

THE KEG ROYALTIES INCOME FUND

FIRST QUARTER REPORT

For the three months ended March 31, 2004

TO OUR UNITHOLDERS

On behalf of the Board of Trustees, I am pleased to present the results of The Keg Royalties Income Fund (the "Fund") for the three months ended March 31, 2004. The Fund's earnings and cash flows have continued to generate distributions to unitholders in the expected amount of 9 cents per unit per month, or \$1.08 per unit on an annual basis.

RESULTS

The Keg has once again reached a new sales record for the first quarter. Total system sales for The Keg for the 13 week period ended April 4, 2004 were \$79,831,000, an increase of \$2,743,000 or 3.6% over the comparable quarter of the prior year. While actual restaurant traffic remained consistent with the prior year, same store sales declined primarily due to the unfavourable impact of the U.S. dollar exchange rate when translating the sales of the U.S. Keg restaurants into Canadian dollars for Fund reporting purposes. There was also an unfavourable impact on comparable sales attributable to the fact that The Keg's New Years Eve sales did not fall into the first quarter of the Fund's 2004 year.

OUTLOOK

Following challenging back-to-back years in 2002 and 2003, the foodservice industry appears to be resuming the growth it has typically enjoyed over the past twenty-five years. The perfect storm of one-time events that plagued the industry in 2003 in particular would appear to have been just that – a series of one-time events.

We feel that The Keg's strategies through the past two difficult years will yield positive sales results through the balance of 2004. Overall growth continues at The Keg. Keg management remains committed to maintaining and improving the legendary high standards that have come to define the brand. Most importantly, The Keg continues to deliver consistently great overall experiences and as a result continues to enjoy the loyalty of its guests.

Sincerely,



C.C. Woodward
Chairman, The Keg Royalties Income Fund
on behalf of the Board of Trustees

May 17, 2004

FINANCIAL HIGHLIGHTS

(\$000's except per unit amounts)	Jan. 1 to Mar. 31, 2004	Jan. 1 to Mar. 31, 2003
Restaurants in the Royalty Pool	86	81
Gross sales reported by Keg restaurants in the Royalty Pool	\$ <u>75,891</u>	<u>73,476</u>
Royalty income	\$ 3,036	2,939
Interest income	<u>1,064</u>	<u>1,055</u>
Total income	4,100	3,994
Expenses	(281)	(301)
Non-controlling interest ⁽¹⁾	<u>(1,562)</u>	<u>(1,405)</u>
Earnings for the period	\$ <u>2,257</u>	<u>2,288</u>
Basic and diluted earnings per Fund unit	\$ <u>.28</u>	<u>.28</u>
Distributable cash per Fund unit ⁽²⁾	\$ <u>.28</u>	<u>.28</u>
Distributions declared per Fund unit	\$ <u>.27</u>	<u>.27</u>

Notes:

⁽¹⁾ Represents the effective interest of KRL in the earnings of the Fund.

⁽²⁾ Distributable cash is not an earnings measure recognized by generally accepted accounting principles ("GAAP") and therefore may not be comparable to similar measures presented by other issuers. Distributable cash per Fund unit is computed on a basis consistent with that described by GAAP for computing earnings per Fund unit.

MANAGEMENT DISCUSSION AND ANALYSIS

OVERVIEW

On May 31, 2002, The Keg Royalties Income Fund (the "Fund"), through its subsidiary The Keg Rights Limited Partnership (the "Partnership"), purchased the Keg trademarks and related property (collectively, the "Keg Rights") from Keg Restaurants Ltd. ("KRL"). The Partnership, in turn, granted KRL an exclusive licence to use the Keg Rights for a term of 99 years pursuant to a licence and royalty agreement. This agreement obligates KRL to make a monthly royalty payment equal to 4% of the gross sales of Keg restaurants in Canada and the United States.

The Fund's operating expenses are limited to administration expenses, interest on long-term debt and amortization of deferred financing fees.

KRL effectively owns 17.58% of the units of the Fund on a fully diluted basis through its ownership of Partnership units and has the obligation to pay monthly royalties to the Fund.

SYSTEM SALES

While the Fund's income is based on a royalty of 4% of sales of Keg restaurants in the Royalty Pool, the total system sales of The Keg chain are of interest to the Fund and its unitholders as the total system sales best reflect the chain's overall performance. The following table sets out The Keg's total system sales for the periods indicated below:

(\$000's)	13 weeks ended	
	April 4, 2004	March 30, 2003
Corporate Keg restaurants	\$ 44,902	\$ 43,387
Franchised Keg restaurants ⁽¹⁾	<u>34,929</u>	<u>33,701</u>
Total system sales	<u>\$ 79,831</u>	<u>\$ 77,088</u>

⁽¹⁾ The amount of system sales for the franchised Keg restaurants is the amount of gross sales reported to KRL by franchised Keg restaurants without independent audit and includes the gross sales of a joint venture restaurant located in Coquitlam, British Columbia.

Total system sales for the 13 weeks ended April 4, 2004 were \$79.8 million compared to \$77.1 million for the 13 weeks ended March 30, 2003, an increase of \$2.7 million or 3.6%. During the 13 weeks ended April 4, 2004, no new restaurants were opened and no restaurants were closed. During the comparable period of the prior year no new restaurants were opened and no restaurants were closed. As at April 4, 2004, there were a total of 88 Keg restaurants as compared with the 84 restaurants at March 30, 2003.

The Keg's same store sales (sales of restaurants that operated during the entire 13 week period of both the current year and the prior year) decreased by 1.2% in Canada and 1.3% in the United States. This decrease is due primarily to the inclusion of the sales from New Years Eve (one of the busiest nights of the year for full service restaurants) in the results of KRL's first quarter in the current year whereas in the prior year they were included in KRL's second quarter. After translating the sales of the U.S. restaurants into their Canadian dollar equivalent, consolidated same store sales for the comparable quarter decreased by 4.1%. This decrease is a function of the fluctuation in the U.S. dollar exchange rate rather than an indication of a slowdown in actual restaurant traffic. The average exchange rate moved from 1.52 for KRL's second quarter in fiscal 2003 to 1.32 for KRL's second quarter in fiscal 2004, significantly reducing the Canadian dollar equivalent of the U.S. restaurant sales.

THE ROYALTY POOL

Annually, on January 1st, the pool of Keg restaurants on which KRL pays a royalty (the “Royalty Pool”) to the Partnership is adjusted to include the gross sales from new Keg restaurants that have opened on or before October 2nd of the prior year, less gross sales from any Keg restaurants that have permanently closed during the year. In return for adding these net sales to the Royalty Pool, KRL receives the right to indirectly acquire additional Fund units (the “Additional Entitlement”). The Additional Entitlement is determined based on 92.5% of the royalty revenue added to the Royalty Pool, divided by the yield of the Fund units. KRL receives 80% of the estimated Additional Entitlement initially, with the balance received on December 31st each year when the actual full year performance of the new restaurants is known with certainty.

On January 1, 2003, three new Keg restaurants that opened during the period from April 1, 2002 through October 2, 2002 were added to the Royalty Pool. The actual gross sales of these three new restaurants were \$13.2 million for the 52 weeks ended September 28, 2003. Two permanently closed Keg restaurants with annual sales of \$3.8 million were removed from the Royalty Pool. This resulted in KRL receiving an Additional Entitlement equivalent to 310,815 Fund units effective as of January 1, 2003. The total number of restaurants in the Royalty Pool increased to 81. The yield of the Fund units was determined to be 11.25% calculated using a weighted average unit price of \$9.60.

