,530,869	2,820,128	8,859,199
Gross profit	3,724,721	9,376,319	2,592,652	7,778,367
<i>Gross margin %</i>	47.3	49.6	47.9	46.8
Operating expenses	3,372,057	7,863,294	2,345,074	7,273,040
<i>Operating expenses %</i>	42.8	41.6	43.3	43.7
Standard EBITDA	352,664	1,513,025	247,578	505,327
Interest on bank indebtedness	358,746	1,048,893	338,421	1,258,545
Depreciation and amortization	228,836	680,061	357,790	1,069,671
Financing costs	7,378	21,062	61,849	422,612
Net loss from operations	(242,296)	(236,991)	(510,482)	(2,245,501)
Non-cash loss on RTO	-	-	-	749,787
Restructuring charges	488,528	488,528	78,648	78,648
Share based payments	49,613	136,280	-	190,666
Share price guarantees	-	-	-	(247,332)
Listing expenses	-	-	-	342,405
Loss on disposal of assets held for sale	80,916	80,916	-	-
Net loss and comprehensive loss	\$ (861,353)	\$ (942,715)	\$ (589,130)	\$ (3,359,675)
Portion attributable to:				
Shareholders	(623,918)	(705,280)	(589,130)	(3,359,675)
Non-controlling interest	(237,435)	(237,435)	-	-
	\$ (861,353)	\$ (942,715)	\$ (589,130)	\$ (3,359,675)

See definition of selected terms under the heading "Non-IFRS Financial Measures"

The Company generated a net loss in Q3 2015 of \$861,353. The net loss excluding the portion attributable to non-controlling interest was \$623,918, up slightly from the loss of \$589,130 in Q3 2014 and largely attributable to the restructuring charges associated with the merger of the Diamond Estates' agency business with that of The Kirkwood Group on October 1, 2014. EBITDA improved to \$352,664 in Q3 2015 from \$247,578 in Q3 2014. Sales for Q3 2015 were \$7,877,312 compared to \$5,412,780 for Q3 2014, representing an increase of 45.5%. Gross profit for Q3 2015 was up 43.7% over the prior year, to \$3,724,721 from \$2,592,652. Gross margin for Q3 2015 was 47.3%, a decrease of 0.6% compared to 47.9% for Q3 2014. Operating expenses for Q3 2015 increased by \$1,026,983 compared to the same period in the prior year.

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On a year to date (YTD) basis, the Company had a net loss for the nine months ended December 31, 2014 of \$942,715 (\$705,280 excluding non-controlling interest) compared to \$3,359,675 for the nine months ending December 31, 2013. EBITDA for YTD 2015 was \$1,513,025 up significantly from \$505,327 in YTD 2014. YTD 2015 sales were \$18,907,188 compared to \$16,637,566 in YTD 2014, representing an increase of 13.6%. YTD gross profit for 2015 increased to \$9,376,319 from \$7,778,367 in YTD 2014, while gross margin for YTD 2015 was up 2.8% to 49.6% compared to 46.8% for YTD 2014. Operating expenses increased by \$590,254 in YTD 2015 over YTD 2014.

As reflected on the interim condensed consolidated statements of cash flows, the company has generated negative cash flow from operations for YTD 2015 of \$40,095 compared to negative cash flow from operations for YTD 2014 of \$1,543,552, an improvement of \$1,583,647. That change is comprised of the following major components:

Increase in gross profit	\$ 1,597,952
Increase in operating expenses	(590,254)
Decrease in interest expense	209,652
Decrease in financing expenses	401,550
Other	(35,253)
	<u>\$ 1,583,647</u>

Sales for Q3 2015 were up \$2,464,532 over Q3 2014 primarily as a result of the merger with The Kirkwood Group that was effective October 1, 2014. The merger brought significant scale to Diamond's western Canadian business where it operates as a distributor and reseller of product in addition to being the sales and marketing agent. This had an impact on the revenue mix in the quarter, as buy-sell accounted for 43.1% of total revenue compared to 19.5% in the same period of the prior year. The gross margin for the agency business fell to 50.3% in Q3 2015 from 67.3% in Q3 2014 due to the addition of the brands from the legacy Kirkwood business.

