FIRST QUARTER REPORT

FOR THE 13-WEEK PERIOD ENDED JUNE 28, 2014

"We are what we repeatedly do. Excellence, then, is not an act, but a habit."

— Aristotle

Indigo

Enrich your life™

Indigo Chapters Coles indigo.ca

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Management's Discussion and Analysis

The following Management's Discussion and Analysis ("MD&A") is prepared as at August 5, 2014 and is based primarily on the unaudited interim condensed consolidated financial statements of Indigo Books & Music Inc. (the "Company" or "Indigo") for the 13-week periods ended June 28, 2014 and June 29, 2013. The Company's unaudited interim condensed consolidated financial statements and accompanying notes are reported in Canadian dollars and have been prepared in accordance with International Accounting Standard ("IAS") 34, "Interim Financial Reporting." The same accounting policies and methods of computation as those used in the preparation of the fiscal 2014 Annual Report were followed in the preparation of these unaudited interim condensed consolidated financial statements.

These unaudited interim condensed consolidated financial statements do not contain all disclosures required by International Financial Reporting Standards ("IFRS") for annual financial statements. This MD&A should be read in conjunction with the unaudited interim condensed consolidated financial statements and notes contained in this Quarterly Report, the audited annual consolidated financial statements and accompanying notes for the 52-week period ended March 29, 2014 and the MD&A included in the Company's fiscal 2014 Annual Report. The Annual Report and additional information about the Company, including the Annual Information Form, can be found on SEDAR at *www.sedar.com*.

Overview

Indigo is Canada's largest book, gift, and specialty toy retailer, operating stores in all ten provinces and one territory in Canada and offering online sales through its *indigo.ca* website. As at June 28, 2014, the Company operated 92 superstores under the banners *Chapters* and *Indigo*, and operated 131 small format stores under the banners *Coles*, *Indigo*, *Indigospirit*, *SmithBooks*, and *The Book Company*. During the first quarter of fiscal 2015, the Company closed three superstores. The Company also has a 50% interest in Calendar Club of Canada Limited Partnership ("Calendar Club"), which operates seasonal kiosks and year-round stores in shopping malls across Canada.

Indigo operates a separate registered charity under the name Indigo Love of Reading Foundation (the "Foundation"). The Foundation provides new books and learning material to high-needs elementary schools across the country through donations from Indigo, its customers, suppliers, and employees.

The weighted average number of common shares outstanding for the first quarter of fiscal 2015 was 25,632,036 as compared to 25,583,491 last year. As at August 5, 2014, the number of outstanding common shares was 25,341,939 with a book value of $204.2 million. The number of common shares reserved for issuance under the employee stock option plan is 3,301,291 as at August 5, 2014. As at June 28, 2014, there were 2,118,350 stock options outstanding of which 218,390 were exercisable.

Results of Operations

The following table summarizes the Company's consolidated results of operations for the periods indicated. The classification of financial information presented below is specific to Indigo and may not be comparable to that of other retailers.

(millions of Canadian dollars)	**13-week period ended June 28, 2014**	**% Revenues**	13-week period ended June 29, 2013	% Revenues
Revenues	**180.8**	**100.0**	171.5	100.0
Cost of sales	**(100.8)**	**55.8**	(99.3)	57.9
Cost of operations	**(67.0)**	**37.1**	(66.4)	38.7
Selling, administrative, and other expenses	**(20.3)**	**11.2**	(20.2)	11.8
Adjusted EBITDA[1]	**(7.3)**	**(4.0)**	(14.4)	(8.4)

1 Earnings before interest, taxes, depreciation, amortization, impairment, and equity investment. Also see "Non-IFRS Financial Measures".

Revenues Increased Despite Operating Seven Fewer Stores

Total consolidated revenues for the 13-week period ended June 28, 2014 increased $9.3 million or 5.4% to $180.8 million from $171.5 million for the same period last year. The increase in revenue was partly driven by a shift in the timing of Easter and the launch of American Girl® specialty boutiques. The majority of the growth came from underlying business improvement with double-digit increases in lifestyle, paper, and toys. Books also experienced growth in the quarter for the first time since fiscal 2010.

Comparable store sales for the first quarter increased 8.3% in superstores and 1.9% in small format stores. The increase was mainly driven by the reasons mentioned above. Comparable store sales are defined as sales generated by stores that have been open for more than 12 months on a 52-week basis. It is a key performance indicator for the Company as this measure excludes sales fluctuations due to store closings, permanent relocation, and chain expansion. As at June 28, 2014, the Company operated five fewer superstores and two fewer small format stores compared to June 29, 2013.

Online sales increased by $2.5 million or 14.0% to $20.3 million for the 13-week period ended June 28, 2014 compared to $17.8 million for the same period last year. Online sales experienced double-digit increases in books, lifestyle, paper, and toys. The number of customers purchasing across both retail and digital channels also increased. This reflects the Company's commitment to developing the digital customer experience and moving towards becoming more omni-channel.

Revenues from other sources include revenues generated through cafés, irewards card sales, revenue from unredeemed gift cards ("gift card breakage"), revenue from unredeemed plum points ("Plum breakage"), corporate sales, and revenue-sharing with Kobo. Revenues from other sources decreased $0.6 million or 9.7% to $5.6 million for the 13-week period ended June 28, 2014 compared to $6.2 million for the same period last year primarily as a result of lower irewards membership income, gift card and Plum breakage. irewards card sales have decreased by $0.4 million compared to the same period last year. This decrease is consistent with the Company's expectations as members moved to the free plum rewards program ("Plum"). Gift card breakage decreased by $0.1 million due to lower gift card sales this year compared to the same period last year.

Revenues by channel are highlighted below:

(millions of Canadian dollars)	**13-week period ended June 28, 2014**	13-week period ended June 29, 2013	% increase (decrease)	Comparable store sales % increase (decrease)
Superstores	**129.7**	122.7	5.7	8.3
Small format stores	**25.2**	24.8	1.6	1.9
Online (including store kiosks)	**20.3**	17.8	14.0	N/A
Other	**5.6**	6.2	(9.7)	N/A
	180.8	171.5	5.4	7.2

Revenues by product line are as follows:

	13-week period ended June 28, 2014	13-week period ended June 29, 2013
Print[1]	**68.1%**	71.5%
General merchandise[2]	**27.4%**	21.9%
eReading[3]	**2.2%**	3.8%
Other[4]	**2.4%**	2.8%
Total	**100.0%**	100.0%

1 Includes books, calendars, magazines, newspapers, and shipping revenue.
2 Includes lifestyle, paper, toys, music, DVDs, electronics, and shipping revenue.
3 Includes eReaders, eReader accessories, Kobo revenue share, and shipping revenue.
4 Includes cafés, irewards, gift card breakage, Plum breakage, and corporate sales.

