BCFerries

Management's Discussion & Analysis of Financial Condition and Financial Performance

For the three and six months ended September 30, 2014

Dated November 21, 2014

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The following is our discussion and analysis of the financial condition and financial performance for British Columbia Ferry Services Inc. as of, and for the three and six months ended, September 30, 2014. This discussion and analysis should be read in conjunction with our unaudited consolidated financial statements and related notes for the six months ended September 30, 2014 and 2013, and our audited consolidated financial statements and related notes for the years ended March 31, 2014 (fiscal 2014) and March 31, 2013, together with our Management's Discussion & Analysis for fiscal 2014. These documents are available on SEDAR at www.sedar.com and on our investor webpage at http://www.bcferries.com/investors/financial_reports.html.

Except where indicated, all financial information herein is expressed in Canadian dollars and determined on the basis of International Financial Reporting Standards (IFRS).

BUSINESS OVERVIEW

British Columbia Ferry Services Inc. is an independent company providing passenger and vehicle ferry services on the west coast of British Columbia. We operate one of the largest and most complex ferry systems in the world. We provide frequent year-round transportation service with 35 vessels operating on 24 routes out of 47 terminals spread over 1,000 miles of coastline. We also manage ferry transportation service on other remote routes through contracts with independent operators.

Our service is an integral part of British Columbia's coastal transportation system and has been designated by the Province of British Columbia (the Province) as an essential service for purposes of the provincial Labour Relations Code. This designation means our services are considered necessary for the protection of the health, safety and welfare of the residents of British Columbia.

We provide a wide range of ferry services for our customers. During the three months ended September 30, 2014 (the second quarter of fiscal 2015), we provided over 45,000 sailings, compared to 48,000 sailings during the same period in the prior year, carrying 6.9 million passengers and 2.5 million vehicles. In the second quarter of fiscal 2015, vehicle and passenger traffic decreased 0.3% compared to the same quarter in the prior year. On our Major Routes, we experienced a 0.3% increase in both vehicle and passenger traffic compared to the same quarter in the prior year while, on our Northern and regulated Other Routes, we experienced a decrease in both vehicle and passenger traffic. For a discussion of our traffic levels, see "Financial and Operational Overview" below.

Significant events during or subsequent to the second quarter of the year ended March 31, 2015 (fiscal 2015) include the following:

- On July 3, 2014, we entered into contracts with Remontowa Shipbuilding S.A. of Gdansk, Poland to build three new intermediate class vessels. These contracts, with a total value of $165 million, form the majority of the total project budget of $252 million. This budget also includes $51 million for Canadian taxes and federal import duties. These are design-build, fixed price contracts that provide us with substantial guarantees related to delivery dates, performance criteria, cost certainty and quality of construction. The new vessels, scheduled for delivery in August 2016, October 2016 and February 2017, will replace the 49-year old *Queen of Burnaby* and the 50-year old *Queen of Nanaimo*. The third vessel will augment service during the peak and shoulder season and provide relief when other vessels are in refit. The new vessels will be dual-fuel capable, so they can operate on liquefied natural gas (LNG) or marine diesel fuel. (See Outlook – Asset Renewal Program" below for more detail.)

- On September 3, 2014, construction of the cable ferry that will provide service between Buckley Bay and Denman Island commenced at Seaspan's Vancouver Shipyards Co. Ltd. of North Vancouver. The vessel will accommodate 50 vehicles and 150 passengers and crew. The cable ferry is expected to be in service in the summer of 2015. (See "Outlook - Asset Renewal Program" below for more detail.)

- On September 22, 2014, we submitted an application to the British Columbia Ferries Commissioner (the Commissioner) for approval to proceed with mid-life upgrades, including conversion to dual fuel, of our two largest vessels, the *Spirit of Vancouver Island* and the *Spirit of British Columbia.* If the application is approved, we expect the conversion and hull modifications will result in significant savings. The *Spirit of Vancouver Island*'s mid-life upgrade is planned to be complete in the spring of 2017 and the *Spirit of British Columbia's* mid-life upgrade in the spring of 2018. We expect a ruling from the Commissioner during the third quarter of fiscal 2015. (See "Outlook - Asset Renewal Program" below for more detail.)

- On September 29, 2014, the Commissioner issued Order 14-02 approving our 12-year capital plan for inclusion with the other information to be submitted under section 40 of the *Coastal Ferry Act* (the Act). On September 30, 2014, we filed with the Commissioner the remaining documents including our efficiency plan and our submission for the fourth performance term. This begins the process of price cap setting by the Commissioner and negotiations with the Province regarding changes in core service levels and related ferry transportation fees for the period April 1, 2016 through March 31, 2020. The efficiency plan focused on four strategies, comprising the use of LNG, business transformation strategies enabled by technology, a strategy for the Southern Gulf Islands and a strategy for the Major Routes. The major catalyst for the Major Routes Strategy was the estimated capital investment of $1.1 billion on the Major Routes, including over $200 million in terminal infrastructure at the Horseshoe Bay terminal, that will be required over the next 10 years. On November 5, 2014, the provincial government announced that it would not support options relating to the strategy for the Major Routes.

The Effect of Rate Regulation

We are regulated by the Commissioner to ensure, among other things, that our tariffs are fair and reasonable. Under the terms of the Act, the tariffs we charge our customers over a performance term are subject to price caps set by the Commissioner. The Commissioner may, under certain circumstances, allow increases in price caps over the set levels. Certain decisions and orders of the Commissioner may give rise to assets or liabilities. Regulatory assets generally represent incurred costs that are probable of future recovery in tariffs or fuel surcharges. Regulatory liabilities represent obligations to customers which will be settled through future tariff reductions or fuel rebates.

IFRS has an interim standard that addresses accounting for rate-regulated activities; however it does not apply to entities that have already transitioned to IFRS, as we have. As a result, we are not permitted to recognize in our financial statements the assets and liabilities that result from the regulated price cap setting process, such as our deferred fuel cost accounts. Rather than being charged to regulatory asset accounts on our Statements of Financial Position, fuel surcharges collected or rebates granted are included in revenue, and increases or decreases in fuel prices from those approved in price caps are included in operating expenses. These items are treated as assets and liabilities for regulatory purposes.

We continually assess whether our regulatory assets are probable of future recovery by considering such factors as applicable regulatory changes. We believe the regulatory assets at September 30, 2014 are probable of future recovery. These regulatory assets are detailed in note 10 to our September 30, 2014 unaudited consolidated financial statements.

If IFRS permitted us to report regulatory assets and liabilities in our financial statements, the effect on our Statements of Comprehensive Income for the three and six months ended September 30, 2014 and 2013 would be as follows:

($ millions)		**Three months ended September 30**		**Six months ended September 30**	
		2014	**2013**	**2014**	**2013**
Total comprehensive income		73.5	64.4	85.0	68.7
Changes in net earnings:					
Regulatory asset or liability	**Statement line item**				
Deferred fuel costs (a)					
Fuel costs incurred	Operations expense	4.7	3.9	8.7	6.6
Fuel surcharges collected	Fuel surcharge revenue	(5.8)	-	(10.2)	-
Payments from the Province	Ferry transportation fees	(1.0)	(0.7)	(1.7)	(1.3)
		(2.1)	3.2	(3.2)	5.3
Tariffs in excess of price cap (b)					
Obligation settled (incurred) during the period	Tariff revenue	-	0.5	-	(2.2)
(Decrease) increase in total net earnings		(2.1)	3.7	(3.2)	3.1
Adjusted total comprehensive income		71.4	68.1	81.8	71.8

(a) Deferred fuel costs: As prescribed by regulatory order, we defer differences between actual fuel costs and approved fuel costs which were used to develop the regulated price caps. The difference between actual fuel costs and approved fuel costs (including fuel hedge gains and losses) is deferred for settlement in future tariffs. Also, as prescribed by regulatory order, we collect fuel surcharges or provide fuel rebates from time to time which are applied against deferred fuel cost account balances. We may also receive payments from the Province to be applied against deferred fuel cost account balances.

(b) Tariffs in excess of price cap: The Act contains provisions which ensure that, if tariffs we charge exceed established price caps, the excess amounts collected will be returned to customers through future tariffs. Tariffs charged did not exceed price caps at September 30, 2014.

FINANCIAL AND OPERATIONAL OVERVIEW

This section provides an overview of our financial and operational performance for the three and six months ended September 30, 2014 and 2013.