On January 1, 2004, seven new Keg restaurants that opened during the period from October 3, 2002 through October 2, 2003 were added to the Royalty Pool. The gross sales of these seven new restaurants have been estimated at \$25.2 million annually. Two permanently closed Keg restaurants with annual sales of \$4.6 million have been removed from the Royalty Pool, resulting in an estimated net increase in Royalty Pool sales of \$20.6 million annually. The total number of restaurants in the Royalty Pool has increased to 86. The yield of the Fund units was determined to be 11.66% calculated using a weighted average unit price of \$9.26. As a result of the contribution of the additional net sales to the Royalty Pool, and assuming 100% of the estimated Additional Entitlement is received, KRL’s Additional Entitlement will be equivalent to 653,193 Fund units, being 6.52% of the Fund units on a fully diluted basis. On January 1, 2004, KRL received 80% of this entitlement representing the equivalent of 522,554 Fund units, being 5.28% of the Fund units on a fully diluted basis. KRL will also receive a proportionate increase in monthly distributions from the Partnership. The balance of the Additional Entitlement will be adjusted to be effective January 1, 2004 once the actual performance of the new restaurants have been confirmed. Including the initial portion of Additional Entitlement described above. KRL has the right to exchange its units in the capital of the Partnership for 1,739,314 Fund units, representing 17.58% of the Fund units on a fully diluted basis. If KRL were to receive 100% of the estimated Additional Entitlement for 2004, it would have the right to exchange its Partnership units for 1,869,952 Fund units, representing 18.66% of the Fund units on a fully diluted basis. All Fund units obtained by KRL in exchange for these Partnership units are subject to a contractual re-sale restriction, which expires on May 31, 2005.

OPERATING RESULTS

Gross sales reported by the restaurants in the Royalty Pool increased from \$73,476,000 to \$75,891,000 for the comparable quarter. The increase of \$2,415,000 or 3.3% reflects the net impact of the addition of five net new restaurants to the Royalty Pool at the beginning of the year and the same store sales declines discussed above.

Royalty income increased by \$97,000 from \$2,939,000 in the first quarter of 2003 to \$3,036,000 in the first quarter of 2004 as a result of the increase in gross sales for the reasons explained above.

Operating expenses for the quarter ended March 31, 2004 were \$281,000 and included general and administrative expenses of \$86,000, interest on the long-term debt in the amount of \$166,000 and amortization on the deferred financing charges of \$29,000. General and administrative expenses decreased by \$9,000 over the comparable quarter in 2003. Interest costs have decreased by \$11,000 in the quarter as a result of a decrease in the average interest rate on the Fund debt from 4.95% in the first quarter of 2003 to 4.60% in the first quarter of 2004.

The non-controlling interest expense, which represents KRL's effective interest in the earnings of the Fund, has increased from \$1,405,000 for the three months ended March 31, 2003 to \$1,562,000 for the three months ended March 31, 2004. This increase is due to KRL's increased effective ownership in the Fund from 12.99% to 17.58% as a result of the new store roll-in on January 1, 2004.

Net earnings decreased by \$31,000 from \$2,288,000 in the first quarter of 2003 to \$2,257,000 in the first quarter of 2004. Earnings per Fund unit were 27.7 cents compared to 28.1 cents for the comparable quarter in the prior year. Cash available for distribution during the quarter amounted to 28.1 cents per Fund unit versus the 28.4 cents per Fund unit available in the comparable quarter of the prior year. Distributions of 27 cents per Fund unit were declared in the first quarter of both 2004 and 2003. The difference between the Fund's earnings and distributable cash is due to non-cash items included in the Fund's operating expenses.

It is currently anticipated that the monthly distributions to unitholders will remain 9.0 cents per unit for the upcoming fiscal year, which equates to an annualized distribution of \$1.08 per unit.

OUTLOOK

According to the Long Term Forecast of the Canadian Restaurant and Foodservices Association, foodservice operators can look forward to a brighter 2004. Following an unprecedented two year decline in real foodservice sales, the forecast calls for sales in Canada's commercial foodservice industry to recover throughout 2004 and 2005 as tourism and global economies continue to improve. A return to real growth in the foodservice industry is predicted, with full service restaurants, the sector in which KRL operates, experiencing a particularly strong recovery.

KRL anticipates that it will record strong sales growth relative to the foodservice industry as a whole in the future, as it has historically. KRL remains committed to growth, both through expansion into new markets and same store sales increases. In addition to building new Kegs in both Canada and the U.S., KRL continues to refurbish, and in some cases relocate, existing Keg restaurants in order to better serve our guests and to protect and enhance the strong leadership position The Keg brand has enjoyed for over thirty years.

RISKS AND UNCERTAINTIES

The Fund continues to recognize certain risks and uncertainties associated with the ordinary course of business, including those associated with the business and operations of KRL, upon which the Fund relies solely for its income.

Management of KRL have advised the Trustees that it continues to monitor the situation regarding the two cases of BSE found in North America during 2003. The widespread testing of herds confirms these are isolated cases; the risk to human health appears to be negligible. Most importantly to the Keg, there has not been any significant negative consumer reaction to beef in North America and there has not been a material impact on its restaurant traffic. KRL management has further advised the Trustees that KRL has maintained an uninterrupted supply of quality beef that meets its demanding specifications despite the border closures and the unfortunate impact on cattle producers. Management of KRL expect the demand for beef to remain strong among consumers and its supply to continue uninterrupted.

FORWARD LOOKING INFORMATION

The information provided in this report includes forward-looking statements with respect to business plans, activities and events anticipated by the Fund and the Fund's future results. Although the Fund believes the assumptions underlying such statements to be reasonable, any of the assumptions may prove to be inaccurate and, as a result, the forward-looking information may prove to be incorrect. The forward-looking information contained in this document is current only as of the date of this document. There should not be an expectation that such information will in all circumstances be updated, supplemented or revised whether as a result of new information, changing circumstances, future events or otherwise.

UNITHOLDER INFORMATION

CORPORATE HEAD OFFICE

The Keg Royalties Income Fund
10100 Shellbridge Way
Richmond, BC V6X 2W7

BOARD OF TRUSTEES

C. C. Woodward
George Killy
George Tidball

BOARD OF DIRECTORS AND OFFICERS OF THE KEG GP LTD., THE GENERAL PARTNER OF THE KEG RIGHTS LIMITED PARTNERSHIP

C. C. Woodward*
Chairman and Director
David Aisenstat
President and Director
Neil Maclean
Secretary, Treasurer and Director
George Killy*
Director
George Tidball*
Director

* Audit Committee and Governance Committee Member

REGISTRAR AND TRANSFER AGENT

Computershare Trust Company of Canada

STOCK EXCHANGE LISTING

Toronto Stock Exchange: KEG.UN

INVESTOR ENQUIRIES

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THE KEG ROYALTIES INCOME FUND

CONSOLIDATED FINANCIAL STATEMENTS

For the three months ended March 31, 2004

CONSOLIDATED BALANCE SHEETS

(Expressed in thousands of dollars)

	March 31, <u>2004</u> (unaudited)	December 31, <u>2003</u> (audited)
ASSETS		
Current assets:		
Due from Keg Restaurants Ltd. (note 6)	\$ 1,607	\$ 1,633
Prepaid expenses and deposits	<u>24</u>	<u>35</u>
	1,631	1,668
Note receivable from Keg Restaurants Ltd.	57,000	57,000
Intangible assets (note 7)	117,174	113,547
Deferred financing charges	<u>134</u>	<u>163</u>
	<u>\$ 175,939</u>	<u>\$ 172,378</u>

LIABILITIES AND UNITHOLDERS' EQUITY

Current liabilities:		
Bank indebtedness	\$ 73	\$ 197
Accounts payable and accrued liabilities	187	198
Interest payable on term loan	7	7
Distributions payable to Fund unitholders	-	734
Distributions payable to non-controlling interest	<u>-</u>	<u>541</u>
	267	1,677
Term loan	14,000	14,000
Non-controlling interest (note 8)	87,203	83,021
Unitholders' equity	<u>74,469</u>	<u>73,680</u>
	<u>\$ 175,939</u>	<u>\$ 172,378</u>

See accompanying notes to consolidated financial statements.

