

XS Cargo Income Fund
Interim Consolidated Financial Statements

Unaudited
March 31, 2007

Amended and Restated May 16, 2007

XS CARGO INCOME FUND
THREE MONTHS ENDED MARCH 31, 2007
EXPLANATORY NOTE

These interim consolidated financial statements for the three months ended March 31, 2007 have been revised to reclassify the Term Loan (Note 4) on the balance sheet and provide additional note disclosure. The restatement had no impact on the consolidated statements of earnings and comprehensive income; (deficit) retained earnings; or cash flows. At March 31, 2007, XS Cargo Income Fund (the "Fund") was not in compliance with the fixed charge coverage ratio covenant included in its credit agreement, and therefore has reclassified \$15,000,000 of the Term Loan as a current liability on the consolidated balance sheet and provided additional note disclosure.

XS Cargo Income Fund
Consolidated Balance Sheets

	March 31, 2007 (unaudited)	December 31, 2006
	\$	\$
Assets		
Current		
Cash and cash equivalents	-	1,017,824
Rebate and other receivables	173,470	439,384
Inventory	25,158,913	22,288,806
Deposits on inventory	3,900,461	6,604,788
Prepaid expenses and deposits	691,641	828,775
	29,924,485	31,179,577
Deferred charges	330,835	331,799
Property and equipment	4,510,516	4,332,028
Intangible assets	6,420,000	6,718,000
Goodwill	101,788,426	101,788,426
	142,974,262	144,349,830
Liabilities		
Current		
Bank indebtedness	4,647,293	-
Accounts payable and accrued liabilities	6,283,875	10,597,933
Deferred revenue	1,615,797	1,528,327
Distributions payable to unitholders (Note 5)	572,438	629,681
Distributions payable to non-controlling interest (Note 6)	326,799	1,103,235
	13,446,202	13,859,176
Term loan (Note 4)	21,250,000	2,500,000
	34,696,202	16,359,176
Term Loan (Note 4)	-	15,000,000
Deferred revenue	540,626	607,513
Unamortized lease inducements	366,783	317,975
	35,603,611	32,284,664
Non-controlling interest (Note 6)	55,578,212	57,493,942
	91,181,823	89,778,606
Unitholders' Equity		
Fund Units (Note 5)	56,131,876	56,131,876
Deficit	(4,339,437)	(1,560,652)
	51,792,439	54,571,224
	142,974,262	144,349,830

The accompanying notes are an integral part of these financial statements

XS Cargo Income Fund
Consolidated Statements of Earnings and Comprehensive Income

	<i>Three Months Ended March 31, 2007 (unaudited) \$</i>	<i>Three Months Ended March 31, 2006 (unaudited) \$</i>
Sales	23,657,656	20,671,865
Cost of goods sold	16,437,941	13,069,342
Gross Margin	7,219,715	7,602,523
Expenses		
Administrative and operating	8,039,345	5,473,139
Amortization of property and equipment	294,978	174,857
Amortization of intangible assets	298,000	298,000
	8,632,323	5,945,996
(Loss) earnings before the undernoted	(1,412,608)	1,656,527
Other expenses		
Interest on bank indebtedness	87,429	39,765
Interest on term loan	342,942	222,632
Foreign exchange loss (gain)	17,479	(25,964)
	447,850	236,433
(Loss) earnings before non-controlling interest	(1,860,458)	1,420,094
Non-controlling interest (Note 6)	(913,473)	696,549
Net (loss) earnings and comprehensive (loss) income for the period (Note 3)	(946,985)	723,545
Basic and diluted (loss) earnings per unit (Note 10)	(0.16)	0.12

The accompanying notes are an integral part of these financial statements

XS Cargo Income Fund
Consolidated Statements of (Deficit) Retained Earnings

	<i>Three Months Ended March 31, 2007 (unaudited) \$</i>	<i>Three Months Ended March 31, 2006 (unaudited) \$</i>
(Deficit) retained earnings, beginning of the period	(1,560,652)	701,871
Net (loss) earnings for the period	(946,985)	723,545
Distributions declared in the period	(1,831,800)	(1,774,556)
Deficit, end of the period	(4,339,437)	(349,140)