Sales for the winery division in Q3 2015 were down slightly by 3.8% or \$135,249 to Q3 2014. This was the result of the Company choosing to focus on improving profitability throughout the current fiscal year. Low margin services and bulk wine sales to third parties were down by \$297,556 as the Company focused on more profitable sales channels that create value by building our brands. The result was continued improvement in gross margin that was up by 5.8% to 43.3% in Q3 2015 versus Q3 2014. Similarly, on a year-to-date basis, sales for the winery division were \$11,836 (0.1%) higher than YTD 2014. Gross margin was 5.8% higher at 45.0% versus 39.2% for YTD 2015 and YTD 2014 respectively.

Operating expenses increased \$1,026,983 or 43.8% in Q3 2015 over Q3 2014 as a result of the merger of the agency businesses. This includes the personnel, office, general and administration costs of the former Kirkwood Group and also includes one-time costs associated with the integration such as travel, information technology, communications, legal, accounting and tax advisors.

Non-operating related expenses were \$619,057 in Q3 2015 compared to \$78,648 in Q3 2014. The difference is primarily attributable to a restructuring charge of \$488,528 associated with redundancies created by the merger of the agency businesses. The Company also incurred a non-cash loss of \$80,916 related to the sale-leaseback of its De Sousa Estates winery to Oakwest Corporation.

The Company incurred a non-cash expense of \$49,613 and \$136,280 in Q3 2015 and YTD 2015 (\$Nil and \$190,666 in Q3 2014 and YTD 2014) based on previously granted options that vested in the reporting period (*see note 16 for further details on options*).

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QUARTERLY PERFORMANCE (UNAUDITED)

The following table highlights certain key quarterly financial highlights. Commentary on the selected highlights is included under "Results of Operations" and "Liquidity and Capital Resources".

	Dec-2014	Sep-2014	Jun-2014	Mar-2014	Dec-2013	Sep-2013	Jun-2013	Mar-2013
	Q3 2015	Q2 2015	Q1 2015	Q4 2014	Q3 2014	Q3 2014	Q1 2014	Q4 2013
	\$	\$	\$	\$	\$	\$	\$	\$
Balance sheet								
Working capital (deficiency)	(939,511)	(137,038)	(273,636)	(108,318)	(98,660)	(1,437,925)	(17,691,674)	(17,669,374)
Bank indebtedness (total)	12,274,083	12,757,982	12,568,764	13,013,129	11,876,916	10,311,902	28,039,002	28,135,557
Term debt	9,422,538	9,525,288	9,828,516	10,000,000	10,000,000	10,000,000	-	-
Shareholders' equity	3,362,565	7,522,030	7,516,723	8,265,487	8,847,560	8,265,487	697,308	1,036,082
Income statement								
Revenue	7,877,312	5,863,300	5,166,577	3,944,085	5,123,058	5,255,455	5,969,330	4,348,566
Gross margin	3,724,721	3,065,300	2,586,199	2,089,672	2,233,513	2,864,104	2,794,664	2,444,739
Standard EBITDA	352,664	796,870	363,491	146,940	247,575	(354,072)	611,823	312,500
Net loss	(861,353)	116,320	(197,681)	(715,758)	(589,132)	(2,431,769)	(338,774)	(862,610)

See definition of selected terms under the heading "Non-IFRS Financial Measures"

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LIQUIDITY AND CAPITAL RESOURCES (UNAUDITED)

	December 31 2014	March 31 2014
Accounts receivable	\$ 4,225,443	\$ 3,035,264
Inventory	16,983,744	12,466,162
Assets held for sale	-	1,880,916
Other	<u>102,884</u>	<u>139,222</u>
Total current assets	21,312,071	17,521,564
Property, plant and equipment	15,535,491	15,992,766
Other	<u>4,443,952</u>	<u>844,677</u>
Total assets	<u>\$ 41,291,514</u>	<u>\$ 34,359,007</u>
Bank indebtedness	\$ 12,274,083	\$ 12,175,284
Bank indebtedness associated with assets held for sale	-	837,845
Current portion of term loan payable	692,894	616,115
Shareholder loan payable	500,000	500,000
Shareholder loan payable	3,057,914	-
Other current liabilities	<u>5,726,691</u>	<u>3,500,639</u>
Total current liabilities	22,251,582	17,629,883
Term loan payable, net of current portion	<u>8,729,644</u>	<u>9,212,401</u>
Total liabilities	30,981,226	26,842,284
Shareholders' equity	6,947,723	7,516,723
Non-controlling interest	<u>3,362,565</u>	<u>-</u>
	<u>\$ 41,291,514</u>	<u>\$ 34,359,007</u>

The Company's consolidated financial position has improved as at December 31, 2014 from that as at March 31, 2014 as a result of the addition of The Kirkwood Group's agency business. Working capital has increased by \$(831,192) to \$(939,511) as at December 31, 2014 compared to a deficiency of \$108,319 as at March 31, 2014. Total bank indebtedness, including that associated with assets held for sale, decreased by \$739,046 to \$12,274,083 as at December 31, 2014 compared to \$13,013,129 as at March 31, 2014. Principal payments of \$405,978 have been made against the Meridian term loan during YTD 2015 (*see notes 8 and 11 for further details on the Meridian credit facility*).