Approved on behalf of the Board of Trustees



C.C. Woodward, Trustee



George Tidball, Trustee

CONSOLIDATED STATEMENTS OF EARNINGS

(Expressed in thousands of dollars, except per unit amounts - unaudited)

	January 1, 2004 to March 31, <u>2004</u>	January 1, 2003 to March 31, <u>2003</u>
Gross sales reported by Keg restaurants in the Royalty Pool (note 3)	\$ <u>75,891</u>	\$ <u>73,476</u>
Revenue:		
Royalty income (note 3)	\$ 3,036	\$ 2,939
Interest income	<u>1,064</u>	<u>1,055</u>
	4,100	3,994
Expenses:		
General and administrative	86	95
Interest and financing fees	166	177
Amortization of deferred financing charges	<u>29</u>	<u>29</u>
	<u>281</u>	<u>301</u>
Earnings before non-controlling interest	3,819	3,693
Non-controlling interest (note 8)	<u>1,562</u>	<u>1,405</u>
Net earnings for the period	\$ <u>2,257</u>	\$ <u>2,288</u>
Basic and diluted earnings per Fund unit (8,153,500 units)	\$ <u>0.28</u>	\$ <u>0.28</u>

CONSOLIDATED STATEMENTS OF UNITHOLDERS' EQUITY

(Expressed in thousands of dollars - unaudited)

	January 1, 2004 to March 31, <u>2004</u>	January 1, 2003 to March 31, <u>2003</u>
Balance, beginning of period	\$ 73,680	\$ 73,803
Net earnings for the period	2,257	2,288
Distributions declared to Fund unitholders (note 5).....	<u>(1,468)</u>	<u>(1,468)</u>
Balance, end of period	\$ <u>74,469</u>	\$ <u>74,623</u>

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Expressed in thousands of dollars - unaudited)

	January 1, 2004 to March 31, <u>2004</u>	January 1, 2003 to March 31, <u>2003</u>
Cash provided by (used for):		
OPERATIONS:		
Net earnings for the period	\$ 2,257	\$ 2,288
Items not involving cash:		
Amortization of deferred financing charges	29	29
Non-controlling interest	1,562	1,405
Change in non-cash operating working capital (note 9(a))	<u>26</u>	<u>(23)</u>
	3,874	3,699
FINANCING:		
Distributions paid to Fund unitholders (note 5)	(2,201)	(2,201)
Distributions paid to non-controlling interest	<u>(1,549)</u>	<u>(1,384)</u>
	<u>(3,750)</u>	<u>(3,585)</u>
Increase in cash	124	114
Bank indebtedness, beginning of period	<u>(197)</u>	<u>(40)</u>
Cash (bank indebtedness), end of period	<u>\$ (73)</u>	<u>\$ 74</u>

See note 9(b) for supplementary cash flow information.

See accompanying notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Tabular amounts expressed in thousands of dollars - unaudited)

For the three months ended March 31, 2004 and March 31, 2003

1. BASIS OF PRESENTATION:

The Keg Royalties Income Fund (the "Fund") prepares its interim consolidated financial statements in accordance with Canadian generally accepted accounting principles on a basis consistent with those used and described in the annual consolidated financial statements for the year ended December 31, 2003. The disclosures contained in these interim consolidated financial statements do not include all the requirements of Canadian generally accepted accounting principles for annual financial statements.

These interim consolidated financial statements should be read in conjunction with the annual consolidated financial statements for the year ended December 31, 2003.

2. CHANGE IN ACCOUNTING POLICY:

Effective January 1, 2004, the Fund prospectively adopted new recommendations of the Canadian Institute of Chartered Accountants on what constitutes Canadian generally accepted accounting principles and its sources. The Class B units issued by The Keg Rights Limited Partnership (the "Partnership"), a subsidiary of the Fund, which are held by Keg Restaurants Ltd. ("KRL") are entitled to receive distributions from the Partnership and are exchangeable for Fund units. As a result of this change, these units are recorded at their fair value at the date of determination of their respective annual entitlement. The increase in value of these Class B units has been accounted for as an additional cost of the purchase of the trademarks, trade names, operating procedures and systems and other intellectual property (collectively, the "Keg Rights") from KRL and accordingly has been reflected as an increase in the value of intangible assets. The effect of this change on the current year's financial statements is to increase the value of intangible assets and non-controlling interest by \$3,627,169 (note 7). There is no impact to net earnings as a result of this change.

3. GROSS SALES:

The gross sales reported by the 86 Keg restaurants on which KRL pays a royalty (the "Royalty Pool") are from January 1, 2004 to March 31, 2004 (January 1, 2003 to March 31, 2003 – 81 Keg restaurants).

The royalty payment from KRL to the Partnership is four percent of system sales for such period reported by Keg restaurants in the Royalty Pool plus a make-whole payment, if required by a restaurant closure, based on four percent of lost system sales. System sales for any period and for any Keg restaurants located in Canada and the United States, as defined in the Licence and Royalty Agreement means the gross sales by such Keg restaurants for such period. Make-whole payments were not required for the period from January 1, 2004 to March 31, 2004 and from January 1, 2003 to March 31, 2003 as there were no restaurant closures.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Tabular amounts expressed in thousands of dollars - unaudited)

For the three months ended March 31, 2004 and March 31, 2003

3. GROSS SALES (CONTINUED):

	January 1, 2004 to March 31, <u>2004</u>	January 1, 2003 to March 31, <u>2003</u>
System sales reported by Keg restaurants in the Royalty Pool	\$ <u>75,891</u>	\$ <u>73,476</u>
Royalty income at 4% of system sales reported above	\$ 3,036	\$ 2,939
Make-whole payment, based on 4% of lost system sales	<u>-</u>	<u>-</u>
Total royalty income	<u>\$ 3,036</u>	<u>\$ 2,939</u>

4. DISTRIBUTABLE CASH:

	January 1, 2004 to March 31, <u>2004</u>	January 1, 2003 to March 31, <u>2003</u>
Earnings for the period	\$ 2,257	\$ 2,288
Amortization of deferred financing charges	29	29
Non-controlling interest	<u>1,562</u>	<u>1,405</u>
	3,848	3,722
Distributable cash required for non-controlling interest	<u>(1,552)</u>	<u>(1,406)</u>
Distributable cash available for Fund unitholders	<u>\$ 2,296</u>	<u>\$ 2,316</u>
Distributions declared to Fund unitholders (8,153,500 units)	<u>\$ 1,468</u>	<u>\$ 1,468</u>

Distributable cash is not an earnings measure recognized by generally accepted accounting principles ("GAAP") and therefore may not be comparable to similar measures presented by other issuers.

5. UNITHOLDER DISTRIBUTIONS:

The \$733,815 difference between the \$1,467,630 in distributions declared and the \$2,201,445 in distributions paid to Fund unitholders during the three months ended March 31, 2004 and March 31, 2003 is due to the declaration of the January distributions on December 31 each year. Annually, two distributions are expected to be declared during the first quarter, three distributions in each of the second and third quarters and four distributions in the fourth quarter. This is done to ensure that the distribution based on December KRL Royalty Pool system sales, which is paid the following month in January, is recorded in the period it was earned for income tax purposes.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Tabular amounts expressed in thousands of dollars - unaudited)

For the three months ended March 31, 2004 and March 31, 2003

6. DUE FROM KEG RESTAURANTS LTD.:

	March 31, <u>2004</u>	December 31, <u>2003</u>
Royalty fee, including GST	\$ 1,245	\$ 1,270
Interest on note receivable from Keg Restaurants Ltd.	<u>362</u>	<u>363</u>
	<u>\$ 1,607</u>	<u>\$ 1,633</u>

The above amounts were received when due from KRL subsequent to the end of the above periods to facilitate the following months distribution to Fund unitholders.