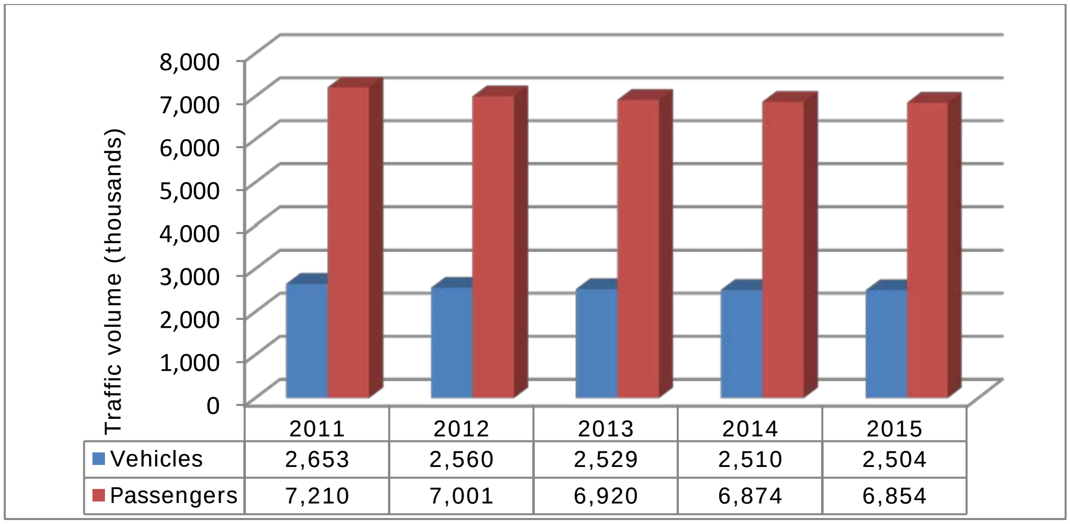
($ millions)	Three months ended September 30			Six months ended September 30		
	2014	**2013**	**Variance**	**2014**	**2013**	**Variance**
Total revenue	284.2	271.5	12.7	497.3	471.4	25.9
Operating expenses	192.6	189.2	(3.4)	375.1	368.0	(7.1)
Operating profit	91.6	82.3	9.3	122.2	103.4	18.8
Net finance and other	15.2	18.0	2.8	31.9	34.8	2.9
Net earnings	76.4	64.3	12.1	90.3	68.6	21.7
Other comprehensive (loss) income	(2.9)	0.1	(3.0)	(5.3)	0.1	(5.4)
Total comprehensive income	73.5	64.4	9.1	85.0	68.7	16.3

Our net earnings in the three months ended September 30, 2014 were $12.1 million ($21.7 million year-to-date) higher and total comprehensive income was $9.1 million ($16.3 million year-to-date) higher than in the same periods of the prior year. Net earnings for the first and second quarters of fiscal 2015 reflect the effects of increased fares, higher ferry transportation fees, fuel surcharges and lower financing costs, partially offset by lower social program fees and operating cost increases. Other comprehensive loss for the three and six months ended September 30, 2014 reflects a $2.4 million loss on interest rate forward contracts related to our April 28, 2014 issuance of $200 million of senior secured bonds in the first quarter of fiscal 2015. (See "Liquidity and Capital Resources" below for more detail.) In the second quarter of fiscal 2015, we incurred a $2.9 million loss reflecting the actuarial valuation of our retirement and death benefit plans. The main driver of the increase in the liability was a lower employee turnover rate than previously estimated.

Vehicle traffic was 0.3% lower in both the three and six months ended September 30, 2014, compared to the same periods in the prior year. Passenger traffic was 0.3% higher in the first quarter of fiscal 2015 but 0.3% lower in the second quarter, resulting in year-to-date passenger traffic levels which are the same as in the prior year. Both vehicle and passenger traffic on our Major Routes increased in the quarter and year-to-date, while on our Northern and regulated Other Routes vehicle and passenger traffic declined in both the quarter and year-to-date. Overall, commercial traffic increased 1.2% in the quarter (0.3% decrease year-to-date) compared to the same periods in the prior year, while drop-trailer traffic, a component of commercial traffic, increased 6.7% (5.5% year-to-date).

Traffic was negatively impacted primarily by a reduction in seniors travel related to the lower BC seniors fare discount on the Major and regulated Other Routes effective April 1, 2014 and the reduction in student travel as a result of the recent teacher's labour dispute.

The following graph illustrates our vehicle and passenger traffic levels for the second quarter of fiscal 2011 through fiscal 2015:



	2011	2012	2013	2014	2015
Vehicles	2,653	2,560	2,529	2,510	2,504
Passengers	7,210	7,001	6,920	6,874	6,854

Safety and Security

Safety continues to be a primary focus. We have implemented several new initiatives to continue the safety improvement momentum that has occurred since the launch of SailSafe safety program, seven years ago. A recent initiative is our Health & Wellness Program which was trialled during the summer and is now being implemented across the company. The goal of this program is to create healthier and more resilient employees in order to reduce employee injuries and absenteeism.

The annual SailSafe Town Hall meetings have been planned and include some significant changes from past years, all designed to increase the level of employee engagement. Up to 500 employees are expected to attend these important safety sessions where, along with the introduction of the new Health & Wellness initiative, the new Safety Management System brochure explaining key improvements to our risk management processes will be rolled out. Along with the ongoing vessel based exercises to test emergency preparedness, we continue to deploy subject matter experts into the field to conduct audits to verify compliance with applicable international and domestic requirements and legislation.

Security is also a priority and several new initiatives have been launched in light of the changing national and international security environment. Overall, in response to guidance from Transport Canada, we have increased our vigilance for the potential of security threats, through improved employee security training and increased communication with all employees. All security plans have been reviewed and several new security policies have been issued in light of the changing security landscape. Our security personnel have regular contact with government security agencies in order to ensure that we have the most up to date information so that we can ensure the safety of the travelling public and our employees.

Training
Each year we invest heavily in operational and safety training.

In the second quarter, we conducted 1,000 days of operational training, 600 days more than usual, however by March 31, 2015, we expect operational training to be at a similar level to the prior year. We also expanded several safety programs and created additional resource material. Vehicle firefighting training updates were completed and a trial firefighting course is planned for the third quarter.

In the second quarter, our Standardized Education and Assessment (SEA) training focused on completing the training for new and returning seasonal employees. Progress continued on the development of new job categories and development of training requirements for the upcoming new vessels and major vessel upgrades, including training related to LNG. Discussions are underway with the British Columbia Institute of Technology, various educational agencies, industry and Transport Canada to ensure that we have the requisite LNG training programs in place by the fall of 2015.

By the end of September 2014, through the simulation training centre (STC) [formally Bridge Team Simulation], we had delivered Bridge Operations Skills and Systems (BOSS) Level 1 training to 89% and BOSS Level 2 training to 34% of deck officers in the fleet. We expect that all deck officers will have completed BOSS Level 1 training by the end of fiscal 2015. Curriculum development, focusing on decision making, is currently underway for BOSS Level 3 training.

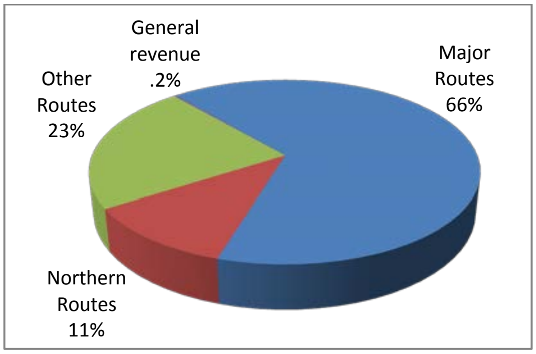
We also developed a STC pilot program to support SEA training by providing situational training on the bridge simulator to better equip our deck officers to handle navigational challenges on routes they are unfamiliar with. Further integration of STC within the SEA program is being explored, beginning with familiarization with our Northern Routes.

We are preparing for facility and program accreditation with DNV GL, one of the leading classification societies and a global leader in maritime education and training accreditation. Achievement of this accreditation will allow us to provide training to external parties.

Collective agreement
The BC Ferry & Marine Workers' Union (Union) submitted a grievance relative to the new Family Day statutory holiday first observed in February 2013. The Union's contention is that the Company is not correctly applying the Collective Agreement in the compensation of employees for this new statutory holiday. Our position is the Collective Agreement language is being correctly applied regarding the Family Day holiday and that no further amendments to employees' pay are required. The matter was submitted to arbitration for resolution and final arguments were heard on October 29, 2014. We are currently awaiting a decision.

Revenue

The following discussion of revenue is based on IFRS results, with reference to the impacts of rate regulation.



In the six months ended September 30, 2014, the greatest portion of our revenues (66%) was earned on our Major Routes. Revenue from the Northern Routes contributed 11% and Other Routes contributed 23%.

Selected operational statistics and total revenues for the three and six months ended September 30, 2014 compared to the same periods in the prior year are shown in the tables below.

	Three months ended September 30		Six months ended September 30	
Operational Statistics	**2014**	**2013**	**2014**	**2013**
Vehicle traffic	2,503,691	2,510,390	4,455,903	4,470,015
Passenger traffic	6,853,595	6,873,948	11,850,830	11,854,135
On-time performance	86.4%	86.9%	88.6%	88.8%
Number of round trips	20,544	22,002	40,234	42,957
Capacity provided (AEQs)	4,687,652	4,833,141	8,938,182	9,217,245
AEQs carried	2,817,724	2,820,471	5,045,174	5,057,875
Capacity utilization	60.1%	58.4%	56.4%	54.9%

In the three and six months ended September 30, 2014, vehicle traffic decreased 0.3% compared to the same periods in the prior year. In the three months ended September 30, 2014, passenger traffic decreased 0.3%, bringing the year-to-date total to the same level as in the prior year. Both vehicle and passenger traffic on our Major Routes increased in the quarter and year-to-date, while on our Northern and regulated Other Routes vehicle and passenger traffic declined in both the quarter and year-to-date.

On-time performance on the Major and regulated Other Routes is defined as the percentage of our sailings departing within 10 minutes of the scheduled time. On-time performance on the Northern Routes is defined as the percentage of our sailings arriving within 10 minutes of the scheduled time. On-time performance can be impacted by delays due to weather, vessel substitution, terminal dock maintenance or closures and periods of unusually high traffic demand. Meeting customer service expectations is an important factor in our focus on on-time performance.

