FIRST QUARTER REPORT

FOR THE 13-WEEK PERIOD ENDED JUNE 28, 2008

Treasure the past...

Imagine the future...

Indigo

Books & Music Inc.

www.indigo.ca

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Management's Discussion and Analysis

The following discussion and analysis is prepared as at July 30, 2008, and is based primarily on the unaudited interim consolidated financial statements of Indigo Books & Music Inc. (the "Company" or "Indigo") for the 13-week periods ended June 28, 2008 and June 30, 2007. It should be read in conjunction with the unaudited interim consolidated financial statements and notes contained in this Quarterly Report, the audited annual consolidated financial statements and accompanying notes for the year ended March 29, 2008, and Management's Discussion and Analysis ("MD&A") included in the Company's fiscal 2008 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 the nation's largest book retailer, operating stores in all 10 provinces and one territory in Canada and offering online sales through its *www.chapters.indigo.ca* web site. As at June 28, 2008, the Company operated 86 superstores under the banners *Chapters*, *Indigo* and the *World's Biggest Bookstore*, and 159 small format stores, under the banners *Coles*, *Indigo*, *Indigospirit*, *SmithBooks* and *The Book Company*. During the first quarter of fiscal 2009, the Company opened one small format store. 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.

In October 2005, Indigo incorporated a separate registered charity under the name Indigo Love of Reading Foundation (the "Foundation"). The Foundation provides new books and learning materials to high-needs elementary schools across the country through donations from Indigo, its customers, suppliers and employees.

As at July 30, 2008, the number of common shares outstanding was 24,736,077 with a book value of $198.1 million. As at June 28, 2008, there were 1,622,952 stock options outstanding of which 603,475 were exercisable. The number of common shares reserved for issuance under the employee stock option plan is 2,228,053.

Results of Operations

The following table summarizes the consolidated statement of operations for the periods indicated. The classification of financial information presented below is specific to Indigo Books & Music Inc., and may not be comparable to that of other retailers.

(millions of dollars)	**13-week period ended June 28, 2008**	**% Revenues**	13-week period ended June 30, 2007	% Revenues
Revenues	**190.6**	**100.0%**	184.9	100.0%
Cost of sales	**107.4**	**56.3%**	105.4	57.0%
Cost of operations	**60.8**	**31.9%**	59.7	32.3%
Selling and administrative expenses	**17.2**	**9.0%**	14.6	7.9%
EBITDA[1]	**5.2**	**2.7%**	5.2	2.8%

1 Earnings before interest, taxes, depreciation and amortization. Also see "Non-GAAP Financial Measures".

Improved Comparable Store Sales Drives Revenues Increase

Total consolidated revenues for the 13-week period ended June 28, 2008 increased $5.7 million or 3.1% to $190.6 million from $184.9 million for the period ended June 30, 2007. The increase in revenues was largely attributable to strong comparable store sales growth in superstores and small format stores, as well as the online channel. Comparable store sales for the quarter increased 3.3% in superstores and 5.4% in small format stores over the same quarter last year. Comparable store sales are defined as sales generated by stores that have been open for more than 12 months. It is a key performance indicator for the Company as this measure excludes sales fluctuations due to store closings, permanent relocation and chain expansion. The Company operated two less superstores in the quarter compared to the same period last year.

Online sales continued to grow during the first quarter, increasing $1.5 million or 7.7% to $21.0 million for the 13-week period ended June 28, 2008 from $19.5 million in the same period last year. Growth in the online channel was primarily attributable to the successful launch of the Indigo Online Community in September 2007. Since inception, over 130,000 members have joined the Online Community, resulting in a material increase in traffic to the website over last year.

Revenues from other sources include revenues generated through corporate sales, revenues from the sale of loyalty cards, the Company's proportionate revenue generated through Calendar Club, and gift card breakage. Revenues from other sources increased $0.2 million or 3.4% from $5.9 million in the first quarter last year to $6.1 million in the same period this year, driven by the continued growth in sales of the Company's loyalty card program and an increase in gift card breakage.

Revenues by channel are highlighted below:

(millions of dollars)	**13-week period ended June 28, 2008**	13-week period ended June 30, 2007	% increase	Comparable store sales % increase
Superstores	**131.5**	129.1	1.9	3.3
Small format stores	**32.0**	30.4	5.3	5.4
Online (including store kiosks)	**21.0**	19.5	7.7	N/A
Other	**6.1**	5.9	3.4	N/A
	190.6	184.9	3.1	3.7

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

	Superstores		Small format stores	
(millions of dollars)	**13-week period ended June 28, 2008**	13-week period ended June 30, 2007	**13-week period ended June 28, 2008**	13-week period ended June 30, 2007
Total revenues	**131.5**	129.1	**32.0**	30.4
Adjustments for stores not in both fiscal periods	**(2.5)**	(4.2)	**(0.8)**	(0.8)
Comparable store sales	**129.0**	124.9	**31.2**	29.6