A reconciliation between total revenues and comparable store sales is provided below:

	Superstores		Small format stores	
(millions of Canadian dollars)	**13-week period ended June 28, 2014**	13-week period ended June 29, 2013	**13-week period ended June 28, 2014**	13-week period ended June 29, 2013
Total revenues	**129.7**	122.7	**25.2**	24.8
Adjustments for stores not in both fiscal periods	**(0.3)**	(3.2)	**(0.5)**	(0.5)
Comparable store sales	**129.4**	119.5	**24.7**	24.3

Cost of Sales Percentage Is Lower Than Last Year

Cost of sales includes the landed cost of goods sold, online shipping costs, inventory shrink and damage reserve, less all vendor support programs. Cost of sales increased $1.5 million to $100.8 million for the 13-week period ended June 28, 2014, compared to $99.3 million for the same period last year. As discussed above, the increase was driven by higher sales volumes resulting in higher landed cost of goods sold. This increase was partially offset by a $1.7 million reduction in inventory provisions driven by the timing of markdowns for the summer clearance sale and by a $1.5 million increase in vendor support which offsets a comparable increase in sales discounts. As a percent of total revenues, cost of sales decreased by 2.1% to 55.8%, compared to 57.9% for the same period last year. The percentage decrease was driven by higher revenues, lower markdowns, and increased vendor support.

Cost of Operations Increased Over Last Year

Cost of operations includes all store, online, and distribution centre costs. Cost of operations for the 13-week period ended June 28, 2014 increased $0.6 million to $67.0 million this year, compared to $66.4 million for the same period last year. The increase was primarily driven by a $0.5 million, or 13.9%, increase in online costs and a $0.8 million increase in store labour compared to the same period last year. Higher online costs were driven by higher distribution centre fulfilment costs resulting from the increase in online sales volumes, while stores were using more labour to support increased sales volume. This increase was partially offset by lower store occupancy costs of $0.4 million compared to the same period last year as a result of the Company operating fewer stores. As a percent of total revenues, cost of operations decreased by 1.6% to 37.1% this year, compared to 38.7% for the same period last year. The percentage decrease was driven by higher revenues, as discussed above.

Selling, Administrative, and Other Expenses Remained Flat

Selling, administrative, and other expenses include all marketing, head office costs, and operating expenses associated with the Company's transformation. For the 13-week period ended June 28, 2014, these expenses increased $0.1 million to $20.3 million, compared to $20.2 million for the same period last year. Marketing expenses decreased by $1.5 million compared to the same period last year due to the timing of various marketing campaigns. This decrease was partially offset by a $0.7 million foreign exchange loss, compared to a $0.1 million foreign exchange gain last year. In the same period last year, expenses were also lower by $0.7 million due to the reversal of a severance provision and a true-up of the Company's fiscal 2013 bonus accrual.

Adjusted EBITDA Improved Versus Last Year

Adjusted EBITDA, defined as earnings before interest, taxes, depreciation, amortization, impairment, and equity investment improved by $7.1 million to a loss of $7.3 million for the 13-week period ended June 28, 2014, compared to a loss of $14.4 million for the same period last year. Adjusted EBITDA as a percent of revenues was a loss of 4.0% this year compared to a loss of 8.4% for the same period last year. As discussed above, the improvement was driven by higher sales and improved margin rates across most merchandise categories as the Company begins to see the benefits of the significant transformational investments made in prior periods.

Depreciation and Amortization Decreased Compared to Last Year
Depreciation and amortization for the 13-week period ended June 28, 2014 decreased by $0.2 million to $6.6 million compared to $6.8 million for the same period last year. Capital expenditures in the first quarter of fiscal 2015 totalled $4.2 million compared to $3.1 million for the same period last year. Capital expenditures in the first quarter of fiscal 2015 included $1.6 million for store construction, renovations, and equipment, $2.0 million for intangible assets (primarily application software and internal development costs), and $0.6 million for technology equipment. None of the $0.6 million expenditure in technology equipment was financed through finance leases. The increase in capital expenditures in the current year resulted from the Company's continued implementation of its transformation strategy.

Net Interest Income Decreased Compared to Last Year
The Company recognized net interest income of $0.4 million for the 13-week period ended June 28, 2014 compared to $0.6 million for the same period last year. The decrease in interest was driven by lower cash balances compared to the same period last year as the Company uses cash to implement its transformation strategy. The Company nets interest income against interest expense.

Loss from Equity Investment Increased Compared to Last Year
The Company uses the equity method to account for its investment in Calendar Club and recognizes its share of Calendar Club's earnings and losses as part of consolidated net earnings and losses. Indigo recognized a net loss from Calendar Club of $0.5 million for the 13-week period ended June 28, 2014 compared to a net loss of $0.4 million for the same period last year.

Income Tax Recovery Decreased Compared to Last Year
The Company did not recognize an income tax recovery for the 13-week period ended June 28, 2014 compared to an income tax recovery of $5.8 million for the same period last year. In fiscal 2014, the Company recorded a valuation allowance against deferred tax assets based on management's best estimate of future taxable income that the Company expected to achieve from reviewing its latest forecast. The Company's view of its latest forecast has not changed since the fiscal 2014 period end, and as such, there is no change to the net deferred tax asset for the first quarter of fiscal 2015, as the increase in the gross amount of the deferred tax asset is offset by an equal increase in the valuation allowance.

Net Loss Improved Versus Last Year

The Company recognized a net loss of $14.0 million for the 13-week period ended June 28, 2014 ($0.55 net loss per common share), compared to a net loss of $15.0 million ($0.59 net loss per common share) for the same period last year. As discussed above, the improvement was driven by higher revenues, partially offset by lower income tax recovery.

