ANNUAL REPORT

FOR THE 52-WEEK PERIOD ENDED MARCH 29, 2008

Treasure the past...

Imagine the future...

Indigo

Books & Music Inc.

www.indigo.ca

The Indigo Mission

To provide booklovers and those they care about with the most inspiring retail and online environments in the world for books and life enriching products and services.

Indigo operates under the following banners:
Indigo Books Music & More; *Chapters*; *The World's Biggest Bookstore*; *Coles*; *SmithBooks*; *Indigospirit*; *The Book Company* and *chapters.indigo.ca*.
The Company employs approximately 6,000 people across the country.

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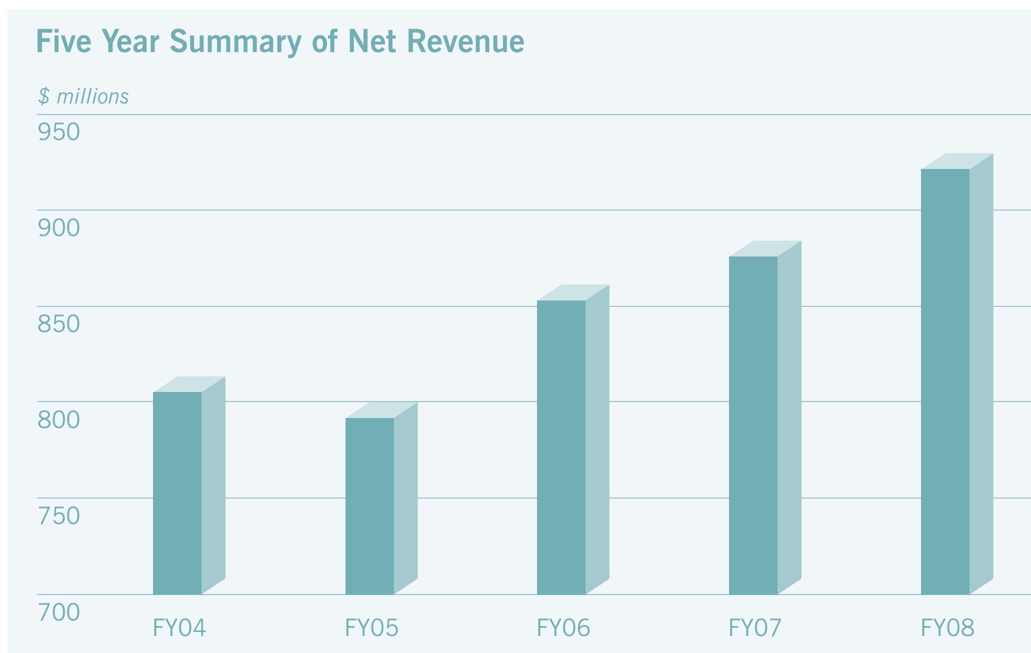
Report of the CEO

Dear Shareholder,

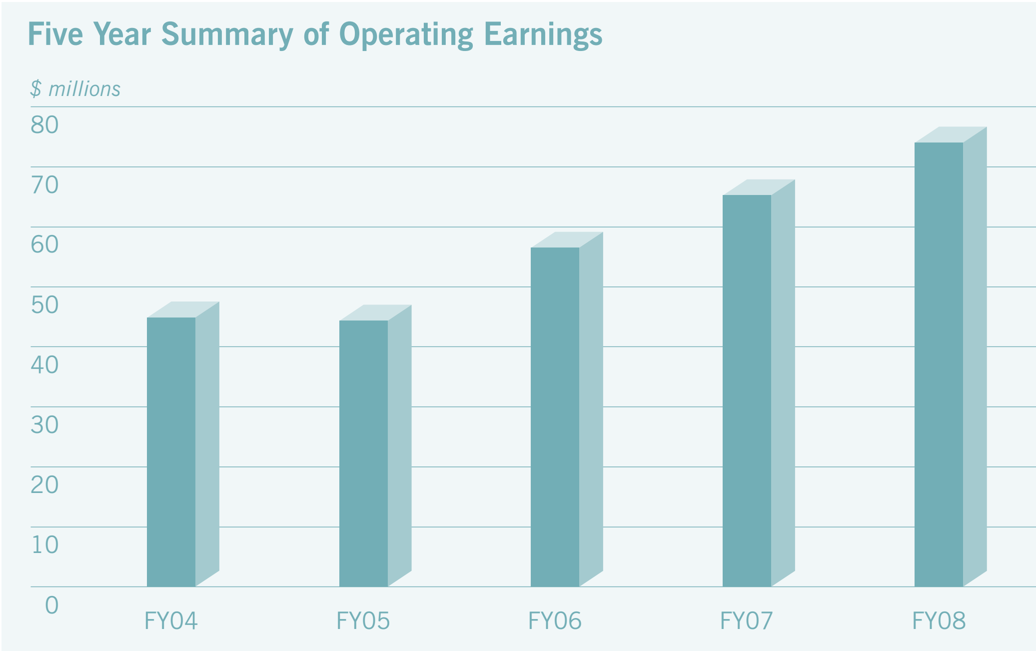
With kind acknowledgement to Charles Dickens I feel compelled to say that the year we just completed was indeed *the best of times and the worst of times*.

On the side of best…
This year our Company achieved record sales and profits, retired our long-term debt, and served more customers than ever in our history. Chapters and Indigo were again nominated as top brands in an independent survey of Canadian consumers, and a new Indigo store won the International Council of Shopping Centers' award for Best New Retail Store Design. We were the place to be across the country for the launch of the seventh and final installment of the Harry Potter series, and we achieved our long-stated objective of becoming the performance leader in our industry in North America.

Revenue for the year was up 5.5%, once again outperforming our North American peers. Same store sales in our Indigo and Chapters superstores grew 4.4%, while small format stores posted a healthy 3.0% increase. Our online channel continued its strong growth trend and was up 16.9% for the year.

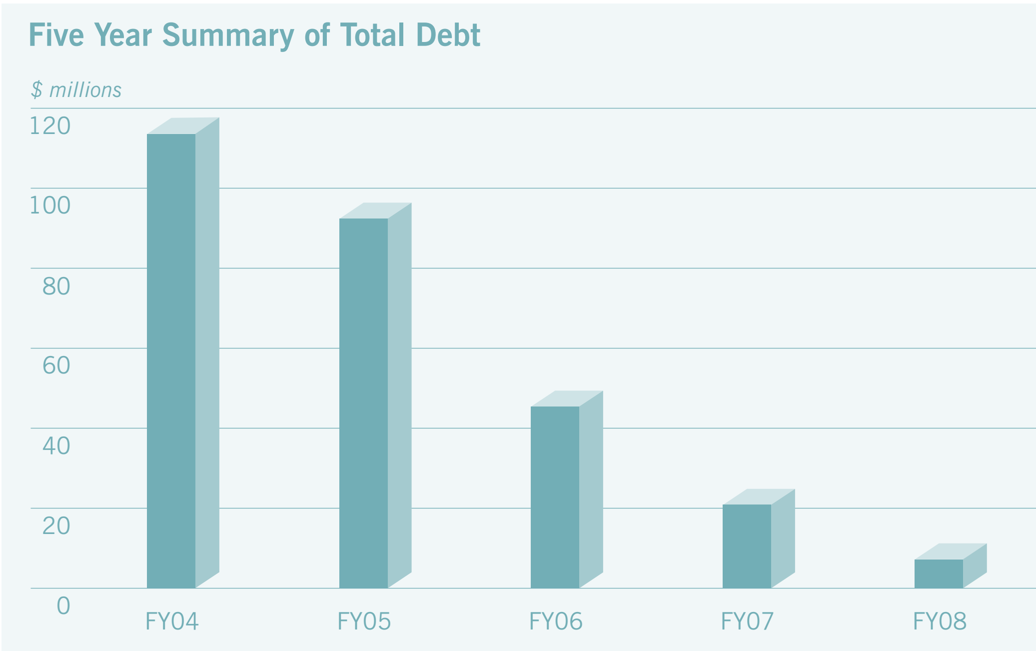


More satisfying are the gains in operating earnings. EBITDA for the year just ended was $73.9 million or 8.0% of revenue. This represents a 12.6% increase over the previous fiscal year.



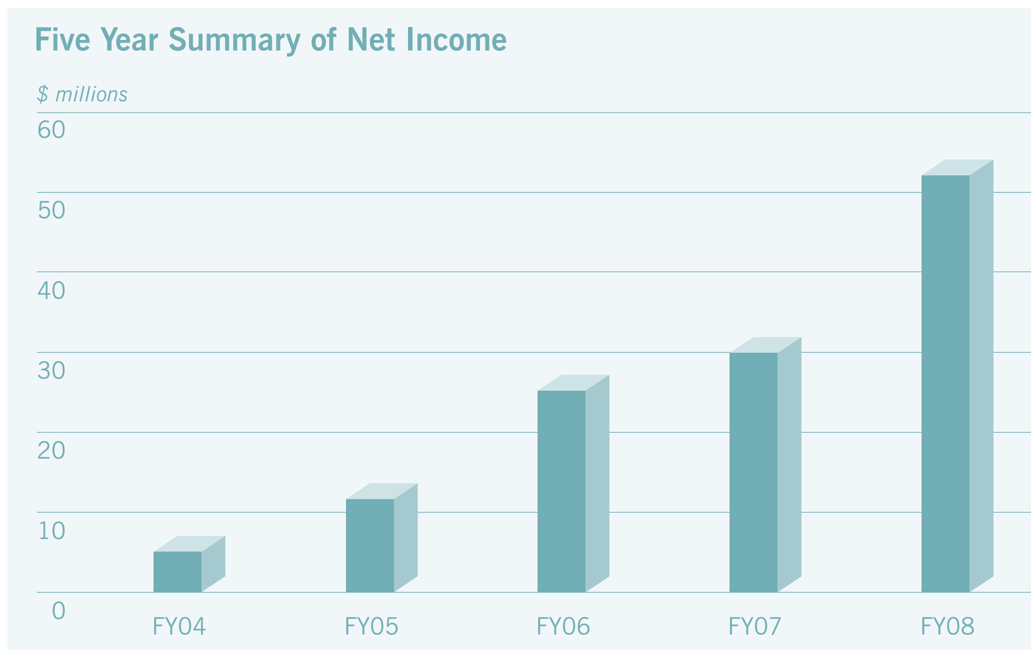
This year we paid down the last of our term debt, ending the year with $6.0 million in capital equipment leases and $55.9 million in cash.

We continue to believe that a healthy balance sheet gives us the flexibility to manage through any major economic downturns and gives us the ability to invest in new growth initiatives.



Solid increases in operating earnings and reduced interest and amortization costs contributed to a 47% increase in our pretax earnings.

Net income for the year was a record $52.8 million. We note that these results include an $8.8 million non-cash tax recovery and that the Company expects to be taxable in the coming fiscal year.



One final comment on performance; at the time of the merger we set very clear internal goals to be the best in class in a wide range of operating metrics, including sales per square foot, inventory turns, EBITDA as a percent of sales, and return on equity. I am proud to report that we surpassed our North American peers on all of these measures and are committed to reaching evening higher standards in the future.

As for the "worst"…
We were trending along an exceptional growth curve when Canada experienced the most significant upswing in the value of the Canadian dollar in recent history. As with most retailers, a strong Canadian dollar has a very meaningful impact on our business.