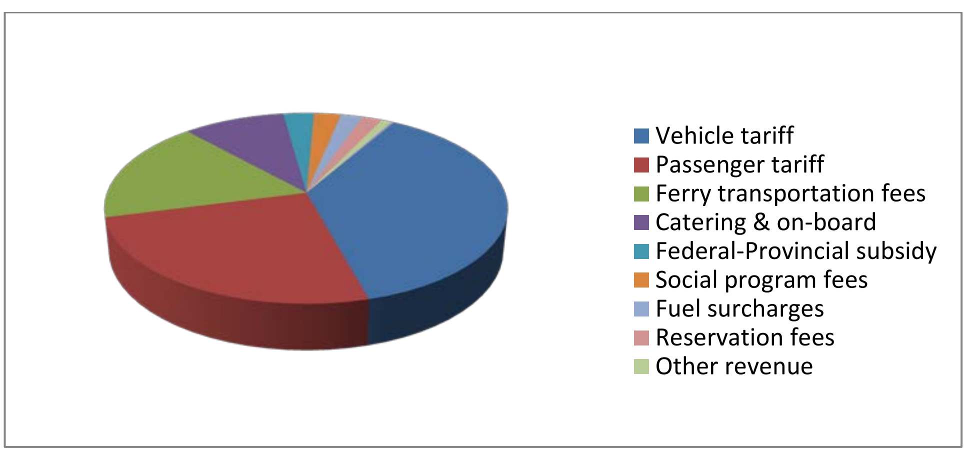
Capacity provided, measured in automobile equivalents (AEQs), is the available space on the vessel multiplied by the number of round trips. Round trips normally stay fairly stable as the Coastal Ferry Services Contract (CFSC) stipulates, among other things, the number of round trips to be provided for each regulated ferry service route. However, the number of round trips provided can be impacted by cancellations due to weather, vessel substitution, terminal dock closures and extra round trips made, or by changes to the number of trips stipulated by the CFSC.

The reduction in round trips and the resulting decrease in capacity provided in the three and six months ended September 30, 2014 compared to the same periods in the prior year was due to the discontinuation of the Discovery Coast Passage Route servicing the mid-coast and replacement with supplementary service, as well as new schedules related to service reductions on our Northern and regulated Other Routes.

An AEQ is a standard unit of measure for an approximation of one car length. AEQs are calculated by using a conversion factor for each vehicle type. For example, a passenger vehicle would be one AEQ while a bus would be three AEQs. The change in AEQs from one period to the next may not be proportionate to the change in vehicle traffic due to variations in the types of vehicles carried.

Capacity utilization is calculated by dividing the AEQ capacity provided on the vessels by the AEQs carried during the period. Capacity utilization is impacted by the number of vehicles carried, the mix of vehicle types (the relative number of buses, commercial vehicles, and passenger vehicles), the size of the vessels utilized and the number of round trips in each period. Utilization in the three and six months ended September 30, 2014 increased compared to the same periods of the prior year as a result of reduced total capacity provided due to fewer round trips, partly offset by a lower number of AEQs carried.

Revenue ($ millions)	**Three months ended September 30**			**Six months ended September 30**		
	2014	**2013**	**Increase (Decrease)**	**2014**	**2013**	**Increase (Decrease)**
Direct Route Revenue						
Vehicle tariff	105.7	103.1	2.6	186.0	181.2	4.8
Passenger tariff	73.9	68.1	5.8	125.0	114.3	10.7
Fuel surcharges	5.8	-	5.8	10.2	-	10.2
Catering & on-board	28.0	27.5	0.5	47.4	46.7	0.7
Social program fees	6.3	8.7	(2.4)	12.6	17.2	(4.6)
Reservation fees	6.1	5.7	0.4	9.5	8.7	0.8
Other revenue	2.6	2.3	0.3	4.6	4.2	0.4
Total Direct Route Revenue	228.4	215.4	13.0	395.3	372.3	23.0
Indirect Route Revenue						
Ferry transportation fees	47.9	48.5	(0.6)	86.6	84.0	2.6
Federal-Provincial subsidy	7.1	7.1	-	14.2	14.2	-
Total Route Revenue	283.4	271.0	12.4	496.1	470.5	25.6
Other general revenue	0.8	0.5	0.3	1.2	0.9	0.3
Total Revenue	284.2	271.5	12.7	497.3	471.4	25.9



Our largest revenue source is vehicle and passenger tariffs. Our year over year tariff revenues may be impacted by such things as changes in overall traffic levels, approved price caps, the proportion of total traffic on routes with higher versus lower tariffs, and the implementation of promotional fare programs.

On April 1, 2014, we implemented average tariff increases in accordance with the Commissioner's Order 12-02 dated September 30, 2012. Tariff increases were 4.2% on average on our Major and regulated Other Routes. On the Northern Routes, we increased tariffs by less than 2% on average and eliminated the incremental tariff for over-height vehicles. These increases are directly associated with increased operating costs, notably fuel, capital replacement and labour. Also, on April 1, 2014, we implemented the Province's decision to reduce the passenger fare discount for BC seniors travelling Mondays to Thursdays from 100% to 50% on the Major and regulated Other Routes.

Effective April 1, 2014, the CFSC was amended to establish the maximum annual amount payable by the Province in respect of senior discounts for fiscal 2015 and fiscal 2016 at $18.0 million and $19.3 million, respectively. These amounts reflect an estimate of what the Province would have paid if there had been no change in the level of senior discounts. To the extent these funds are not required for the reimbursement of discounts provided seniors under the amended policy, the excess will be directed to the ferry transportation fees. These amounts are to be allocated to the regulated Northern and Other Routes. Since the implementation of this policy change, travel by BC seniors Mondays through Thursdays is down 13% from the same period in the prior year.

Surcharges and/or rebates are implemented as a direct result of rising and declining fuel prices. On January 17, 2014, due to the high cost of diesel fuel, we implemented a fuel surcharge of 3.5% on average on our Major Routes and our regulated Other Routes. At the time of the general rate increase on April 1, 2014, no changes were made to the nominal values of the fuel surcharges. Accordingly, these fuel surcharges average 3.4% of the current tariff. For the purpose of rate regulation, these amounts are applied to our deferred fuel cost accounts. No surcharges were put in place on our Northern Routes and no surcharges were in place in the first two quarters of fiscal 2014 on any of our regulated routes. (See "The Effect of Rate Regulation" above for more detail.)

From time to time, we utilize promotional fares designed to stimulate growth in traffic or direct traffic towards our less busy sailings while ensuring compliance with approved price cap orders. In calculating the price cap, vehicle and passenger tariffs, as well as reservation fees, are combined. The utilization of promotional fare incentives may cause the average vehicle and passenger tariff rate to be under or over the allowed increase in any one period.

Year to year changes in operational statistics and revenue for the three and six months ended September 30, 2014 and 2013 for the Major, Northern and Other Routes are discussed separately below.

Major Routes

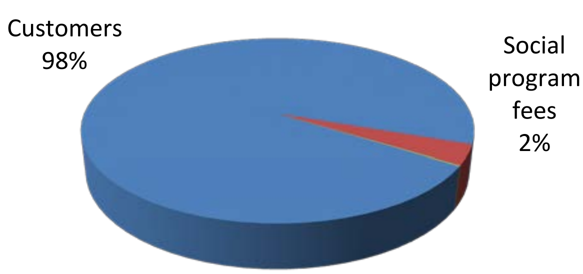
Our Major Routes consist of three regulated routes connecting Metro Vancouver with mid and southern Vancouver Island and our regulated route connecting Horseshoe Bay and Langdale. These are our four busiest routes, carrying more than 60% of our vehicle traffic and more than 65% of our passenger traffic during the three and six months ended September 30, 2014 and 2013.

	Three months ended September 30		Six months ended September 30	
Operational Statistics	**2014**	**2013**	**2014**	**2013**
Vehicle traffic	1,533,269	1,528,944	2,698,704	2,684,415
Passenger traffic	4,543,676	4,530,573	7,774,449	7,708,184
On-time performance	77.3%	78.3%	79.5%	78.9%
Number of round trips	3,665	3,661	6,788	6,783
Capacity provided (AEQs)	2,623,596	2,619,638	4,877,482	4,871,424
AEQs carried	1,780,744	1,773,950	3,165,651	3,151,966
Capacity utilization	67.9%	67.7%	64.9%	64.7%

In the three months ended September 30, 2014, vehicle traffic increased 0.3% (0.5% year-to-date) and passenger traffic increased 0.3% (0.9% year-to-date) compared to the same period in the prior year. Overall, commercial traffic decreased 0.1% in the quarter (1.1% year-to-date), while drop-trailer traffic, a component of total commercial traffic, increased 6.7% in the quarter (5.5% year-to-date).

In the three months ended September 30, 2014, on-time performance was 1% lower than the same period in the prior year as a result of heavy foot traffic on our route connecting Horseshoe Bay and Langdale. The 0.6% improvement year-to-date was mainly a result of significant maintenance activities in the first six months of the prior year at our Horseshoe Bay and Langdale terminals, resulting in berth closures and other conditions negatively impacting arrivals and departures.

Utilization on these routes during the three and six months ended September 30, 2014 was marginally higher compared to the same periods in the prior year as a result of a higher number of AEQs carried, mainly offset by increased capacity.



In the six months ended September 30, 2014, revenue from our Major Routes consisted of 98% from customers and 2% from the Province.