Seasonality and First Quarter Results

Indigo's business is highly seasonal and follows quarterly sales and profit (loss) fluctuation patterns, which are similar to those of other retailers that are highly dependent on the December holiday sales season. A disproportionate amount of revenues and profits are earned in the third quarter. As a result, quarterly performance is not necessarily indicative of the Company's performance for the rest of the year. The following table sets out revenues, net earnings (loss) attributable to shareholders of the Company, basic and diluted earnings (loss) per share for the preceding eight fiscal quarters.

	Fiscal quarters							
(millions of Canadian dollars, except per share data)	**Q1 Fiscal 2015**	Q4 Fiscal 2014	Q3 Fiscal 2014	Q2 Fiscal 2014	Q1 Fiscal 2014	Q4 Fiscal 2013	Q3 Fiscal 2013	Q2 Fiscal 2013
Revenues	**180.8**	184.3	332.4	179.4	171.5	184.0	322.6	185.6
Total net earnings (loss)	**(14.0)**	(14.4)	8.5	(10.1)	(15.0)	(8.2)	22.0	(4.0)
Basic earnings (loss) per share	**$ (0.55)**	$ (0.56)	$ 0.33	$ (0.39)	$ (0.59)	$ (0.32)	$ 0.86	$ (0.16)
Diluted earnings (loss) per share	**$ (0.55)**	$ (0.56)	$ 0.33	$ (0.39)	$ (0.59)	$ (0.32)	$ 0.86	$ (0.16)

Overview of Consolidated Balance Sheets

Total Assets

As at June 28, 2014, total assets decreased $44.1 million to $501.2 million, compared to $545.3 million as at June 29, 2013. The decrease was primarily due to a $40.7 million decrease in cash and cash equivalents. The Company used its cash to make significant investments in capital assets and working capital as part of its transformation strategy. Capital asset purchases for the last four quarters totalled $30.3 million as the Company invested in store renovations, supply chain efficiency, and updated information systems. The Company also used $16.6 million of cash towards working capital in the last four quarters. The Company's changing product assortment now includes more items with shorter payment terms, which drove the increased use of cash towards working capital.

On a fiscal year-to-date basis, total assets decreased $11.4 million to $501.2 million, compared to $512.6 million as at March 29, 2014. The decrease was primarily driven by decreases in cash and cash equivalents and inventories. The $6.9 million decrease in cash and cash equivalents and $5.8 million decrease in inventories are both consistent with the seasonal nature of the business.

Total Liabilities

As at June 28, 2014, total liabilities decreased $10.4 million to $202.7 million, compared to $213.1 million as at June 29, 2013. The decrease was primarily the result of a $8.0 million decrease in current and long-term accounts payable and accrued liabilities. As discussed above, the Company's changing product assortment now includes more items with shorter payment terms, resulting in a decrease in accounts payable and accrued liabilities.

On a fiscal year-to-date basis, total liabilities increased $1.8 million to $202.7 million, compared to $200.9 million as at March 29, 2014. The increase was primarily due to a $1.9 million increase in current and long-term accounts payable and accrued liabilities as a result of the timing of payments at quarter-end.

Total Equity

Total equity at June 28, 2014 decreased $33.8 million to $298.4 million, compared to $332.2 million as at June 29, 2013. The decrease in total equity was primarily due to net loss of $30.0 million and dividend payments of $5.6 million in the last four quarters. Share capital increased by $0.4 million due to the exercise of stock options. Contributed surplus increased $1.4 million due to the expensing of employee stock options and Directors' deferred share units. In the same period last year, the Company offered a one-time cash repurchase to certain option holders, which resulted in a $0.5 million net reduction to contributed surplus.

Working Capital and Leverage

The Company's working capital position usually declines from the end of its fiscal year until the third fiscal quarter due to the seasonal nature of the business. The Company relies on cash and accounts payable to fund the business before generating a disproportionate amount of cash during the December holiday season. The Company reported working capital of $179.1 million as at June 28, 2014, compared to $203.5 million as at June 29, 2013 and $189.7 million as at March 29, 2014. The decrease in working capital was mainly driven by lower cash and cash equivalents due to money spent in the Company's transformation.

The Company's leverage position (defined as Total Liabilities to Total Equity) was 0.7:1 at the end of the current quarter compared to 0.6:1 as at June 29, 2013 and 0.6:1 as at March 29, 2014.

Overview of Consolidated Statements of Cash Flows

Cash and cash equivalents decreased $6.9 million for the 13-week period ended June 28, 2014 compared to a decrease of $19.2 million in the same period last year. The decrease in the current quarter was driven by cash flows used in operating activities of $2.1 million and investing activities of $3.8 million along with a negative effect of foreign currency exchange rate changes on cash and cash equivalents of $1.1 million, partly offset by cash flows generated from financing activities of $0.1 million.

Cash Flows from Operating Activities

The Company used cash flows of $2.1 million for operating activities for the 13-week period ended June 28, 2014 compared to using $13.3 million in the same period last year, a decrease of $11.2 million. This improvement was mainly driven by lower net loss for the first quarter of fiscal 2015 compared to the same period last year. Excluding the $5.8 million impact from deferred tax assets last year, pre-tax net loss was $14.0 million in the current period compared to $20.9 million in the same period last year. The Company also generated $3.6 million of cash from working capital this year, compared to $1.0 million last year.

Cash Flows from Investing Activities

Total cash spent on capital projects for the 13-week period ended June 28, 2014 was $4.2 million compared to $3.1 million spent last year, as outlined below:

(millions of Canadian dollars)	**13-week period ended June 28, 2014**	13-week period ended June 29, 2013
Store construction, renovations and equipment	**1.6**	0.9
Intangible assets (primarily application software and internal development costs)	**2.0**	1.8
Technology equipment	**0.6**	0.4
	4.2	3.1

The Company used cash flows of $3.8 million for investing activities in the first quarter of fiscal 2015 compared to $2.5 million used by investing activities in the same period last year, an increase of $1.3 million. The increase resulted from

greater spending on capital projects as the Company continues to implement its transformation strategy. The Company received $0.4 million of interest in the first quarter of fiscal 2015 compared to $0.6 million in the same period last year.