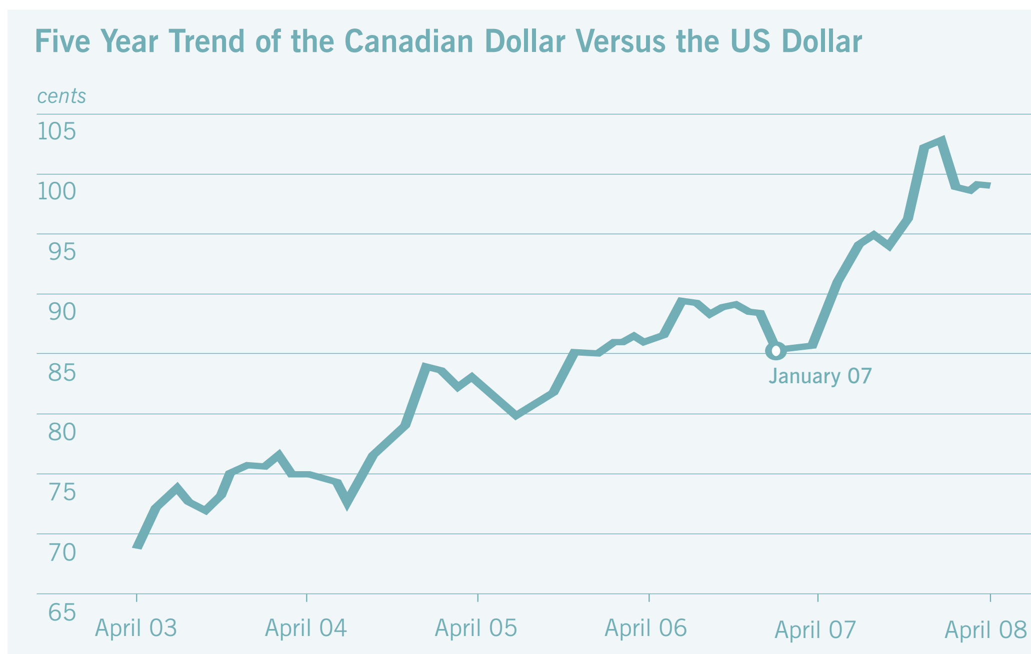
First, a significantly strengthened Canadian dollar, over time, results in lower Canadian book prices and lower absolute margin dollars. While history suggests that lower prices eventually drive higher sales – in the short term there is an impact on our top line.

Second, consumers today expect real-time adjustments from their retailers. In our case this is particularly difficult as publishers, not we, set retail prices and related profit margins in both currencies. Further complicating things is that book prices, and relevant exchange rates, are often set months before a new book hits our shelves. And of course, there are thousands of books on offer to our customers that have been in our stores for a year or more with exchange rates set at the initial time of printing.

We did our best, particularly during the all-important holiday season, to communicate the realities of our

business and to provide discounts to our customers to help mitigate the frustrations they were feeling. And we continue to both take prices down and engage with our customers on this subject. Nonetheless, in the short term, discounts and lower retail prices had the impact of blunting the significant momentum which we had built throughout last year and the first two quarters of this year. We are however convinced, and history confirms, that over time lower prices mean that consumers can, and will, purchase more.

The chart below illustrates the path of the Canadian dollar over the last five years. It is worth noting that during this period Indigo sales and profits have grown to more than offset the decline in top-line book prices.



Strategic Focus

In addition to serving more customers than ever, selling more product than ever, and reacting to the day-to-day demands of a retail business that operates seven days a week, 18-hours a day, the Company did a number of things to invest in our future.

This past year Indigo completed the work associated with the first year of our three-year strategic plan. Our overall objective over our planning horizon is to demonstrate industry leading growth and profitability and to create a foundation for sustainable high performance.

The four strategies to achieve this objective are as follows:

1. Re-imagine the Indigo/Chapters experience to address evolving consumer values and needs.
2. Simplify core processes to drive productivity and quality of work life.
3. Achieve best in class employee engagement.
4. Launch a new concept for our consumers.

A few words on each of these and our accomplishments this year in each area.

Re-imagine the Indigo/Chapters experience

It is 11 years since Indigo first launched into the marketplace. Much has happened since then both in our industry and in the larger media, entertainment and information environment which serve our customers. For this reason it is time to rethink and refresh.

This year we did the following: we advanced the design of our Large Format stores to best incorporate our expanding business in paper, gift, games, and kids' toys. The ten new Large Format stores we will open over the next 16 months will reflect these store design advances. At the same time, this work sets the basis for our planned store renovation program.

In addition, we conceived and developed a highly advanced new kiosk which will allow customers to very easily search for books, locate them in the store, purchase them online, view their wish lists, access real-time information about books featured in the media, and provide feedback to us on ideas and concerns.

Our new kiosk will also provide real-time information to our buyers about books which are being searched for by customers but not available in a given location, helping us to make intelligent adjustments in store-specific selection.

Both the software and hardware for our kiosks were designed by us and we expect them to be a breakthrough experience for staff and customers. The new kiosks will be launched in our stores this fall.

To advance chapters.indigo.ca and our overall relationship with our customers, we conceived and launched Indigo Community – our online social network for booklovers. Within six months, Indigo Community signed up over 100,000 members who create personal library shelves, join groups, engage with friends, exchange information about books and ideas and, of course, make purchases – both online and in-store. We see a lot of potential for this initiative and continue to learn and grow along with our customers.

There is still much to do on our "Re-imagine" initiative and I look forward to reporting more on this next year.

Simplify core processes and achieve breakthroughs in productivity and quality of work life

Last year in this section we noted that we had implemented a new warehouse management system which was giving us more headaches than we had anticipated. I am pleased to say the system was stabilized over this past year, and we began achieving some of the cost saving advantages that we had projected. We continue to see a good deal of opportunity to simplify our supply chain from end-to-end both lowering costs and improving inventory positions throughout our system.

This coming year we have committed to three major initiatives: A new labour scheduling tool to help optimize how we plan and manage labour in our stores, and a comprehensive review of our merchandising change-over process with a view to eliminating inefficiencies and removing "pain points" that cause frustration with both our home office and store staff. In addition we will begin work on a next generation of supply chain improvements.

We are confident these initiatives will help drive continued improvements in operating results and employee satisfaction.

Achieve industry leading employee engagement

We know that there is a direct correlation between employee engagement and superior results. This year we put attention toward two major drivers of employee engagement – a meaningful fit between employee expectations and what we as an organization provide; and managerial skill development. While overall moving the dial on employee engagement is a multi-year and, in fact, a continuous initiative, I am pleased to report that our employee survey results this year showed positive advances in all areas of the business.

And on the subject of employees…I would be remiss if I did not use this opportunity to comment on the incredible people who make up this organization. Our employee turnover is among the lowest in our industry. It is not surprising to come across people in our stores who have been with us 10, 15 or even 25 years. Daily I hear stories which reinforce the passion and commitment that our employees bring to work every day.

Recently I was attending a basketball game when a gentleman I had never met came over to tell me about arriving at our Bay and Bloor store in Toronto, only to discover it was already ten minutes past closing. An employee noticed him, invited him in and got him everything he wanted. A few days later I was visiting our store in Richmond Hill where I noted that we were running low on a hot new book. "Not to worry" said the General Manager who advised me that a manager from another store, 25 minutes away, was driving up 50 copies as soon as his shift was over to cover the situation until their next warehouse delivery. Examples like this are found daily throughout the Company both in our stores and in Home Office. There is simply no doubt that Indigo employees going the extra mile is at the heart of our success.

I am happy, therefore, to use this public opportunity to express the thanks of the executive team for the effort and spirit of our entire employee group. You are the best!

Launch a new concept

Over the course of this year, and as I write this letter, Indigo is working on a new retail concept which we intend to test launch in October 2008. For the moment we are keeping the specifics of the concept "under wraps"; however, I can tell you that it will appeal to a customer base we know well, and it will focus on a growing trend toward environmentally friendly products. In addition, as a retail and etail concept, it will leverage existing Indigo skills. Our plans for FY '09 include opening two stores prior to Holiday with more to follow in FY '10. I look forward to providing more on this in next year's Letter.

Giving Back: Indigo Love of Reading Foundation

Each year for the last four years I have taken pride in reporting on work we do in public schools across Canada.

We have made the idea of high levels of literacy for children a company-wide commitment. Our Love of Reading Foundation, which to-date has donated $6 million to high-needs schools, employs two people who work full-time at administering our school programs and reaching out into the communities across the land to encourage more applications for grants. At store level, employees support the sale of special products whose profits help fund our efforts. And company-wide employees find ways to raise money and contribute to our Foundation. Everyone at Indigo feels great to be making a difference in the area of literacy for young people.

It is stunning to most people to learn that well over 35% of adult Canadians are not functionally literate. This problem started in grade school - not in adulthood. It is equally surprising to most people to learn that our public schools, which are charged with inspiring children to read and developing their literacy, receive less than 1/3 of a new book per child per year for their libraries. This compares with 30 years ago when public schools got the equivalent of three new books per child per year for their libraries. The result is that public school libraries are dying unless the school is fortunate enough to serve a parent population able to fund the libraries themselves.

This year we launched our Indigo Love of Reading website at **www.indigoloveofreading.org**, produced and distributed *Writing on the Wall*, a powerful documentary on the literacy crises in economically challenged schools, and again donated $1.5 million to grant recipients bringing to $6 million the total amount of money we have granted to date. We feel great about this.

We encourage our shareholders to visit our site to learn more about our work. In addition, should any shareholder wish to receive a copy of *Writing on the Wall*, please feel free to contact us.

The Foundation's long-term goal is to engage with Provincial Leaders all across Canada and encourage them to make school libraries and school librarians a focus of their educational investments. Toward this end, we were pleased that this year Premier Dalton McGuinty of Ontario agreed to provide $120 million of new monies over four years for books and librarians. We look forward to working with other political leaders.

Looking Forward

Ours is an industry experiencing meaningful long-term change. The digitization of content, the steady growth of etail and online entertainment all combine to put pressure on the world of book retailing. Choice swamped consumers are bombarded daily with options to fill their time. And yet, each year we grow and find new ways to strengthen our bond with our existing customers. This is the challenge and opportunity of our time…to find, in a changing world, new ways to serve and satisfy booklovers. We feel we are up to the challenge, and we look forward to having you, our shareholders, continue this journey with us.

Heather Reisman
Chair and Chief Executive Officer

Management's Responsibility for Financial Reporting

Management of Indigo Books & Music Inc. ("Indigo") is responsible for the preparation and integrity of the financial statements as well as the information contained in this report. The following consolidated financial statements of Indigo have been prepared in accordance with Canadian generally accepted accounting principles, which involve management's best estimates and judgments based on available information.

Indigo's accounting procedures and related systems of internal control are designed to provide reasonable assurance that its assets are safeguarded and its financial records are reliable. In recognizing that the Company is responsible for both the integrity and objectivity of the consolidated financial statements, management is satisfied that the consolidated financial statements have been prepared according to and within reasonable limits of materiality and that the financial information throughout this report is consistent with these consolidated financial statements.

Ernst & Young LLP, Chartered Accountants, Licensed Public Accountants, serve as Indigo's auditors. Ernst & Young's report on the accompanying consolidated financial statements follows. Their report outlines the extent of their examination as well as an opinion on the consolidated financial statements. The Board of Directors of Indigo, along with the management team, have reviewed and approved the consolidated financial statements and information contained within this report.

Heather Reisman
Chair and Chief Executive Officer

Jim McGill
Chief Financial Officer

Management's Discussion and Analysis

The following Management's Discussion and Analysis ("MD&A") is prepared as at May 15, 2008 and is based primarily on the consolidated financial statements of Indigo Books & Music Inc. (the "Company" or "Indigo") for the 52-week periods ended March 29, 2008 and March 31, 2007. It should be read in conjunction with the consolidated financial statements and notes contained in the attached Annual Report. 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* website. As at March 29, 2008, the Company operated 86 superstores under the banners *Chapters*, *Indigo* and the *World's Biggest Bookstore*, and 158 small format stores, under the banners *Coles*, *Indigo*, *Indigospirit*, *SmithBooks* and *The Book Company*. During fiscal 2008, the Company opened three new small format stores, which were offset by the closure of three small format stores. The Company also closed two superstores during the fourth quarter of fiscal 2008. 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 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 current year was 24,744,334 as compared to 24,359,451 last year. The increase was mainly due to employees exercising stock options and the issuance of 14,964 shares in exchange for directors' deferred stock units when a Board member retired. As at May 15, 2008, the number of outstanding common shares was 24,843,147 with a book value of $198.9 million. The number of common shares reserved for issuance under the employee stock option plan is 2,234,315. As at March 29, 2008, there were 1,649,379 stock options outstanding with 549,702 of them exercisable.