Cost of Sales Showed Improvement over First Quarter Last Year

Cost of sales includes the landed cost of goods sold, online shipping costs, inventory shrink and damage provision, less all vendor support programs. As a percent of total revenues, cost of sales decreased 0.7% to 56.3% in the first quarter, compared to 57.0% in the same period last year. Cost of sales were higher in the first quarter of last fiscal year because the Company implemented a new sourcing logic that manages the flow of products from suppliers, and as a result, more products were sent direct-to-store during this implementation, negatively impacting cost of sales. The improvement in cost of sales during the current quarter was partially offset by higher online shipping costs this year.

Cost of Operations (as a Percent of Revenues) Declined over Last Year

Cost of operations includes all store, online, distribution centre and Calendar Club costs. Cost of operations increased $1.1 million primarily due to increased volume and higher minimum wage rates in most provinces. As a percent of total revenues, cost of operations decreased 0.4% to 31.9% of sales in the first quarter, compared to 32.3% in the same period last year.

Selling and Administrative Expenses Increased in the First Quarter
Selling and administrative expenses include all marketing and head office costs. Selling and administration expenses increased $2.6 million compared to the same quarter last year. The increase was due to planned investment in various head office areas and Pistachio, a new store concept that is expected to open in the fall of 2008. In addition, the Company realized a loss on foreign exchange in the first quarter compared to a gain in the same quarter last year and had a favourable trademark settlement in the first quarter last year. As a percent of total revenues, selling and administrative expenses increased from 7.9% last quarter to 9.0% this quarter.

EBITDA Remained Stable Year over Year
EBITDA, defined as earnings before interest, taxes, depreciation and amortization, remained unchanged at $5.2 million for the 13-week period ended June 28, 2008, compared to the same period last year.

Amortization Costs Continued to Decrease
Amortization for the 13-week period ended June 28, 2008 decreased $0.5 million to $7.1 million, compared to $7.6 million for the 13-week period ended June 30, 2007. Capital expenditures in the current quarter totalled $6.9 million, and included $3.5 million on store and head office construction, renovations and equipment, and $3.4 million on technology-related projects. Of the $6.9 million in capital expenditure, $1.0 million was financed through capital leases.

Interest Expense Continued to Decline
Interest expense decreased $0.6 million from the same period last year. The Company generated interest income of $0.3 million in the first quarter of this year due to a positive cash position, compared to an interest expense of $0.3 million in the first quarter last year.

Income Tax Recovery in the First Quarter
The Company recognized an income tax recovery of $0.4 million in the first quarter of this year. The Company did not have an income tax recovery in the same period last year as the income tax recovery was fully offset by an increase in the income tax valuation allowance.

Net Loss Recorded for the Current Fiscal Quarter
Net loss for the first quarter was $1.2 million or $0.05 net loss per common share, compared to a net loss of $2.8 million or $0.12 net loss per common share last year. The reduction in net loss was mainly due to reduced interest and amortization expenses and an income tax recovery, as noted above.

Other Comprehensive Loss

The Company adopted new accounting standards related to financial instruments on April 1, 2007. The Company had a hedging program in place as at April 1, 2007 whereby it entered into foreign currency contracts to mitigate the risk of fluctuations in the cost of product it purchased in US dollars. Upon adoption of the new Financial Instruments Standards last fiscal year, the Company reclassified $0.1 million to other comprehensive income relating to losses on derivatives designated as cash flow hedges prior to April 1, 2007. The Company did not enter into any interest rate and foreign currency derivative contracts during the first quarter of the current fiscal year.

Seasonality and First Quarter Results

Indigo's business is highly seasonal and follows quarterly revenues and earnings (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 earnings 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), and basic and diluted earnings (loss) per share for the preceding eight fiscal quarters.

	Fiscal quarters							
(thousands of dollars, except per share data)	**Q1 Fiscal 2009**	Q4 Fiscal 2008	Q3 Fiscal 2008	Q2 Fiscal 2008	Q1 Fiscal 2008	Q4 Fiscal 2007	Q3 Fiscal 2007	Q2 Fiscal 2007
Revenues	**190,602**	206,236	322,552	209,173	184,917	201,896	320,491	182,305
Net earnings (loss)	**(1,225)**	3,130	49,179	3,339	(2,840)	(4,206)	40,977	(976)
Basic earnings (loss) per share	**$ (0.05)**	$ 0.13	$ 1.98	$ 0.14	$ (0.12)	$ (0.17)	$ 1.68	$ (0.04)
Diluted earnings (loss) per share	**$ (0.05)**	$ 0.12	$ 1.94	$ 0.13	$ (0.12)	$ (0.17)	$ 1.62	$ (0.04)