Cash Flows from Financing Activities

The Company generated cash flows of $0.1 million from financing activities for the 13-week period ended June 28, 2014 compared to using $4.0 million in the same period last year, an improvement of $4.1 million. The Company did not make any dividend payments in the current quarter compared to making $2.8 million of dividend payments in the same period last year. The decrease in dividend payments resulted from the suspension of quarterly dividend payments beyond December 3, 2013. Last year, the Company also used $1.0 million of cash in the first quarter to repurchase stock options.

Liquidity and Capital Resources

The Company has a highly seasonal business which generates the majority of its revenues and cash flows during the December holiday season. Indigo has minimal accounts receivable and a significant portion of book products are purchased on trade terms with the right to return. Indigo's main sources of capital are cash flows generated from operations, long-term debt, and cash and cash equivalents.

Based on the Company's liquidity position and cash flow forecast, management expects its current cash position and cash flows generated from operations to be sufficient to meet its working capital needs and debt service requirements for fiscal 2015. In addition, the Company has the ability to reduce capital spending to fund debt requirements if necessary; however, a long-term decline in capital expenditures may negatively impact revenues and profit growth. No dividend has been declared this quarter.

There can be no assurance that operating levels will not deteriorate over the ensuing fiscal year, which could result in the Company being unable to meet its current working capital and debt service requirements. In addition, other factors not presently known to management could materially and adversely affect Indigo's future cash flows. In such events, the Company would be required to obtain additional capital as is necessary to satisfy its working capital and debt service requirements from other sources. Alternative sources of capital could result in increased dilution to shareholders and may be on terms that are not favourable to the Company.

Accounting Policies

Critical Accounting Judgments and Estimates

The discussion and analysis of Indigo's operations and financial condition are based upon the unaudited interim condensed consolidated financial statements, which have been prepared in accordance with IFRS and IAS 34. The preparation of these unaudited interim condensed consolidated financial statements in conformity with IFRS requires management to undertake a number of judgments and estimates about the recognition and measurement of assets, liabilities, revenues, and expenses. These judgments and estimates are based on management's historical experience and other assumptions which the Company believes to be reasonable under the circumstances. Actual results may differ from the judgments and estimates made by management, and actual results will seldom equal estimates.

Material judgments and estimates are made with respect to: revenue recognition from unredeemed gift cards and plum points; fair value of plum points; inventory shrinkage; reserves for slow-moving or damaged products and products that have been permanently marked down; vendor settlement; fair value of share-based instruments and number of equity instruments expected to vest; identification of cash generating units ("CGUs") and expected future cash flows from CGUs; depreciation and amortization periods; lease classification; and recognition and valuation of deferred tax assets.

The Company evaluates its judgments and estimates on an ongoing basis and methods used to calculate critical accounting estimates are consistent with prior periods. The significant accounting policies and significant judgments and estimates of the Company are described in notes 3 and 4 of the consolidated financial statements contained in the Company's fiscal 2014 Annual Report.

Accounting Standards Implemented in the First Quarter of Fiscal 2015

Adoption of these amendments and standards in the first quarter of fiscal 2015 impacted the Company's results of operations, financial position, and disclosures as follows:

Impairment of Assets ("IAS 36")

In May 2013, the International Accounting Standards Board ("IASB") issued amendments to IAS 36 which require disclosures about assets or CGUs for which an impairment loss was recognized or reversed during the period. The amendments are effective for annual periods beginning on or after January 1, 2014 and must be applied prospectively. Additional information will be disclosed through notes to financial statements as required.

Levies ("IFRIC 21")
The IASB has issued IFRIC 21, an interpretation which provides guidance on when to recognize a liability for a levy imposed by a government, both for levies that are accounted for in accordance with IAS 37, "Provisions, Contingent Liabilities, and Contingent Assets," and those where the timing and amount of the levy is certain. A levy is an outflow of resources embodying economic benefits that is imposed by governments on entities in accordance with legislation. This interpretation is effective for annual periods beginning on or after January 1, 2014 and must be applied retrospectively. Implementation of IFRIC 21 had no impact on the Company's results of operations, financial position, or disclosures.

Financial Instruments: Presentation ("IAS 32")
The IASB issued amendments to IAS 32 that clarify its requirements for offsetting financial instruments. These amendments must be applied retrospectively and are effective for annual periods beginning on or after January 1, 2014. Implementation of these amendments had no impact on the Company's results of operations, financial position, or disclosures.

New Accounting Pronouncements

Revenue from Contracts with Customers ("IFRS 15")
In May 2014, the IASB issued IFRS 15, a new standard that specifies how and when to recognize revenue as well as requiring entities to provide users of financial statements with more informative, relevant disclosures. IFRS 15 supersedes IAS 18, "Revenue," IAS 11, "Construction Contracts," and a number of revenue-related interpretations. Application of IFRS 15 is mandatory for all IFRS reporters and it applies to nearly all contracts with customers: the main exceptions are leases, financial instruments, and insurance contracts. IFRS 15 must be applied for reporting periods beginning on or after January 1, 2017 and early adoption is permitted. The Company is assessing the impact of adopting this standard on its results of operations, financial position, and disclosures.

Financial Instruments ("IFRS 9")
In July 2014, the IASB finalized IFRS 9 effective for periods beginning on or after January 1, 2018. IFRS 9 provides guidance on the classification and measurement of financial assets and financial liabilities and is the first phase of the IASB's project to replace IAS 39, "Financial Instruments: Recognition and Measurement." The Company is assessing the impact of the new standard on its results of operations, financial position, and disclosures.

Except as discussed above, the IASB has not issued any other new standards, amendments to standards, or interpretations that impact the Company during the 13-week period ended June 28, 2014. Indigo's evaluations of previously issued new standards, amendments to standards, and interpretations are consistent with those disclosed in note 5 of the Company's fiscal 2014 Annual Report. New accounting pronouncements have not been applied in preparing these unaudited interim condensed consolidated financial statements, except as discussed above.

General Development of the Business

The Company's strategic objectives are substantially the same as those disclosed in the MD&A section of its fiscal 2014 Annual Report.

Risks and Uncertainties

The risks and uncertainties faced by the Company are substantially the same as those disclosed in the MD&A section of its fiscal 2014 Annual Report.