Results of Operations

The following three tables summarize selected financial and operational information for the Company 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. The selected financial information is derived from the audited consolidated financial statements for the 52-week periods ended March 29, 2008, March 31, 2007 and April 1, 2006.

Key elements of the consolidated statement of earnings for the periods indicated are shown in the following table:

(millions of dollars)	FY08	% Revenues	FY07	% Revenues
Revenues	922.9	100.0%	875.0	100.0%
Cost of sales	524.7	56.9%	493.9	56.4%
Cost of operations	257.6	27.9%	249.3	28.5%
Selling and administrative expenses	66.7	7.2%	66.1	7.6%
EBITDA[1]	73.9	8.0%	65.7	7.5%

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

Selected financial information of the Company for the last three fiscal years are shown in the following table:

(thousands of dollars, except per share data)	52-week period ended March 29, 2008	52-week period ended March 31, 2007	52-week period ended April 1, 2006
Revenues			
Superstores	620,036	591,039	573,562
Small format stores	159,724	157,111	160,870
Online (including store kiosks)	101,345	86,745	79,514
Other	41,773	40,148	37,876
	922,878	875,043	851,822
Net earnings	52,808	30,004	25,337
Total assets	421,004	397,267	390,697
Long-term debt (including current portion)	6,028	20,490	31,832
Basic earnings per share	$2.13	$1.23	$1.05
Diluted earnings per share	$2.08	$1.19	$1.02

Selected operating information of the Company for the last three fiscal years are shown in the following table:

	52-week period ended March 29, 2008	52-week period ended March 31, 2007	52-week period ended April 1, 2006
Comparable Store Sales[1]			
Superstores	4.4%	2.5%	10.2%
Small format stores	3.0%	2.2%	4.3%
Stores Opened			
Superstores	–	2	2
Small format stores	3	1	4
	3	3	6
Stores Closed			
Superstores	2	–	2
Small format stores	3	7	6
	5	7	8
Number of Stores Open at Year-End			
Superstores	86	88	86
Small format stores	158	158	164
	244	246	250
Selling Square Footage at Year-End (in thousands)			
Superstores	2,042	2,090	2,058
Small format stores	422	425	441
	2,464	2,515	2,499

1 See "Non-GAAP Financial Measures".

Strong Growth in Revenues Driven by the Successful Release of *Harry Potter and the Deathly Hallows*

Total consolidated revenues for the 52-week period ended March 29, 2008 increased $47.9 million or 5.5% to $922.9 million from $875.0 million for the 52-week period ended March 31, 2007. The increase in revenues was mostly attributable to the successful release of *Harry Potter and the Deathly Hallows* in July 2007, an improvement in comparable store sales in the core retail business, and continued growth in the online channel. The improvement was partially offset by the increase in sales discounts given in response to the currency pricing issue, as discussed below.

Comparable store sales increased 4.4% in superstores and 3.0% in small format stores in fiscal 2008. 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. Excluding sales from *Harry Potter*, comparable store sales increased 3.7% in superstores and 2.2% in small format stores. At fiscal year end, the Company operated two fewer superstores and the same number of small format stores compared to the previous year.

Online sales continued to strengthen during fiscal 2008, improving 16.9% to $101.4 million for the 52-week period ended March 29, 2008 compared to $86.7 million in the same period last year. Online sales benefited from the release of *Harry Potter and the Deathly Hallows*, which materially increased customer traffic to the website, positively impacting sales of other products. Excluding sales from *Harry Potter*, Online sales increased 9.7% over the same period last year. Additional growth in revenues was achieved through the successful launch of the Indigo Online Community in September 2007. The Community provides a place where Canadian booklovers can connect and share their passion for books, authors, and reading. Since inception, over 100,000 members have joined the Online Community, resulting in a material increase in traffic to the *www.chapters.indigo.ca* website over last year.

Revenues from other sources include revenues generated through corporate sales, income from the sale of loyalty cards, the Company's proportionate revenues generated through Calendar Club, and gift card breakage. Revenues from other sources increased 4.0% from $40.2 million last year to $41.8 million for the current year. Continued sales growth in the Company's loyalty card program and an increase in gift card breakage offset the decline in Calendar Club and corporate sales revenues.

The rapid rise in the value of the Canadian dollar versus the US dollar during the last six months of calendar 2007 created significant public discussion on the relative price of Canadian and US products. Book and calendar prices were particularly open to this discussion given that both the US and Canadian prices are printed on the cover.

List prices are set by the publisher at the time of printing, which in many cases is six to twelve months before a book is purchased by the consumer. US publishers often include a premium in the Canadian price to reflect the higher cost of doing business in Canada. Short-term fluctuations in the value of the Canadian dollar, up or down, are not reflected in the price of a given title until the publisher has sold its entire inventory and reprints the book with a new price. Therefore, only recently printed titles in the fourth quarter of fiscal 2008 will reflect the stronger Canadian dollar in their price. Indigo continues to work with its publishers to address this pricing disparity issue.

In the first nine months of fiscal 2008, the Canadian list price of products sold in stores and online reflected exchange rates in effect prior to the rapid rise in the Canadian dollar. In response to public concern, the Company implemented a discounting strategy in the third quarter to reduce the retail selling price on many of its popular books to an amount comparable to, or better than, the US list price. As a result, the average retail selling price in stores during fiscal 2008 declined compared to last year. The impact of the decline in price was offset by an increase in units sold in stores, allowing total retail revenues for fiscal 2008 to increase compared to fiscal 2007.

Revenues by channel are highlighted below:

(millions of dollars)	FY08	FY07	% increase	Comparable store sales % increase	Comparable store sales % increase (normalized for *Harry Potter*)
Superstores	620.0	591.0	4.9	4.4	3.7
Small format stores	159.7	157.1	1.7	3.0	2.2
Online (including store kiosks)	101.4	86.7	16.9	N/A	N/A
Other	41.8	40.2	4.0	N/A	N/A
	922.9	875.0	5.5	4.1	3.4

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

	Superstores		Small format stores	
(millions of dollars)	52-week period ended March 29, 2008	52-week period ended March 31, 2007	52-week period ended March 29, 2008	52-week period ended March 31, 2007
Total revenues	620.0	591.0	159.7	157.1
Adjustments for stores not in both fiscal periods	(15.9)	(12.4)	(5.8)	(7.8)
Comparable store sales	604.1	578.6	153.9	149.3
Harry Potter comparable sales	(3.9)	–	(1.3)	–
Comparable store sales (excluding *Harry Potter*)	600.2	578.6	152.6	149.3

Cost of Sales Increased Slightly as a Percent of Revenues

Cost of sales include 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 increased 0.5% to 56.9% in fiscal 2008, compared to 56.4% last year. The change in cost of sales resulted primarily from increased discounts given in response to customer concerns over pricing disparity between US and Canadian list prices, higher than average discounts offered on *Harry Potter* in both the retail and online channels, and an increase in online shipping costs. Furthermore, the Company established a $1.0 million special provision to provide for the costs of discontinuing certain product lines in its entertainment business for a selected list of stores.

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

Cost of operation include all store, online, distribution centre and Calendar Club costs. Cost of operations increased $8.3 million primarily due to increased volume and higher minimum wage rates in most provinces. As a percent of total revenues, cost of operations decreased by 0.6% to 27.9% of sales compared to 28.5% of sales last year.

Selling and Administrative Expenses (as a Percent of Revenues) Decreased in Fiscal 2008

Selling and administrative expenses include all marketing and head office costs. Selling and administration expenses increased $0.6 million compared to last year. During fiscal 2008, the Company invested in various marketing initiatives to address the public's concerns regarding pricing differences between US and Canadian list prices. Further investments were made in information technology and new business opportunities. The investments were largely offset by a favourable property tax settlement and gains realized on foreign exchange. In addition, no bonuses were earned under the Long Term Performance and Retention Incentive Program in fiscal 2008. As a percent of total revenues, selling and administrative expenses decreased from 7.6% last year to 7.2% this year.

EBITDA Increased to 8.0% of Revenues

EBITDA, defined as earnings before interest, taxes, depreciation, amortization and capital assets write-off, increased $8.2 million to $73.9 million for the 52-week period ended March 29, 2008, compared to $65.7 million for the 52-week period ended March 31, 2007. EBITDA as a percent of revenues increased to 8.0% this year from 7.5% last year. The improvement in EBITDA was primarily due to strong sales performance and reductions in cost of operations and selling and administrative expenses as a percent of total revenues, partially offset by an increase in cost of goods sold and shipping costs, as explained above.

Amortization Decreased Slightly in Fiscal 2008

Amortization for the 52-week period ended March 29, 2008 decreased $1.1 million to $29.8 million, compared to $30.9 million for the 52-week period ended March 31, 2007. Capital expenditures in fiscal 2008 totalled $21.6 million and included $10.1 million on store construction, renovations and equipment, and $11.5 million on technology-related projects. Of the $21.6 million in capital expenditures, $2.1 million was financed through capital leases.

In fiscal 2006, the Company began work on two projects, a new online order management system and a new product database system. The Company decided to discontinue the implementation of the online order management system in the third quarter of fiscal 2007 and wrote-off $1.6 million in assets associated with this project. In the fourth quarter of fiscal 2007, the Company wrote-off an additional $0.8 million in assets associated with the product database system project. Both write-offs were due to unplanned scope and cost increases. There were no capital assets written off in fiscal 2008.

Non-Cash Adjustment to the Restructuring Provision

In the fourth quarter of fiscal 2007, the Company recognized $0.3 million into income for recovery of construction costs from a subtenant, which was initially expensed through the restructuring provision.

Interest Expense Declined 97.1%

Interest expense decreased by $2.7 million to $0.1 million from $2.8 million last year. This was due to the reduction in total debt outstanding for the Company. Average total debt (including bank indebtedness and long-term debt) was $11.2 million in fiscal 2008 compared to $45.9 million over the same period last year.

Non-Cash Income Tax Recovery

The Company recorded an $8.8 million non-cash tax recovery in fiscal 2008. The recovery was the net impact of three major factors: (i) an income tax expense based on fiscal 2008 net earnings, plus (ii) an income tax expense due to corporate income tax rate reductions announced and substantively enacted by the Canadian federal government leading to a reduction in the gross amount of future tax assets, offset by (iii) an income tax recovery resulting from the elimination of the income tax valuation allowance, as the Company has 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.

Net Earnings Improved by 76.0%

Net earnings increased $22.8 million or $0.90 per common share to $52.8 million ($2.13 per common share) from $30.0 million ($1.23 per common share) last year. The improvement was primarily due to strong operating results, the decrease in interest expenses and the $8.8 million non-cash income tax recovery, noted above.

Other Comprehensive Income

The Company adopted new accounting standards related to financial instruments on April 1, 2007, as explained in the section of the MD&A entitled Accounting Standards Adopted in Fiscal 2008 and in Note 3 to the consolidated financial statements.

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 purchases in US dollars. Upon adoption of the new Financial

Instruments Standards, 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. As at the end of fiscal 2008, the Company did not have any interest rate and foreign currency derivative contracts outstanding.

Seasonality and Fourth 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), basic and diluted earnings (loss) per share for the preceding eight fiscal quarters.