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On September 17, 2014, the Company signed a new credit agreement with Meridian Credit Union ("MCU"), its primary lender, to replace the previous agreement dated July 24, 2013. The new credit agreement continues to provide a revolving line of credit of up to \$13,000,000, but is now subject to increased margin limits on inventory of \$11,000,000, up from \$10,000,000. The interest rate on the De Sousa Loan (for the Beamsville winery) has been reduced 50 basis points to prime plus 2.50%. Enhancements to the covenants include:

- the inclusion of the winery licenses (an intangible asset) at 50% in the calculation of net effective worth
- the debt to effective net worth ratio falling to 3.25:1 on March 31, 2016
- maintaining at least three product listings with the Liquor Control Board of Ontario

The credit agreement now specifies the following overall terms:

(I) Credit facilities

- (a) Operating line of \$13,000,000, due on demand, bearing interest at prime plus 2.5%, interest payable monthly; the operating line is limited to:
 - (i) 85% of acceptable Canadian receivables aged 120 days and under, less certain exclusions, plus
 - (ii) 75% of all other acceptable receivables aged 90 days and under, less certain exclusions, plus
 - (iii) 90% of acceptable wine inventory to a maximum of \$11,000,000, less
 - (iv) priority payables or claims purporting to have priority over Meridian
- (b) De Sousa term loan of \$804,985, due on demand, repayable in monthly principal payments of \$8,215 plus interest at prime plus 2.50%
- (c) Real estate and equipment term loan of \$9,577,101, maturing 3 years from initial advance date, bears interest at a fixed rate of 5.40%, repayable in equal monthly blended payments of principal and interest of \$94,319

(II) Security

The above credit facilities are secured by general security agreements, a collateral mortgage over both the Beamsville property and buildings and the Niagara Cellars property and buildings, assignment of fire and liability insurance over both properties and buildings, and corporate guarantees and postponements of claim in favour of Meridian by both De Sousa Wine Cellars Corporation and De Sousa Wines Toronto Inc., each of which is supported by respective general security agreements.

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(III) Financial covenants

- (a) Achieve a minimum effective net worth of not less than \$7,000,000, which is defined as: shareholders' equity plus loans from shareholders postponed to Meridian less loans to shareholders and related parties and less 50% of intangible assets;
- (b) To maintain a debt to effective net worth of 3.75/1.00 measured monthly, improving to 3.25/1.00 by March 31, 2016; and
- (c) Maintain a debt servicing coverage ("DSC") ratio of not less than 1.25/1.00, calculated on a rolling four quarter basis with the fourth quarter ending March 31, 2015

From the signing of the initial credit agreement on July 24, 2013 through to December 31, 2014, the Company has been in compliance with the covenants relating to minimum effective net worth and debt to effective net worth. The DSC ratio covenant was not measured for fiscal 2014 by virtue of an amendment to the credit agreement dated March 25, 2014, and will be measured for the first time for the rolling four quarter period ended March 31, 2015.

In March, 2014, the Company's largest shareholder advanced \$500,000 to the Company in the form of a loan. This loan is unsecured, bears interest at 8% per annum and has been included in the determination of effective net worth under the provisions of the MCU credit agreement.

Note payable - non-controlling interest

As more fully described in note 5, the Company and its partner, TKG, each beneficially transferred the inventories of their respective agency businesses to KDC in exchange for respective notes payable upon commencement of the partnership on October 1, 2014. During the quarter, each partner independently operated their respective sales agency for the benefit of the partnership pending the final valuation and transfer of inventory and other assets being vended into KDC (subject to final tax elections, financing arrangements, etc.). Accordingly, the Company has recorded a note payable to TKG as at December 31, 2014 for KDC working capital balances included on the interim condensed statement of financial position.