Overview of Consolidated Balance Sheets

Total Assets

As at June 28, 2008, total assets were $37.0 million more than total assets at June 30, 2007. The change in assets was primarily due to an increase in cash and cash equivalents and future tax assets, partially offset by a reduction in the Company's inventory position and a decrease in net capital assets. Cash and cash equivalents increased $50.2 million, primarily due to higher sales and reduced investment in inventories. Inventories decreased $17.1 million compared to the first quarter last year, as the Company implemented an improved open-to-buy process in the second half of last fiscal year creating better controls over the amount of inventories being purchased. Net capital assets declined by $5.2 million as the Company did not spend as much on capital additions ($24.8 million) over the past 12 months relative to capital asset amortization ($29.2 million).

Future tax assets increased by $9.2 million compared to the same quarter last year. During the third quarter of last fiscal year, the Company determined that it could more likely than not utilize all of its tax loss carryforwards based on expected future earnings and the expiry date of its loss carryforwards and, therefore, an income tax valuation allowance was no longer required. The elimination of the income tax valuation allowance led to higher future tax assets and it was partially offset by the corporate income tax rate reductions announced and substantively enacted by the Canadian federal government.

On a fiscal year-to-date basis, total assets decreased $9.0 million compared to March 29, 2008. The decrease in total assets was primarily due to the reduction in inventories and accounts receivable, partially offset by the increase in cash and cash equivalents. The inventory position and accounts receivable decreased by $9.0 million and $1.6 million respectively and cash and cash equivalents increased by $1.1 million.

Total Liabilities

Total liabilities as at June 28, 2008 were $19.9 million less than total liabilities at June 30, 2007. The decrease in total liabilities was primarily due to a $14.6 million decrease in total debt (including bank indebtedness and long-term debt). During the first quarter of last fiscal year, the Company renegotiated its credit agreement with its bank. As part of the refinancing, the Company used its operating line to repay $13.0 million of long-term debt that was outstanding under the old agreement. Other contributing factors to the decrease in total liabilities were a $1.6 million decrease in deferred revenue, a $2.3 million reduction in deferred rent and a $1.4 million decrease in derivative liabilities as the Company no longer uses any derivative contracts to hedge its foreign currency denominated purchases.

On a year-to-date basis, total liabilities decreased $7.1 million compared to March 29, 2008. The decrease in total liabilities was mainly due to reductions in accounts payable and accrued liabilities of $7.0 million which is consistent with the reduction in inventories, as noted above.

Shareholders' Equity

Shareholders' equity at June 28, 2008 increased $56.9 million compared to June 30, 2007. The improvement was primarily due to net earnings of $54.4 million in the last four quarters. Share capital increased $0.8 million due to the exercise of employee stock options and it was partially offset by the repurchase of common shares under the normal course issuer bid. Contributed surplus increased by $0.8 million due to the expensing of $1.1 million of employee stock options and Directors' deferred stock units, and was partially offset by a $0.3 million reduction due to the exercise of employee stock options and conversion of Director's deferred stock units. In accordance with the new accounting standards on financial instruments adopted by the Company last year, the Company recognized a $1.4 million accumulated other comprehensive loss on its foreign exchange contracts as part of shareholders' equity last year, compared to nil of this year.

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, a short term operating line of credit, and accounts payable as three of the primary vehicles to fund the business before generating a disproportionate amount of cash during the December holiday season. The Company reported working capital of $73.1 million as at June 28, 2008, compared to $26.9 million as at June 30, 2007 and $76.6 million at the end of fiscal 2008.

The Company's leverage position (defined as Total Liabilities to Total Shareholders' Equity) improved to 1.0:1 at the end of the current quarter from 1.6:1 last year due to the reduction in total debt and the increase in shareholders' equity, as described above. The Company's leverage position has also improved from 1.1:1 as at March 29, 2008 for the same reasons.

Overview of Consolidated Statements of Cash Flows

Cash and cash equivalents increased $1.1 million during the first quarter of fiscal 2009, compared to a decrease of $6.8 million last year.

Cash Flows from Operating Activities

The Company generated positive cash flow from operating activities of $9.7 million during the first quarter. This was an increase of $12.2 million over the same period a year ago, when cash flow generated from operating activities was negative $2.5 million. The positive change in cash flow generated year over year was primarily due to a $14.1 million decrease in the amount of cash used to reduce accounts payable and accrued liabilities. The improvement in operating cash flow was partially offset by a $1.3 million reduction in deferred revenues.

Cash Flows Used in Investing Activities

In the first quarter, net cash flows used in investing activities were $5.9 million compared to $2.9 million used in the same quarter last year. The Company spent $5.9 million on capital projects in the current quarter, including $3.5 million in store and head office construction, renovations and equipment and $2.4 million in technology-related projects. During the first quarter last year, the Company spent $2.9 million on capital projects including $1.6 million for store construction, renovations and equipment and $1.3 million for technology-related projects.