	Fiscal quarters ended on or about:			
(thousands of dollars, except per share data)	June 30	September 29	December 29	March 29
Fiscal 2008 Revenues	**184,917**	**209,173**	**322,552**	**206,236**
Net earnings (loss)	**(2,840)**	**3,339**	**49,179**	**3,130**
Basic earnings (loss) per share	**$(0.12)**	**$0.14**	**$1.98**	**$0.13**
Diluted earnings (loss) per share	**$(0.12)**	**$0.13**	**$1.94**	**$0.12**
Fiscal 2007 Revenues	170,351	182,305	320,491	201,896
Net earnings (loss)	(5,791)	(976)	40,977	(4,206)
Basic earnings (loss) per share	$(0.24)	$(0.04)	$1.68	$(0.17)
Diluted earnings (loss) per share	$(0.24)	$(0.04)	$1.62	$(0.17)

The Company realized a moderate increase in consolidated revenues in the fourth quarter of fiscal 2008, which improved $4.3 million or 2.1%, to $206.2 million compared to $201.9 million in the same quarter last fiscal year. Fourth quarter sales benefited from an early Easter holiday which fell in March 2008. For the period, comparable store sales increased 3.4% in superstores and 2.4% in small format stores.

Online sales increased $0.3 million or 1.0%, to $24.7 million in the fourth quarter this year from $24.4 million last year. The growth was not as strong in the quarter compared to the rest of the year due to: (i) average price decreases due to the stronger Canadian dollar; (ii) strong sales of *The Secret* (both book and DVD) in the fourth quarter of fiscal 2007; and (iii) fourth quarter sales in fiscal 2007 benefited from heavy pre-orders of *Harry Potter and the Deathly Hallows*, as customers increased their average transaction size to qualify for the free shipping promotion.

Net earnings in the fourth quarter of fiscal 2008 were $3.1 million, compared to a loss of $4.2 million in the same quarter last fiscal year.

Overview of Consolidated Balance Sheets

Total Assets

As at March 29, 2008, total assets were $23.7 million greater than total assets at March 31, 2007. The increase in assets was primarily due to an increase in the Company's cash and cash equivalents. Cash and cash equivalents increased $42.3 million due to improved sales compared to last year. The increase was partially offset by a lower inventory position and lower net capital assets. Inventories decreased $17.8 million compared to last year, as the Company implemented an improved open-to-buy process in fiscal 2008 creating better controls over the amount of inventory being purchased. Further, inventory levels were higher last year due to the delay in processing of some returns owing to the implementation of the new warehouse management system in 2006. Net capital assets decreased $8.8 million due to capital assets amortization of $29.7 million and disposal of $0.7 million. It was partially offset by net capital asset additions of $21.6 million over the past year.

Other changes in total assets included an $8.8 million increase in future tax assets. During the 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, which was partially offset by a reduction in the amount of future tax assets due to the corporate income tax rate reductions announced and substantively enacted by the Canadian federal government.

Total Liabilities

As at March 29, 2008, total liabilities were $31.2 million less than total liabilities at March 31, 2007. The decrease in liabilities was primarily due to a $14.5 million decrease in total debt (including bank indebtedness and long-term debt) and a $16.5 million reduction in accounts payable and accrued liabilities. During the first quarter of fiscal 2008, the Company renegotiated its credit agreement with its bank. As part of the refinancing, the Company repaid $13.0 million of long-term debt that was outstanding under the old agreement. The reduction in accounts payable and accrued liabilities is consistent with the reduction in inventories, as noted above.

Shareholders' Equity

As at March 29, 2008, shareholders' equity was $54.9 million greater than shareholders' equity at March 31, 2007. The increase in shareholders' equity was primarily due to net earnings of $52.8 million in fiscal 2008. Share capital increased $1.3 million due to the exercise of employee stock options and shares being issued to a retiring Board member in exchange for his outstanding directors' deferred stock units. Contributed surplus increased $1.1 million due to expensing of employee stock options and directors' deferred stock units, partially offset by a $0.3 million reduction due to the exercise of employee stock options.

Working Capital and Leverage

As at March 29, 2008, the Company's working capital position was $76.6 million, an increase from $28.8 million as of March 31, 2007. The improvement resulted from growth in sales and reduction in total debt, as previously discussed.

The Company's leverage position (defined as Total Liabilities to Total Shareholders' Equity) improved from 1.7:1 at the end of fiscal 2007 to 1.1:1 at the end of the current fiscal year due to the above-noted reduction in total debt and increase in shareholders' equity.

Overview of Consolidated Statements of Cash Flows

Cash and cash equivalents increased $42.3 million during fiscal 2008 compared to an increase of $7.7 million in fiscal 2007.

Cash Flows from Operating Activities

The Company generated positive cash flows from operating activities of $76.9 million during fiscal 2008. This was an increase of $23.6 million over the same period a year ago, when cash flow generated from operating activities was $53.2 million. The positive change in cash flows was primarily due to a $22.8 million improvement in net earnings (from net earnings of $30.0 million last year to net earnings of $52.8 million this year), and a $27.3 million reduction in the Company's investment in inventories due to the new open-to-buy process noted above. The improvement in operating cash flows was partially offset by a $12.4 million reduction in accounts payable and accrued liabilities, an $8.8 million increase in future tax assets and a $5.0 million reduction in prepaid expenses.

Cash Flows Used in Investing Activities

Net cash flows used in investing activities were $18.8 million in fiscal 2008 compared to $20.0 million in fiscal 2007. In fiscal 2008, total cash spent on capital projects was $19.5 million compared to $20.1 million spent in fiscal 2007 as outlined below:

(millions of dollars)	FY08	FY07
Store construction, renovations and equipment	10.1	12.3
Technology-related projects	9.4	7.8
	19.5	20.1

Store renovations are typically done upon lease renewal and at selected points throughout a lease term. The amounts spent in fiscal 2008 and fiscal 2007 are reflective of the average term of leases in the Company's portfolio and the required dates for store renovations.

During fiscal 2008, the Company received $0.7 million of cash proceeds from the disposal of equipment. In the same period last year, cash proceeds from disposal totaled $0.1 million.

Cash Flows Used in Financing Activities

Net cash flows used in financing activities were $15.7 million in fiscal 2008 compared to $25.6 million in fiscal 2007. The Company used $16.8 million to reduce its long-term debt in fiscal 2008 and received $1.1 million proceeds from share issuance. This compares to a use of $27.8 million to reduce its long-term debt and operating line offset by cash proceeds of $2.3 million from share issuance in fiscal 2007.

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. Indigo invests its cash in highly liquid assets and the Company does not invest in asset-backed commercial paper. 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 is forecasting lower borrowing needs. As at March 29, 2008, no funds were drawn against this facility.

The Company's contractual obligations due over the next five years are summarized below:

(millions of dollars)	Less than 1 year	1-3 years	4-5 years	After 5 years	Total
Capital lease obligations	2.6	3.2	0.2	–	6.0
Operating leases	58.3	95.4	65.8	47.5	267.0
Total obligations	60.9	98.6	66.0	47.5	273.0

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 revenues 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 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.

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 will be limited to 2,905 common shares, other than block purchase exceptions. All common shares purchased under the NCIB will be cancelled and returned to treasury.

Accounting Policies

Critical Accounting Estimates

The discussion and analysis of Indigo's operations and financial condition are based upon the 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 to the consolidated financial statements.

The following items in the consolidated financial statements involve significant estimation or judgment:

Inventory Valuation

Indigo uses the cost method to account for inventory and cost of sales. Under this method, inventory is recorded at the individual article (stock keeping unit or sku) level. The average cost of an article is continually updated based on the cost of each purchase recorded into inventory. When the Company permanently reduces the retail price of an item, there is a corresponding reduction in inventory recognized in the period if the markdown incurred brings the retail price below the cost of the item. The Company also reduces inventory for estimated shrinkage that has occurred between annual physical inventory counts. The net result is that inventory is valued at the lower of cost, determined on a moving average cost basis, or market, being net realizable value.

Indigo records provisions for slow-moving and damaged products and for gift and paper products that have been marked down based on assumptions about future sales demand, inventory levels and product quality. Management reviews the provisions regularly and assesses whether they are appropriate based on actual experience. In addition, the Company records a vendor settlement provision to cover any disputes between the Company and its vendors. Management estimates this provision based on historical experience of settlements with its vendors.

Given that inventory and cost of sales are significant components of the consolidated balance sheets and consolidated statements of earnings, any changes in assumptions and estimates could have a material impact on the Company's financial position.

Assessment of Impairment of Long-Lived Assets and Goodwill

The Company's long-lived assets consist mainly of capital assets. Long-lived assets are reviewed by the Company whenever events or changes in circumstances indicate that their carrying values are not recoverable, resulting in a potential impairment. A potential impairment has occurred if the projected future undiscounted cash flows are less than the carrying value of the assets. When this is the case, the impairment loss is measured as the excess of the carrying value of the assets over its fair

value, which is determined as the present value of the cash flows being generated from the assets. The evaluation is performed for the lowest level of the group of assets and liabilities with identifiable cash flows that are independent of those of other assets and liabilities.

The recoverability assessment requires judgment and estimates for future generated cash flows. The underlying estimates for future cash flows include estimates for future sales, gross margin rates, expenses and are based upon past and expected performance.

Capital assets make up a significant amount of the Company's total assets. To the extent that there is a significant change to the Company's assumptions, there may potentially be a significant impact on the Company's consolidated financial statements.

In accordance with Canadian GAAP, the Company does not amortize goodwill. Goodwill is tested for impairment annually or more frequently if there is any indication of impairment. The carrying values of the net assets are compared to the estimated fair values at the reporting unit level. Fair values are estimated based on the discounted cash flow method which depends on variables such as future earnings trends, capital expenditures and the discount rate. Any change in these variables may result in future impairment of goodwill. The Company performed its annual impairment test on March 29, 2008, and the results of this test indicated no impairment of goodwill.

Gift Cards

Effective in the third quarter of fiscal 2007, the Company changed its accounting policy relating to gift cards with no impact on prior period results. This policy change was made based on the Company's review of the gift card accounting clarifications provided by the Securities and Exchange Commission ("SEC") and the introduction of legislation by the Ontario government banning gift card expiry dates and excessive service charges. The Company sells gift cards to its customers and recognizes the revenue as the gift cards are redeemed. The Company also recognizes revenue from unredeemed gift cards (gift card breakage) if the likelihood of the gift card being redeemed by the customer is considered to be remote. The Company determines its average gift card breakage rate based on historical redemption rates. Once the breakage rate is determined, the resulting revenue is recognized over the estimated period of redemption, commencing when the gift cards are sold, based on historical redemption patterns.

Income Taxes

The Company follows the liability method of tax allocation for accounting for income taxes. Under the liability method of tax allocation, future tax assets and liabilities are determined based on differences between the financial reporting and tax bases of assets and liabilities and are measured using the substantively enacted tax rates and laws that are expected to be in effect when the differences are estimated to reverse.

Indigo currently has future tax assets associated with its non-capital loss carryforwards, which are available to reduce taxable income in the future. The Company evaluates the likelihood of using all or a portion of the loss carryforwards based on expected future earnings derived from internal forecasts, earning/loss trends in recent years, and the expiry date of its loss carryforwards. Based on this information, the Company determines the appropriate amount of income tax valuation allowance that is required to reduce the value of its total loss carryforwards to an amount which it estimates it can more likely than not utilize. During the third quarter of fiscal 2008, 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. Any changes in estimates would affect the income tax expense on the consolidated statement of earnings and future tax assets on the consolidated balance sheets. If the actual amount differs from the current estimates, the future tax value of these loss carryforwards may change significantly and the Company may incur a non-cash tax expense.

Financial Instruments

During fiscal 2008, Indigo used derivative financial instruments to manage risks of its foreign currency and interest rate exposures. The Company entered into foreign currency derivative contracts to hedge future purchases of US Dollar denominated goods and services. The Company also used interest rate swap agreements to manage the fixed and floating interest rate mix of the Company's total debt portfolio. The risks associated with the use of derivative financial instruments are discussed further under the "Risks and Uncertainties" section. As at the end of fiscal 2008, the Company did not have any interest rate and foreign currency derivative contracts outstanding.

The fair value of financial instruments was the estimated amount the Company would receive or pay to terminate the contracts at the reporting date. Such fair value estimates were not necessarily indicative of the amounts the Company might receive or pay in actual market transactions.

The following methods and assumptions are used to estimate the fair value of each type of financial instrument by reference to various market value data and other valuation techniques, as appropriate.