Major Routes cont'd

Revenue ($ thousands)	**Three months ended September 30**			**Six months ended September 30**		
	2014	**2013**	**Increase (Decrease)**	**2014**	**2013**	**Increase (Decrease)**
Direct Route Revenue						
Vehicle tariff	87,103	84,329	2,774	154,493	149,651	4,842
Passenger tariff	58,724	53,713	5,011	100,417	91,116	9,301
Fuel surcharges	4,846	-	4,846	8,499	-	8,499
Catering & on-board	24,708	24,273	435	42,403	41,622	781
Social program fees	3,516	5,438	(1,922)	7,179	10,653	(3,474)
Reservation fees	5,994	5,627	367	9,328	8,513	815
Parking	1,456	1,339	117	2,526	2,356	170
Other revenue	915	848	67	1,772	1,705	67
Total Direct Route Revenue	187,262	175,567	11,695	326,617	305,616	21,001
Indirect Route Revenue						
Ferry transportation fees	249	261	(12)	499	522	(23)
Total Route Revenue	187,511	175,828	11,683	327,116	306,138	20,978

Average tariff ($)	**Three months ended September 30**			**Six months ended September 30**		
	2014	**2013**	**Increase**	**2014**	**2013**	**Increase**
Vehicle tariff ($000's)	87,103	84,329		154,493	149,651	
Vehicle traffic	1,533,269	1,528,944		2,698,704	2,684,415	
Average tariff per vehicle	56.81	55.16	1.65	57.25	55.75	1.50
Passenger tariff ($000'S)	58,724	53,713		100,417	91,116	
Passenger traffic	4,543,676	4,530,573		7,774,449	7,708,184	
Average tariff per passenger	12.92	11.85	1.07	12.92	11.82	1.10

In the three months ended September 30, 2014, average tariff revenue per vehicle increased $1.65 or 3.0% ($1.50 or 2.7% year-to-date) compared to the same periods in the prior year. In the three months ended September 30, 2014, average tariff revenue per passenger increased $1.07 or 9.0% ($1.10 or 9.3% year-to-date). The increase in average tariff revenues reflects the price cap increases authorized by the Commissioner. The average tariff revenue per passenger also reflects the Province's reduction made to BC Senior discounts resulting in seniors now paying a portion of their fares. The increase in both traffic and average fares during the second quarter of fiscal 2015 resulted in a tariff revenue increase of $7.8 million ($14.1 million year-to-date).

On January 17, 2014, due to the high cost of diesel fuel, we implemented fuel surcharges of 3.5% on our Major Routes. No surcharges were in place in the first two quarters of fiscal 2014. For regulatory purposes, these amounts are applied to our deferred fuel cost accounts. (See "The Effect of Rate Regulation" above for more detail.)

All vessels that provide service on our Major Routes have a gift shop and options for food service. In the three months ended September 30, 2014, catering and on-board sales increased 1.8% (1.9% year-to-date) compared to the same periods in the prior year as a result of both higher passenger traffic and higher average sales per passenger. Food sales remain strong, providing approximately 75% of the total catering and on-board revenue. Sales of quality apparel continue to grow and now comprise over 10% of total catering and on-board revenue.

Major Routes cont'd

Social program fees are reimbursements from the Province of discounts provided on fares for BC seniors, students travelling to and from school, persons with disabilities and persons travelling under the Ministry of Health Travel Assistance Program (MTAP). On April 1, 2014, we implemented the Province's decision to reduce the passenger fare discount for BC seniors travelling Mondays to Thursdays from 100% to 50%. Since this reduction, 18% fewer seniors used the program in the three months ended September 30, 2014 (16% year-to-date) compared to the same periods in the prior year. The $1.9 million ($3.5 million year-to-date) reduction in social program fees consists of a $2.1 million ($3.8 million year-to-date) reduction in social program fees as a result of fewer seniors travelling, offset somewhat by an increase in the number of people using the MTAP program and higher fares.

Reservation fees increased primarily as a result of higher usage and higher traffic.

Revenue from parking increased as a result of higher usage of our parking facilities.

Ferry transportation fees represent funds received from the Province related to the import duty remission on one of our foreign-built vessels. These funds reduce over time as the vessel depreciates. For the purpose of rate regulation, this amount is applied to our deferred fuel cost accounts. (See "The Effect of Rate Regulation" above for more detail.)

Northern Routes

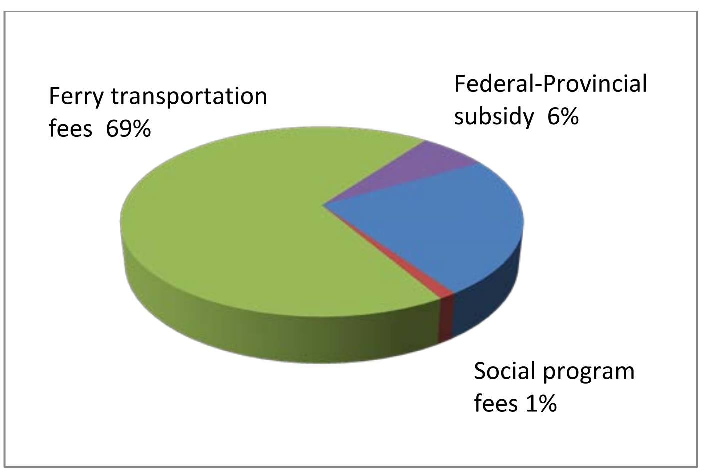
Our Northern Routes consisted of three regulated routes operating on the British Columbia coast north of Port Hardy on Vancouver Island. An amendment to the CFSC, effective April 1, 2014, discontinued the Discovery Coast Passage Route with direct service to the mid-coast from Port Hardy that provided service for three months during the summer peak season. This route was replaced with an extension of one of our other Northern Routes to the mid-coast, which now provides a supplemental indirect service with a much smaller vessel.

	Three months ended September 30		Six months ended September 30	
Operational Statistics	**2014**	**2013**	**2014**	**2013**
Vehicle traffic	12,216	13,108	18,311	19,691
Passenger traffic	37,725	39,763	54,125	57,861
On-time performance	90.4%	95.7%	89.9%	93.4%
Number of round trips	92.5	147.5	147.5	233
Capacity provided (AEQs)	25,256	33,695	38,898	53,392
AEQs carried	14,437	15,317	22,158	23,472
Capacity utilization	57.2%	45.5%	57.0%	44.0%

In the three months ended September 30, 2014, vehicle traffic decreased 6.8% (7.0% year-to-date) and passenger traffic decreased 5.1% (6.5% year-to-date) compared to the same periods in the prior year. We believe this is partially due to changes in route schedules and the discontinuation of the Discovery Coast Passage route and replacement with supplementary service. These service adjustments introduced by the Province have generated savings in fuel and labour that more than offset the decline in revenue as a result of lower traffic levels.

On-time performance in the three and six months ended September 30, 2014 was lower than the same periods in the prior year, mainly as a result of the discontinuation of the Discovery Coast Passage route to the mid-coast that had very high on-time performance.

Capacity utilization on these routes during the three and six months ended September 30, 2014 was significantly higher than the same periods in the prior year as a result of decreased capacity provided due to a reduction in the number of round trips and the replacement with a smaller vessel for service to the mid-coast partially offset by the lower number of AEQs carried.



In the six months ended September 30, 2014, revenue from our Northern Routes consisted of 24% from customers and 76% from the Province (1% social program fees, 69% ferry transportation fees, and 6% from payments under the Federal-Provincial subsidy agreement).

Northern Routes cont'd

Revenue ($ thousands)	Three months ended September 30			Six months ended September 30		
	2014	**2013**	**Increase (Decrease)**	**2014**	**2013**	**Increase (Decrease)**
Direct Route Revenue						
Vehicle tariff	3,640	4,168	(528)	5,470	6,117	(647)
Passenger tariff	3,824	4,133	(309)	5,162	5,654	(492)
Catering & on-board	1,112	1,241	(129)	1,518	1,687	(169)
Social program fees	393	413	(20)	672	745	(73)
Stateroom rental	561	463	98	883	767	116
Hostling & other	97	77	20	136	142	(6)
Total Direct Route Revenue	9,627	10,495	(868)	13,841	15,112	(1,271)
Indirect Route Revenue						
Ferry transportation fees	23,526	24,501	(975)	38,227	38,843	(616)
Federal-Provincial subsidy	1,819	1,820	(1)	3,638	3,640	(2)
Total Route Revenue	34,972	36,816	(1,844)	55,706	57,595	(1,889)

Average tariff ($)	Three months ended September 30			Six months ended September 30		
	2014	**2013**	**Decrease**	**2014**	**2013**	**Decrease**
Vehicle tariff ($000's)	3,640	4,168		5,470	6,117	
Vehicle traffic	12,216	13,108		18,311	19,691	
Average tariff per vehicle	297.97	317.97	20.00	298.73	310.65	11.92
Passenger tariff ($000'S)	3,824	4,133		5,162	5,654	
Passenger traffic	37,725	39,763		54,125	57,861	
Average tariff per passenger	101.36	103.94	2.58	95.37	97.72	2.35

In the three months ended September 30, 2014, average tariff revenue per vehicle decreased $20.00 or 6.3% ($11.92 or 3.8% year-to-date) compared to the same periods in the prior year. Average tariff revenue per passenger during the same period decreased $2.58 or 2.5% ($2.35 or 2.4% year-to-date). Average tariff revenues reflect the price cap increases implemented April 1, 2014. We believe the reduction in average tariff is partially due to a higher proportionate share of traffic paying a reduced rate. The reduction in traffic levels and decreases in average fares resulted in a total tariff revenue decrease of $0.8 million ($1.1 million year-to-date).