Accounts receivable	\$ 1,515,203
Inventories	3,033,264
Intangible assets	(1,615,039)
Accounts payables	124,486
Notes payable - partner companies	<u>\$ 3,057,914</u>

Equivalent working capital balances owing by KDC to the Company have been eliminated on consolidation.

SUBSEQUENT EVENTS

The Company entered into two new credit agreements with Meridian Credit Union ("MCU"), its primary lender, in January, 2015, as follows:

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Revised credit agreement for Company dated January 12, 2015

- (a) The operating line decreased from \$13,000,000 to \$10,000,000, interest rate unchanged (prime plus 2.5%). The margin limit for inventory fell from \$11,000,000 to \$8,500,000 at 70% of the value of inventory from 90% previously.
- (b) \$1,500,000 of the prior line of credit was converted to an instalment based non-revolving loan, amortized over 10 years, repayable in equal blended payments of principal and interest of \$16,338, bearing interest at fixed rate of 4.99%, due January 15, 2019. Should the Company issue new shareholder equity exceeding \$3,000,000, MCU is entitled to an immediate lump-sum payment of \$500,000.
- (c) A non-revolving loan of \$1,250,000, \$750,000 of which is to be used for investment in Kirkwood Diamond Canada Partnership and \$500,000 of the prior line of credit converted to a instalment based non-revolving loan, amortized over 30 months, repayable in equal blended payments of principal and interest of \$48,435, bearing interest at a fixed 12%, due by July 15, 2015. Should the Company issue new shareholder equity exceeding \$3,000,000, MCU is entitled to immediate repayment of 100% of the remaining loan balance.
- (d) The security positions granted, margining calculations, reporting requirements and financial covenants are generally unchanged, except that the minimum effective net worth required increased from \$7,000,000 to \$7,500,000.

Credit agreement for Kirkwood Diamond Canada dated January 23, 2015

- (a) Operating line of up to \$3,000,000.
- (b) Payments of interest only, interest at prime plus 2%.
- (c) Credit facility secured by (i) general security agreement, (ii) assignment of fire insurance, (iii) guarantee and postponement of claim from The Kirkwood Group Ltd. in the amount of \$1,500,000 and (iv) inter-creditor amongst concerned parties agreement limiting liability of the Company to \$1,500,000.
- (d) Margining calculations and reporting requirements similar to the Company's own credit facility.
- (e) Financial covenants include maintaining (i) an effective net worth of \$1,500,000, and (ii) an interest coverage ratio of 1.25 | 1.00.

CAPITALIZATION

Diamond can issue an unlimited number of common shares. The Company has common shares and other equity instruments outstanding at each reporting date as follows:

	December 31, 2014	March 31, 2014	Change in period
Common shares	73,403,749	73,403,749	-
Broker warrants	399,973	399,973	-
Stock options	6,682,400	3,132,400	3,550,000
Total equity instruments	80,486,122	76,936,122	3,550,000

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The only change in equity instruments during YTD 2015 was the granting of 3,550,000 options as follows:

- (a) On June 5, 2014, a grant of 500,000 options was made to the Company's new CFO. The options are exercisable at \$0.25 per share with a term of five years and vest as at 25% of the number of options granted on each anniversary date over 4 years.
- (b) Concurrent with the sale and leaseback of the winery, the Company has executed an agreement with Oakwest on November 10, 2014 which will provide financial and operational consulting services over the lease term. In consideration of these services, the Company will pay \$1 per year and has issued 1,400,000 stock options to Oakwest exercisable at \$0.12 per option with a term of five years. The options vested as to 20% immediately and the remainder evenly on each anniversary date over the next 4 years. The Company has also issued 600,000 stock options under the same terms to David Beutel, Chair of its Board of Directors and a Vice President at Oakwest.
- (c) On November 24, 2014, the Board of Directors approved the grant of 1,050,000 options to key management personnel. The shares are exercisable at \$0.11 per share with a term of five years and vest evenly on each anniversary date over 5 years.

STRATEGIC OUTLOOK AND DIRECTION

Diamond is committed to building enduring, high quality beverage alcohol brands that celebrate life and achievement in a socially responsible manner. The Company believes in the development of leading brands that recognize the consumer's interest in wines and spirits, addressing their desire to explore with the many exciting offerings that the Company has available. Vertically integrated, Diamond combines a modern and efficient production facility for Niagara wines with a national marketing agency for its broad portfolio of leading international wines and spirits. The Company is well positioned to add to its throughput of wine production and leverage its national sales force to increase the number of brands under agency without a significant change in its cost structure.