7. INTANGIBLE ASSETS:

On May 31, 2002, the Partnership acquired the Keg Rights from KRL for \$113,546,820 of which \$30,487,380 was paid in cash, \$9,059,440 was paid by the issuance of 905,944 Class A Partnership units ("Class A Units"), \$17,000,000 was paid by the issuance of 3,376,700 Class B Partnership units ("Class B Units") and \$57,000,000 was paid by the issuance of 5,700,000 Class C Partnership units ("Class C Units").

Concurrently with the acquisition of the Keg Rights, the Partnership granted KRL a licence to use the Keg Rights for a term of 99 years for which KRL pays the Partnership a royalty of four percent of the system sales reported by KRL for restaurants included in the Royalty Pool (note 3).

On January 1, 2004, the number of Keg restaurants in the Royalty Pool was increased by seven restaurants opened during the period from October 3, 2002 to October 2, 2003 less two restaurants which had permanently closed (2003 – net increase of one restaurant). In exchange for adding these restaurants to the Royalty Pool, and assuming 100% of the estimated entitlement for these restaurants is received, KRL's additional entitlement will be equivalent to 653,193 Fund units (2003 – 310,815 Fund units). KRL will also receive a proportionate increase in monthly distributions from the Partnership. On January 1, 2004, KRL received 80% of this entitlement, representing the equivalent of 522,554 Fund units. The yield of the Fund units was determined to be 11.66% (2003 – 11.25%) calculated using a weighted average unit price of \$9.26 (2003 - \$9.60).

As described in note 2, the Fund has adopted a policy of accounting for the entitlement of the Class B Units based on the fair value of these units at the date of determination of the entitlement which results in an increase in intangible assets and non-controlling interest.

	March 31, <u>2004</u>
Intangible assets (Keg Rights):	
Initial consideration	\$ 113,547
2003 adjustment to Royalty Pool	1,419
2004 initial adjustment to Royalty Pool	<u>2,208</u>
	<u>\$ 117,174</u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Tabular amounts expressed in thousands of dollars - unaudited)

For the three months ended March 31, 2004 and March 31, 2003

8. NON-CONTROLLING INTEREST:

Non-controlling interest relates to KRL's interest in the Partnership, as follows:

	March 31, <u>2004</u>	December 31, <u>2003</u>
Class A Units	\$ 9,059	\$ 9,059
Entitled Class B Units	7,823	1,565
Non-entitled Class B Units	12,804	15,435
Class C Units	<u>57,000</u>	<u>57,000</u>
	86,686	83,059
Non-controlling interest in earnings of the Partnership, net of distributions declared, beginning of period	(38)	(9)
Non-controlling interest in earnings of the Partnership	1,562	5,571
Distributions declared to non-controlling interest	<u>(1,007)</u>	<u>(5,600)</u>
	<u>517</u>	<u>(38)</u>
Balance, end of period	<u>\$ 87,203</u>	<u>\$ 83,021</u>

As described in note 7, KRL added seven new restaurants (2003 – three restaurants) to the Royalty Pool and two permanently closed restaurants were removed from the Royalty Pool (2003 – two restaurants) on January 1, 2004.

In accordance with the terms of the Partnership agreements, the Fund provided entitlements for KRL to receive distributions on an estimated 653,193 (2003 – 310,815) Class B Units in exchange for the addition of these restaurants to the Royalty Pool, 80% of which was received by KRL on January 1, 2004. As described in note 2, the Fund has adopted a policy of accounting for the entitlement of Class B Units as an increase in the value of the entitled units based on their estimated fair value at the determination date of the entitlement which results in an increase in intangible assets and non-controlling interest.

9. SUPPLEMENTARY CASH FLOW INFORMATION:

	January 1, 2004 to March 31, <u>2004</u>	January 1, 2003 to March 31, <u>2003</u>
(a) Change in non-cash operating working capital:		
Due from Keg Restaurants Ltd. (note 6)	\$ 26	\$ 28
Prepaid expenses and deposits	11	4
Accounts payable and accrued liabilities	<u>(11)</u>	<u>(55)</u>
	<u>\$ 26</u>	<u>\$ (23)</u>
(b) Supplementary information:		
Interest received	\$ 1,065	\$ 1,055
Interest paid	166	177

KEG RESTAURANTS LTD.

SECOND QUARTER REPORT
13 weeks ended April 4, 2004

Provided as a supplement to the consolidated financial statements of
The Keg Royalties Income Fund

FINANCIAL HIGHLIGHTS

The following table sets out selected financial information and other data of Keg Restaurants Ltd. (“KRL”), which should be read in conjunction with the attached unaudited, consolidated financial statements of KRL for the 13 and 27 weeks ended April 4, 2004.

SELECTED FINANCIAL INFORMATION OF KRL

	13 weeks ended April 4, 2004	13 weeks ended March 30, 2003	27 weeks ended April 4, 2004	26 weeks ended March 30, 2003
	(in thousands of dollars)			
System sales ⁽¹⁾	\$ 79,831	\$ 77,088	\$ 164,405	\$ 150,168
Corporate restaurant sales ⁽²⁾	45,271	43,755	92,479	86,318
Retail operating contribution (loss) ⁽³⁾	24	(2)	-	(12)
Franchise fee income	1,622	1,569	3,388	3,004
Operating costs and expenses	<u>(42,584)</u>	<u>(41,211)</u>	<u>(88,146)</u>	<u>(81,527)</u>
Operating earnings	\$ 4,333	\$ 4,111	\$ 7,721	\$ 7,783
Equity income ⁽⁴⁾	1,552	1,405	3,013	2,722
Royalty fee expense	<u>(3,036)</u>	<u>(2,940)</u>	<u>(6,053)</u>	<u>(5,667)</u>
EBITDA ⁽⁵⁾	\$ 2,849	\$ 2,576	\$ 4,681	\$ 4,838

Notes:

- (1) Represents the gross sales of all restaurants owned by KRL and the gross sales reported to KRL by franchised Keg restaurants without independent audit.
- (2) Includes gross sales for all restaurants owned by KRL and its proportionate share of gross sales from a joint venture restaurant located in Coquitlam, BC.
- (3) Represents the revenue net of related expenses of a wholly owned subsidiary, which sells Keg branded food and liquor products.
- (4) Represents the equity income from KRL's investment in The Keg Rights Limited Partnership and its 17.6% (2003 – 12.6%) effective interest in The Keg Royalties Income Fund, which began on May 31, 2002.
- (5) EBITDA is earnings before amounts for interest, taxes, depreciation and amortization and loss on disposal of property, plant and equipment. EBITDA is not a recognized measure under Canadian Generally Accepted Accounting Principles.

MANAGEMENT DISCUSSION AND ANALYSIS

OVERVIEW

Keg Restaurants Ltd. (“KRL”) is the owner/operator and franchisor of casual dining steakhouse restaurants operating under the trade name “The Keg Steakhouse & Bar” in Canada and select markets in the United States. The revenue of KRL is derived from sales from corporate Keg restaurants, its proportionate share of a joint venture Keg restaurant, franchise fee income and revenue from sales of food and liquor products marketed under the Keg brand name. Sales from corporate Keg restaurants are affected by the number of new corporate Keg restaurants that are opened or closed. Franchise fee income is affected by the amount of sales generated by existing franchised Keg restaurants and the number of franchised Keg restaurants that are opened or closed.