Cash Flows Used in Financing Activities

Net cash flows used in financing activities were $2.7 million during the first quarter compared to $1.4 million in the same period last year. The increase in cash flow used in financing activities was primarily due to the $1.2 million repurchase of common shares under the Company's normal course issuer bid.

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, as its customers pay largely by cash or credit card, and it purchases products on trade terms with the right to return a significant portion of its products. Indigo's main sources of capital are cash flow generated from operations, a revolving line of credit and long-term debt. In the first quarter of fiscal 2008, the Company refinanced its debt and reduced the borrowing capacity under the line of credit to $60.0 million as the Company was forecasting lower borrowing needs.

Based on current operating levels, management expects cash flow generated from operations along with the available borrowing capacity under the Company's credit facility to be sufficient to meet its working capital needs and debt service requirements for the next fiscal year. Indigo also has the ability to reduce capital spending to fund debt requirements if necessary, however, a long-term decline in capital expenditures may negatively impact revenue and profit growth.

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 flow. 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 Estimates

The discussion and analysis of Indigo's operations and financial condition are based upon the unaudited interim consolidated financial statements, which have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). The preparation of these consolidated financial statements requires the Company to estimate the effect of several variables that are inherently uncertain. These estimates and assumptions can affect the reported amounts of assets, liabilities, revenues and expenses. Indigo bases its estimates on historical experience and other assumptions which the Company believes to be reasonable under the circumstances. The Company also evaluates its estimates on an ongoing basis. The significant accounting policies of the Company are described in Note 2 of the consolidated financial statements in the fiscal 2008 Annual Report, and the Company's critical accounting estimates are disclosed in the MD&A section of its fiscal 2008 Annual Report.

In the first quarter of fiscal 2009, there were no significant changes to the provisions for slow-moving and damaged products and for gift and paper products that have been marked down. There were also no material changes to the provision for restructuring costs, future tax assets and goodwill. Furthermore, the method of determining gift card breakage is consistent with that used in previous periods.

Accounting Standards Adopted in Fiscal 2009

Financial Instruments

Section 3862 and 3863 of the CICA Handbook, "Financial Instruments – Disclosures" and "Financial Instruments – Presentation", replace the existing Section 3861, "Financial Instruments – Disclosures and Presentation". The new sections revise and enhance disclosure requirements, and carry forward unchanged existing presentation requirements. These new sections place increased emphasis on disclosures about the nature and extent of risks arising from financial instruments and how the entity manages those risks. These standards were adopted by the Company for the fiscal year beginning March 30, 2008 and its implementation did not have an impact on the classification and valuation of the Company's consolidated financial statements.

Capital Disclosures

Section 1535 of the CICA Handbook, Capital Disclosures, specifies the disclosure of : (i) the Company's objectives, policies and process for managing capital; (ii) quantitative information about what it manages as capital; and (iii) whether the Company has complied with any externally imposed capital requirement and the consequences of such non-compliance. This standard is effective for the Company's fiscal year beginning March 30, 2008. The resulting disclosures from implementation are presented in Note 3 to the consolidated financial statements.

Inventories

The CICA issued Handbook Section 3031 "Inventories" which prescribes the accounting treatment for inventories. This section provides guidance on the determination of cost and its subsequent recognition as an expense, including any write-down to net realizable value. It also provides guidance on the cost formulas that are used to assign costs to inventories. This standard was adopted by the Company for the fiscal year beginning March 30, 2008. The resulting disclosures from implementation are presented in Note 3 to the consolidated financial statements.

General Standards of Financial Statement Presentation

The CICA amended Section 1400 of the handbook which requires management to make an assessment of an entity's ability to continue as a going concern when preparing financial statements. In assessing whether the going concern assumption is appropriate, management must take into account all available information about the future, which is at least, but is not limited to, twelve months from the balance sheet date. This standard was adopted by the Company for the fiscal year beginning March 30, 2008 and its implementation did not have an impact on the classification and valuation of the Company's consolidated financial statements.

International Financial Reporting Standards

In February 2008, the Canadian Accounting Standards Board confirmed its plan to converge with International Financial Reporting Standards ("IFRS"). The Company must prepare the interim and annual financial statement in accordance with IFRS for fiscal years beginning on or after January 1, 2011.

The Company began its IFRS conversion project in 2008 and has formally established a project team. The project team consists of members from finance and is being overseen by the Company's Chief Financial Officer. Regular reporting is made to senior management and to the Audit Committee of the Company's Board of Directors. The Company uses an external advisor to assist in the conversion project.

The Company is currently in the preliminary diagnostic phase, which involves a high level review of the difference between IFRS and Canadian GAAP. The Company will address the design, planning, solution development and implementation of the conversion in subsequent phases.