The Canadian wine and spirits market continues to grow strongly, outpacing most consumer categories. Statistics Canada recently reported¹ that in the twelve months ending March 31, 2013, Canadian wine sales increased 4.9% to 506.6 million litres (\$6.8 billion) from 2012. This is equivalent to 17.4 litres per capita, up 4.3 litres since 2003, which is a 33% increase. Sales of spirits were up 2.9% in the same period from the previous year to \$5.4 billion. On a volume basis, it was up 2.7% to 222.4 million litres, or 7.6 litres per capita in 2013.

Diamond will continue to focus on further developing its existing brands of Vintner Quality Alliance ("VQA") certified wines that include Lakeview Cellars, EastDell, Seasons, 20 Bees, Dan Aykroyd, Hat Trick, Fresh and its new International Canadian Blend ("ICB") brand, Riders Valley. The ICB segment represents 73% of wine sold within the Ontario market². This continued focus will include additional investment in marketing, promotion and advertising to insure top of mind awareness and preference for our brands.

Within its portfolio of international brands, the Company's emphasis will be on building awareness, sales and profit for its existing customer base and will continue to identify new brand entrants that the Company can represent within the Canadian market. These will include international wines and spirits from a variety of regions globally with a specific focus on brands that currently do not have distribution within the Canadian marketplace or which are dissatisfied with their current distribution arrangements.

¹ <http://www.statcan.gc.ca/daily-quotidien/140410/dq140410a-eng.htm>

² <http://www.wgao.ca/industry-facts>

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RISKS FACTORS

BUSINESS RISKS

The following risk factors should be carefully considered in evaluating the Company and the industry it operates in. The risks presented below may not be all of the risks that Diamond may face. It is believed that these are the factors that could cause actual results to be different from expected and historical results. New risks may emerge and management may not be able to predict all of them, or be able to predict how they may cause actual results to be different from those contained in any forward-looking statements.

ADDITIONAL FINANCING

Diamond will require additional financing in order to make further investments or take advantage of future opportunities. The ability of Diamond to arrange such financing in the future will depend in part upon prevailing capital market conditions, as well as upon the business success of Diamond. There can be no assurance that Diamond will be successful in its efforts to arrange additional financing on terms satisfactory to Diamond. If additional financing is raised by the issuance of shares or other forms of convertible securities from treasury, control of Diamond may change and shareholders may suffer additional dilution. If adequate funds are not available, or are not available on acceptable terms, Diamond may not be able to take advantage of opportunities, or otherwise respond to competitive pressures and remain in business.

PROFITABILITY

There is no assurance that Diamond will earn profits in the future, or that profitability will be sustained. There is no assurance that future revenues will be sufficient to generate the funds required to continue Diamond's business development and marketing activities. If Diamond does not have sufficient capital to fund its operations, it may be required to reduce its sales and marketing efforts or forego certain business opportunities.

DEPENDENCE ON MANAGEMENT AND KEY PERSONNEL

Diamond will depend on the business and technical expertise of its management team and there is little possibility that this dependence will decrease in the near term. Diamond's success will depend in large measure on certain key personnel. The loss of the services of such key personnel may have a material adverse effect on Diamond's business, financial condition, results of operations and prospects. The contributions of the existing management team to the immediate and near term operations of Diamond are likely to be of central importance. In addition, the competition for qualified personnel in the industry is competitive and there can be no assurance that Diamond will be able to continue to attract and retain all personnel necessary for the development and operation of its business. Investors must rely upon the ability, expertise, judgment, discretion, integrity and good faith of the management of Diamond.

GOVERNMENT REGULATION OF LIQUOR INDUSTRY

Diamond will operate in the highly regulated retail liquor industry in the Province of Ontario and throughout Canada. The Alcohol and Gaming Commission of Ontario (the "AGCO"), the Liquor Control Board of Ontario (the "LCBO") and similar Liquor Boards throughout Canada, may issue decisions, enact rules, new legislation or regulations or may make changes to existing legislation or regulations, all of which can impact the operation of Diamond both favourably and unfavourably. There is no assurance that new legislation or regulations or changes to existing legislation or regulations or decisions of any regulatory bodies in the retail liquor industry in Canada will not adversely affect the operations, profitability, or distributable cash of Diamond.

SIGNIFICANT COMPETITION

The alcoholic beverage industry in Canada is intensely competitive, consisting of many large and small Canadian corporations and international corporations with some possessing extensive experience and financial resources.