There were no fuel surcharges or rebates in place on our Northern Routes during these periods.

Reimbursements from the Province for social program fees decreased primarily as a result of lower usage of the MTAP program and fewer seniors travelling, partially offset by higher fares. No changes were made to the social program discounts for BC seniors on the Northern Routes.

Revenue from catering and on-board services decreased in the quarter and year-to-date compared to the same periods in the prior year as a result of lower passenger levels, partially offset by higher average sales per passenger.

Stateroom rental increased mainly due to higher usage.

Hostling and other revenues increased in the three months ended September 30, 2014, mainly due to higher usage of parking, hostling and reservation services.

Northern Routes cont'd

Ferry transportation fees received from the Province decreased $1.0 million in the quarter ($0.6 million year-to-date) compared to the same periods in the prior year as a result of the following:

- $2.0 million ($2.7 million year-to-date) reduction as a result of a lower percentage of total ferry transportation fees being allocated to the Northern Routes due to the elimination of one of the routes, partially offset by an overall increase in fees received under the CFSC; partially offset by:
- $0.7 million ($1.6 million year-to-date) increase in ferry transportation fees in respect of senior discounts; and
- $0.3 million ($0.5 million year-to-date) increase in fees related to the price of fuel. For regulatory purposes, the amounts received relating to the price of fuel are applied to our deferred fuel cost accounts (see "The Effect of Rate Regulation" above for more detail).

The Federal-Provincial subsidy has decreased marginally by the change in the annual Consumer Price Index (CPI) (Vancouver).

Other Routes

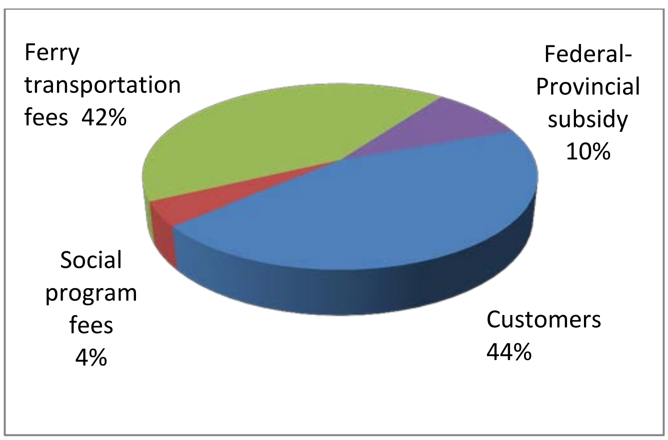
Our Other Routes consist of 18 regulated routes and eight small unregulated routes primarily serving the northern and southern Gulf Islands and the northern Sunshine Coast. One of the regulated routes and all of the unregulated routes are operated under contract by alternative service providers. We receive fees from the Province for the provision of contracted services on these routes, which are included in the ferry transportation fees in the table below.

	Three months ended September 30		Six months ended September 30	
Operational Statistics[1]	**2014**	**2013**	**2014**	**2013**
Vehicle traffic	958,206	968,338	1,738,888	1,765,909
Passenger traffic	2,272,194	2,303,612	4,022,256	4,088,090
On-time performance	88.2%	88.4%	90.3%	90.4%
Number of round trips	16,786.5	18,194	33,298	35,941
Capacity provided (AEQs)	2,038,800	2,179,808	4,021,802	4,292,429
AEQs carried	1,022,543	1,031,204	1,857,367	1,882,437
Capacity utilization	50.2%	47.3%	46.2%	43.9%

In the three months ended September 30, 2014, vehicle traffic decreased 1.0% (1.5% year-to-date) and passenger traffic decreased 1.4% (1.6% year-to-date) compared to the same periods in the prior year. We believe this is mainly due to lower student travel as a result of the teachers' labour dispute and lower senior travel Mondays through Thursdays as a result of the reductions made to BC senior discounts.

On-time performance in the three and six months ended September 30, 2014 was at a similar level to the same periods in the prior year.

Capacity utilization in the three and six months ended September 30, 2014 increased compared to the same periods in the prior year as a result of decreased capacity provided due to a reduction in the number of round trips, partially offset by the lower number of AEQs carried.



In the six months ended September 30, 2014, revenue from our Other Routes consisted of 44% from customers and 56% from the Province (4% social program fees, 42% ferry transportation fees, and 10% from payments under the Federal-Provincial subsidy agreement).

[1] The statistics provided exclude the unregulated routes

Other Routes cont'd

Revenue ($ thousands)	Three months ended September 30			Six months ended September 30		
	2014	**2013**	**Increase (Decrease)**	**2014**	**2013**	**Increase (Decrease)**
Direct Route Revenue						
Vehicle tariff	14,979	14,539	440	26,042	25,454	588
Passenger tariff	11,371	10,279	1,092	19,429	17,553	1,876
Fuel surcharges	940	-	940	1,649	-	1,649
Social program fees	2,364	2,816	(452)	4,768	5,774	(1,006)
Catering & on-board	1,585	1,563	22	2,605	2,587	18
Reservation fees	112	96	16	170	144	26
Parking & other	158	37	121	201	63	138
Total Direct Route Revenue	31,509	29,330	2,179	54,864	51,575	3,289
Indirect Route Revenue						
Ferry transportation fees	24,146	23,690	456	47,896	44,642	3,254
Federal-Provincial subsidy	5,270	5,273	(3)	10,540	10,546	(6)
Total Route Revenue	60,925	58,293	2,632	113,300	106,763	6,537

Average tariff ($)	Three months ended September 30			Six months ended September 30		
	2014	**2013**	**Increase**	**2014**	**2013**	**Increase**
Vehicle tariff ($000's)	14,979	14,539		26,042	25,454	
Vehicle traffic	958,206	968,338		1,738,888	1,765,909	
Average tariff per vehicle	15.63	15.01	0.62	14.98	14.42	0.56
Passenger tariff ($000'S)	11,371	10,279		19,429	17,553	
Passenger traffic	2,272,194	2,303,612		4,022,256	4,088,090	
Average tariff per passenger	5.00	4.46	0.54	4.83	4.29	0.54

In the three months ended September 30, 2014, average tariff revenue per vehicle increased $0.62 or 4.1% ($0.56 or 3.9% year-to-date) compared to the same periods in the prior year. Average tariff revenue per passenger during the same period increased $0.54 or 12.2% ($0.54 or 12.5% year-to-date). The increase in average tariff revenues reflects the price cap increases authorized by the Commissioner, the Province's reduction of the passenger fare discount for BC Seniors travelling Monday to Thursday from 100% to 50%, resulting in seniors now paying a portion of their fares. The increase in average fares, partially offset by the reduction in traffic, resulted in a total tariff revenue increase in the quarter of $1.5 million ($2.5 million year-to-date).

On January 17, 2014, due to the high cost of diesel fuel, we implemented fuel surcharges of 3.5% on our regulated Other Routes. No surcharges were in place in the first or second quarter of fiscal 2014. For regulatory purposes, these amounts are applied to our deferred fuel cost accounts. (See "The Effect of Rate Regulation" above for more detail.)

On April 1, 2014, we implemented the Province's decision to reduce the passenger fare discount for BC seniors travelling Mondays to Thursdays from 100% to 50%. As a result, in the three months ended September 30, 2014, 12% fewer seniors (10% year-to-date) used the program compared to the same periods in the prior year. The reduction in social program fees as a result of fewer seniors travelling was partially offset by an increase in the number of persons travelling under the MTAP program and higher fares.

Other Routes cont'd

Revenue from catering and on-board services remained at a similar level to the same periods in the prior year. Higher sales per passenger was mainly offset by lower passenger traffic levels. In the prior year, vessel substitutions on routes where these services were offered impacted the average sales per passenger.

Fees for reservations increased due to higher usage, partially offset by lower traffic levels.

Parking and other revenues increased mainly due to charter fees, commissions from new vendors at two of our terminal locations and dock rental fees.

Ferry transportation fees received from the Province increased $0.5 million in the quarter ($3.3 million year-to-date) compared to the same periods in the prior year as a result of the following:

- $1.1 million ($2.6 million year-to-date) increase in ferry transportation fees in respect of senior discounts; partially offset by:
- $0.6 million decrease ($0.7 million increase year-to-date) as a result of timing differences over the months from the number of round trips and a higher percentage of total ferry transportation fees allocated to the regulated Other Routes with the elimination of one Northern Route, and an overall increase in fees received under the CFSC.

The Federal-Provincial subsidy has decreased marginally by the change in the annual Consumer Price Index (CPI) (Vancouver).

Expenses
Expenses for the three and six months ended September 30, 2014 and 2013 are summarized in the tables below:

Operating expenses ($ millions)	**Three months ended September 30**			**Six months ended September 30**		
	2014	**2013**	**Increase (Decrease)**	**2014**	**2013**	**Increase (Decrease)**
Operations	125.4	124.7	0.7	240.4	238.9	1.5
Maintenance	12.4	12.2	0.2	29.1	27.8	1.3
Administration	8.0	7.5	0.5	15.6	14.5	1.1
Total operations, maintenance & administration	145.8	144.4	1.4	285.1	281.2	3.9
Cost of retail goods sold	11.1	10.7	0.4	19.1	18.4	0.7
Depreciation and amortization	35.7	34.1	1.6	70.9	68.4	2.5
Total operating expenses	192.6	189.2	3.4	375.1	368.0	7.1

We continue to take proactive measures to contain and reduce expenses while continuing to ensure that safety remains our top priority.