Operating costs and expenses include food and beverage costs, premises costs, and labour costs of corporate Keg restaurants, marketing and advertising expenses net of franchisee contributions, as well as general and administrative costs associated with the operations of KRL in providing services to the corporate and franchised Keg restaurants.

On May 31, 2002, KRL completed a transaction in which KRL sold the Keg trademarks and related property (collectively, the “Keg Rights”) to The Keg Rights Limited Partnership (the “Partnership”), a subsidiary of The Keg Royalties Income Fund (the “Fund”). The Partnership in turn licensed the use of these Keg Rights to KRL under a licence and royalty agreement for a term of 99 years. KRL pays the Partnership a royalty of 4% of system sales (the “Royalty”). The Royalty was initially based on the 80 Keg restaurants in existence on March 31, 2002.

Annually, on January 1st, the pool of Keg restaurants on which KRL pays a royalty to the Partnership (the “Royalty Pool”) is adjusted to include the gross sales from new Keg restaurants that have opened on or before October 2nd of the prior year, less gross sales from any Keg restaurants that have permanently closed during the year. In return for adding these net sales to the Royalty Pool, KRL receives the right to indirectly acquire additional Fund units (the “Additional Entitlement”). The Additional Entitlement is determined based on 92.5% of the royalty revenue added to the Royalty Pool, divided by the yield of the Fund units. KRL receives 80% of the estimated Additional Entitlement initially, with the balance received on December 31st each year when the actual full year performance of the new restaurants is known with certainty.

On January 1, 2003, three new Keg restaurants that opened during the period from April 1, 2002 through October 2, 2002 were added to the Royalty Pool. The actual gross sales of these three new restaurants were \$13.2 million for the 52 weeks ended September 28, 2003. Two permanently closed Keg restaurants with annual sales of \$3.8 million were removed from the Royalty Pool. This resulted in KRL receiving an Additional Entitlement equivalent to 310,815 Fund units effective as of January 1, 2003. The total number of restaurants in the Royalty Pool increased to 81. The yield of the Fund units was determined to be 11.25% calculated using a weighted average unit price of \$9.60.

OVERVIEW (CONTINUED)

On January 1, 2004, seven new Keg restaurants that opened during the period from October 3, 2002 through October 2, 2003 were added to the Royalty Pool. The gross sales of these seven new restaurants have been estimated at \$25.2 million annually. Two permanently closed Keg restaurants with annual sales of \$4.6 million have been removed from the Royalty Pool, resulting in an estimated net increase in Royalty Pool sales of \$20.6 million annually. The total number of restaurants in the Royalty Pool has increased to 86. The yield of the Fund units was determined to be 11.66% calculated using a weighted average unit price of \$9.26. As a result of the contribution of the additional net sales to the Royalty Pool, and assuming 100% of the estimated Additional Entitlement is received, KRL's Additional Entitlement will be equivalent to 653,193 Fund units, being 6.52% of the Fund units on a fully diluted basis. On January 1, 2004, KRL received 80% of this entitlement representing the equivalent of 522,554 Fund units, being 5.28% of the Fund units on a fully diluted basis. KRL will also receive a proportionate increase in monthly distributions from the Partnership. Including the initial portion of the Additional Entitlement described above, KRL has the right to exchange its units in the capital of the Partnership for 1,739,314 Fund units, representing 17.58% of the Fund units on a fully diluted basis. The balance of the Additional Entitlement will be adjusted to be effective January 1, 2004 once the actual performance of the new restaurants have been confirmed. If KRL were to receive 100% of the estimated Additional Entitlement for 2004, it would have the right to exchange its Partnership units for 1,869,952 Fund units, representing 18.66% of the Fund units on a fully diluted basis. All Fund units obtained by KRL in exchange for these Partnership units are subject to a contractual re-sale restriction, which expires on May 31, 2005.

SECOND QUARTER OPERATING RESULTS

System sales for the 13 weeks ended April 4, 2004 were \$79,831,000 compared to \$77,088,000 for the 13 weeks ended March 30, 2003, an increase of \$2,743,000 or 3.6%. During the 13 weeks ended April 4, 2004, no new restaurants were opened and no restaurants were closed. During the 13 week period of the prior year, no new restaurants were opened and no restaurants were closed. As at April 4, 2004, there were a total of 88 restaurants as compared with the 84 restaurants at March 30, 2003.

Same store sales (sales of restaurants that operated during the entire period of both the current year and the prior year) decreased by 1.2% in Canada and 1.3% in the United States. This decrease is due primarily to the inclusion of the sales from New Years Eve (one of the busiest nights of the year for full service restaurants), in the results of the first quarter of the current year whereas in the prior year it fell in the second quarter. After translating the sales of the U.S. restaurants into their Canadian dollar equivalent, consolidated same store sales for the comparable quarter decreased by 4.1%. This decrease is a function of the fluctuation in the U.S. dollar exchange rate rather than an indication of a slowdown in actual restaurant traffic. The average exchange rate moved from 1.52 for the second quarter of fiscal 2003 to 1.32 for the second quarter of fiscal 2004, significantly reducing the Canadian dollar equivalent of the U.S. restaurant sales.

Franchise fee income climbed from \$1,569,000 during the second quarter of the prior year to \$1,622,000 during the second quarter of the current year, an increase of \$53,000 or 3.4%. This increase resulted from additional franchise fees earned from one franchised restaurant that opened in the second half of the prior fiscal year and one franchised restaurant that opened during the current fiscal year.

SECOND QUARTER OPERATING RESULTS (CONTINUED)

Operating costs and expenses increased to \$42,584,000 for the 13 week period ended April 4, 2004 from \$41,211,000 for the 13 week period ended March 30, 2003. The increase of \$1,373,000 was primarily due to three expense categories. Restaurant variable operating costs increased by \$912,000 due to the increased sales for the period. Restaurant fixed costs increased by \$555,000 due to increased facility costs related to two additional corporate restaurants and significantly higher insurance costs. General and administrative expenses, which include marketing and advertising expenses as well as corporate administrative expenses, increased by \$319,000 for the period. Marketing and advertising expenses decreased by \$100,000 due to the timing of certain marketing expenditures. Corporate administrative expenses increased by \$419,000 mainly as a result of the addition of new corporate marketing personnel and non-recurring costs related to the relocation of the corporate office in Richmond, BC.

Operating earnings increased by \$222,000 from \$4,111,000 for the 13 weeks ended March 30, 2003 to \$4,333,000 for the 13 weeks ended April 4, 2004. Management views operating earnings as a key figure as it indicates the funds generated by KRL which are available to meet its royalty payment obligations to the Fund, interest and income tax obligations, and to pay any discretionary expenses.

Investment income from KRL's effective interest in the Fund amounted to \$1,552,000 (2003 - \$1,405,000) and the royalty expense paid for the use of the Keg Rights totalled \$3,036,000 (2003 - \$2,940,000) during the 13 weeks ended April 4, 2004, resulting in a net expense of \$1,484,000 (2003 - \$1,535,000). These figures do not include interest of \$1,078,000 (2003 - \$1,066,000) on a \$57,000,000 note payable to the Fund, which has been included in interest expense for the year.

EBITDA for the 13 week period of the current year was \$2,849,000 compared to \$2,576,000 for the 13 week period of the prior year. The increase in EBITDA of \$273,000 for the quarter is due to the net impact of the increase in operating earnings of \$222,000, and the decrease of \$51,000 in net expenses related to the Fund, as explained above.

The net loss before taxes for the 13 weeks ended April 4, 2004 amounted to \$391,000 compared to a net loss of \$245,000 for the 13 weeks ended March 30, 2003.