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MANAGEMENT OF GROWTH

Diamond may be subject to growth-related risks including capacity constraints and pressure on its internal systems and controls. The ability of Diamond to manage growth effectively will require it to continue to implement and improve its operational and financial systems and to expand, train and manage its employee base. The inability of Diamond to deal with this growth may have a material adverse effect on Diamond's business, financial condition, results of operations and prospects.

ISSUANCE OF DEBT

From time to time, Diamond may enter into transactions to acquire assets or the shares of other organizations or seek to obtain additional working capital. These transactions may be financed in whole or in part with debt, which may increase Diamond's debt levels above industry standards for companies of similar size. Depending on future plans, Diamond may require additional equity and/or debt financing that may not be available or, if available, may not be available on favourable terms to Diamond. The level of Diamond's indebtedness, from time to time, could impair its ability to obtain additional financing on a timely basis to take advantage of business opportunities that may arise.

LABOUR COSTS AND SHORTAGES AND LABOUR RELATIONS

The success of Diamond's business depends on a large number of both hourly and salaried employees. Changes in the general conditions of the employment market could affect the ability of Diamond to hire or retain staff at current wage levels. The occurrence of either of these events could have an adverse effect on Diamond's results of operations. Diamond does not currently have unionized staff but no assurance can be made that some or all of the employees of Diamond will not unionize in the future. If successful, such an occurrence could increase labour costs and thereby have an adverse effect on Diamond's results of operations.

AGRICULTURAL RISK

The production and sale of wine is dependent upon a consistent supply of high-quality grapes available at reasonable prices. Should some or all of the wineries that Diamond works with be unable to produce the quality of grapes necessary to produce wine, such a shortfall in product could adversely affect the operations, profitability, and/or distributable cash of Diamond.

Diamond expects to continue to increase its share of the premium wine business in Canada, principally through the sale of VQA wines, and as a result is more dependent on the quality and supply of domestically grown premium quality grapes. If any of Diamond's vineyards experience certain weather variations, natural disasters, pestilence, other severe environmental problems or other occurrences, Diamond may not be able to secure a sufficient supply of grapes and there could be a decrease in our production of certain products from those regions and/or an increase in costs. In the past, where there was a significant reduction in domestically sourced grapes, the Government of Ontario, in conjunction with the Wine Council of Ontario and the Ontario Grape Growers Marketing Board, agreed to temporarily increase the blending of imported wines, which enables Diamond to continue to supply wines to the market. There is no certainty that such intervention will be available to the same extent in the future, if at all. The inability to secure premium quality grapes could impair the ability of Diamond to supply wines to its customers.

FOREIGN EXCHANGE

Foreign exchange risk exists on the purchases of all agency brand inventories purchased in foreign currencies for British Columbia and Alberta, which are predominately in Euros and Australian dollars. Diamond currently does not enter into foreign exchange contracts.

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ENERGY COSTS

Diamond could experience an increase in energy costs which could result in higher transportation, freight and other operating costs. Diamond's future operating expenses and margins will be dependent on its ability to manage the impact of cost increases. Diamond cannot guarantee that it will be able to pass along increased energy costs to its customers through increased prices.

TAXATION

Canada imposes excise and other taxes on beverage alcohol products in varying amounts which have been subject to change. Significant increases in excise and other taxes on beverage alcohol products could materially and adversely affect Diamond's financial condition or results of operations. In addition, federal and provincial governmental agencies extensively regulate the beverage alcohol products industry concerning such matters as licensing, trade practices, permitted and required labelling, advertising and relations with consumers and retailers. Certain federal and provincial regulations also require warning labels and signage. New or revised regulations or increased licensing fees, requirements or taxes could also have a material adverse effect on Diamond's financial condition or results of operations.

TRADEMARKS

Diamond considers its trademarks, particularly certain brand names and product packaging, advertising and promotion design and artwork to be of significant importance to its business and ascribes a significant value to these intangible assets. Diamond will rely on trademark laws and other arrangements to protect its proprietary rights. There can be no assurance that the steps taken by Diamond to protect its intellectual property rights will preclude competitors from developing confusingly similar brand names or promotional materials. Diamond believes that its proprietary rights do not infringe upon the proprietary rights of third parties, but there can be no assurance in this regard.