The $0.7 million ($1.5 million year-to-date) increase in operations expenses compared to the same periods in the prior year was mainly due to:

- $0.4 million ($1.4 million year-to-date) increase in fuel expense, reflecting an increase of $1.6 million or 1.0% ($3.6 million or 2.1% year-to-date) due to higher fuel prices, partially offset by a $1.2 million or 3.1% ($2.2 million or 3.2% year-to-date) decrease in fuel consumption. While IFRS does not permit us to account for rate-regulated activities, we are in fact rate-regulated. For purposes of rate regulation, $4.7 million ($8.7 million year-to-date) of our fuel expense was recorded in deferred fuel cost accounts for future recovery. (See “The Effect of Rate Regulation” above for more detail.);
- $0.3 million ($0.3 million year-to-date) increase in advertising costs regarding fare reductions for extra-length vehicles;
- $0.2 million (0.2 million year-to-date) increase in data communications costs; and
- $0.1 million ($0.2 million year-to-date) increase in credit card service fees;

partially offset by:

- $0.3 million ($0.6 million year-to-date) decrease in several operational areas.

Maintenance costs were $0.9 million higher in the quarter and year-to-date, reflecting variations in vessel maintenance and refit scheduling.

The $0.5 million ($1.1 million year-to-date) increase in administration costs was mainly due to licencing costs related to new hardware and software that has come into service, and legal fees.

The $0.4 million ($0.7 million year-to-date) increase in cost of retail goods sold reflects the increase in overall sales and rising food costs.

Depreciation and amortization increased $1.6 million ($2.5 million year-to-date), reflecting higher depreciation and amortization resulting from the new capital assets that have entered service. (See “Investing in our Capital Assets” below for details of significant capital asset expenditures.)

Net finance and other expenses ($ millions)	**Three months ended September 30**			**Six months ended September 30**		
	2014	**2013**	**Increase (Decrease)**	**2014**	**2013**	**Increase (Decrease)**
Finance expense						
Bond interest	14.6	16.7	(2.1)	30.7	32.5	(1.8)
KfW bank group (KfW) loans	1.7	1.9	(0.2)	3.5	3.9	(0.4)
Interest on finance lease	0.5	0.5	-	1.0	1.0	-
Short-term debt	0.1	0.3	(0.2)	0.2	0.4	(0.2)
Capitalized interest	(0.8)	(0.7)	(0.1)	(1.5)	(1.5)	-
Total finance expense	16.1	18.7	(2.6)	33.9	36.3	(2.4)
Less: finance income	(0.9)	(0.7)	(0.2)	(2.0)	(1.5)	(0.5)
Total net finance and other expenses	15.2	18.0	(2.8)	31.9	34.8	(2.9)

In the three months ended September 30, 2014, net finance and other expenses decreased $2.8 million ($2.9 million year-to-date) compared to the same periods in the prior year due to:

- $2.1 million ($1.8 million year-to-date) decrease in bond interest reflecting the lower effective interest rates on the new bonds;
- $0.2 million ($0.5 million year-to-date) increase in finance income;
- $0.2 million ($0.4 million year-to-date) decrease in interest on KfW loans, reflecting $9.0 million in principal repayments on the 2.95% KfW loan and lower interest rates on the Tranche B than on the Tranche A components of the 12-year KfW loans;
- $0.2 million lower short-term interest in the quarter and year-to-date; and
- $0.1 million higher capitalized interest in the quarter.

Liquidity and Capital Resources
We fund our operations and capital acquisitions with cash flow generated from operations, as well as bank financing and debt issues.

We expect that our cash requirements, in the near term, will be met through operating cash flows and by accessing our credit facility from time to time. At September 30, 2014, our unrestricted cash and cash equivalents and other short-term investments totalled $172 million.

On April 28, 2014, we completed a private placement of $200 million of 30-year senior secured bonds with accredited investors. These bonds bear interest at a rate of 4.289% per annum, payable semi-annually. The net proceeds of this new issue, together with additional cash on hand, was used to repay our $250 million bond Series 04-1, which matured on May 27, 2014 and to fund the debt service reserve related to these bonds. These bonds were rated “A” (DBRS) and “AA-” (S&P). We managed our interest rate risk and secured a favourable interest rate on these bonds by entering into interest rate hedges. The effective rate of this issue, net of hedging, is 4.45%, the lowest effective bond interest rate in the 11-year history of our company.

Our $155 million credit facility matures April 2019. The facility is available to fund capital expenditures and other general corporate purposes. At September 30, 2014, there were no draws on this credit facility.

We target maintaining a strong investment-grade credit rating to allow capital market access at reasonable interest rates. Our credit ratings at September 30, 2014 were “A” (DBRS) with a stable trend and “AA-” (S&P) with a stable outlook.

Sources & Uses of Cash
Our liquidity needs are met through a variety of sources, including cash generated from operations, issuance of bonds, and borrowings under our credit facility. Our primary uses of funds are operational expenses, capital asset acquisitions and upgrades, and payments on our long-term debt.

Sources and uses of cash and cash equivalents for the six months ended September 30, 2014 and 2013 are summarized in the table below:

	Six months ended September 30		
($ millions)	**2014**	**2013**	**Increase (Decrease)**
Cash and cash equivalents, beginning of period	71.4	36.6	34.8
Cash from operating activities:			
Net earnings	90.3	68.6	21.7
Items not affecting cash	96.4	99.8	(3.4)
Changes in non-cash operating working capital	(11.4)	(10.7)	(0.7)
Net interest paid	(34.3)	(38.4)	4.1
Cash generated by operating activities	141.0	119.3	21.7
Cash used in financing activities	(67.8)	(105.0)	37.2
Cash used in investing activities	(28.4)	(37.0)	8.6
Net increase (decrease) in cash and cash equivalents	44.8	(22.7)	67.5
Cash and cash equivalents, end of period	116.2	13.9	102.3

For the six months ended September 30, 2014, cash generated by operating activities increased by $21.7 million compared to the same period in the prior year, due to an increase in net earnings and a decrease in interest paid, offset by items not affecting cash and changes in non-cash operating working capital.

Cash used in financing activities in the six months ended September 30, 2014 was $67.8 million. This amount consisted of the redemption of our $250 million bond Series 04-1; repayment of $8.3 of KfW loans; $8.9 million in bond financing costs; and $0.6 million repayment of finance lease obligations; partially offset by proceeds of $200 million from our April 2014 bond Series 14-1 issuance.

Cash used in financing activities in the six months ended September 30, 2013 was $105.0 million, mainly due to $145 million in long-term debt repayments, offset by $40.0 million proceeds from short-term debt.

Cash used in investing activities in the six months ended September 30, 2014 decreased by $8.6 million compared to the same period in the prior year, due to a $16.1 million increase in cash provided by short-term investments, partially offset by a $6.2 million increase in cash used for capital expenditures and a $1.3 million smaller decrease in debt service reserve requirements. (See “Investing in Our Capital Assets” below for detail of significant capital expenditures.)

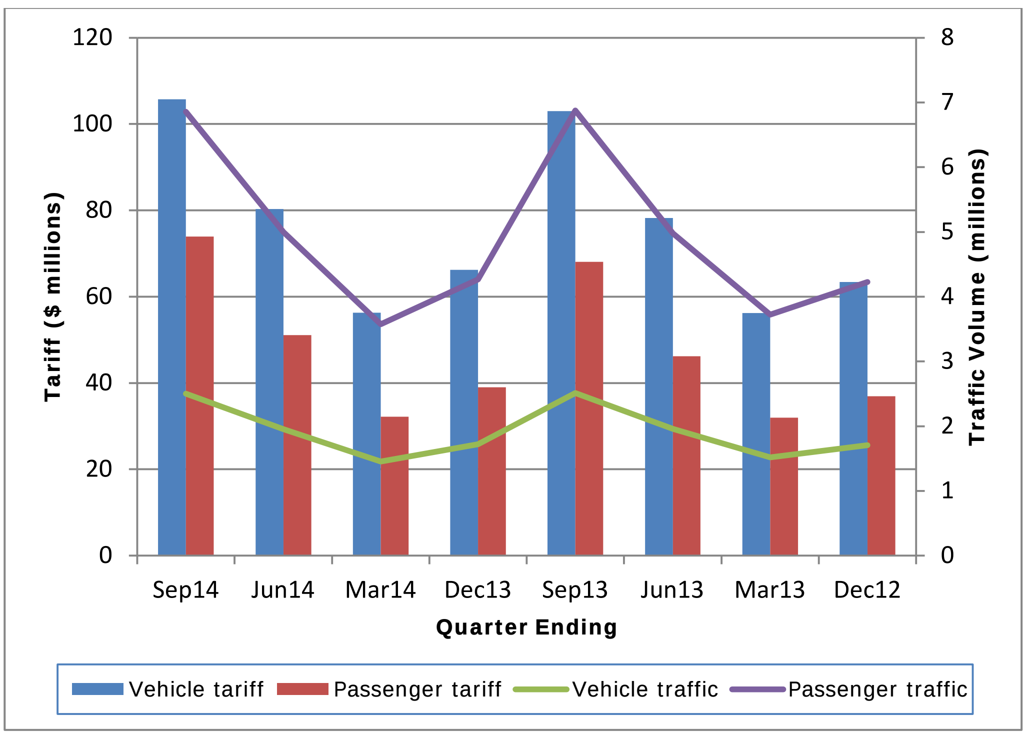
SUMMARY OF QUARTERLY RESULTS

The table below compares earnings by quarter for the most recent eight quarters:

($ millions)	Quarter Ended (unaudited)							
	Sep 14	**Jun 14**	**Mar 14**	**Dec 13**	**Sep 13**	**Jun 13**	**Mar 13**	**Dec 12**
Total revenue	284.2	213.1	153.9	174.8	271.5	200.0	150.5	169.6
Operating profit (loss)	91.6	30.6	(21.3)	3.7	82.3	21.2	(20.2)	0.2
Net earnings (loss)	76.4	13.9	(38.3)	(12.3)	64.3	4.3	(37.1)	(17.2)
Other comprehensive (loss) income	(2.9)	(2.4)	(5.0)	-	0.1	-	1.1	-
Total comprehensive income (loss)	73.5	11.5	(43.3)	(12.3)	64.4	4.3	(36.0)	(17.2)

Quarterly results are affected by the seasonality of leisure travel patterns. The second quarter, covering the summer period, experiences the highest traffic levels and the highest net earnings. The third and fourth quarters reflect a seasonal reduction in traffic. We utilize these periods to perform upgrades and major maintenance and refit programs, as well as to undertake mandatory inspections on the majority of our vessels.