The fair values of cash and cash equivalents, accounts receivable, bank indebtedness and accounts payable and accrued liabilities approximate their carrying values, given their short-term maturities.

The fair value of long-term debt is estimated based on the discounted cash payments of the debt at Indigo's estimated incremental borrowing rates for debt of the same remaining maturities. The fair value of the long-term debt approximates its carrying value.

Accounting Standards Adopted in Fiscal 2008

Financial Instruments

The Canadian Institute of Chartered Accountants ("CICA") issued three new standards relating to financial instruments: Comprehensive Income; Financial Instruments – Recognition and Measurement; and Hedges.

Section 1530 of the CICA Handbook, "Comprehensive Income", establishes standards for reporting and display of comprehensive income and defines other comprehensive income to include revenues, expenses, gains and losses that, in accordance with primary sources of generally accepted accounting principles, are recognized in comprehensive income, but excluded from net earnings.

Section 3855 of the CICA Handbook, "Financial Instruments – Recognition and Measurement", describes the standards for recognizing and measuring financial assets, financial liabilities and non-financial derivatives.

Section 3865 of the CICA Handbook, "Hedges", describes when and how hedge accounting may be applied. It replaces Accounting Guideline 13, "Hedging Relationships", which was adopted by the Company in April 2004.

These new standards have been created to harmonize with the generally accepted accounting principles already in use in the United States. These new standards were adopted by the Company for the fiscal year beginning April 1, 2007 with no material impact on the consolidated financial statements as a result of their adoption.

Accounting Changes

In July 2006, the Accounting Standards Board issued a replacement of the CICA Handbook Section 1506, Accounting Changes. The new standard allows for voluntary changes in accounting policy only when they result in the financial statements providing reliable and more relevant information, requires changes in accounting policy to be applied retrospectively unless doing so is impracticable, requires prior period errors to be corrected retrospectively and calls for enhanced disclosures about the effects of changes in accounting policies, estimates and errors on the financial statements. It also requires disclosure of information relevant to assessing the possible impact that the application of a new GAAP standard will have on the Company's financial statements in the period of initial application. The impact that the adoption of this section will have on the Company's financial position and results of operations will depend on the nature of the future accounting changes. The Company has determined that the adoption of this section, effective April 1, 2007, did not have a material impact on its consolidated financial statements.

New Accounting Pronouncements

The following accounting standards will be adopted by the Company in the future:

Financial Instruments

Section 3862 and Section 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 have to be adopted by the Company for the fiscal year beginning March 30, 2008. The Company is currently evaluating the impact of this new standard and it will result in additional disclosures.

Capital Disclosures

Section 1535 of the CICA Handbook, Capital Disclosures, specifies the disclosure of: (i) the Company's objectives, policies and processes 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 non-compliance. This standard is effective for the Company's fiscal year beginning March 30, 2008.

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 must be adopted by the Company for the fiscal year beginning March 30, 2008. The Company is currently assessing the impact of this new standard on its consolidated financial statements.

General Standards of Financial Statement Presentation

The CICA amended Handbook Section 1400 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 must be adopted by the Company for the fiscal year beginning March 30, 2008. The Company is currently assessing the impact of this new standard on its consolidated financial statements.

Goodwill and Intangible Assets

Section 3064 of the CICA Handbook, "Goodwill and Intangible Assets", replaces the existing Section 3062 "Goodwill and Other Intangible Assets" and Section 3450 "Research and Development Costs". In conjunction with the issuance of this new standard, the CICA has amended Section 1000 "Financial Statement Concepts". These changes clarify the criteria for asset recognition for an internally developed intangible asset and reinforce the distinction between costs that should be expensed and those that should be capitalized. These standards have been created to harmonize with the International Financial Reporting Standards and they have to be adopted by the Company for the fiscal year beginning March 29, 2009. The Company is currently assessing the impact of this new standard on its 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 is currently working on a conversion plan towards IFRS but it is too early to assess the financial impact of the conversion at this point.

Risks and Uncertainties

Competition

The retail book selling business is highly competitive. Specialty bookstores, independents, other book superstores, regional multi-store operators, supermarkets, drug stores, warehouse clubs, mail order clubs, Internet booksellers, mass merchandisers and other retailers offering books are all sources of competition for the Company. Aggressive merchandising or discounting by competitors in either the retail or online sectors could reduce the Company's market share and its operating margins.

Economic Environment

Traditionally, retail businesses are highly susceptible to market conditions in the economy. A decline in consumer spending, especially over the December holiday season, could have an adverse effect on the Company's financial condition. Other variables, such as unanticipated increases in merchandise costs, increases in labour costs, increases in shipping rates or interruptions in shipping service, higher interest rates or unemployment rates, could also unfavourably impact the Company's financial performance.

External Events

Weather conditions, as well as events such as political or social unrest, natural disasters, disease outbreaks, or acts of terrorism, could have a material adverse effect on the Company's financial performance. Moreover, if such events were to occur at peak times in the Company's annual business cycle, the impact of these events on operating performance could be significantly greater than it would otherwise have been.

Regulatory Environment

The distribution and sale of books is a regulated industry in which foreign ownership is generally not permitted under the Investment Canada Act. As well, the sourcing and importation of books is governed by the Book Importation Regulations to the Copyright Act (Canada). There is no assurance that the existing regulatory framework will not change in the future or that it will be effective in preventing foreign-owned retailers from competing in Canada.

Credit, Foreign Exchange, and Interest Rate Risks

Foreign exchange risk is largely limited to currency fluctuations between the Canadian and US Dollars. The Company has minimal requirements for Euros, British Pounds, Hong Kong Dollars or other currencies. Indigo historically used foreign currency derivative contracts to hedge its foreign exchange risks. Given Indigo has determined that its foreign currency risk is manageable going forward, the Company decided to stop its hedging program as at the end of the fiscal year.

The Company's interest rate risk is limited to the fluctuation of floating rates on its outstanding operating line. Counterparty credit risk is considered to be negligible as the Company only deals with highly rated financial institutions.

Leases

The average unexpired lease term of Indigo's superstores and small format stores is approximately 4.2 years and 3.0 years, respectively. The Company attempts to renew these leases as they come due on favourable terms and conditions, but is susceptible to volatility in the market for supercentre and shopping mall space. Unforeseen increases in occupancy costs, or costs incurred as a result of unanticipated store closing and relocation could unfavourably impact the Company's performance.

Dependence on Key Personnel

Indigo's continued success will depend to a significant extent upon its management group. The loss of the services of key personnel, particularly Ms. Reisman, could have a material adverse effect on Indigo.

Legal Proceedings

In the normal course of business, Indigo becomes involved in various claims and litigation. While the final outcome of such claims and litigation pending as at March 29, 2008 cannot be predicted with certainty, management believes that any such amount would not have a material impact on the Company's financial position.

Disclosure Controls and Procedures

The Company's management is responsible for establishing and maintaining the Company's disclosure controls and procedures to ensure that information used internally and disclosed externally is complete and reliable. The Chief Executive Officer and the Chief Financial Officer of the Company have evaluated the effectiveness of the Company's disclosure controls and procedures and have concluded that they are adequate and effective as of the fiscal year ended March 29, 2008.

Internal Controls over Financial Reporting

Management is also 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 GAAP. Management has evaluated the design of the Company's internal controls and procedures over financial reporting as of the end of fiscal year ended March 29, 2008, and believes the design to be effective to provide such reasonable assurance.

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 taken and continues to take steps to address these control issues and has in place a number of compensating controls to mitigate the risk of an error in its financial reporting.

There were no changes in internal control over financial reporting that occurred during the Company's fourth quarter that have materially affected, or are reasonably likely to materially affect, the Company's internal control over 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 GAAP. 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, amortization and capital assets write-off.

A reconciliation between comparable store sales and revenue (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)	52-week period ended March 29, 2008	52-week period ended March 31, 2007
EBITDA	73.9	65.7
Amortization of capital assets	29.7	30.7
Capital assets write-off	–	2.4
Amortization of pre-opening store costs	0.1	0.2
Recovery of restructuring costs	–	(0.3)
Interest on long-term debt and financing charges	0.8	1.3
Interest (income) on bank indebtedness	(0.7)	1.5
Earnings before income taxes	44.0	29.9

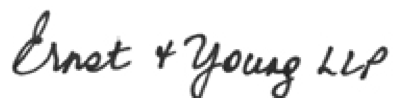
Auditors' Report

To the Shareholders of Indigo Books & Music Inc.

We have audited the consolidated balance sheets of Indigo Books & Music Inc. as at March 29, 2008 and March 31, 2007 and the consolidated statements of earnings, retained earnings (deficit), comprehensive earnings and cash flows for the 52-week periods then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at March 29, 2008 and March 31, 2007 and the results of its operations and its cash flows for the 52-week periods then ended in accordance with Canadian generally accepted accounting principles.



Chartered Accountants
Licensed Public Accountants

Toronto, Canada,
May 15, 2008

Consolidated Balance Sheets

(thousands of dollars)	As at March 29, 2008	As at March 31, 2007
ASSETS		
Current		
Cash and cash equivalents	55,933	13,639
Accounts receivable	8,996	9,848
Inventories	206,259	224,059
Income taxes recoverable	21	194
Prepaid expenses	4,929	4,578
Future tax assets (note 5)	6,745	9,205
Total current assets	282,883	261,523
Capital assets, net (note 4)	67,348	76,186
Future tax assets (note 5)	43,250	32,035
Goodwill (note 6)	27,523	27,523
Total assets	421,004	397,267
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current		
Accounts payable and accrued liabilities (notes 3 and 9)	193,323	206,542
Deferred revenue	10,350	10,621
Current portion of long-term debt (notes 7 and 13)	2,648	15,562
Total current liabilities	206,321	232,725
Long-term accrued liabilities	7,549	10,807
Long-term debt (notes 7 and 13)	3,380	4,928
Total liabilities	217,250	248,460
Commitments and contingencies (notes 7 and 13)		
Shareholders' equity		
Share capital (note 8)	198,938	197,592
Contributed surplus (note 8)	2,564	1,752
Retained earnings (deficit)	2,252	(50,537)
Total shareholders' equity	203,754	148,807
Total liabilities and shareholders' equity	421,004	397,267

See accompanying notes

On behalf of the Board:

Heather M. Reisman
Director

Michael Kirby
Director

Consolidated Statements of Earnings

(thousands of dollars, except per share data)	52-week period ended March 29, 2008	52-week period ended March 31, 2007
Revenues	922,878	875,043
Cost of sales, operations, selling and administration	848,934	809,386
	73,944	65,657
Amortization of capital assets	29,665	30,670
Capital assets write-off (note 10)	–	2,372
Amortization of pre-opening store costs	144	205
	29,809	33,247
Earnings before the undernoted items	44,135	32,410
Recovery of restructuring costs (note 9)	–	(315)
Interest on long-term debt and financing charges (note 7)	786	1,307
Interest expense (income) on bank indebtedness (note 7)	(704)	1,504
Earnings before income taxes	44,053	29,914
Income tax recovery (note 5)	(8,755)	(90)
Net earnings for the period	52,808	30,004
Net earnings per common share (note 8)		
Basic	$2.13	$1.23
Diluted	$2.08	$1.19

See accompanying notes

Consolidated Statements of Retained Earnings (Deficit)

(thousands of dollars)	52-week period ended March 29, 2008	52-week period ended March 31, 2007
Deficit, beginning of period, as reported	(50,537)	(80,541)
Transitional adjustment on adoption of new accounting policies (note 3)	(19)	–
Deficit, beginning of period, as restated	(50,556)	(80,541)
Net earnings for the period	52,808	30,004
Retained earnings (deficit), end of period	2,252	(50,537)

See accompanying notes

Consolidated Statements of Comprehensive Earnings

(thousands of dollars)	52-week period ended March 29, 2008	52-week period ended March 31, 2007
Net earnings for the period	**52,808**	30,004
Other comprehensive loss, net of tax		
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	(144)	–
Comprehensive earnings for the period	**52,664**	30,004