IMPORTANCE OF INVENTORY, WAREHOUSE AND DISTRIBUTION SYSTEMS

Diamond's inventory, warehouse and distribution systems are critical components of its operations. Diamond's ability to maintain and upgrade the capabilities of these systems is important to its future performance. If Diamond is unable to maintain the inventory, warehouse and distribution systems or fails to adequately upgrade these systems, Diamond's operations could be adversely affected with the further material adverse effect being on financial results of operations.

WHOLESALE COST INCREASES

Wholesale costs are dependent on a number of factors, including inflation and fuel prices. Any attempt to pass on an increase in wholesale costs to consumers through product price increases could have a material adverse effect on Diamond's sales while a failure to effectively pass any such increases on to consumers could have a material adverse effect on Diamond's result of operations.

DISTRIBUTION BUSINESS

Diamond's business model includes a number of wine and alcohol brands that are represented on an agency basis. There is a risk that such agency brands are sold to an entity that has a pre-existing distribution agency relationship with a provider other than Diamond, and Diamond's revenues and profitability could suffer as result. Furthermore, Diamond's distribution business depends on the ability to retain its current brands as well as attracting additional brands in the future, and a failure to do so could negatively impact revenues and profitability of Diamond.

CREDIT RISK

Credit risk arises from credit exposure to customers through outstanding accounts receivable. The maximum exposure to credit risk is equal to the carrying value of the Company's financial assets. The objective of managing counter-party credit risk is to prevent losses in financial assets. The Company assesses the credit quality of its counter-parties, taking into account their financial position, past experience and other factors. As the large majority of the Company's accounts receivable balances are collectable from government-controlled liquor boards, management believes the Company's credit risk relating to accounts receivable is at an acceptably low level.

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EXPOSURE TO INTEREST RATE FLUCTUATIONS

The Company has a high level of floating rate debt. Interest rate risk exists as an increase in interest rates would increase the Company's overall financing costs and have a material impact on Diamond's financial position over the long term.

ENVIRONMENTAL COMPLIANCE

Environmental liabilities may potentially arise when companies are in the business of manufacturing products and, thus, required to handle potentially hazardous materials. As an owner and lessor of property, the Company is subject to various federal and provincial laws relating to environmental matters. Such laws provide that the Company could be held liable for the cost of removal and remediation of hazardous substances on its properties. Management is of the opinion that the risk of environmental liabilities is considered minimal.

PACKAGING

The Company purchases glass, bag in box and other components used in the bottling and packaging of wine. The largest component in the packaging of wine is glass, of which there are few domestic or international suppliers. Diamond sources glass from various distributors and manufacturers both domestically and internationally to insure an adequate supply. As there is currently only one commercial supplier of glass in Canada, any interruption in supply could have an adverse impact on the Company's ability to supply its markets.

INDUSTRY CONSOLIDATION

In recent years, the global beverage alcohol industry has experienced a significant amount of consolidation. Industry consolidation can have varying degrees of impact and, in some cases, may even create exceptional opportunities. Either way, management believes that the Company is well positioned to deal with this or other changes to the competitive landscape in Canada.

RISKS RELATED TO COMMON SHARE INVESTMENTS

PRICE VOLATILITY OF PUBLICLY TRADED SECURITIES

In recent years, the securities markets in the United States and Canada have experienced a high level of price and volume volatility, and the market prices of securities of many companies have experienced wide fluctuations in price. There can be no assurance that continuing fluctuations in price will not occur. It may be anticipated that any quoted market for Diamond's shares will be subject to market trends generally, notwithstanding any potential success of Diamond in creating revenues, cash flows or earnings. The value of Diamond's shares will be affected by such volatility. A public trading market in the Common Shares having the desired characteristics of depth, liquidity and orderliness depends on the presence in the marketplace of willing buyers and sellers of common shares at any given time, which presence is dependent on the individual decisions of investors over which Diamond has no control. There can be no assurance that an active trading market in securities of Diamond will be established and sustained. The market price for Diamond's securities could be subject to wide fluctuations, which could have an adverse effect on the market price of Diamond. The stock market has, from time to time, experienced extreme price and volume fluctuations, which have often been unrelated to the operating performance, net asset values or prospects of particular companies. If an active public market for Diamond's shares does not develop, the liquidity of a shareholder's investment may be limited and the share price may decline.

DILUTION

Diamond may make future acquisitions or enter into financings or other transactions involving the issuance of securities of Diamond which may be dilutive to the existing shareholders.