The accompanying notes are an integral part of these financial statements

XS Cargo Income Fund
Consolidated Statements of Cash Flows

	<i>Three Months Ended March 31, 2007 (unaudited)</i> \$	<i>Three Months Ended March 31 2006, (unaudited)</i> \$
Cash provided by (used for) the following activities		
Operating Activities		
Net loss for the period	(946,985)	723,545
Items not affecting cash:		
Non-controlling interest	(913,473)	696,549
Amortization of property and equipment	294,978	174,857
Amortization of intangible assets	298,000	298,000
Unit based compensation (<i>Note 8</i>)	43,500	30,000
Deferred charges, net of costs recognized	964	(66,267)
Deferred revenue, net of revenue recognized	20,584	370,877
Lease inducements received, net of amortization of lease inducements	48,808	(14,924)
	(1,153,624)	2,212,637
Net change in non-cash working capital	(4,076,788)	(11,597,566)
	(5,230,412)	(9,384,929)
Financing Activities		
Proceeds from bank indebtedness	4,647,293	6,043,348
Proceeds from term loan	3,750,000	-
Distributions paid on Fund Units	(1,889,046)	(1,717,312)
Distributions paid to non-controlling interest	(1,822,193)	(1,653,239)
	4,686,054	2,672,797
Investing Activities		
Purchases of property and equipment	(473,466)	(730,364)
Decrease in cash and cash equivalents	(1,017,824)	(7,442,496)
Cash and cash equivalents, beginning of period	1,017,824	7,442,496
Cash and cash equivalents, end of period	-	-
Supplementary cash flow information		
Interest paid	430,371	262,397

The accompanying notes are an integral part of these financial statements

XS Cargo Income Fund

Notes to the Interim Consolidated Financial Statements

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1. The Fund

XS Cargo Income Fund (the "Fund") is an unincorporated open-ended trust established under the laws of the Province of Alberta pursuant to the Fund Declaration of Trust dated April 6, 2005. The Fund has been created to invest in the broadline closeout retail business, through an indirect acquisition of the controlling interest of XS Cargo Limited Partnership ("XS Cargo LP") and its general partner ("GP") (collectively "XS Cargo"), and such other investments as the trustees may determine. Income tax obligations related to the distributions of the Fund are obligations of the Unitholder.

The Fund commenced business operations on May 17, 2005, when it completed an initial public offering (the "IPO") of 6,106,000 trust units ("Fund Units"), at a price of \$10 per unit, for aggregate gross proceeds of \$61,060,000. Concurrent with the closing of the IPO, the Fund acquired a 51% indirect interest in XS Cargo LP and XS Cargo LP acquired the net assets (the "Acquired Business") of Famous Brands (Edmonton) Inc. (the "Vendor"). XS Cargo LP operates 38 (December 31, 2006 – 35) closeout retail stores in Alberta, British Columbia, Manitoba, Saskatchewan, Ontario, Newfoundland, Nova Scotia and New Brunswick.

2. Basis of presentation

The accompanying unaudited interim consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles ("GAAP") for interim financial statements. The accounting principles and methods of computation adopted in these financial statements are the same as those for the audited financial statements for the year ended December 31, 2006, except as described in note 3. However, the interim consolidated financial statements do not include all information and footnote disclosures required under Canadian GAAP for annual financial statements. Accordingly, these unaudited consolidated interim financial statements should be read in conjunction with audited financial statements and notes thereto, for the year ended December 31, 2006.

3. Change in accounting policies

Effective January 1, 2007, the Fund adopted Canadian Institute of Chartered Accountants ("CICA") Handbook sections 1530 – Comprehensive Income, 3855 – Financial Instruments – Recognition and Measurement, and 3865 – Hedges.