See accompanying notes

Consolidated Statements of Cash Flows

(thousands of dollars)	52-week period ended March 29, 2008	52-week period ended March 31, 2007
CASH FLOWS FROM OPERATING ACTIVITIES		
Net earnings for the period	52,808	30,004
Add (deduct) items not affecting cash		
Amortization	29,809	30,875
Stock-based compensation (note 8)	751	546
Directors' compensation (note 8)	341	298
Future tax assets (note 5)	(8,755)	–
Loss on disposal of capital assets	105	241
Capital assets write-off (note 10)	–	2,372
Amortization and write-off of deferred financing charges	258	304
Other	(19)	–
Net change in non-cash working capital balances related to operations		
Accounts receivable	852	(3,911)
Inventories	17,800	(9,461)
Prepaid expenses	(495)	4,518
Income taxes recoverable	173	(38)
Deferred revenue	(271)	1,589
Accounts payable and accrued liabilities	(16,477)	(4,100)
Cash flows from operating activities	76,880	53,237
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of capital assets	(19,532)	(20,068)
Proceeds from sale of capital assets	691	67
Cash flows used in investing activities	(18,841)	(20,001)
CASH FLOWS FROM FINANCING ACTIVITIES		
Decrease in bank indebtedness	–	(12,728)
Repayment of long-term debt (note 7)	(16,811)	(15,155)
Proceeds from share issuances (note 8)	1,066	2,303
Cash flows used in financing activities	(15,745)	(25,580)
Net increase in cash and cash equivalents during the period	42,294	7,656
Cash and cash equivalents, beginning of period	13,639	5,983
Cash and cash equivalents, end of period	55,933	13,639

See accompanying notes

Notes to Consolidated Financial Statements

March 29, 2008

1. NATURE OF OPERATIONS

Indigo Books & Music Inc. (the "Company" or "Indigo"), the nation's largest book retailer, was formed as a result of an amalgamation of Chapters Inc. and Indigo Books & Music, Inc. under the laws of the Province of Ontario, pursuant to a Certificate of Amalgamation dated August 16, 2001. The Company operates a chain of retail bookstores across all 10 provinces and one territory in Canada, including 86 superstores (March 31, 2007 – 88) under the *Chapters*, *Indigo* and *World's Biggest Bookstore* names, as well as 158 small format stores (March 31, 2007 – 158) under the banners *Coles*, *Indigo*, *Indigospirit*, *SmithBooks* and *The Book Company*. The Company operates *www.chapters.indigo.ca*, an e-commerce retail destination, which sells books, videos, DVDs, music and toys. The Company also operates seasonal kiosks and year-round stores in shopping malls across Canada through its Calendar Club of Canada Limited Partnership. 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 material to high-needs elementary schools across the country through donations from Indigo, its customers, suppliers and employees.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of consolidation

These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP") and include the accounts of the Company and its subsidiary companies. All significant intercompany balances and transactions have been eliminated on consolidation.

Use of estimates

The preparation of financial statements in accordance with Canadian GAAP requires management to make estimates and assumptions that affect: the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements; and the reported amounts of revenues and expenses during the reporting periods. Actual results may differ from those estimates.

Joint venture

The accounts of the Company reflect its proportionate interest in retail activities conducted through a joint venture.

Revenue recognition

The Company recognizes revenue when title passes to the customer. Revenue for retail customers is recognized at the point of sale and revenue for online customers is recognized when the product is shipped. The Company reports its revenues net of sales discounts and returns and is inclusive of amounts invoiced for shipping.

Deferred revenue

For an annual fee, the Company offers customers loyalty cards that entitle the cardholder to receive discounts on purchases. Each card is issued with a 12-month expiry period. The fee revenue related to the issuance of a card is deferred and is amortized to earnings over the expiry period, based upon historical sales volumes.

Gift cards

The Company sells gift cards to its customers and recognizes the revenue as the gift cards are redeemed. The Company also recognizes income from unredeemed gift cards (gift card breakage) if the likelihood of the gift card being redeemed by the customer is considered to be remote. The Company determines its average gift card breakage rate based on historical redemption rates. Once the breakage rate is determined, the resulting revenue is recognized over the estimated period of redemption, commencing when the gift cards are sold, based on historical redemption patterns. Gift card breakage is included in revenues in the Company's consolidated statements of earnings.

Income taxes

The Company follows the liability method of tax allocation for accounting for income taxes. Under the liability method of tax allocation, future tax assets and liabilities are determined based on differences between the financial reporting and tax bases of assets and liabilities and are measured using the substantively enacted tax rates and laws that are expected to be in effect when the differences are expected to reverse.

Earnings per share

Basic earnings per share are determined by dividing the net earnings attributable to common shareholders by the weighted average number of common shares outstanding during the period. Diluted earnings per share are calculated in accordance with the treasury stock method and are based on the weighted average number of common shares and dilutive common share equivalents outstanding during the period. The weighted average number of shares used in the computation of both basic and fully diluted earnings per share may be the same due to the anti-dilutive effect of securities.

Cash and cash equivalents

Cash and cash equivalents consist of cash on hand, balances with banks and highly liquid investments that are readily convertible to cash with less than three months to maturity at the date of acquisition.

Inventories

Inventories are valued at the lower of cost, determined on a moving average cost basis, and market, being net realizable value. Vendor rebates are recorded as a reduction in the price of the vendor's products and corresponding inventory is recorded net of vendor rebates.

Prepaid expenses

Prepaid expenses include pre-opening store costs, license fees and maintenance contracts. All costs associated with the opening of new stores, with the exception of rent, are deferred and amortized over the respective store's first 12 months of operations. Other costs are amortized over the term of the contract.

Capital assets

Capital assets are recorded at cost and amortized over their estimated useful lives on a straight-line basis. The amortization periods are as follows:

Furniture, fixtures and equipment	5 – 10 years
Computer equipment and development costs	3 – 5 years
Leasehold improvements	over the term of the lease to a maximum of 10 years
Equipment under capital lease	3 – 5 years

Long-lived assets are reviewed for impairment when events or changes in circumstances indicate that their carrying value exceeds the sum of the undiscounted cash flows expected from their use and eventual disposition. The evaluation is performed for the lowest level of a group of assets and liabilities. An impairment loss, if required, is measured as the excess of the carrying value of the asset over its fair value.

Leased premises

The Company conducts a substantial part of its business from leased premises. Leasehold improvements are amortized over the lesser of their economic life or the "lease term", representing the initial lease term and including renewal periods only where renewal has been determined to be reasonably assured.

Leasehold improvements are reviewed for impairment and impairment losses are measured, as described above under capital assets policy. The Company also uses this lease term to evaluate whether its leases are operating or capital leases. As at March 29, 2008 and March 31, 2007, all of the Company's leases on premises were accounted for as operating leases.

Inducements received from landlords, including leasehold improvement allowances, are amortized over the lease term.

Goodwill

Goodwill represents the excess of the cost over the value assigned to the net identifiable assets acquired at the date of acquisition. Goodwill is not amortized but is subject to review for impairment at the reporting unit level on an annual basis and at any other time if events occur or circumstance changes that suggest goodwill could be impaired. Fair value is determined using the discounted cash flow method.

Deferred financing fees

Financing fees are deferred on a straight-line basis, which approximates the effective yield method, and are amortized over the term of the respective indebtedness.

Stock-based compensation

The fair value of each stock option granted is estimated on the date of the grant using the Black-Scholes option pricing model and expensed over the option's vesting period. Any consideration paid by employees on exercise of stock options is credited to share capital, with a corresponding reduction to contributed surplus.

Foreign currency translation

Transactions in foreign currencies are translated at rates of exchange at the time of the transaction. Monetary assets and liabilities denominated in a foreign currency are translated at foreign exchange rates in effect at the consolidated balance sheet dates with the resultant gains or losses included in net earnings for the period.

3. ACCOUNTING CHANGES

Financial Instruments, Comprehensive Income, and Hedges

The Canadian Institute of Chartered Accountants ("CICA") issued new standards relating to financial instruments: Financial Instruments – Recognition and Measurement; Financial Instruments – Disclosure and Presentation; Comprehensive Income; and Hedges. These new standards were adopted by the Company as of April 1, 2007.

Financial Instruments

Section 3855 of the CICA Handbook, "Financial Instruments – Recognition and Measurement", describes the standards for recognizing and measuring financial assets, financial liabilities and derivatives. The new standard requires the Company to revalue certain of its financial assets and liabilities, including derivatives designated in qualifying hedging relationships and embedded derivatives in certain contracts, at fair value on the initial date of implementation and at each subsequent financial reporting date.

This standard also requires the Company to classify financial assets and liabilities according to their characteristics and management's intentions for the purposes of ongoing measurement. Classification for financial assets include:

a) held for trading – measured at fair value with changes in fair value recorded in net earnings;
b) held to maturity – recorded at amortized cost using the effective interest rate method, with gains and losses recognized in net earnings in the period that the asset is de-recognized or impaired;
c) available for sale – measured at fair value with changes in fair value recognized in other comprehensive income for the current period until realized through de-recognition or impairment; and
d) loans and receivables – recorded at amortized cost using the effective interest rate method, with gains and losses recognized in net earnings in the period that the asset is de-recognized or impaired.

Classification for financial liabilities include:

a) held for trading – measured at fair value with changes in fair value recorded in net earnings; and
b) other – measured at amortized cost using the effective interest rate method, with gains and losses recognized in net earnings in the period that the liability is de-recognized.

In accordance with the new standards, the Company's financial assets and liabilities are generally classified and measured as follows:

Asset/Liability	Category	Measurement
Cash and cash equivalents	Held for trading	Fair value
Accounts receivable	Loans and receivables	Amortized cost
Bank indebtedness	Other liabilities	Amortized cost
Accounts payable	Other liabilities	Amortized cost
Other accrued liabilities	Other liabilities	Amortized cost
Long-term debt	Other liabilities	Amortized cost

Other balance sheet accounts, such as inventories, prepaid expenses, future income taxes, capital assets, goodwill, deferred financing charges and deferred revenue are not within the scope of the new accounting standards as they are not financial instruments.

Embedded derivatives are required to be separated and measured at fair values if certain criteria are met. Management reviewed all material contracts and determined that the Company does not currently have any significant embedded derivatives that require separate accounting and disclosure.

Comprehensive Income

Section 1530 of the CICA Handbook, "Comprehensive Income", establishes standards for reporting and display of comprehensive income and defines other comprehensive income to include revenues, expenses, gains and losses that, in accordance with primary sources of Canadian GAAP, are recognized in comprehensive income, but excluded from net earnings. The Company has chosen to report a new financial statement entitled "Consolidated Statements of Comprehensive Earnings" for changes in the fair value of certain of these financial assets and liabilities (i.e., the effective portion of changes in the fair value of a derivative designated in a cash flow hedging relationship). Any "accumulated other comprehensive income" (i.e., the portion of comprehensive income not already included in net earnings) will be presented as a separate line item in shareholders' equity.

Hedges

Section 3865 of the CICA Handbook, "Hedges", describes when and how hedge accounting may be applied. It replaces Accounting Guideline 13, "Hedging Relationships", which was adopted by the Company in April 2004. The Company has used derivative financial instruments to manage the risks of its foreign currency and interest rate exposures. The Company has entered into foreign currency option contracts to hedge future purchases of US dollar denominated goods and services. The fair value of these contracts is included in derivative liabilities. The changes in fair value of these contracts are included in other comprehensive income/loss to the extent the hedges continue to be effective. When the inventory is sold, the corresponding gain or loss deferred in accumulated other comprehensive income/loss is re-classified to cost of sales, operations, selling and administration. To the extent the change in fair value of the derivative is not completely offset by the change in fair value of the hedged item, the ineffective portion of the hedging relationship is recorded immediately in net earnings.