The following graph demonstrates the seasonality of our revenue and shows the relationship of traffic volume and tariff revenue over the most recent eight quarters:



INVESTING IN OUR CAPITAL ASSETS

Capital Expenditures
Capital expenditures in the three months ended September 30, 2014 totalled $26.6 million ($52.7 million year-to-date).

($ millions)	September 30, 2014 3 Months	September 30, 2014 6 Months
Terminal marine structures	16.0	26.8
Vessel upgrades and modifications	3.6	12.1
Information technology	5.0	10.2
Terminal and building upgrades and equipment	2.0	3.6
Total capital expenditures	26.6	52.7

Terminal Marine Structures
Capital expenditures for terminal marine structures in the three and six months ended September 30, 2014 included the following:

($ millions) Terminal	Description	September 30, 2014 3 Months	September 30, 2014 6 Months
Port McNeill	Replacement of trestle, ramp, apron and towers	3.5	8.4
Denman Island and Buckley Bay	Modifications to accommodate the new cable ferry	9.0	13.1
McLoughlin Bay	Berth modifications	0.1	1.2
Various	Other projects	3.4	4.1
		16.0	26.8

At Port McNeill terminal, a $13 million project to replace the trestle, wingwalls, ramp, apron, towers, and dolphin and reposition the new ramp to accommodate all minor and intermediate vessels is underway. This project is expected to be complete by the end of the third quarter of fiscal 2015.

Modifications at Denman Island and Buckley Bay terminals, as part of the project for our new cable ferry service, include two contracts totalling $15 million awarded for the supply of two concrete floating pontoons, construction of two berths, expansion of the Denman West holding compound and all associated upland development. These modifications are expected to be complete by the end of the third quarter of fiscal 2015. (See “Outlook – Asset Renewal Program” below for more detail.)

At McLoughlin Bay, the $9 million project for berth modifications includes installation of three pontoon sections and modification of the berth to improve ship-to-shore tie-up. This project is complete.

Other projects currently in progress include a $10 million project to replace the ramp, tower, wingwalls, floating lead, three dolphins and extend the life of the trestle at Sointula as well as upgrades at Langdale, Heriot Bay and Swartz Bay terminals.

Vessel Upgrades and Modifications
Capital expenditures for vessel upgrades and vessel modifications in the three and six months ended September 30, 2014 included the following:

($ millions)	September 30, 2014	
	3 Months	6 Months
Major overhauls and inspections	0.6	5.2
Queen of Capilano mid-life upgrade	0.5	0.9
New intermediate vessels	0.3	0.6
Queen of Oak Bay three-quarter life upgrade	0.1	0.6
Navigational equipment upgrades	0.1	0.6
Cable ferry	0.1	0.3
Other projects	1.9	3.9
	3.6	12.1

The $5.2 million in major overhauls and inspections completed in the six months ended September 30, 2014 or currently underway include:
- $1.8 million for the *North Island Princess*;
- $1.3 million for the *Queen of Coquitlam*;
- $1.1 million for the *Northern Expedition*; and
- $1.0 million for the *Queen of Nanaimo.*

A $13 million project for a mid-life upgrade of the *Queen of Capilano* includes upgrades to the electrical system, replacement of generators, upgrades to the fire protection system, standardization of the bridge and upgrades to the emergency evacuation systems. The upgrade commenced in October 2012 and is expected to be complete for the summer of 2015.

On July 3, 2014, we entered into contracts with Remontowa Shipbuilding S.A. of Gdansk, Poland to build three new intermediate class vessels. These contracts, with a total value of $165 million, form the majority of the total project budget of $252 million. These are design-build, fixed price contracts that provide us with substantial guarantees related to delivery dates, performance criteria, cost certainty and quality of construction. The new vessels, scheduled for delivery in August 2016, October 2016 and February 2017, will replace the 49-year old *Queen of Burnaby* and the 50-year old *Queen of Nanaimo*. The new vessels will be designed to operate as dual-fuel capable, so they can run on LNG or marine diesel fuel.

The three-quarter life upgrade of the *Queen of Oak Bay* includes significant pipe and steel renewal, upgrades to the electrical system, replacement of the steering gear system, upgrades to the fire protection system, standardization of the bridge and replacing the emergency generator. The upgrade commenced in August 2013 and is expected to be completed in two phases by the end of fiscal 2016.

Fiscal 2015 is our third year of a four-year program to upgrade vessels with new navigational equipment. This year the emphasis will be on upgrading the radar equipment and gyro compasses on several vessels to improve navigational safety. This will take us further towards bridge standardization. We expect to spend $1 million in fiscal 2015 of the total four-year program budget of $4.7 million.

On September 3, 2014, construction of the cable ferry that will provide service between Buckley Bay and Denman Island commenced at Seaspan's Vancouver Shipyards Co. Ltd. of North Vancouver. The vessel will accommodate 50 vehicles and 150 passengers and crew. The cable ferry is expected to be in service in the summer of 2015. (See "Outlook – Asset Renewal Program" below for more detail.)

Other projects include the replacement of rescue boats and davits on the *Spirit of British Columbia*, new searchlights for the *Northern Expedition,* the *Coastal Celebration,* the *Coastal Renaissance* and *Coastal Inspiration* and the rebuilding of two spare tail shafts for potential use in upcoming overhauls.

Information Technology

Capital expenditures for information technology in the three and six months ended September 30, 2014 included the following:

($ millions)	**September 30, 2014**	
	3 Months	**6 Months**
Customer service program	2.5	6.2
Payroll system replacement	1.1	2.0
Hardware upgrades	0.7	1.1
Oracle eBusiness upgrade	0.6	0.6
Other projects	0.1	0.3
	5.0	10.2

Our customer service program will replace our aged point of sale and reservations systems and allow us to respond in a more timely fashion to changing business needs and to support marketing, travel services, and pricing initiatives. The main elements of this multi-year program will be implemented in stages starting in 2015. We believe this program will significantly improve our ability to efficiently respond to the changing needs of our customers.

Our payroll system replacement initiative will replace both our aged payroll and labour distribution systems and provide processing efficiencies and flexibility. It is expected to be complete in fiscal 2016.

Hardware upgrades include the replacement of aged computers, printers, servers, closed-circuit cameras and electronic signage.

Terminal and Building Upgrades and Equipment
Capital expenditures for terminal and building upgrades and equipment in the three and six months ended September 30, 2014 included the following:

($ millions)	September 30, 2014	
	3 Months	**6 Months**
Asphalt resurfacing, signage and security at Tsawwassen terminal	0.3	1.2
Vehicles and other equipment	0.6	0.8
Upgrades at our maintenance facility	0.3	0.3
Energy efficiency upgrades at Horseshoe Bay and Swartz Bay terminals	0.1	0.2
Other terminal projects	0.7	1.1
	2.0	3.6

Several improvement projects are substantially complete or underway at Tsawwassen terminal including asphalt resurfacing, upgrade of way-finding signage, installation of digital destination signs at the toll booths and upgrade of lighting for security purposes.

Vehicles and other equipment include garbage compactors and several items of machinery and equipment at our maintenance facility in Richmond.

Upgrades at our maintenance facility include asphalt resurfacing, roof replacement on one building as well as security upgrades.

OUTLOOK

We do not anticipate that economic conditions will materially change in the near term, although we expect that service reductions and changes in the BC seniors discount may result in a small reduction in our traffic levels. We are continuing our program of cost containment and deferrals, while maintaining safe, reliable service. However, we have no plans to reduce our planned refit and maintenance programs, training and safety programs or capital programs.

We continue to explore strategies to create an affordable and sustainable ferry system beyond 2016, including standardized vessels, LNG propulsion, other alternative technologies, passenger only vessels, a new reservation and point-of-sale system, increased operational efficiencies and seeking federal infrastructure funding to renew our fleet and terminals.

Traffic

In the six months ended September 30, 2014, vehicle traffic decreased 0.3% while passenger traffic was at the same level compared to the same period in the prior year. Traffic levels are discussed above in "Financial and Operational Overview".

We believe the outlook for the travel industry and the US economy have each improved, though not significantly. We also see signs of modest improvement in local leisure travel spending. We expect these improvements will result in a limited recovery in discretionary traffic levels. We believe these improvements will be mainly offset by reductions in traffic due to reductions in service levels and in BC seniors travel. In the near term, we anticipate no significant increase or decrease in overall traffic volume.