As the Fund has no items of other comprehensive income, net loss for the period is equivalent to comprehensive loss.

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4. Credit facilities

Term loan

Term loan consists of a committed non-revolving term loan facility. The maximum available on the term loan facility is \$25,000,000, of which \$21,250,000 was outstanding at March 31, 2007 (December 31, 2006 - \$17,500,000). The term loan is collateralized by a first charge on all present and after acquired personal property and an assignment of inventory. Interest on the term facility is charged at the lender's Canadian prime rate or U.S. base rate plus 0.25% to 0.75% or the bankers' acceptance rate plus 1.75% to 2.25%, depending on the Fund's senior debt to earnings before interest, taxes, depreciation and amortization ("EBITDA") ratio. The credit agreement includes limits on incurring additional indebtedness or granting encumbrances without the consent of the lender and is subject to the maintenance of senior debt to EBITDA, current assets to current liabilities and fixed charge coverage ratios and minimum equity.

During the three months ended March 31, 2007, interest was charged at a rate of prime plus 0.25% and totaled \$342,942 (March 31, 2006 - \$222,632). As at March 31, 2007, prime rate was 6.0% (December 31, 2006 - 6.0%). The principal balance of the term loan is due on May 16, 2008. The credit agreement requires the principal to be reduced to \$15,000,000 by September 30, 2007.

Operating loan

The Fund has available under its credit facilities a \$12,500,000 (\$20,000,000 available from August to December) demand revolving loan. Under the terms of the credit agreement, the operating loan is collateralized along with the term loan as described above. Interest on the operating loan will vary between the lender's prime rate and the lender's prime rate plus 0.50% depending on the Fund's ratio of senior debt to EBITDA. During the three months ended March 31, 2007, the Fund paid interest of \$87,429 (March 31, 2006 - \$39,765) on amounts drawn on the operating loan at a rate of prime. As at March 31, 2007 \$4,647,293 (December 31, 2006 - \$Nil) was outstanding under the operating loan.

Financial covenants

Both the Term Loan and Operating Loan ("Loans") require the Fund to maintain certain financial covenants, including a maximum senior debt to EBITDA ratio of 2.5:1.0, a minimum current ratio of 1.5:1.0 and a minimum fixed charge coverage ratio of 0.85:1.0. Additionally, the covenants limit the Fund's ability to undertake mergers, acquisitions, new indebtedness, declare distributions in excess of distributable cash and other changes in the business without approval of the lender. At March 31, 2007, the Fund was not in compliance with the fixed charge coverage covenant; therefore the Term Loan has been classified as a current liability.

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5. Unitholders' Equity

Fund Units

The following units are issued and outstanding:

	Number of Units #	Issue Costs \$	Net Capital Contributions \$
<u>Fund Units Issued, March 31, 2007 and December 31, 2006</u>	6,106,000	4,928,124	56,131,876

An unlimited number of Fund Units may be created and issued pursuant to the Declaration of Trust. Each Fund Unit is transferable and represents an equal undivided beneficial interest in any distributions from the Fund, whether of net income, net realized capital gains or other amounts and in the net assets of the Fund in the event of a termination or winding up of the Fund. All Fund Units have equal voting rights and privileges. There were no changes in the number or amount of Fund Units issued during the period.

Distributions to Unitholders

The Fund's policy is to distribute annually to unitholders available cash from operations after cash required for capital expenditures, working capital reserve and other reserves considered advisable by the trustees of the Fund. The policy allows the Fund to make stable monthly distributions to its unitholders based on its estimate of distributable cash for the year. Distributions totaling \$0.30 per Fund Unit (\$1,831,800) were declared by the Fund during the three months period ended March 31, 2007. The distribution declared for the month of March 2007 in the amount of \$0.09375 per Fund Unit (\$572,438) was included in distributions payable to unitholders at March 31, 2007 and was paid on April 15, 2007.