YEAR-TO-DATE OPERATING RESULTS

KRL's year end falls on the Sunday closest to September 30th, in any year. As a result of the floating year end date, approximately every fifth fiscal year contains 53 weeks of operation. The fiscal year ending October 3, 2004 will contain 53 weeks of sales and related costs and the period ending April 4, 2004 will contain 27 weeks of sales and related costs.

YEAR-TO-DATE OPERATING RESULTS (CONTINUED)

System sales for the 27 weeks ended April 4, 2004 were \$164,405,000 compared to \$150,168,000 for the 26 weeks ended March 30, 2003, an increase of \$14,237,000 or 9.5%. System sales due to the extra week of operation were \$5,519,000 so on a comparable basis, system sales increased by \$ 8,718,000 or 5.8%. During the 27 weeks ended April 4, 2004, two new corporate restaurants and one new franchised restaurant were opened and one corporate restaurant was closed. During the 26 week period of the prior year, one new corporate restaurant and two new franchised restaurants were opened, and no restaurants were closed.

Same store sales (sales of restaurants that operated during the entire 27 week period of the current year and the 26 week period of the prior year) increased by 1.4%. After adjusting for the extra week of operation, same store sales for the comparable 26 week periods increased by 1.3% in Canada and 0.8% in the United States. After translating the sales of the U.S. restaurants into their Canadian dollar equivalent, consolidated same store sales for the comparable 26 week periods decreased by 2.1%. This decrease is a function of the fluctuation in the U.S. dollar exchange rate rather than an indication of a slowdown in actual restaurant traffic. The average exchange rate moved from 1.54 for the 26 week period in fiscal 2003 to 1.32 for the 27 week period in fiscal 2004, significantly reducing the Canadian dollar equivalent of the U.S. restaurant sales.

Franchise fee income climbed from \$3,004,000 for the 26 week period of the prior year to \$3,388,000 for the 27 week period of the current year, an increase of \$384,000 or 12.8%. This increase resulted from additional franchise fees earned from the extra week of operation, as well as from two franchised restaurants that opened in the second half of the prior fiscal year and one franchised restaurant that opened during the current fiscal year.

Operating costs and expenses increased to \$88,146,000 for the 27 week period ended April 4, 2004 from \$81,527,000 for the 26 week period ended March 30, 2003. The increase of \$6,619,000 was primarily due to four expense categories. Restaurant variable operating costs increased by \$3,775,000 due to the increased sales for the period. Food costs increased by \$629,000 primarily as a result of significantly higher beef prices in the United States than in the comparable period of the prior year. The increase in beef prices in the United States was due to the partial closure of the U.S. border to Canadian beef. Restaurant fixed costs increased by \$1,195,000 due to increased facility costs related to three additional corporate restaurants and significantly higher insurance costs. General and administrative expenses, which include marketing and advertising expenses as well as corporate administrative expenses, increased by \$618,000 for the period. Marketing and advertising expenses decreased by \$39,000 due to the timing of certain marketing expenditures. Corporate administrative expenses increased by \$657,000 mainly as a result of the extra week of operations, the addition of new corporate marketing personnel and non-recurring costs related to the relocation of the corporate office in Richmond, BC.

Operating earnings decreased by \$62,000 from \$7,783,000 for the 26 weeks ended March 30, 2003 to \$7,721,000 for the 27 weeks ended April 4, 2004 due to the cost increases noted above. Management views operating earnings as a key figure as it indicates the funds generated by KRL which are available to meet its royalty payment obligations to the Fund, interest and income tax obligations, and to pay any discretionary expenses.

YEAR-TO-DATE OPERATING RESULTS (CONTINUED)

Investment income from KRL's effective interest in the Fund amounted to \$3,013,000 (2003 - \$2,722,000) and the royalty expense paid for the use of the Keg Rights totalled \$6,053,000 (2003 - \$5,667,000) during the 27 weeks ended April 4, 2004, resulting in a net expense of \$3,040,000 (2003 - \$2,945,000). These figures do not include interest of \$2,210,718 (2003 - \$2,131,644) on a \$57,000,000 note payable to the Fund, which has been included in interest expense for the year.

EBITDA for the 27 week period of the current year was \$4,681,000 compared to \$4,838,000 for the 26 week period of the prior year. The decline in EBITDA of \$157,000 for the year is due to the net impact of the decrease in operating earnings of \$62,000, and the increase of \$95,000 in net expenses related to the Fund, as explained above.

The net loss before taxes for the 27 weeks ended April 4, 2004 amounted to \$1,632,000 compared to a net loss of \$790,000 for the 26 weeks ended March 30, 2003.

LIQUIDITY AND CAPITAL RESOURCES

KRL must invest in the maintenance of the corporate Keg restaurants on an annual basis and it is estimated that the costs of these maintenance capital expenditures is \$2,300,000 per annum.

KRL will use cash flow from operations to fund seasonal fluctuations in working capital and maintenance capital expenditures. Management plans to continue to utilize traditional bank financing to fund the opening of new corporate Keg restaurants in Canada. Subsequent to KRL's fiscal year end certain Canadian expansion costs incurred in the prior year have been financed in this manner as noted below. Management further anticipates additional loan facilities for the expansion of corporate Keg restaurants in the United States on similar terms and conditions as exist currently, and financing in this regard was also completed subsequent to KRL's fiscal year end, also as noted below.

On September 30, 2003, KRL entered into a CDN\$5,250,000 credit facility agreement with a major Canadian chartered bank. This secured facility includes a demand loan in the amount of \$4,000,000, the proceeds of which have been used solely for the expansion of restaurant operations in Canada and a maximum of \$1,250,000 available for outstanding letters of credit. In October 2003, KRL's wholly owned subsidiary, Keg Restaurants U.S., Inc. obtained secured debt financing in the amount of US\$3,500,000 for expansion of U.S. restaurant operations.

OUTLOOK

According to the Long Term Forecast of the Canadian Restaurant and Foodservices Association, foodservice operators can look forward to a brighter 2004. Following an unprecedented two year decline in real foodservice sales, the forecast calls for sales in Canada's commercial foodservice industry to recover throughout 2004 and 2005 as tourism and global economies continue to improve. A return to real growth in the foodservice industry is predicted, with full service restaurants, the sector in which KRL operates, experiencing a particularly strong recovery.

OUTLOOK (CONTINUED)

KRL anticipates that it will record strong sales growth relative to the foodservice industry as a whole in the future, as it has historically. KRL remains committed to growth, both through expansion into new markets and same store sales increases. In addition to building new Kegs in both Canada and the U.S., we continue to refurbish, and in some cases relocate, existing Keg restaurants in order to better serve our guests and to protect and enhance the strong leadership position The Keg brand has enjoyed for over thirty years.

RISKS AND UNCERTAINTIES

Management of KRL continues to anticipate certain risks and uncertainties associated with the ordinary course of business. Such risks and uncertainties include the competitive nature of the restaurant industry, the availability and quality of raw materials, the ability of KRL to maintain and grow Keg restaurants, government regulation and fluctuation in foreign currency, among others.

Management continues to monitor the situation regarding the two cases of BSE found in North America during 2003. The widespread testing of herds confirms these are isolated cases; the risk to human health appears to be negligible. Most importantly to the Keg, there has not been any significant negative consumer reaction to beef in North America and there has not been a material impact on our restaurant traffic. KRL has maintained an uninterrupted supply of quality beef that meets our demanding specifications despite the border closures and the unfortunate impact on cattle producers. We expect the demand for beef to remain strong among consumers and our supply to continue uninterrupted.