Gift Cards

Effective in the third quarter of fiscal 2007, the Company changed its accounting policy relating to gift cards with no impact on prior period results. This policy change was made based on the Company's review of the gift card accounting clarifications provided by the Securities and Exchange Commission ("SEC") and the introduction of legislation by the Ontario government banning gift card expiry dates and excessive service charges. The Company sells gift cards to its customers and recognizes the revenue as the gift cards are redeemed. The Company also recognizes revenue from unredeemed gift cards (gift card breakage) if the likelihood of the gift card being redeemed by the customer is considered to be remote. The Company determines its average gift card breakage rate based on historical redemption rates. Once the breakage rate is determined, the resulting revenue is recognized over the estimated period of redemption, commencing when the gift cards are sold, based on historical redemption patterns. There was no material impact to the Company's net earnings and net earnings per share in prior periods as a result of this change in accounting policy.

The Company recorded $2.9 million in gift card breakage in fiscal 2008, and $1.2 million in gift card breakage in fiscal 2007. As at March 29, 2008, the provision for unredeemed gift card liability is $32.7 million and is included in accounts payable and accrued liabilities (March 31, 2007 – $27.3 million).

New Accounting Pronouncements

Financial Instruments

Section 3862 and Section 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 have to be adopted by the Company for the fiscal year beginning March 30, 2008. The Company is currently evaluating the impact of this new standard and it will result in additional disclosures.

Capital Disclosures

Section 1535 of the CICA Handbook, Capital Disclosures, specifies the disclosure of: (i) the Company's objectives, policies and processes 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 non-compliance. This standard is effective for the Company's fiscal year beginning March 30, 2008.

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 must be adopted by the Company for the fiscal year beginning March 30, 2008. The Company is currently assessing the impact of this new standard on its consolidated financial statements.

General Standards of Financial Statement Presentation

The CICA amended Handbook Section 1400 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 must be adopted by the Company for the fiscal year beginning March 30, 2008. The Company is currently assessing the impact of this new standard on its consolidated financial statements.

Goodwill and Intangible Assets

Section 3064 of the CICA Handbook, “Goodwill and Intangible Assets”, replaces the existing Section 3062 “Goodwill and Other Intangible Assets” and Section 3450 “Research and Development Costs”. In conjunction with the issuance of this new standard, the CICA has amended Section 1000 “Financial Statement Concepts”. These changes clarify the criteria for asset recognition for an internally developed intangible asset and reinforce the distinction between costs that should be expensed and those that should be capitalized. These standards have been created to harmonize with the International Financial Reporting Standards and they have to be adopted by the Company for the fiscal year beginning March 29, 2009. The Company is currently assessing the impact of this new standard on its 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 is currently working on a conversion plan towards IFRS but it is too early to assess the financial impact of the conversion at this point.

4. CAPITAL ASSETS

Capital assets consist of the following:

	March 29, 2008		March 31, 2007	
(thousands of dollars)	Cost	Accumulated amortization	Cost	Accumulated amortization
Furniture, fixtures and equipment	114,658	89,959	111,204	82,537
Computer equipment and development costs	94,012	76,130	85,265	65,684
Leasehold improvements	89,674	71,410	84,667	64,034
Equipment under capital lease	12,885	6,382	12,086	4,781
	311,229	243,881	293,222	217,036
Less accumulated amortization	243,881		217,036	
Net book value	67,348		76,186	

The depreciation expense associated with capital leases was $2.9 million (2007 – $3.5 million).

5. INCOME TAXES

Future income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of the Company's future tax assets and liabilities are as follows:

(thousands of dollars)	March 29, 2008	March 31, 2007
Current future tax assets		
Reserves and allowances	6,745	9,205
Net current future tax assets	6,745	9,205

(thousands of dollars)	March 29, 2008	March 31, 2007
Non-current future tax assets		
Tax loss carryforwards	8,332	12,354
Share issue costs	–	32
Book amortization in excess of cumulative eligible capital deduction	416	462
Book amortization in excess of capital cost allowance	34,502	46,457
Non-current future tax assets before valuation allowance	43,250	59,305
Valuation allowance	–	(27,270)
Net non-current future tax assets	43,250	32,035

Significant components of income tax recovery attributable to continuing operations are as follows:

(thousands of dollars)	52-week period ended March 29, 2008	52-week period ended March 31, 2007
Current income tax recovery	–	(90)
Future income tax expense relating to origination and reversal of temporary differences	11,282	(8,340)
Decrease in valuation allowance	(27,270)	(29,918)
Future income tax expense relating to utilization of loss carryforwards	4,440	19,317
Future income tax expense relating to utilization of tax losses acquired	–	12,476
Other, net	(114)	244
Adjustment to future income tax assets resulting from reduction in substantively enacted tax rates	2,907	6,221
Total income tax recovery	(8,755)	(90)

The reconciliation of income taxes attributable to continuing operations computed at the statutory income tax rates to income tax recovery is as follows:

(thousands of dollars)	52-week period ended March 29, 2008	52-week period ended March 31, 2007
Tax at combined federal and provincial tax rates (2008: 34.45%, 2007: 35.25%)	15,176	10,576
Tax effect of expenses not deductible for income tax purposes	546	401
Decrease in valuation allowance	(27,270)	(29,918)
Tax effect of utilization of tax losses acquired	–	12,476
Large Corporations Tax	–	(90)
Adjustment to future income tax assets resulting from reduction in substantively enacted tax rates	2,907	6,221
Other, net	(114)	244
	(8,755)	(90)

As at March 29, 2008, the Company has combined non-capital loss carryforwards of approximately $25.7 million for income tax purposes that expire as follows if not utilized:

(thousands of dollars)	
2009	16,628
2010	2,737
2014	5,289
2015	1,018
	25,672

6. GOODWILL

The Company performed its annual impairment test on March 29, 2008 and March 31, 2007 using the discounted cash flow method. The results of this test indicated there was no goodwill impairment.

As part of the purchase price allocation for the acquisition of Indigo Books & Music, Inc. ("Old Indigo"), no future tax asset was recognized for the unused tax losses of Old Indigo that existed at the date of acquisition. When unused tax losses acquired in a business combination that are not recognized as a future tax asset by the acquirer at the date of the acquisition are subsequently recognized by the acquirer, the benefit is applied to reduce any unamortized goodwill related to the acquisition. The Company utilized all acquired unused tax losses which were not recognized in fiscal years prior to 2008 and as such, goodwill remained unchanged for the period ended March 29, 2008. For the period ended March 31, 2007, the Company utilized a portion of the acquired unused tax losses which were not recognized and, accordingly, reduced goodwill by $12.5 million.

7. BANK INDEBTEDNESS AND LONG-TERM DEBT

On April 11, 2007, the Company renegotiated its credit agreement with its bank. The credit agreement in place as of the current fiscal year end provides for a revolving line of credit of up to $60.0 million, based on defined levels of inventories and accounts receivable, bearing interest, at the Company's option, at either the bank's prime rate or the bankers' acceptance rate plus 0.00% to 1.50% depending on certain financial ratios. As at March 29, 2008, no funds were drawn against this facility. At March 29, 2008, the Company's interest rate would be the bankers' acceptance rate plus 1.00% which would result in an effective interest rate of 4.58%. The revolving line of credit is to be repaid in full and expires on October 15, 2008.

As part of the refinancing, the Company repaid $13.0 million of long-term debt that was outstanding under the old agreement. The repayment was originally due in July 2007. 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 income in April 2007.

The revolving line of credit is collateralized by a first-ranking security over the Company's inventories, receivables and intellectual properties, and is dependent upon continued compliance with certain financial covenants. As at March 29, 2008, the Company was compliant with all its banking covenants.

The credit agreement that was in place for the Company as at the end of last fiscal year provided for the following:

(i) A revolving line of credit of up to $90.0 million, based on defined levels of inventories and accounts receivable, bearing interest, at the Company's option, at either the bank's prime rate or the bankers' acceptance rate plus 0.50% to 2.50% depending on certain financial ratios. At March 31, 2007, the Company's interest rate was the bankers' acceptance rate plus 1.50% which resulted in an effective interest rate of 5.81%. The Company has an annual clean down provision on this revolving line of credit. The Company was required to reduce the amount outstanding under this facility to $25.0 million or less for a period of 30 consecutive days in fiscal 2005, and to nil in subsequent years. The revolving line of credit was to be repaid in full and expired on July 31, 2007. As at March 31, 2007, no funds were drawn against this facility.

(ii) A long-term debt facility of $49.0 million bearing interest at the same rates as the revolving line of credit, to be repaid as follows: payments of $12.0 million on each of December 31, 2004, December 31, 2005, December 31, 2006, and $13.0 million on July 31, 2007.

The revolving line of credit and long-term debt were collateralized by a first-ranking security over all the property and assets of the Company, and were dependent upon continued compliance with certain financial covenants. As at March 31, 2007, the Company was compliant with all its banking covenants.

On April 2, 2004, the Company entered into an interest rate derivative agreement to fix the interest rate on its long-term debt. The agreement involved the exchange of 30-day bankers' acceptance floating interest rates for fixed interest rates on a notional amount of $49.0 million. There were reductions in the notional amounts of the derivative agreement that coincided with the principal repayments of the underlying long-term debt. The fixed interest rate on the notional amount was 3.06%. The agreement expired on July 31, 2007, but was terminated in April 2007 as part of the debt refinancing, as noted above.

The Company has entered into capital lease agreements for certain equipment. The obligation under these capital leases is $6.0 million, of which $2.6 million is included in the current portion of long-term debt. These capital leases have an average interest rate of 5.2% and an average term of 51 months.

As at March 29, 2008, the Company had outstanding letters of credit totalling $0.3 million (March 31, 2007 – $0.4 million).

8. SHARE CAPITAL

Share capital consists of the following:

Authorized

Unlimited Class A preference shares with no par value, voting, convertible into common shares on a one-for-one basis at the option of the shareholder

Unlimited common shares, voting

	52-week period ended March 29, 2008		52-week period ended March 31, 2007	
	Number of shares	Amount $ (thousands)	Number of shares	Amount $ (thousands)
Balance, beginning of period	**24,647,554**	**197,592**	24,225,918	194,861
Issued during the period				
Directors' deferred stock units converted	**14,964**	**85**	–	–
Options exercised	**180,629**	**1,261**	421,636	2,731
Balance, end of period	**24,843,147**	**198,938**	24,647,554	197,592

During fiscal 2008, the Company issued 14,964 shares in exchange for directors' deferred stock units when a Board member retired.

In calculating diluted earnings per share amounts under the treasury stock method, the numerator remains unchanged from the basic earnings per share calculations as the assumed exercise of the Company's stock options and the conversion of the deferred stock units do not result in an adjustment to earnings.

The reconciliation of the denominator in calculating diluted earnings per share amounts is as follows:

(in thousands)	52-week period ended March 29, 2008	52-week period ended March 31, 2007
Weighted average number of common shares outstanding, basic	**24,744**	24,359
Effect of dilutive securities		
– Stock options	**513**	641
– Deferred stock units	**138**	130
Weighted average number of common shares outstanding, diluted	**25,395**	25,130

The Company has established an employee stock option plan (the "Plan") for key employees. The number of common shares reserved for issuance under the Plan is 2,234,315. One quarter of the options granted prior to May 21, 2002 were exercisable on the date of issue with the remainder exercisable in equal installments on the anniversary date for the next three years. Most options granted since May 21, 2002 have one fifth of the options granted exercisable one year after the date of issue with the remainder exercisable in equal installments on the anniversary date over the next four years. A small number of options have special vesting schedules that were approved by the Board.

The fair value of stock options that were granted in fiscal 2008 was $2.7 million (2007 – $0.4 million), and $0.8 million (2007 – $0.5 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. In fiscal 2008, $0.2 million (2007 – $0.4 million) was transferred from contributed surplus as a result of stock options exercised.