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DIVIDENDS

Diamond has not paid any dividends on its outstanding common shares. Any payments of dividends on the common shares of Diamond will be dependent upon the financial requirements to finance future growth, the financial condition of Diamond and other factors which Diamond's board of directors may consider appropriate in the circumstance. It is unlikely that Diamond will pay dividends in the immediate or foreseeable future.

GLOBAL FINANCIAL CRISIS

Recent market events and conditions, including disruptions in the international credit markets and other financial systems and the deterioration of global economic conditions, have caused significant volatility to commodity prices. These conditions worsened in 2008 and continued in 2009, causing a loss of confidence in the broader U.S. and global credit and financial markets and resulting in the collapse of, and government intervention in, major banks, financial institutions and insurers and creating a climate of greater volatility, less liquidity, widening of credit spreads, a lack of price transparency, increased credit losses and tighter credit conditions. Notwithstanding various actions by governments, concerns about the general condition of the capital markets, financial instruments, banks, investment banks, insurers and other financial institutions (including a downgrade of the US sovereign debt credit rating from AAA, by certain credit rating agencies in 2011) caused the broader credit markets to further deteriorate and stock markets to decline substantially. These factors have negatively impacted the ability to raise capital, and sales cycles, will continue to impact the performance of the global economy going forward. If market conditions do not recover in a timely manner, future revenues may be adversely impacted. Volatility in the global financial markets may impact the ability of Diamond to obtain equity or debt financing in the future on terms favourable to Diamond, if at all. If such increased levels of volatility and market turmoil continue, Diamond's operations could be adversely impacted and the trading price of its common shares may be adversely affected.

FINANCIAL MARKET TURMOIL

Global financial market and economic conditions can pose a significant threat to economic growth in almost all sectors and economies, causing a decline in consumer and business confidence, a reduction in credit availability and a dampening in business and household spending.

CRITICAL ACCOUNTING ESTIMATES

The preparation of these unaudited interim condensed consolidated financial statements requires management to make certain estimates, judgments and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and reported amounts of expenses during the reporting period.

Significant assumptions about the future and other sources of estimation uncertainty that management has made at the end of the reporting period, that could result in a material adjustment to the carrying amounts of assets and liabilities, in the event that actual results differ from assumptions made, include, but are not limited to, the following:

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Fair value of biological assets

Determining the fair value of grape vines involves making assumptions about how market participants assign the value of a vineyard between vines, land, and other assets. The fair value of vineyards was determined by comparing reports from accredited appraisers to market values of similar properties and determining the portion of this fair value that was in respect of vines. Changes in the fair value of vines may occur as a result of changes in numerous factors, including, vine health and expected future yields.

To estimate the fair value of vines in the middle and later stages of development, the estimated fair value of mature vines was reduced by the net discounted cash outflows necessary to bring the vines to a fully developed state.

Fair value of grapes at the point of harvest

Where possible, the fair value of grapes at the point of harvest is determined by reference to local market prices for grapes of a similar quality and the same varietal. For grapes for which local market prices are not readily available, the average price of similar grapes is used. The fair value of grapes is included in the cost of bulk wine inventory.

Property, plant and equipment

Property, plant and equipment represent a significant proportion of the asset base of the Company as they amount to 37.6% of total assets as at December 31, 2014 (March 31, 2014 - 46.5%). Therefore, estimates and assumptions made to determine their carrying value and related depreciation are critical to the Company's financial position and performance.

IFRS requires management to test for impairment of property, plant and equipment if events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Impairment testing is an area involving management judgement, requiring assessment as to whether the carrying value of assets can be supported by the net present value of future cash flows derived from such assets using cash flow projections which have been discounted at an appropriate rate.

The charge in respect of periodic depreciation is derived after determining an estimate of an asset's expected useful life and the expected residual value at the end of its life. The useful lives and residual values of the Company's assets are determined by management at the time the asset is acquired and reviewed annually for appropriateness. The lives are based on historical experience with similar assets as well as anticipation of future events which may impact their life

Gross versus net presentation

When deciding the most appropriate basis for presenting revenue or costs of revenue, both the legal form and substance of the agreement between the Company and its business partners are reviewed to determine each party's respective role in the transaction. Where the Company's role in a transaction is that of principal, revenue is recognized on a gross basis. This requires revenue to comprise the gross value of the transaction billed to the customer, after trade discounts, with any related expenditure charged as an operating cost. Where the Company's role in a transaction is that of an agent, revenue is recognized on a net basis with revenue representing the margin earned.