Financial performance

We expect positive net earnings in fiscal 2015, reflecting adjustments to service levels, increases to average fares in accordance with the Commissioner's Order 12-02 and continued cost management, coupled with a gradual improvement in the overall economy.

We expect a modest increase in total revenue in fiscal 2015, reflecting the April 1, 2014 tariff increases, lower social program fees, higher catering and on-board revenues and higher ferry transportation fees.

We expect a modest increase in total expenses in fiscal 2015, reflecting higher depreciation and amortization, wage and benefit increases, higher fuel costs and other operational related costs. We continue to manage our costs prudently without compromising safe operations.

Asset renewal program

Our capital expenditures are expected to increase over the next several years as we begin to replace aged minor and intermediate-sized vessels, make significant improvements at our terminals serving our Major Routes, and renew our information technology infrastructure.

The project for the new cable ferry, for service on our Buckley Bay to Denman Island route, commenced with the first steel cut in September 2014. With a crossing of approximately 1,900 metres, this will be the longest cable ferry service in the world. It is expected to provide cost savings in the order of $80 million, before inflation, over its expected 40-year life compared to the current service and will also provide environmental benefits. It is an innovative initiative and is part of our ongoing efforts to identify and pursue opportunities that have the potential to enhance our cost effectiveness in delivering safe, reliable and quality ferry service.

Subject to obtaining the Commissioner's approval, we plan to convert our two largest vessels, the *Spirit of Vancouver Island* and the *Spirit of British Columbia*, to dual fuel, as well as make modifications to their hulls to reduce fuel consumption. We expect the conversion and modifications will result in an average savings of approximately $9 million per year over the remaining 27 year life cycle of the two vessels, before inflation. The *Spirit of Vancouver Island*'s mid-life upgrade and LNG conversion is planned to be complete in the spring of 2017 and the *Spirit of British Columbia's* mid-life upgrade and LNG conversion to be complete in the spring of 2018. Our application for approval of these capital projects has been submitted to the Commissioner and we expect a ruling during the third quarter of fiscal 2015.

In July 2014, we signed contracts with Remontowa Shipbuilding S.A. of Gdansk, Poland to build three new intermediate class vessels. These new vessels, scheduled for delivery in August 2016, October 2016 and February 2017, will be designed to operate as dual-fuel capable, so they can run on LNG or marine diesel fuel. These vessels will set a new standard of efficiency with standardized bridges, engine rooms and lifesaving equipment moving us to a higher safety standard and improving interoperability.

FINANCIAL RISKS

Exposure to credit risk, liquidity risk and market risk arises in the normal course of our business. We manage market risk arising from the volatility in foreign currency, interest rate and fuel price exposures in part through the use of derivative financial instruments including forward contracts, swaps and options. We do not utilize derivative financial instruments for trading or speculative purposes.

A discussion of financial risks can be found on pages 54 through 56 of our fiscal 2014 Management's Discussion & Analysis. Our risk profile is substantially unchanged during the six months ended September 30, 2014. Our 2014 Management's Discussion & Analysis is available on our investor webpage at http://www.bcferries.com/investors/financial_reports.html.

BUSINESS RISK MANAGEMENT

Understanding and managing operational risk is an important part of our business. We have processes in place throughout our company to manage risks that inevitably arise in the normal course of business. A discussion of enterprise wide risk management can be found on pages 57 through 63 of our fiscal 2014 Management's Discussion & Analysis. Our risk profile is substantially unchanged during the six months ended September 30, 2014. Our 2014 Management's Discussion & Analysis is available on our investor webpage at http://www.bcferries.com/investors/financial_reports.html.

We do not believe that material uncertainties exist in regards to our future. As part of our risk management strategies, we have considered many items such as profitability levels, cash generating potential, cash utilization requirements including debt repayment schedules and future capital expenditures, and working capital requirements. We have taken measures to allow us to weather the economic downturn and ensure a viable, profitable future.

Critical Accounting Policies and Estimates
Our discussion and analysis of our financial condition and financial performance is based upon our consolidated financial statements, which have been prepared in accordance with IFRS.

Our significant accounting policies are contained in note 1 to our March 31, 2014 and September 30, 2014 consolidated financial statements. Certain of these policies involve critical accounting estimates because they require us to make particularly subjective or complex judgments about matters that are inherently uncertain and because of the likelihood that materially different amounts could be reported under different conditions or using different assumptions. These judgements, estimates and assumptions are subject to change as new events occur, as more experience is acquired, as additional information is obtained and as the general operating environment changes.

Discussion of the most critical accounting policies and estimates that we have used in the preparation of our consolidated financial statements can be found on pages 64 and 65 of our fiscal 2014 Management's Discussion & Analysis. The following describes the changes to critical accounting policies we have used in the preparation of our consolidated financial statements for the three and six months ended September 30, 2014, or expect to use in the future. Our 2014 Management's Discussion & Analysis is available on our investor webpage at http://www.bcferries.com/investors/financial_reports.html.

Adoption of New Accounting Standards
The following is a discussion of mandatory accounting changes that were effective for us April 1, 2014:

International Financial Reporting Interpretations Committee (IFRIC) 21 *Levies*:

- provides guidance on when to recognize a liability for a levy imposed by a government. The retrospective application of this IFRIC did not have an impact on our consolidated financial statements.

Future Accounting Changes
There are no relevant changes in accounting standards applicable to our fiscal year beginning April 1, 2015. The following is a discussion of accounting changes that will be effective for us in future periods:

Amendments to IAS16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets*, explicitly state that revenue-based methods of depreciation cannot be used for property, plant and equipment. The amendments will be effective for us April 1, 2016. We do not expect the application of these amendments to have any impact on our consolidated financial statements.

IFRS 15 *Revenue from Contracts with Customers* replaces IAS 18 *Revenue* and IAS 11 *Construction Contracts*, providing guidance on the amount and/or timing of recognition of revenue. Mandatory adoption of IFRS 15 for us will be April 1, 2017. We do not expect the application of this standard to have any impact on our consolidated financial statements.

IFRS 9 *Financial Instruments* replaces IAS 39 *Financial Instruments,* providing guidance on the classification, measurement and disclosure of financial instruments and introducing a new hedge accounting model. Mandatory adoption of IFRS 9 for us will be April 1, 2018. The new standard is available for early adoption, with certain exceptions. We have evaluated the impact of IFRS 9 on our consolidated financial statements and have adopted IFRS 9 (2013) effective October 1, 2014. We do not expect the adoption of this standard to have any impact on our consolidated financial statements other than certain additional disclosures.

FORWARD LOOKING STATEMENTS

This Management's Discussion and Analysis contains certain "forward looking statements". These statements relate to future events or future performance and reflect management's expectations regarding our growth, results of operations, performance, business prospects and opportunities and industry performance and trends. They reflect management's current internal projections, expectations or beliefs and are based on information currently available to management. Some of the market conditions and factors that have been considered in formulating the assumptions upon which forward looking statements are based include traffic, the Canadian Dollar relative to the US Dollar, fuel costs, construction costs, the state of the local economy, fluctuating financial markets, demographics, tax changes, and the requirements of the CFSC.

Forward looking statements included in this document include statements with respect to: economic conditions, traffic levels, tariff revenue, and fiscal 2015 net earnings; whether our regulatory assets are probable of future recovery; our short-term and long-range business plans, capital expenditure levels, and asset renewal programs for vessels and terminals; our customer service program, payroll system replacement initiative, vessel replacement program for the *Queen of Burnaby* and the *Queen of Nanaimo*, cable ferry initiative, Spirit Class mid-life upgrades, and safety and training projects; our expectations regarding ferry transportation fee amounts, food sales, and sales of quality apparel; total revenue and expense projections, how our cash requirements will be met in the near term, and the amount of savings to be achieved through service level adjustments; and our expectations regarding the impacts of IFRS 9 and IFRS 15 and amendments to IAS 16 and IAS 38 on our consolidated financial statements. In some cases, forward looking statements can be identified by terminology such as "may", "will", "should", "expect", "plan", "anticipate", "believe", "estimate", "predict", "potential", "continue" or the negative of these terms or other comparable terminology. A number of factors could cause actual events or results to differ materially from the results discussed in the forward looking statements. In evaluating these statements, prospective investors should specifically consider various factors including, but not limited to, the risks and uncertainties associated with traffic volume and tariff revenue risk, safety and security, asset risk, accident risk, tax risk, environmental risk, regulatory risk, labour disruption risk, risk of default under material contracts and aboriginal land claims.

Actual results may differ materially from any forward looking statement. Although management believes that the forward looking statements contained in this Management's Discussion and Analysis are based upon reasonable assumptions, investors cannot be assured that actual results will be consistent with these forward looking statements. These forward looking statements are made as of the date of this Management's Discussion and Analysis, and British Columbia Ferry Services Inc. assumes no obligation to update or revise them to reflect new events or circumstances except as may be required by applicable law.

In addition to providing measures prepared in accordance with IFRS, we present certain supplemental non-IFRS measures. These include, but are not limited to, total comprehensive income adjusted for the effect of rate regulation, vehicle and passenger traffic, on-time performance, capacity provided and utilized, AEQs carried, number of round trips, and average tariff revenue per vehicle and per passenger. These measures do not have any standardized meaning prescribed by IFRS and therefore are unlikely to be comparable to similar measures presented by other companies. These supplemental non-IFRS measures are provided to assist readers in determining our ability to generate cash from operations and improve the comparability of our results from one period to another. We believe these measures are useful in assessing operating performance of our ongoing business on an overall basis.