Disclosure Controls and Procedures

Management is responsible for establishing and maintaining a system of disclosure controls and procedures to provide reasonable assurance that all material information relating to the Company is gathered and reported on a timely basis to senior management, including the Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO"), so that appropriate decisions can be made by them regarding public disclosure.

Internal Controls over Financial Reporting

Management is also responsible for establishing and maintaining adequate internal controls over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements for external purposes in accordance with IFRS.

All internal control systems, no matter how well designed, have inherent limitations. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to consolidated financial statement preparation and presentation. Additionally, management is necessarily required to use judgment in evaluating controls and procedures.

As required by National Instrument 52-109, "Certification of Disclosure in Issuers' Annual and Interim Filings," the CEO and CFO have evaluated, or caused to be evaluated under their supervision, the effectiveness of such internal controls over financial reporting using the framework established in the Internal Control –

Integrated Framework ("COSO Framework") published in 1992 by the Committee of Sponsoring Organizations of the Treadway Commission.

Changes in Internal Controls over Financial Reporting

Management has also evaluated whether there were changes in the Company's internal controls over financial reporting that occurred during the period beginning on March 30, 2014 and ended on June 28, 2014 that have materially affected, or are reasonably likely to materially affect, the Company's internal controls over financial reporting. The Company has determined that no material changes in internal controls over financial reporting have occurred in this period.

Cautionary Statement Regarding Forward-Looking Statements

The above discussion includes forward-looking statements. All statements other than statements of historical facts included in this discussion that address activities, events, or developments that the Company expects or anticipates will or may occur in the future are forward-looking statements. These statements are based on certain assumptions and analysis made by the Company in light of its experience, analysis, and its perception of historical trends, current conditions, and expected future developments as well as other factors it believes are appropriate in the circumstances. However, whether actual results and developments will conform to the expectations and predictions of the Company is subject to a number of risks and uncertainties, including the general economic, market or business conditions; competitive actions by other companies; changes in laws or regulations; and other factors, many of which are beyond the control of the Company. Consequently, all of the forward-looking statements made in this discussion are qualified by these cautionary statements and there can be no assurance that results or developments anticipated by the Company will be realized or, even if substantially realized, that they will have the expected consequences to, or effects on, the Company.

Non-IFRS Financial Measures

The Company prepares its consolidated financial statements in accordance with IFRS. In order to provide additional insight into the business, the Company has also provided non-IFRS data, including comparable store sales and adjusted EBITDA, in the discussion and analysis section above. These measures are specific to Indigo and have no standardized meaning prescribed by IFRS. Therefore, these measures may not be comparable to similar measures presented by other companies.

Comparable stores sales and adjusted EBITDA are key indicators used by the Company to measure performance against internal targets and prior period results. Both measures are commonly used by financial analysts and investors to compare Indigo to other retailers. Comparable store sales are defined as sales generated by stores that have been open for more than 12 months on a 52-week basis. It is a key performance indicator for the Company as this measure excludes sales fluctuations due to store closings, permanent relocation, and chain expansion. Adjusted EBITDA is defined as earnings before interest, taxes, depreciation, amortization, impairment, and equity investment. The method of calculating adjusted EBITDA is consistent with that used in prior periods.

A reconciliation between comparable store sales and revenues (the most comparable IFRS measure) was included earlier in this report. A reconciliation between adjusted EBITDA and earnings (loss) before income taxes (the most comparable IFRS measure) is provided below:

(millions of Canadian dollars)	**13-week period ended June 28, 2014**	13-week period ended June 29, 2013
Adjusted EBITDA	**(7.3)**	(14.4)
Depreciation of property, plant and equipment	**(3.7)**	(4.0)
Amortization of intangible assets	**(2.9)**	(2.7)
Interest on long-term debt and financing charges	**0.0**	0.0
Interest income on cash and cash equivalents	**0.4**	0.6
Share of loss from equity investment	**(0.5)**	(0.4)
Loss before income taxes	**(14.0)**	(20.9)

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NOTICE OF NO AUDITOR REVIEW OF INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Under National Instrument 51-102, Part 4, subsection 4.3(3)(a), if an auditor has not performed a review of the interim condensed consolidated financial statements, they must be accompanied by a notice indicating that the financial statements have not been reviewed by an auditor.

The accompanying unaudited interim condensed consolidated financial statements of the Company have been prepared by and are the responsibility of the Company's management.

The Company's independent auditor has not performed a review of these interim condensed consolidated financial statements.

Heather Reisman
Chair & Chief Executive Officer

Laura Carr
Chief Financial Officer

Dated as of the 5th day of August, 2014.

Consolidated Balance Sheets

(Unaudited)

(thousands of Canadian dollars)	**As at June 28, 2014**	As at June 29, 2013	As at March 29, 2014
ASSETS			
Current			
Cash and cash equivalents (note 5)	**150,667**	191,346	157,578
Accounts receivable	**8,802**	9,010	5,582
Inventories (note 6)	**213,185**	207,029	218,979
Prepaid expenses	**6,182**	5,288	5,184
Total current assets	**378,836**	412,673	387,323
Property, plant and equipment	**56,931**	56,144	58,476
Intangible assets	**20,723**	21,283	21,587
Equity investment	**79**	597	598
Deferred tax assets	**44,604**	54,570	44,604
Total assets	**501,173**	545,267	512,588
LIABILITIES AND EQUITY			
Current			
Accounts payable and accrued liabilities	**138,553**	145,892	136,428
Unredeemed gift card liability	**46,776**	46,901	46,827
Provisions	**911**	1,828	928
Deferred revenue	**13,002**	13,753	12,860
Income taxes payable	**–**	11	–
Current portion of long-term debt (note 12)	**446**	757	584
Total current liabilities	**199,688**	209,142	197,627
Long-term accrued liabilities	**2,719**	3,368	2,896
Long-term provisions	**153**	78	164
Long-term debt (note 12)	**177**	527	227
Total liabilities	**202,737**	213,115	200,914
Equity			
Share capital (note 7)	**204,204**	203,805	203,812
Contributed surplus (note 8)	**9,198**	7,789	8,820
Retained earnings	**85,034**	120,558	99,042
Total equity	**298,436**	332,152	311,674
Total liabilities and equity	**501,173**	545,267	512,588