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6. Non-controlling interest

	<i>XS Cargo LP Exchangeable LP Units #</i>	<i>XS Cargo LP Subordinated LP Units #</i>	<i>Total #</i>
Balance – March 31, 2007 and December 31, 2006	3,485,858	2,404,058	5,889,916
	\$	\$	\$
Exchangeable and Subordinated Units	33,967,936	23,426,336	57,394,272
Net accrued contingent unit based compensation award (Note 8)			99,670
Balance – December 31, 2006	33,967,936	23,426,336	57,493,942
Non-controlling interest – earnings	(540,625)	(372,848)	(913,473)
Distributions declared	(1,045,757)	-	(1,045,757)
	32,381,554	23,053,488	55,534,712
Net accrued contingent unit based compensation award (Note 8)			43,500
			55,578,212

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XS Cargo LP Exchangeable LP Units (“Exchangeable LP Units”)

The Exchangeable LP Units issued by XS Cargo LP have economic and voting rights equivalent to the Fund Units (note 5), except in connection with the exchangeability terms as described below. They are exchangeable directly or indirectly, on a one-for-one basis for Fund Units at the option of the holder, under the terms of the Exchange Agreement. The Exchangeable LP Units are not required to be exchanged for Fund Units before transferring to third parties. As a result, they have been presented as non-controlling interest, in accordance with the CICA Emerging Issues Committee Abstract #151.

Each Exchangeable LP Unit entitles the holder to receive distributions from XS Cargo LP pro rata with distributions made by XS Cargo LP on Fund Units.

XS Cargo LP Subordinated LP Units (“Subordinated LP Units”)

The Subordinated LP Units have economic and voting rights equivalent to the Fund Units (note 5), except in connection with the subordination terms as described below. As a result, they have been treated as non-controlling interest, in accordance with the CICA Emerging Issues Committee Abstract #151.

Distributions are to be made monthly on the Fund Units (note 5) and Exchangeable LP Units to the extent cash is available to make cash distributions. Distributions on the Subordinated LP Units are subordinated and are made quarterly in an amount equal to the amount distributed on Fund Units and Exchangeable LP Units to the extent cash is available to make such distributions.

The Subordinated LP Units will be automatically exchanged for Exchangeable LP Units on a one-for-one basis and the subordination provisions will apply until the end of any fiscal year ending on or after December 31, 2006 if, for that fiscal year the Fund has earned EBITDA (earnings before interest, taxes, depreciation and amortization) of at least \$14.432 million and the Fund has paid distributions of at least \$1.125 per Fund Unit for such fiscal year. For the year ended December 31, 2006, the criteria were not met for the automatic exchange to occur.

Fund Special Voting Units

	Number	Amount
	#	\$
Issued and outstanding – March 31, 2007 and December 31, 2006	5,889,916	-

Fund Special Voting Units are non-participating and are used solely for providing voting rights to persons holding Exchangeable LP Units and Subordinated LP Units. Fund Special Voting Units are not transferable separately from Exchangeable LP Units and Subordinated LP Units to which they relate. The Fund Special Voting Units are not entitled to any beneficial interest in any distribution from the Fund or in the net assets of the Fund in the event of a termination or winding up of the Fund. Each Fund Unit and Fund Special Voting Unit entitles the holder thereof to one vote at all meetings of the Unitholders.

If the Exchangeable LP Units or the Subordinated LP Units are purchased in accordance with the Exchange Agreement, a like number of Fund Special Voting Units will be redeemed by the Fund for a nominal amount.