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:

	52-week period ended March 29, 2008	52-week period ended March 31, 2007
Risk-free interest rate	4.2%	4.2%
Expected volatility	21.3%	32.5%
Expected time until exercise	4 years	4 years
Expected dividend yield	0.0%	0.0%

Effective March 30, 2003, the Company elected to adopt the new recommendations issued by the CICA relating to stock-based compensation on a prospective basis. In accordance with the new standard, the Company changed its method of accounting for stock options from the intrinsic value method to the fair value method, which estimates the fair value of the stock options granted on the date of grant and expenses this value over the vesting period. 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 earnings would have decreased to the amounts listed below. The pro forma impact of accounting for these options at fair value will continue to be disclosed until the last of these options vest in 2008.

Pro Forma Earnings (thousands of dollars, except per share data)	52-week period ended March 29, 2008	52-week period ended March 31, 2007
Net earnings – reported	52,808	30,004
Net earnings – pro forma	52,479	29,675
Basic net earnings per common share – reported	$2.13	$1.23
Basic net earnings per common share – pro forma	$2.12	$1.22
Diluted net earnings per common share – reported	$2.08	$1.19
Diluted net earnings per common share – pro forma	$2.07	$1.18

A summary of the status of the Plan and changes during both periods is presented below:

	March 29, 2008		March 31, 2007	
	Number #	Weighted average exercise price $	Number #	Weighted average exercise price $
Outstanding options, beginning of period	1,258,046	7.71	1,798,888	6.92
Granted	690,000	16.05	85,000	14.29
Forfeited	(118,038)	7.89	(204,206)	8.20
Exercised	(180,629)	5.90	(421,636)	5.46
Outstanding options, end of period	1,649,379	11.38	1,258,046	7.71
Options exercisable, end of period	549,702	7.59	570,732	7.11

Options outstanding and exercisable

	March 29, 2008				
	Outstanding			Exercisable	
Range of exercise prices $	Number #	Weighted average exercise price $	Weighted average remaining contractual life (in years)	Number #	Weighted average exercise price $
4.00 – 5.99	435,700	4.92	5.9	313,400	4.87
6.00 – 9.99	320,492	7.68	6.6	161,115	7.42
10.00 – 27.99	878,153	15.35	9.1	60,153	12.52
28.00 – 33.99	6,730	32.70	1.5	6,730	32.70
34.00 – 64.00	8,304	57.01	3.4	8,304	57.01
4.00 – 64.00	1,649,379	11.38	7.7	549,702	7.59

On October 31, 2002, the Company established a Directors' Deferred Stock Unit Plan. Under this plan, directors will receive their annual retainer fees and other Board-related compensation in the form of deferred stock units ("DSUs"). The number of shares reserved for issuance under this plan is 250,000. The Company issued 23,062 DSUs with a value of $0.3 million during the period ended March 29, 2008 (2007 – $0.3 million). The fair value of the outstanding DSUs as at March 29, 2008 was $1.4 million and was recorded in contributed surplus.

9. RESTRUCTURING COSTS

In fiscal 2002, the Company recorded a $40.3 million restructuring charge as a result of the merger between Chapters Inc. and Old Indigo. As of the end of fiscal 2005, the Company had approximately $6.5 million of restructuring costs that were unpaid and had been included in accounts payable and accrued liabilities. This provision of $6.5 million included estimates for rent subsidies, legal fees, commissions and disposal costs for stores that were identified for closures at that time.

In the fourth quarter of fiscal 2007, the Company recognized $0.3 million into income for the recovery of construction costs from a subtenant, which was initially expensed through the restructuring provision. As at March 29, 2008, the Company had approximately $0.2 million (2007 – $0.3 million) of restructuring costs that were unpaid and included in accounts payable and accrued liabilities. The current provision includes only rent subsidies for these properties (net of a reserve against the sublet income) until the end of each property's lease term.

10. CAPITAL ASSETS WRITE-OFF

In fiscal 2006, the Company began work on two projects, a new online order management system and a new product database system. The Company decided to discontinue the implementation of the online order management system in the third quarter of fiscal 2007 and wrote-off $1.6 million in assets associated with this project. In the fourth quarter of fiscal 2007, the Company wrote-off an additional $0.8 million in assets associated with the product database system project. Both write-offs were due to unplanned scope and cost increases. There were no capital assets written off in fiscal 2008.

11. JOINT VENTURE

The Company participates in a joint venture through a 50% equity ownership in the Calendar Club of Canada Limited Partnership to sell calendars, games and gifts through seasonal kiosks and year-round stores.

The following amounts represent the total assets, liabilities, revenues and expenses and cash flows of the Company's joint venture in which the Company participates and its proportionate share therein:

	Total		Proportionate share	
(thousands of dollars)	2008	2007	2008	2007
Current assets	4,255	5,070	2,128	2,535
Long-term assets	2,157	2,210	1,079	1,105
Current liabilities	3,209	4,210	1,605	2,105
Revenue	32,158	34,582	16,079	17,291
Expenses	29,889	30,147	14,945	15,073
Net earnings	2,269	4,435	1,134	2,218
Cash flows provided by (used in)				
Operating activities	2,689	7,520	1,346	3,760
Investing activities	(621)	(868)	(311)	(434)
Financing activities	(2,136)	(4,637)	(1,068)	(2,319)
Net cash flow	(68)	2,015	(33)	1,007

12. CONSOLIDATED STATEMENTS OF CASH FLOWS

Supplemental cash flow information:

(thousands of dollars)	52-week period ended March 29, 2008	52-week period ended March 31, 2007
Interest paid	642	2,909
Income taxes paid (recovered)	(173)	199
Assets acquired under capital lease	2,091	3,509

13. COMMITMENTS AND CONTINGENCIES

(a) Commitments

As at March 29, 2008, the Company had the following commitments:

(i) *Operating lease obligations*

The Company had operating lease commitments in respect of its stores, support office premises and certain equipment. The leases expire at various dates between 2008 and 2019 and are subject to renewal options in certain cases. Annual store rent consists of a base amount plus additional payments based on store sales.

(ii) *Capital lease obligations*

The Company entered into capital lease agreements for certain equipment. The obligations under these capital leases is $6.0 million, of which $2.6 million is included in the current portion of long-term debt.

The Company's contractual obligations due over the next five fiscal years and thereafter are summarized below:

(millions of dollars)	Operating leases	Capital leases	Total
2009	58.3	2.6	60.9
2010	52.0	2.3	54.3
2011	43.4	0.9	44.3
2012	37.7	0.1	37.8
2013	28.1	0.1	28.2
Thereafter	47.5	–	47.5
Total obligations	267.0	6.0	273.0

(b) Legal claims

In the normal course of business, the Company becomes involved in various claims and litigation. While the final outcome of such claims and litigation pending as at March 29, 2008 cannot be predicted with certainty, management believes that any such amount would not have a material impact on the Company's financial position.

14. ACCUMULATED OTHER COMPREHENSIVE INCOME

Changes in accumulated other comprehensive income during fiscal 2008 are presented as follows:

(thousands of dollars)	52-week period ended March 29, 2008
Adjusted opening balance due to adoption of new accounting policies – financial instruments	144
Other comprehensive loss for the period	(144)
Balance, end of period	–

15. FINANCIAL INSTRUMENTS

The following methods and assumptions were used to estimate the fair value of each type of financial instrument by reference to various market value data and other valuation techniques, as appropriate:

(i) The fair values of cash and cash equivalents, accounts receivable, bank indebtedness and accounts payable and accrued liabilities approximate their carrying values given their short maturities.

(ii) The fair values of long-term debt are estimated based on the discounted cash payments of the debt at the Company's estimated incremental borrowing rates for debt of the same remaining maturities. The fair value of the long-term debt approximates its carrying value.

16. SUBSEQUENT EVENT

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 will be limited to 2,905 common shares, other than block purchase exceptions. All common shares purchased under the NCIB will be cancelled and returned to treasury.

17. 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.

Corporate Governance Policies

A presentation of Indigo's corporate governance policies is included in the Management Information Circular which is mailed to all shareholders. If you would like to receive a copy of this information, please contact Investor Relations at Indigo.

Executive Management and Board of Directors

EXECUTIVE MANAGEMENT

Heather Reisman
Chair & Chief Executive Officer

Kathleen Flynn
General Counsel & Secretary

Joyce Gray
Executive Vice President, Retail & Customer Experience

Deirdre Horgan
Chief Marketing Officer

Ross Marancos
Senior Vice President, Supply Chain

Jim McGill
Chief Financial Officer

Michael Serbinis
Chief Information Officer

Joel Silver
Chief Merchant

Tova White
Senior Vice President, Human Resources & Organizational Development

BOARD OF DIRECTORS

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K. Adams & Associates Limited

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Chairman
Navantis Inc.

Jonathan Deitcher
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RBC Investments

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Serendipity Point Films

Bruce Mau
Chairman & Creative Director
Bruce Mau Design

Heather Reisman
Chair & Chief Executive Officer
Indigo Books & Music Inc.

Gerald Schwartz
Chairman, President & CEO
Onex Corporation

Five Year Summary of Financial Information

For the years ended (millions of dollars, except per share data)	March 29, 2008	March 31, 2007	April 1, 2006	April 2, 2005	April 3, 2004
SELECTED INCOME STATEMENT INFORMATION					
Revenues					
Superstores	620.0	591.0	573.5	532.5	548.2
Small format stores	159.7	157.1	160.9	154.9	169.4
Online	101.4	86.7	79.5	64.8	52.1
Other	41.8	40.2	37.9	37.0	38.3
Total Revenues	922.9	875.0	851.8	789.2	808.0
EBITDA[1]	73.9	65.7	56.6	44.2	45.2
Restructuring and take-over costs (recovery)	–	(0.3)	(2.1)	(0.9)	–
EBIT	44.1	32.7	29.6	18.1	20.8
Net earnings per common share	$2.13	$1.23	$1.05	$0.49	$0.21
SELECTED BALANCE SHEET INFORMATION					
Working capital	76.6	28.8	0.7	(20.6)	(30.7)
Total assets	421.0	397.3	390.7	392.4	399.7
Long-term debt (including current portion)	6.0	20.5	31.8	39.3	51.4
Shareholders' equity	203.8	148.8	115.7	88.9	76.3
Long-term debt/(long-term debt + shareholders' equity)	0.03:1	0.12:1	0.22:1	0.31:1	0.40:1
Weighted average number of shares outstanding	24,744,334	24,359,451	24,133,726	24,067,426	23,964,752
Common shares outstanding at end of period	24,843,147	24,647,554	24,255,918	24,081,352	23,964,752
STORE OPERATING STATISTICS					
Number of stores at end of period					
Superstores	86	88	86	86	87
Small format stores	158	158	164	166	167
Campus bookstores	–	–	–	–	5
Selling square footage at end of period (in thousands)					
Superstores	2,042	2,090	2,058	2,086	2,105
Small format stores	422	425	441	448	451
Campus bookstores	–	–	–	–	10
Comparable store sales					
Superstores	4.4%	2.5%	10.2%	(0.5%)	2.7%
Small format stores	3.0%	2.2%	4.3%	(2.3%)	(0.1%)
Sales per selling square foot					
Superstores	304	283	279	255	260
Small format stores	378	370	365	346	376

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

Investor Information

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STOCK LISTING

Toronto Stock Exchange

TRADING SYMBOL

IDG

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ANNUAL MEETING

The Annual Meeting represents an opportunity for shareholders to review and participate in the management of the Company as well as meet with its directors and officers.

Indigo's Annual Meeting will be held on June 25, 2008 at 10:00 a.m. at The MaRS Centre, South Tower, 101 College Street, Suite 100, Toronto, Ontario, Canada.

Shareholders are encouraged to attend and guests are welcome.

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Our Values

- We exist to add joy to customers' lives. We anticipate their needs and exceed their expectations.
- Excellence matters in everything we do.
- Success is only attainable through outstanding people working together in an open environment that promotes knowledge and growth.
- Books, reading, and storytelling are an integral part of advancing society.
- Innovation is the key to growth and can come from anyone, anytime.
- We have a responsibility to give back to the communities in which we operate.

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