See accompanying notes

On behalf of the Board:

Heather Reisman, Director

Michael Kirby, Director

Consolidated Statements of Loss and Comprehensive Loss

(Unaudited)

(thousands of Canadian dollars, except per share data)	**13-week period ended June 28, 2014**	13-week period ended June 29, 2013
Revenues (note 9)	**180,802**	171,525
Cost of sales	**(100,849)**	(99,289)
Gross profit	**79,953**	72,236
Operating, selling and administrative expenses (note 9)	**(93,810)**	(93,309)
Operating loss	**(13,857)**	(21,073)
Interest on long-term debt and financing charges	**(9)**	(27)
Interest income on cash and cash equivalents	**377**	584
Share of loss from equity investment	**(519)**	(371)
Loss before income taxes	**(14,008)**	(20,887)
Income tax recovery	**–**	5,839
Net loss and comprehensive loss for the period	**(14,008)**	(15,048)
Net loss per common share (note 10)		
Basic	**$ (0.55)**	$ (0.59)
Diluted	**$ (0.55)**	$ (0.59)

See accompanying notes

Consolidated Statements of Changes in Equity

(Unaudited)

(thousands of Canadian dollars)	Share Capital	Contributed Surplus	Retained Earnings	Total Equity
Balance, March 30, 2013	203,805	8,128	138,389	350,322
Loss for the 13-week period ended June 29, 2013	–	–	(15,048)	(15,048)
Exercise of options (notes 7 and 8)	–	–	–	–
Stock-based compensation (note 8)	–	503	–	503
Directors' compensation (note 8)	–	133	–	133
Dividends paid	–	–	(2,783)	(2,783)
Repurchase of options (note 8)	–	(975)	–	(975)
Balance, June 29, 2013	203,805	7,789	120,558	332,152
Balance, March 29, 2014	**203,812**	**8,820**	**99,042**	**311,674**
Loss for the 13-week period ended June 28, 2014	**–**	**–**	**(14,008)**	**(14,008)**
Exercise of options (notes 7 and 8)	**392**	**(61)**	**–**	**331**
Stock-based compensation (note 8)	**–**	**335**	**–**	**335**
Directors' compensation (note 8)	**–**	**104**	**–**	**104**
Balance, June 28, 2014	**204,204**	**9,198**	**85,034**	**298,436**

See accompanying notes

Consolidated Statements of Cash Flows

(Unaudited)

(thousands of Canadian dollars)	**13-week period ended June 28, 2014**	13-week period ended June 29, 2013
CASH FLOWS FROM OPERATING ACTIVITIES		
Net loss for the period	**(14,008)**	(15,048)
Add (deduct) items not affecting cash		
Depreciation of property, plant and equipment	**3,698**	4,039
Amortization of intangible assets	**2,868**	2,713
Loss on disposal of capital assets	**7**	10
Stock-based compensation (note 8)	**335**	503
Directors' compensation (note 8)	**104**	133
Deferred tax assets	**–**	(5,839)
Other	**1,145**	(575)
Net change in non-cash working capital balances (note 11)	**3,587**	976
Interest on long-term debt and financing charges	**9**	27
Interest income on cash and cash equivalents	**(377)**	(584)
Share of loss from equity investment	**519**	371
Cash flows used in operating activities	**(2,113)**	(13,274)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of property, plant and equipment	**(2,160)**	(1,290)
Addition of intangible assets	**(2,004)**	(1,832)
Interest received	**377**	640
Cash flows used in investing activities	**(3,787)**	(2,482)
CASH FLOWS FROM FINANCING ACTIVITIES		
Repayment of long-term debt	**(186)**	(197)
Interest paid	**(10)**	(36)
Proceeds from share issuances (note 7)	**331**	–
Dividends paid	**–**	(2,783)
Repurchase of options	**–**	(975)
Cash flows from (used in) financing activities	**135**	(3,991)
Effect of foreign currency exchange rate changes on cash and cash equivalents	**(1,146)**	531
Net decrease in cash and cash equivalents during the period	**(6,911)**	(19,216)
Cash and cash equivalents, beginning of period	**157,578**	210,562
Cash and cash equivalents, end of period	**150,667**	191,346

See accompanying notes

Notes to the Interim Condensed Consolidated Financial Statements

June 28, 2014
(Unaudited)

1. CORPORATE INFORMATION

Indigo Books & Music Inc. (the "Company" or "Indigo") is a corporation domiciled and incorporated under the laws of the Province of Ontario in Canada. The Company's registered office is located at 468 King Street West, Toronto, Ontario, M5V 1L8, Canada. The unaudited interim condensed consolidated financial statements of the Company comprise the Company, its equity investment in Calendar Club of Canada Limited Partnership ("Calendar Club"), and its wholly-owned subsidiary, Soho Inc. The Company is the ultimate parent of the consolidated organization.

2. BASIS OF PREPARATION

Statement of compliance

These unaudited interim condensed consolidated financial statements have been prepared using accounting policies consistent with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") and in accordance with International Accounting Standard ("IAS") 34, "Interim Financial Reporting." The same accounting policies and methods of computation as those used in the preparation of the fiscal 2014 Annual Report were followed in the preparation of these unaudited interim condensed consolidated financial statements. These unaudited interim condensed consolidated financial statements should be read in conjunction with the Company's fiscal 2014 Annual Report.

The unaudited interim condensed consolidated financial statements for the 13-week period ended June 28, 2014 (including comparatives) were approved by the Board of Directors on August 5, 2014.

Significant judgments and estimates

The preparation of these unaudited interim condensed consolidated financial statements in conformity with IFRS requires management to undertake a number of judgments and estimates about the recognition and measurement of assets, liabilities, revenues, and expenses. These judgments and estimates are

based on management's historical experience and other assumptions which the Company believes to be reasonable under the circumstances. Actual results may differ from the judgments and estimates made by management, and actual results will seldom equal estimates.

Material judgments and estimates are made with respect to: revenue recognition from unredeemed gift cards and plum rewards program ("Plum") points; fair value of Plum points; inventory shrinkage; reserves for slow-moving or damaged products and products that have been permanently marked down; vendor settlement; fair value of share-based instruments and number of equity instruments expected to vest; identification of cash generating units ("CGUs") and expected future cash flows from CGUs; depreciation and amortization periods; lease classification; and recognition and valuation of deferred tax assets.