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 2008 Annual Report.

Internal Controls over Financial Reporting

Management is responsible for the design of 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 Canadian generally accepted accounting principles.

For the quarter ended June 28, 2008, there were no material changes in internal controls over financial reporting that have materially affected, or are reasonably likely to materially affect, the Company's internal controls over financial reporting.

The Company implemented a new warehouse management software application in July of 2006. Subsequent to the implementation of this application, management identified the need for improvement to the access and change controls within the application. Management has and continues to take steps to address these controls issues and has in place a number of compensating controls to mitigate the risk of an error in its financial reporting.

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 with 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 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-GAAP Financial Measures

The Company prepares its consolidated financial statements in accordance with Canadian generally accepted accounting principles. In order to provide additional insight into the business, the Company has also provided non-GAAP data, including comparable store sales and EBITDA, in the discussion and analysis section above. Neither measure has a standardized meaning prescribed by GAAP, and is therefore specific to Indigo and may not be comparable to similar measures presented by other companies.

Comparable stores sales and 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. It is a key performance indicator for the Company as this measure excludes sales fluctuations due to store closings, permanent relocation and chain expansion. EBITDA is defined as earnings before interest, taxes, depreciation and amortization.

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

(millions of dollars)	**13-week period ended June 28, 2008**	13-week period ended June 30, 2007
EBITDA	**5.2**	5.2
Amortization of property and equipment	**7.1**	7.6
Amortization of pre-opening store costs	**0.0**	0.1
Interest on long-term debt and financing charges	**0.1**	0.2
Interest expense (income) on bank indebtedness	**(0.4)**	0.1
Earnings (loss) before income taxes	**(1.6)**	(2.8)

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NOTICE OF NO AUDITOR REVIEW OF INTERIM 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 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 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 financial statements.

Heather Reisman
Chair & Chief Executive Officer

Jim McGill
Chief Financial Officer

Dated as of the 30th day of July, 2008.

Consolidated Balance Sheets

(Unaudited)

(thousands of dollars)	**As at June 28, 2008**	As at June 30, 2007	As at March 29, 2008
ASSETS			
Current			
Cash and cash equivalents	**57,052**	6,870	55,933
Accounts receivable	**7,389**	7,417	8,996
Inventories	**197,188**	214,313	206,259
Income taxes recoverable	**21**	194	21
Prepaid expenses	**5,250**	5,085	4,929
Future tax assets	**6,745**	9,205	6,745
Total current assets	**273,645**	243,084	282,883
Property and equipment	**67,146**	72,303	67,348
Future tax assets	**43,647**	32,035	43,250
Goodwill	**27,523**	27,523	27,523
Total assets	**411,961**	374,945	421,004
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current			
Bank indebtedness	**–**	12,520	–
Accounts payable and accrued liabilities	**187,126**	187,207	193,323
Deferred revenue	**10,832**	12,431	10,350
Derivative liabilities	**–**	1,400	–
Current portion of long-term debt (note 7)	**2,618**	2,661	2,648
Total current liabilities	**200,576**	216,219	206,321
Long-term accrued liabilities	**6,736**	9,009	7,549
Long-term debt	**2,847**	4,861	3,380
Total liabilities	**210,159**	230,089	217,250
Shareholders' equity			
Share capital (note 5)	**198,424**	197,622	198,938
Contributed surplus (notes 5 and 6)	**2,867**	1,994	2,564
Retained earnings (deficit)	**511**	(53,396)	2,252
Accumulated other comprehensive loss (note 8)	**–**	(1,364)	–
Total shareholders' equity	**201,802**	144,856	203,754
Total liabilities and shareholders' equity	**411,961**	374,945	421,004

See accompanying notes

Consolidated Statements of Earnings (Loss)

(Unaudited)

(thousands of dollars, except per share data)	**13-week period ended June 28, 2008**	13-week period ended June 30, 2007
Revenues	**190,602**	184,917
Cost of sales, operations, selling and administration	**185,398**	179,764
	5,204	5,153
Amortization of property and equipment	**7,111**	7,610
Amortization of pre-opening store costs	**–**	54
	7,111	7,664
Loss before the undernoted items	**(1,907)**	(2,511)
Interest on long-term debt and financing charges	**108**	247
Interest expense (income) on bank indebtedness	**(393)**	82
Loss before income taxes	**(1,622)**	(2,840)
Income tax recovery	**(397)**	–
Net loss for the period	**(1,225)**	(2,840)
Net loss per common share (note 4)		
Basic	**$ (0.05)**	$ (0.12)
Diluted	**$ (0.05)**	$ (0.12)
Weighted average number of common shares outstanding	**24,833**	24,648

See accompanying notes

Consolidated Statements of Retained Earnings (Deficit)

(Unaudited)