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Distributions to non-controlling interest

The Fund's policy is to distribute annually to holders of Fund Units, Exchangeable LP Units and Subordinated LP Units available cash from operations after cash required for capital expenditures, working capital reserve and other reserves considered advisable by the trustees of the Fund. The policy allows the Fund to make stable monthly distributions to holders of Exchangeable LP Units and quarterly distributions to holders of Subordinated LP Units based on its estimate of distributable cash for the year. Distributions totaling \$0.30 per Exchangeable LP Unit (\$1,045,757) and \$Nil per Subordinated LP Unit were declared by the Fund during the three months ended March 31, 2007. Distributions declared on Exchangeable LP Units for the month of March 2007 in the amount of \$0.09375 per unit (\$326,799) were included in distributions payable to non-controlling interest and were paid on April 15, 2007. Distributions on the Subordinated LP Units have been suspended.

7. Long-term incentive plan

The Fund has adopted a long-term incentive plan (the "Plan") to provide key senior management, officers and directors of the Fund with compensation opportunities that will enhance the ability of the Fund to attract, retain and motivate key personnel and reward these key employees for significant performance and associated per unit cash flow growth. Fund bonuses, in the form of the Units of the Fund, will be provided to eligible employees on an annual basis where the distributable cash of the Fund exceeds certain specified threshold amounts. The Plan is managed through a separate trust, which is considered a variable interest entity. As the Fund is the primary beneficiary, the Fund consolidates the Plan in its financial statements.

If the distributable cash flow per unit exceeds the base distribution, a percentage of the distributable cash (the participation rate) is contributed by the Fund into a separate trust. The funds in the trust are used to purchase units of the Fund in the open market, to be provided to eligible employees as bonus compensation. Threshold amounts and participation rates are as follows:

Excess percentage	Participation rate
5% or less	Nil
Greater than 5% and up to 10%	10% of any excess over 5%
Greater than 10% and up to 20%	10% of any excess over 5%, plus 20% of any excess over 10%
Greater than 20%	10% of any excess over 5%, plus 20% of any excess over 10%, plus 25% of any excess over 20%

The Fund records annual awards under the Plan as compensation expense over the vesting period. For the year ended December 31, 2006, the distributable cash per unit of the Fund exceeded the threshold amount. As a result, the Fund will transfer \$22,898 to the LTIP trust in the second quarter of 2007. As no grant date has occurred in respect of this award, no compensation expense was recorded under the Plan for the three month period ended March 31, 2007.

8. Unit-based compensation

Under the terms of the Acquisition Agreement between the Vendor and the Fund, the Fund assumed certain obligations under an employment agreement with the Chief Financial Officer. Under the employment agreement, the Fund may issue a maximum of 6,944 of XS Cargo Exchangeable LP Units and 4,789 Subordinated LP Units per year based on performance until 2009. If awarded, the units are issued on the anniversary date of the IPO, May 17, 2005. The Fund accrues a contingent award throughout the year, based on the estimated fair value of the units at the grant date. The estimated value is included in administrative and operating expenses and increases non-controlling interest on the balance sheet. For the three months ended March 31, 2007, the Fund has recognized compensation cost of \$43,500 (March 31, 2006 - \$30,000). The Fund has accrued a contingent award of \$143,170 (December 31, 2006 - \$99,670), which if granted, will be issued in May 2007.

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9. Variable interest entity

The Fund has a vendor supply and volume rebate agreement with Samra Imports Ltd., (“Samra”). Samra imports products from China which it sells to the Fund and other customers. Samra is the Fund’s largest supplier accounting for approximately 19% of the Fund’s purchases since the commencement of the agreement and the Fund is Samra’s largest customer. The purpose of the agreement is to outline the supply terms and to provide the Fund with a rebate based on its significant volume of purchases from Samra. The Fund has determined that Samra is a variable interest entity and that the supply and rebate agreement represents a variable interest in Samra. The Fund has determined, however, that it is not the primary beneficiary under the supply and rebate agreement since the Fund is not entitled to receive a majority of Samra’s expected residual returns or absorb a majority of its expected losses. As Samra is a separate legal entity, in which the Fund has now ownership interest, XS Cargo does not have direct access to Samra’s assets and Samra’s creditors do not have recourse against XS Cargo.