3. CHANGES IN ACCOUNTING POLICIES

Adoption of these amendments and standards in the first quarter of fiscal 2015 impacted the Company's results of operations, financial position, and disclosures as follows:

Impairment of Assets ("IAS 36")

In May 2013, the International Accounting Standards Board ("IASB") issued amendments to IAS 36 which require disclosures about assets or CGUs for which an impairment loss was recognized or reversed during the period. The amendments are effective for annual periods beginning on or after January 1, 2014 and must be applied prospectively. Additional information will be disclosed through notes to financial statements as required.

Levies ("IFRIC 21")

The IASB has issued IFRIC 21, an interpretation which provides guidance on when to recognize a liability for a levy imposed by a government, both for levies that are accounted for in accordance with IAS 37, "Provisions, Contingent Liabilities, and Contingent Assets," and those where the timing and amount of the levy is certain. A levy is an outflow of resources embodying economic benefits that is imposed by governments on entities in accordance with legislation. This interpretation is effective for annual periods beginning on or after January 1, 2014 and must be applied retrospectively. Implementation of IFRIC 21 had no impact on the Company's results of operations, financial position, or disclosures.

Financial Instruments: Presentation ("IAS 32")
The IASB issued amendments to IAS 32 that clarify its requirements for offsetting financial instruments. These amendments must be applied retrospectively and are effective for annual periods beginning on or after January 1, 2014. Implementation of these amendments had no impact on the Company's results of operations, financial position, or disclosures.

New Accounting Pronouncements

Revenue from Contracts with Customers ("IFRS 15")
In May 2014, the IASB issued IFRS 15, a new standard that specifies how and when to recognize revenue as well as requiring entities to provide users of financial statements with more informative, relevant disclosures. IFRS 15 supersedes IAS 18, "Revenue," IAS 11, "Construction Contracts," and a number of revenue-related interpretations. Application of IFRS 15 is mandatory for all IFRS reporters and it applies to nearly all contracts with customers: the main exceptions are leases, financial instruments, and insurance contracts. IFRS 15 must be applied for reporting periods beginning on or after January 1, 2017 and early adoption is permitted. The Company is assessing the impact of adopting this standard on its results of operations, financial position, and disclosures.

Financial Instruments ("IFRS 9")
In July 2014, the IASB finalized IFRS 9 effective for periods beginning on or after January 1, 2018. IFRS 9 provides guidance on the classification and measurement of financial assets and financial liabilities and is the first phase of the IASB's project to replace IAS 39, "Financial Instruments: Recognition and Measurement." The Company is assessing the impact of the new standard on its results of operations, financial position, and disclosures.

Except as discussed above, the IASB has not issued any other new standards, amendments to standards, or interpretations that impact the Company during the 13-week period ended June 28, 2014. Indigo's evaluations of previously issued new standards, amendments to standards, and interpretations are consistent with those disclosed in note 5 of the Company's fiscal 2014 Annual Report. New accounting pronouncements have not been applied in preparing these unaudited interim condensed consolidated financial statements, except as discussed above.

4. SEASONALITY OF OPERATIONS

The business of Indigo follows a seasonal pattern, with sales of merchandise being highest in the third fiscal quarter due to consumer holiday buying patterns. As a result, a disproportionate portion of total annual revenues are typically earned in the third fiscal quarter. Therefore, the results of operations for the 13-week periods ended June 28, 2014 and June 29, 2013 are not indicative of the results of other periods.

5. CASH AND CASH EQUIVALENTS

Cash and cash equivalents consist of the following:

(thousands of Canadian dollars)	**June 28, 2014**	June 29, 2013	March 29, 2014
Cash	**86,181**	68,227	57,098
Restricted cash	**3,600**	816	3,369
Cash equivalents	**60,886**	122,303	97,111
Cash and cash equivalents	**150,667**	191,346	157,578

Restricted cash represents cash pledged as collateral for letter of credit obligations issued to support the Company's purchases of offshore merchandise.

6. INVENTORIES

The cost of inventories recognized as an expense was $101.6 million for the 13-week period ended June 28, 2014 (2013 – $97.0 million). Inventories consist of the landed cost of goods sold and exclude online shipping costs, inventory shrink and damage reserve, and all vendor support programs. The amount of inventory write-downs as a result of net realizable value lower than cost was $2.3 million for the 13-week period ended June 28, 2014 (2013 – $4.0 million), and there were no reversals of inventory write-downs that were recognized for the 13-week period ended June 28, 2014 (2013 – nil). The amount of inventory with net realizable value equal to cost was $1.8 million as at June 28, 2014 (June 29, 2013 – $1.1 million).

7. SHARE CAPITAL

Share capital consists of the following:

	13-week period ended June 28, 2014		13-week period ended June 29, 2013		52-week period ended March 29, 2014	
	Number of shares	**Amount C$ (thousands)**	Number of shares	Amount C$ (thousands)	Number of shares	Amount C$ (thousands)
Balance, beginning of period	**25,298,239**	**203,812**	25,297,389	203,805	25,297,389	203,805
Issued during the period						
Options exercised	**43,700**	**392**	–	–	850	7
Balance, end of period	**25,341,939**	**204,204**	25,297,389	203,805	25,298,239	203,812

8. SHARE-BASED COMPENSATION

As at June 28, 2014, 2,118,350 stock options were outstanding with exercise prices ranging from $7.20 to $15.21. Of these outstanding stock options, 218,390 were exercisable. As at June 29, 2013, there were 631,500 stock options outstanding of which 95,500 were exercisable.

The Company uses the fair value method of accounting for stock options, which estimates the fair value of the stock options granted on the date of grant, net of estimated forfeitures, and expenses this value over the vesting period. For the 13-week period ended June 28, 2014, the pre-forfeiture rate fair values of options granted were $1.3 million (2013 – less than $0.1 million).