(thousands of dollars)	**13-week period ended June 28, 2008**	13-week period ended June 30, 2007
Retained earnings (deficit), beginning of period, as reported	**2,252**	(50,537)
Transitional adjustment on adoption of new accounting policies	**–**	(19)
Retained earnings (deficit), beginning of period, as restated	**2,252**	(50,556)
Net loss for the period	**(1,225)**	(2,840)
Shares repurchase excess (note 5)	**(516)**	–
Retained earnings (deficit), end of period	**511**	(53,396)

See accompanying notes

Consolidated Statements of Comprehensive Loss

(Unaudited)

(thousands of dollars)	**13-week period ended June 28, 2008**	13-week period ended June 30, 2007
Net loss for the period	**(1,225)**	(2,840)
Other comprehensive loss, net of tax		
Losses on derivatives designated as cash flow hedges (net of tax – $nil)	–	(1,364)
Reclassification to earnings of losses on derivatives designated as cash flow hedges prior to April 1, 2007 (net of tax – $nil)	–	(144)
Other comprehensive loss, net of tax	–	(1,508)
Comprehensive loss for the period	**(1,225)**	(4,348)

See accompanying notes

Consolidated Statements of Cash Flows

(Unaudited)

(thousands of dollars)	**13-week period ended June 28, 2008**	13-week period ended June 30, 2007
CASH FLOWS FROM OPERATING ACTIVITIES		
Net loss for the period	**(1,225)**	(2,840)
Add (deduct) items not affecting cash		
Amortization	**7,111**	7,664
Stock-based compensation (note 6)	**233**	140
Directors' compensation (note 5)	**105**	110
Future tax assets	**(397)**	–
Loss on disposal of property and equipment	**13**	–
Amortization and write-off of deferred financing charges (note 7)	–	139
Other	–	17
Net change in non-cash working capital balances related to operations		
Accounts receivable	**1,607**	2,431
Inventories	**9,071**	9,746
Prepaid expenses	**(321)**	(561)
Deferred revenue	**482**	1,810
Accounts payable and accrued liabilities	**(7,010)**	(21,133)
Cash flows from (used in) operating activities	**9,669**	(2,477)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of property and equipment	**(5,888)**	(2,939)
Cash flows used in investing activities	**(5,888)**	(2,939)
CASH FLOWS FROM FINANCING ACTIVITIES		
Increase in bank indebtedness	–	12,520
Repayment of long-term debt (note 7)	**(1,597)**	(13,895)
Proceeds from share issuances (note 5)	**99**	22
Repurchase of common shares (note 5)	**(1,164)**	–
Cash flows used in financing activities	**(2,662)**	(1,353)
Net increase (decrease) in cash and cash equivalents during the period	**1,119**	(6,769)
Cash and cash equivalents, beginning of period	**55,933**	13,639
Cash and cash equivalents, end of period	**57,052**	6,870

See accompanying notes

Notes to the Interim Consolidated Financial Statements

June 28, 2008
(Unaudited)

1. DISCLOSURE

These unaudited interim consolidated financial statements do not contain all disclosures required by Canadian generally accepted accounting principles for audited annual consolidated financial statements and accordingly, these financial statements should be read in conjunction with the most recently prepared audited annual consolidated financial statements for the 52-week period ended March 29, 2008. Results of operations for the 13-week periods ended June 28, 2008 and June 30, 2007 and the balances at these dates are unaudited.

2. SEASONALITY OF OPERATIONS

The business of Indigo Books & Music Inc. (the "Company" or "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, 2008 and June 30, 2007 are not indicative of the results of other periods.

3. CHANGES IN ACCOUNTING POLICIES

These consolidated financial statements follow the same accounting policies and methods of their application as the most recent annual audited financial statements for the 52-week period ended March 29, 2008, except as noted below.

Financial Instruments

Section 3862 and 3863 of the CICA Handbook, "Financial Instruments – Disclosures" and "Financial Instruments – Presentation", replace the existing Section 3861, "Financial Instruments – Disclosures and Presentation". The new sections revise and enhance disclosure requirements, and carry forward unchanged existing presentation requirements. These new sections place increased emphasis on disclosures about the nature and extent of risks arising from financial instruments and how the entity manages those risks. These standards were adopted by the Company for the fiscal year beginning March 30, 2008 and its implementation did not have an impact on the classification and valuation of the Company's consolidated financial statements.

Financial Risk Management

The Company's activities expose it to a variety of financial risks, including risks related to foreign exchange, interest rate, credit and liquidity.

Foreign exchange risk

The Company's foreign exchange risk is largely limited to currency fluctuations between the Canadian and US dollars. Decreases in the value of the Canadian dollar relative to the US dollar affect less than 10% of the Company's total cost of purchase and could impact negatively on the company's net income. The Company does not use foreign currency derivative contracts to hedge its foreign exchange risk.