During the three months ended March 31, 2007, the Fund purchased approximately \$1,800,000 (March 31, 2006 - \$2,500,000) of inventory from Samra. Included in accounts payable, as at March 31, 2007, is a balance of \$608,689 (December 31, 2006 - \$Nil), owing to Samra related to those purchases. Samra issued the Fund a volume rebate for purchases made from for the three months ended March 31, 2007 in the amount of \$80,000, which is included in rebate and other receivables.

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10. Basic and diluted earnings per unit

The following table outlines the adjustments to the numerator and denominator to calculate the basic and diluted earning per unit:

	Basic Earnings per Unit	Dilution Adjustments		Diluted Earnings per Unit
March 31, 2007				
Net loss	\$(946,985)	\$(913,473)	(a)	\$(1,860,458)
Average Units outstanding	6,106,000	5,889,916	(b)	11,995,916
Earnings per Unit	(0.16)			(0.16)
	Basic Earnings per Unit	Dilution Adjustments		Diluted Earnings per Unit
March 31, 2006				
Net earnings	\$723,545	\$696,549	(a)	\$1,420,094
Average Units outstanding	6,106,000	5,878,183	(b)	11,984,183
Earnings per Unit	0.12			0.12

(a) Adjustment to add back non-controlling interest if Exchangeable LP Units and Subordinated LP Units are converted to Fund Units

(b) Adjustment to reflect the conversion of Exchangeable LP Units and Subordinated LP Units to Fund Units on a one-for-one basis

11. Seasonal nature of the business

The Fund's results for the period are not necessarily indicative of the results that may be expected for the full year due to seasonal variations in sales levels. The business historically experiences a higher level of sales in the fourth quarter and a lower level of sales in the first quarter due to seasonal shopping patterns. Occupancy-related expenses, certain administrative and operating expenses, amortization, and interest expense remain relatively steady throughout the year.

12. Segmented information

The Fund identifies operating segments based on business activities, management responsibility and geography. The Fund operates within a single operating segment, being the operation of closeout retail stores in Canada. All of the Fund's assets are located in Canada.

XS Cargo Income Fund
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13. Subsequent events

Subsequent to March 31, 2007, XS Cargo entered into lease agreements to open new stores in Belleville, Ontario; Peterborough, Ontario and Sarnia, Ontario.

On April 1, 2007, the Fund commenced conversion to a new point of sale and inventory allocation system. The total implementation costs are expected to be \$2,500,000, which includes hardware, software and implementation services.

On May 9, 2007, the Fund announced a reduction in the monthly distribution rate to \$0.046875 per Fund Unit and Exchangeable LP Unit, beginning with the May 2007 distribution, which is payable on June 15, 2007 to unitholders of record at the close of business on May 31, 2007. On an annualized basis, the reduced distribution rate is \$0.5625 per Fund Unit and Exchangeable LP Unit.

14. Restatement of previously issued financial statements

The Fund's credit agreement was amended in February 2007, at which time the Fund's distribution rate was \$1.2375 annually per Fund Unit, Exchangeable LP Unit and Subordinated LP Unit or \$14,844,946 annually in total. The Fund subsequently announced a reduction in its distribution rate to \$0.5625 per Fund Unit and Exchangeable LP Unit and suspended distributions on Subordinated LP Units, resulting in an annualized distribution amount of \$5,395,420 in total. The credit agreement and financial covenants were not adjusted to reflect the new distribution rates. Consequently, the Fund is not in compliance with the fixed charge coverage ratio covenant, which is applied on a historical basis.

As a result of the breach of the existing fixed charge coverage covenant, the Fund amended and restated its March 31, 2007 interim financial statements to reclassify \$15,000,000 of the Term Loan as a current liability on the balance sheet and provide additional note disclosure. The restatement has no impact on the consolidated statements of earnings and comprehensive income; (deficit) retained earnings or cash flows.