The fair value of the employee stock options is estimated at the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions during the periods presented:

	13-week period ended June 28, 2014	13-week period ended June 29, 2013
Black-Scholes option pricing assumptions		
Risk-free interest rate	**1.2%**	1.2%
Expected volatility	**33.9%**	35.9%
Expected time until exercise	**3.0 years**	3.0 years
Expected dividend yield	**–**	4.0%
Other assumptions		
Forfeiture rate	**26.8%**	25.7%

Directors' compensation

The Company has established a Directors' Deferred Share Unit Plan ("DSU Plan"). Under the DSU Plan, Directors receive their annual retainer fees and other Board-related compensation in the form of deferred share units ("DSUs").

The number of shares reserved for issuance under this plan is 500,000. The Company issued 9,869 DSUs with a value of $0.1 million for the 13-week period ended June 28, 2014 (2013 – 12,082 DSUs with a value of $0.1 million). The number of DSUs to be issued to each Director is based on a set fee schedule. The grant date fair value of the outstanding DSUs as at June 28, 2014 was $3.4 million (June 29, 2013 – $3.0 million) and was recorded in contributed surplus. The fair value of DSUs is equal to the traded price of the Company's common shares on grant date.

9. SUPPLEMENTARY OPERATING INFORMATION

Supplemental product line revenue information:

	13-week period ended June 28, 2014	13-week period ended June 29, 2013
Print[1]	**123,074**	122,666
General merchandise[2]	**49,531**	37,487
eReading[3]	**3,892**	6,499
Other[4]	**4,305**	4,873
Total	**180,802**	171,525

1 Includes books, calendars, magazines, newspapers, and shipping revenue.
2 Includes lifestyle, paper, toys, music, DVDs, electronics, and shipping revenue.
3 Includes eReaders, eReader accessories, Kobo revenue share, and shipping revenue.
4 Includes cafés, irewards, gift card breakage, Plum breakage, and corporate sales.

Supplemental operating and administrative expenses information:

(thousands of Canadian dollars)	**13-week period ended June 28, 2014**	13-week period ended June 29, 2013
Wages, salaries and bonuses	**39,119**	37,100
Short-term benefits expense	**4,794**	4,557
Termination benefits expense	**170**	(173)
Retirement benefits expense	**342**	327
Stock-based compensation	**335**	503
Total employee benefits expense	**44,760**	42,314

Termination benefits arise when the Company terminates certain employment agreements.

10. LOSS PER SHARE

Loss per share is calculated based on the weighted average number of shares outstanding during the period. The Company's stock options were anti-dilutive as the Company reported a loss and, therefore, were not included in the June 28, 2014 and June 29, 2013 diluted loss per share calculations.

11. STATEMENTS OF CASH FLOWS

Supplemental cash flow information:

(thousands of Canadian dollars)	**13-week period ended June 28, 2014**	13-week period ended June 29, 2013
Net change in non-cash working capital balances:		
Accounts receivable	**(3,220)**	(1,884)
Inventories	**5,794**	9,504
Prepaid expenses	**(998)**	(1,135)
Accounts payable and accrued liabilities	**1,948**	(4,921)
Unredeemed gift card liability	**(51)**	(268)
Provisions	**(28)**	(340)
Deferred revenue	**142**	20
	3,587	976

12. CAPITAL MANAGEMENT

The Company's main objectives when managing capital are to safeguard its ability to continue as a going concern while maintaining adequate financial flexibility to invest in new business opportunities that will provide attractive returns to shareholders. The primary activities engaged by the Company to generate attractive returns include construction and related leasehold improvements of stores, the development of new business concepts, and investment in information technology and distribution capacity to support the online and retail networks. The Company's main sources of capital are its current cash position, cash flows generated from operations, and long-term debt. Cash flow is used to fund working capital needs, capital expenditures, and debt service requirements. There were no changes to these objectives for the 13-week period ended June 28, 2014. The Company primarily manages its capital by monitoring its available cash balance to ensure that sufficient funds are available for long-term debt and interest payments over the next year.

The following table summarizes selected capital structure information for the Company:

(thousands of Canadian dollars)	**June 28, 2014**	June 29, 2013	March 29, 2014
Current portion of long-term debt	**446**	757	584
Long-term debt	**177**	527	227
Total debt	**623**	1,284	811
Total equity	**298,436**	332,152	311,674
Total capital under management	**299,059**	333,436	312,485

13. RELATED PARTY TRANSACTIONS

The Company's related parties include its key management personnel, shareholders, defined contribution retirement plan, equity investment in Calendar Club, and subsidiary. Unless otherwise stated, none of the transactions incorporate special terms and conditions and no guarantees were given or received. Outstanding balances are usually settled in cash.

Transactions with key management personnel

Key management of the Company includes members of the Board of Directors as well as members of the Executive Committee. Key management personnel remuneration includes the following expenses:

(thousands of Canadian dollars)	**13-week period ended June 28, 2014**	13-week period ended June 29, 2013
Wages, salaries, bonus and consulting	**1,189**	1,208
Short-term benefits expense	**48**	58
Termination benefits expense	**–**	(277)
Retirement benefits expense	**12**	17
Stock-based compensation	**229**	271
Directors' compensation	**104**	133
Total remuneration	**1,582**	1,410

Transactions with shareholders

During the first quarter of fiscal 2015, Indigo purchased goods and services from companies in which Mr. Gerald W. Schwartz, who is the controlling shareholder of Indigo, holds a controlling or significant interest. For the 13-week period ended June 28, 2014, Indigo paid less than $0.1 million for these goods and services (2013 – $0.6 million). As at June 28, 2014, Indigo had no amounts payable to these companies and had $2.8 million of restricted cash pledged as collateral for letter of credit obligations issued to support the Company's purchases of merchandise from these companies (June 29, 2013 – no amounts payable and no restricted cash). All transactions were in the normal course of business for both Indigo and the related companies.

Transactions with defined contribution retirement plan

The Company's transactions with the defined contribution retirement plan include contributions paid to the retirement plan as disclosed in note 9. The Company has not entered into other transactions with the retirement plan.

Transactions with associate

The Company's associate, Calendar Club, is a seasonal operation which is dependent on the December holiday sales season to generate revenues. During the year, the Company loans cash to Calendar Club for working capital requirements and Calendar Club repays the loans once profits are generated in the third quarter. The net amount of these transactions for the 13-week period ended June 28, 2014 was $2.0 million paid by Indigo (2013 – $1.6 million paid by Indigo).

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