Interest rate risk

The Company's interest rate risk is limited to the fluctuation of floating rates on its outstanding operating line. The Company did not use its operating line during the quarter and does not use any interest rate swaps to fix the interest rate on its operating line.

Credit risk

The Company's credit risk is considered to be negligible as the Company only deals with highly rated financial institutions. In addition, the Company has minimal accounts receivable as its customers pay mainly by cash or credit card. The maximum exposure to credit risks at the reporting date is equal to the carrying value of the account receivables.

Liquidity risk

The Company manages liquidity risk by maintaining available financial assets in excess of financial obligations due at any point in time. The Company achieves this objective by maintaining sufficient cash and cash equivalents or through the availability of funding from its revolving line of credit.

Capital Disclosures

Section 1535 of the CICA Handbook, Capital Disclosures, specifies the disclosure of: (i) the Company's objectives, policies and process for managing capital; (ii) quantitative information about what it manages as capital; and (iii) whether the Company has complied with any externally imposed capital requirement and the consequences of such non-compliance. This standard is effective for the Company's fiscal year beginning March 30, 2008.

Capital Management

The Company's objectives when managing capital are to safeguard the entity's ability to continue as a going concern while maintaining adequate financial flexibility to invest in new business opportunities that will provide attractive returns to the shareholders. The primary activities engaged by the Company to generate attractive returns include the construction and related leasehold improvements of new and relocated stores, the development of new business concepts, and investment in information technology and distribution capacity to support the expansion of the store and online network. The Company's main sources of capital are cash flow generated from operations, a revolving line of credit and long-term debt. This cash flow is used to fund its capital expenditures, working capital needs and debt service requirements. There were no changes to these objectives during the 13-week period ended June 28, 2008.

The Company monitors its capital structure principally through measuring its total debt to shareholders' equity ratio and ensures its ability to service its debt obligation by tracking its interest and other fixed charges coverage ratios. Total debt is defined as the total of bank indebtedness and long-term debt (including the current portion). The Company has certain borrowing base and debt covenants and is in compliance with those covenants.

The following table summarizes selected capital structure information for the Company for the periods indicated.

(thousands of dollars)	**13-week period ended June 28, 2008**	13-week period ended June 30, 2007
Bank indebtedness	**–**	12,520
Current portion of long-term debt	**2,618**	2,661
Long-term debt	**2,847**	4,861
Total debt	**5,465**	20,042
Shareholders' equity	**201,802**	144,856
Total debt : Shareholders' equity	**0.03:1**	0.14:1

Inventories

The CICA issued Handbook Section 3031 "Inventories" which prescribes the accounting treatment for inventories. This section provides guidance on the determination of cost and its subsequent recognition as an expense, including any write-down to net realizable value. It also provides guidance on the cost formulas that are used to assign costs to inventories. This standard was adopted by the Company for the fiscal year beginning March 30, 2008.

Inventories are valued at the lower of cost, determined on a moving average cost basis, and market, being net realizable value. Costs include all direct and reasonable expenditures that are incurred in bringing inventories to their present location and condition. Vendor rebates are recorded as a reduction in the price of the products and corresponding inventory is recorded net of vendor rebates.

The cost of inventories recognized as an expense for the 13-week period ended June 28, 2008 was $108.3 million. The amount of inventory write-downs as a result of net realizable value lower than cost was $0.5 million for the period, and there were no reversal of inventory write-downs that were recognized in prior periods. The full value of the inventories was pledged as security under the Company's credit agreement with its bank.

General Standards of Financial Statement Presentation

The CICA amended Section 1400 of the handbook which requires management to make an assessment of an entity's ability to continue as a going concern when preparing financial statements. In assessing whether the going concern assumption is appropriate, management must take into account all available information about the future, which is at least, but is not limited to, twelve months from the balance sheet date. This standard was adopted by the Company for the fiscal year beginning March 30, 2008 and its implementation did not have an impact on the the classification and valuation of the Company's consolidated financial statements.

4. LOSS PER SHARE

Loss per share is calculated based on the weighted average number of common shares outstanding during the period. The Company's stock options and Director's deferred stock units ("DSUs") were anti-dilutive and therefore, were not included in the June 28, 2008 and June 30, 2007 diluted loss per share calculations.