FORWARD LOOKING INFORMATION

The information provided in this report includes forward-looking statements with respect to business plans, activities, prospects, opportunities and events anticipated or being pursued by management of KRL and KRL's future results. Although management of KRL believes the assumptions underlying such statements to be reasonable, any of the assumptions may prove to be inaccurate and, as a result, the forward-looking information may prove to be incorrect. The anticipated results or events upon which current expectations are based may differ materially from actual results or events. The forward-looking information contained in this document is current only as of the date of this document. There should not be an expectation that such information will in all circumstances be updated, supplemented or revised whether as a result of new information, changing circumstances, future events or otherwise.


CONSOLIDATED BALANCE SHEETS

(Expressed in thousands of dollars)

	<u>April 4,</u> <u>2004</u> (unaudited)	<u>September 28,</u> <u>2003</u> (audited)
ASSETS		
Current assets:		
Cash	\$ 1,755	\$ 1,313
Restricted cash	-	750
Accounts receivable	3,568	2,839
Inventories	4,045	3,848
Prepaid expenses and deposits	4,984	3,183
Current portion of notes receivable	<u>207</u>	<u>143</u>
	14,559	12,076
Long-term investments (note 4)	31,709	28,829
Notes receivable	66	68
Due from related company	-	219
Property, plant and equipment	47,476	46,013
Deferred charges	3,395	3,177
Future income taxes	<u>6,292</u>	<u>6,340</u>
	<u>\$ 103,497</u>	<u>\$ 96,722</u>
LIABILITIES AND SHAREHOLDER'S DEFICIENCY		
Current liabilities:		
Accounts payable and accrued liabilities	\$ 15,664	\$ 22,571
Unearned revenue	7,283	5,450
Current portion of long-term debt	<u>1,572</u>	<u>543</u>
	24,519	28,564
Note payable to The Keg Royalties Income Fund	57,000	57,000
Long-term debt	13,138	6,158
Deferred gain on sale of intangible assets	40,176	37,105
Due to related company	3,000	-
Shareholder's deficiency:		
Share capital	1	1
Cumulative translation adjustment	(2,700)	(2,153)
Deficit	<u>(31,637)</u>	<u>(29,953)</u>
	<u>(34,336)</u>	<u>(32,105)</u>
	<u>\$ 103,497</u>	<u>\$ 96,722</u>

See accompanying notes to consolidated financial statements.

Approved on behalf of the Board



 David Aisenstat, Director



 Neil Maclean, Director

CONSOLIDATED STATEMENTS OF OPERATIONS AND DEFICIT

(Expressed in thousands of dollars - unaudited)

	13 weeks ended April 4, 2004	13 weeks ended March 30, 2003	27 weeks ended April 4, 2004	26 weeks ended March 30, 2003
System sales (note 3)	<u>\$ 79,831</u>	<u>\$ 77,088</u>	<u>\$ 164,405</u>	<u>\$ 150,168</u>
Revenue:				
Restaurant sales	\$ 45,271	\$ 43,755	\$ 92,479	\$ 86,318
Retail sales	<u>789</u>	<u>722</u>	<u>1,264</u>	<u>1,252</u>
	46,060	44,527	93,743	87,570
Operating costs:				
Restaurant operating costs	38,893	37,839	80,599	74,599
Retail operations	<u>765</u>	<u>774</u>	<u>1,264</u>	<u>1,264</u>
	<u>39,658</u>	<u>38,613</u>	<u>81,863</u>	<u>75,863</u>
Earnings from operations	6,402	5,914	11,880	11,707
Equity income (note 4)	1,552	1,405	3,013	2,722
Franchise fee income	1,622	1,569	3,388	3,004
Other investment income	<u>-</u>	<u>-</u>	<u>-</u>	<u>1</u>
	9,576	8,888	18,281	17,434
Royalty expense	3,036	2,940	6,053	5,667
General and administrative expenses	<u>3,691</u>	<u>3,372</u>	<u>7,547</u>	<u>6,929</u>
Earnings before undernoted items	2,849	2,576	4,681	4,838
Amortization	1,978	1,711	3,747	3,405
Amortization of deferred gain	(95)	(95)	(190)	(190)
Interest	1,352	1,209	2,742	2,405
Loss (gain) on disposal of property, plant and equipment	<u>5</u>	<u>(4)</u>	<u>14</u>	<u>8</u>
Loss before income taxes	(391)	(245)	(1,632)	(790)
Income taxes:				
Current	(3)	16	4	34
Future	<u>(6)</u>	<u>63</u>	<u>48</u>	<u>78</u>
	<u>(9)</u>	<u>79</u>	<u>52</u>	<u>112</u>
Net loss for the period	(382)	(324)	(1,684)	(902)
Deficit, beginning of period	<u>(31,255)</u>	<u>(11,999)</u>	<u>(29,953)</u>	<u>(11,421)</u>
Deficit, end of period	<u>\$ (31,637)</u>	<u>\$ (12,323)</u>	<u>\$ (31,637)</u>	<u>\$ (12,323)</u>

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Expressed in thousands of dollars - unaudited)

	13 weeks ended April 4, <u>2004</u>	13 weeks ended March 30, <u>2003</u>	27 weeks ended April 4, <u>2004</u>	26 weeks ended March 30, <u>2003</u>
Cash provided by (used for):				
OPERATIONS:				
Net loss for the period	\$ (382)	\$ (324)	\$ (1,684)	\$ (902)
Items not involving cash:				
Amortization	1,978	1,711	3,747	3,405
Amortization of deferred gain	(95)	(95)	(190)	(190)
Share of equity earnings from investments	(1,552)	(1,405)	(3,013)	(2,723)
Loss (gain) on disposition of property, plant and equipment	5	(4)	14	8
Future income tax expense (recovery)	(6)	63	48	78
Change in non-cash operating working capital (note 7(a))	<u>(3,509)</u>	<u>(3,263)</u>	<u>(7,702)</u>	<u>(5,343)</u>
	(3,561)	(3,317)	(8,780)	(5,667)
INVESTMENTS:				
Additions to property, plant and equipment and deferred charges	(2,555)	(3,766)	(6,288)	(6,977)
Net proceeds (costs) from disposition of property, plant and equipment	22	(13)	22	8
Proceeds from disposition of property, plant and equipment held for resale	-	2,237	-	2,237
Distributions and advances from investments	1,008	1,382	3,394	2,693
Notes receivable	(24)	13	(62)	26
Restricted cash	<u>-</u>	<u>-</u>	<u>750</u>	<u>-</u>
	(1,549)	(147)	(2,184)	(2,013)
FINANCING:				
Shareholder loan	(46)	1,193	(20)	1,190
Due to related company	1,838	-	3,219	-
Issuance of long-term debt	-	-	8,590	-
Repayment of long-term debt	<u>(190)</u>	<u>(124)</u>	<u>(383)</u>	<u>(278)</u>
	<u>1,602</u>	<u>(1,069)</u>	<u>11,406</u>	<u>912</u>
Increase (decrease) in cash	(3,508)	(2,395)	442	(6,768)
Cash, beginning of period	<u>5,263</u>	<u>6,486</u>	<u>1,313</u>	<u>10,859</u>
Cash, end of period	<u>\$ 1,755</u>	<u>\$ 4,091</u>	<u>\$ 1,755</u>	<u>\$ 4,091</u>

See note 7(b) for supplementary cash flow information.

See accompanying notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Tabular amounts expressed in thousands of dollars - unaudited)

13 weeks ended April 4, 2004 and March 30, 2003

27 weeks ended April 4, 2004 and 26 weeks ended March 30, 2003

1. BASIS OF PRESENTATION:

Keg Restaurants Ltd. ("KRL") prepares its interim consolidated financial statements in accordance with Canadian generally accepted accounting principles on a basis consistent with those used and described in the annual consolidated financial statements for the 52 weeks ended September 28, 2003. The disclosures contained in these interim consolidated financial statements do not include all requirements of Canadian generally accepted accounting principles for annual financial statements.