5. SHARE CAPITAL

Share capital consists of the following:

	13-week period ended June 28, 2008		13-week period ended June 30, 2007		52-week period ended March 31, 2008	
	Number of shares	**Amount $ (thousands)**	Number of shares	Amount $ (thousands)	Number of shares	Amount $ (thousands)
Balance, beginning of period	**24,843,147**	**198,938**	24,647,554	197,592	24,647,554	197,592
Issued during the period						
Directors' deferred stock units converted	**–**	**–**	–	–	14,964	85
Options exercised	**18,250**	**134**	4,000	30	180,629	1,261
Repurchase of common shares	**(80,865)**	**(648)**	–	–	–	–
Balance, end of period	**24,780,532**	**198,424**	24,651,554	197,622	24,843,147	198,938

On May 6, 2008, the Company announced its intent to make a normal course issuer bid ("NCIB"), subject to final acceptance of its notice of intention by the Toronto Stock Exchange. The Toronto Stock Exchange approved the NCIB on May 8, 2008. Under the NCIB, Indigo may purchase up to 1,242,157 of its common shares, representing approximately 5% of its total outstanding common shares. Daily purchases are limited to 2,905 common shares, other than block purchase exceptions. During the 13-week period ended June 28, 2008, the Company repurchased 80,865 common shares at an average price of $14.40 per share for a total cash consideration of $1.2 million under the NCIB and they were cancelled and returned to treasury. The cash consideration exceeded the carrying value of the shares repurchased by $0.5 million and the amount was charged to retained earnings.

On October 31, 2002, the Company established a Director's Deferred Stock Unit Plan. Under the Plan, Directors receive their annual retainer fees and other Board-related compensation in the form of DSUs. The Company issued 7,259 DSUs with a value of $0.1 million during the 13-week period ended June 28, 2008. The value of the outstanding DSUs as at June 28, 2008 was $1.3 million and was recorded into contributed surplus. During fiscal 2008, the Company issued 14,964 shares in exchange for directors' deferred stock units when a Board member retired.

6. STOCK-BASED COMPENSATION

As at June 28, 2008, 1,622,952 stock options were outstanding with exercise prices ranging from $4.45 to $63.53. Of these outstanding stock options, 603,475 were exercisable. As at June 30, 2007, there were 1,341,546 options outstanding of which 626,152 were exercisable.

The Company used the fair value method of accounting for stock options, which estimates the fair value of the stock options granted on the date of grant and expenses this value over the vesting period. During the 13-week period ended June 28, 2008, $0.2 million was recognized as an expense with the offset recorded in contributed surplus. Any consideration paid by employees on exercise of stock options is credited to share capital with a corresponding reduction to contributed surplus.

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 assumptions during the period presented:

	13-week period ended June 30, 2007
Risk-free interest rate	4.1%
Expected volatility	18.2%
Expected time until exercise	4 years
Expected dividend yield	0.0%

The Company did not issue any stock options to employees during the 13-week period ended June 28, 2008.

On a pro forma basis, if the Company had used the fair value method of accounting for stock options issued before March 29, 2003, the Company's net loss for the first quarter of last fiscal year would have increased to the amounts listed below. The pro forma impact of accounting for these options at fair value on the current year earnings will no longer be disclosed as all options issued before March 29, 2003 were vested by the fourth quarter of fiscal 2008.

Pro Forma Earnings (thousands of dollars, except per share data)	13-week period ended June 30, 2007
Net loss – reported	(2,840)
Net loss – pro forma	(2,922)
Basic net loss per common share – reported	$ (0.12)
Basic net loss per common share – pro forma	$ (0.12)
Diluted net loss per common share – reported	$ (0.12)
Diluted net loss per common share – pro forma	$ (0.12)

7. DEFERRED FINANCING CHARGES

On April 11, 2007, the Company renegotiated its credit agreement with its bank. The new credit agreement provides the Company with a revolving line of credit of up to $60.0 million. As part of the refinancing, the Company repaid $13.0 million of long-term debt that was originally due in July 2007, and wrote off $0.1 million in deferred financing charges associated with the old agreement. The Company incurred $0.1 million of deferred financing charges associated with the new agreement which has been netted with long-term debt in the consolidated balance sheets. As a result of the long-term debt repayment, the Company also terminated the interest rate swap associated with the long-term debt and recognized $0.1 million into earnings in April 2007.

8. ACCUMULATED OTHER COMPREHENSIVE LOSS

Changes in accumulated other comprehensive loss during the first quarter of last fiscal year, are presented as follows:

(thousands of dollars)	13-week period ended June 30, 2007
Adjusted opening balance due to adoption of new accounting policies – financial instruments	144
Other comprehensive loss for the period	(1,508)
Balance, end of period	(1,364)

The Company did not have any interest rate or foreign currency derivative contracts outstanding as at the end of the first quarter of the current fiscal year.

9. CONSOLIDATED STATEMENTS OF CASH FLOWS

Supplemental cash flow information:

(thousands of dollars)	**13-week period ended June 28, 2008**	13-week period ended June 30, 2007
Interest paid (received)	**(275)**	287
Assets acquired under capital lease	**1,034**	788

10. COMPARATIVE CONSOLIDATED FINANCIAL STATEMENTS

The comparative consolidated financial statements have been reclassified from statements previously presented to conform to the presentation of the current year consolidated financial statements.

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