These interim consolidated financial statements should be read in conjunction with the annual consolidated financial statements for the 52 weeks ended September 28, 2003.

2. CHANGE IN ACCOUNTING POLICY:

Effective January 1, 2004, KRL prospectively adopted new recommendations of the Canadian Institute of Chartered Accountants on what constitutes Canadian generally accepted accounting principles and its sources. The Class B units issued by The Keg Rights Limited Partnership (the "Partnership"), a subsidiary of The Keg Royalties Income Fund (the "Fund"), which are held by KRL are entitled to receive distributions from the Partnership and are exchangeable for Fund units. As a result of this change, these units are recorded at their fair value at the date of determination of their respective annual entitlement. The effect of this change on the current period's financial statements is to increase the long-term investments and deferred gain on sale of intangible assets by \$3,261,037 (note 4).

3. SYSTEM SALES:

System sales for any period and for any Keg restaurants located in Canada and the United States means the gross sales by such Keg restaurants for such period.

Gross sales are the sales reported to KRL by owners of Keg restaurants in Canada and the United States under franchise agreements, without audit or other form of independent assurance, and the sales of Keg restaurants in Canada and the United States owned by KRL and its subsidiaries. In each case, these sales are reported net of discounts for coupons and other promotional items and applicable sales taxes.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Tabular amounts expressed in thousands of dollars - unaudited)

13 weeks ended April 4, 2004 and March 30, 2003

27 weeks ended April 4, 2004 and 26 weeks ended March 30, 2003

4. LONG-TERM INVESTMENTS:

	April 4, <u>2004</u>	September 28, <u>2003</u>
The Keg Rights Limited Partnership		
905,944 Class A units of the Partnership	\$ 9,059	\$ 9,059
833,370 Entitled Class B units of the Partnership (September 28, 2003 – 269,351 units)	7,823	1,356
2,543,330 Non-entitled Class B units of the Partnership (September 28, 2003 – 3,107,349 units)	12,804	15,644
5,700,000 Class C units of the Partnership	57,000	57,000
Equity income to date	10,237	7,224
Distributions and advances from the Partnership to date	<u>(9,693)</u>	<u>(6,299)</u>
	87,230	83,984
Portion of gain on sale of Keg Rights relating to KRL's ownership interest in the Partnership	<u>(55,556)</u>	<u>(55,190)</u>
	31,674	28,794
Saskatoon Property Partnership	34	34
The Keg GP Ltd.	<u>1</u>	<u>1</u>
	<u>\$ 31,709</u>	<u>\$ 28,829</u>

On January 1, 2004, KRL added seven new restaurants (2003 – three restaurants) to the Royalty Pool and two permanently closed restaurants were removed from the Royalty Pool (2003 – two restaurants). In accordance with the terms of the Partnership agreements, the Fund provided entitlements for KRL to receive distributions on an estimated 653,193 (2003 – 310,815) Class B units of the Partnership in exchange for the addition of these restaurants to the Royalty Pool, 80% of which was received by KRL on January 1, 2004. The balance of the entitlement for 2004 will be adjusted to be effective January 1, 2004 once the actual performance of the new restaurants has been confirmed. As of April 4, 2004, 833,370 Class B units of the Partnership (September 28, 2003 – 269,351) were entitled to receive distributions.

As described in note 2, KRL has adopted a policy of accounting for the entitlement of Class B units of the Partnership as an increase in the value of the entitled units based on their estimated fair value at the determination date of the entitlement which results in an increase in long-term investments and deferred gain on sale of intangible assets.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Tabular amounts expressed in thousands of dollars - unaudited)

13 weeks ended April 4, 2004 and March 30, 2003

27 weeks ended April 4, 2004 and 26 weeks ended March 30, 2003

5. DEFERRED GAIN ON SALE OF INTANGIBLE ASSETS:

	April 4, 2004	September 28, 2003
Cash	\$ 30,487	\$ 30,487
905,944 Class A units of the Partnership	9,059	9,059
833,370 Entitled Class B units of the Partnership (September 28, 2003 – 269,351 units)	7,823	1,356
2,543,330 Non-entitled Class B units of the Partnership (September 28, 2003 - 3,107,349 units)	12,804	15,644
5,700,000 Class C units of the Partnership	<u>57,000</u>	<u>57,000</u>
	117,173	113,546
Disposition costs	(322)	(322)
Net book value of intangible assets	<u>(20,423)</u>	<u>(20,423)</u>
Total gain on sale of intangible assets	96,428	92,801
Portion of gain relating to KRL's ownership in the Partnership	<u>(55,556)</u>	<u>(55,190)</u>
	40,872	37,611
Accumulated amortization	<u>(696)</u>	<u>(506)</u>
	<u>\$ 40,176</u>	<u>\$ 37,105</u>

As described in note 2, the deferred gain on sale of intangible assets increased due to the Class B units of the Partnership being recorded at their fair value at the date of determination of their respective annual entitlement.

6. SEGMENT DISCLOSURES:

KRL's principal business activity is the operation and franchising of Keg Steakhouse and Bar restaurants in Canada and the United States; accordingly, KRL is considered to operate in only one reportable segment.

Geographic information:

	13 weeks ended April 4, 2004	13 weeks ended March 30, 2003	27 weeks ended April 4, 2004	26 weeks ended March 30, 2003
Restaurant sales:				
Canada	\$ 27,530	\$ 26,476	\$ 57,623	\$ 52,827
United States	<u>17,741</u>	<u>17,279</u>	<u>34,856</u>	<u>33,491</u>
	<u>\$ 45,271</u>	<u>\$ 43,755</u>	<u>\$ 92,479</u>	<u>\$ 86,318</u>
Franchise fee revenue:				
Canada	\$ 1,599	\$ 1,541	\$ 3,340	\$ 2,950
United States	<u>23</u>	<u>28</u>	<u>48</u>	<u>54</u>
	<u>\$ 1,622</u>	<u>\$ 1,569</u>	<u>\$ 3,388</u>	<u>\$ 3,004</u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Tabular amounts expressed in thousands of dollars - unaudited)

13 weeks ended April 4, 2004 and March 30, 2003

27 weeks ended April 4, 2004 and 26 weeks ended March 30, 2003

6. SEGMENT DISCLOSURES (CONTINUED):

	April 4, <u>2004</u>	September 28, <u>2003</u>
Property, plant and equipment:		
Canada	\$ 22,716	\$ 19,601
United States	<u>24,760</u>	<u>26,412</u>
	<u>\$ 47,476</u>	<u>\$ 46,013</u>

7. SUPPLEMENTARY CASH FLOW INFORMATION:

	13 weeks ended April 4, <u>2004</u>	13 weeks ended March 30, <u>2003</u>	27 weeks ended April 4, <u>2004</u>	26 weeks ended March 30, <u>2003</u>
(a) Change in non-cash operating working capital:				
Accounts receivable	\$ 531	\$ (1,177)	\$ (729)	\$ (964)
Inventories	448	269	(197)	(253)
Prepaid expenses and deposits	(1,292)	617	(1,801)	(1,470)
Accounts payable and accrued liabilities ..	(672)	(926)	(6,887)	(4,165)
Unearned revenue	(2,483)	(2,067)	1,833	1,429
Cumulative translation adjustment	<u>(41)</u>	<u>21</u>	<u>79</u>	<u>80</u>
	<u>\$ (3,509)</u>	<u>\$ (3,263)</u>	<u>\$ (7,702)</u>	<u>\$ (5,343)</u>
(b) Supplementary information:				
Interest received	\$ 15	\$ 55	\$ 37	\$ 114
Interest paid	1,693	1,286	3,024	2,531
Income taxes paid	3	14	10	31