



## Letter to Unitholders

The travel industry has suffered a number of setbacks recently. They include the war in Iraq, the outbreak of Severe Acute Respiratory Syndrome ("SARS"), and financial problems within the airline industry. In spite of all that, revenues in the quarter were the same as the previous year, demonstrating the benefits of our diverse portfolio. While we have adopted strategies to deal with short-term concerns, in particular SARS in the Greater Toronto Area ("GTA") our long-term priority continues to be to maximize distributable income while continuing to execute our strategy to build value over the longer term.

First quarter revenues were even with year ago even though last year's first quarter included a large one-time contract in Edmonton. When adjusted to exclude that contract, revenue per available room ("RevPAR") was ahead 2.6%, outpacing the hotel industry and the limited service sector. Nevertheless, hotel operating income declined by \$924,000 or 7.2%, mainly as the result of higher energy costs, property taxes and insurance costs.

The quality and diversity of our portfolio, and relative stability of the limited service sector of the hotel industry, contributed to InnVest's resilience in these challenging markets.

## Financial Review

The first quarter is traditionally the weakest quarter for hotel revenues, reflecting customers' seasonal travel patterns, and is therefore not indicative of results for the full year. For the three months ended March 31, 2003, hotel revenues were \$47.3 million, the same as the first quarter in 2002. Occupancy for the first quarter of 2003 was 53.6%, 2.4% lower than a year ago, while the average daily room rate ("ADR") for the quarter was \$77.79, or 2.3% above the prior year.

Hotel expenses for the first quarter were 2.8% higher than the previous year, primarily due to higher consumption of electricity and natural gas because of the long and cold winter, partially offset by continued cost management initiatives started in 2002. As a result, hotel operating income for the quarter was \$12.0 million, representing 25.3% of operating revenues.

InnVest's balance sheet remained strong, with \$23.3 million of cash (\$11.3 million unrestricted and \$12.0 million restricted for capital improvements) and financial leverage of 38.8% debt to gross asset value (defined as total assets before accumulated depreciation less future income tax liability). Additionally, InnVest has significant unutilized credit facilities to support its business plan.

## Comparisons with Forecasts

First quarter revenues were below forecast by \$1.3 million, or 2.8%. As in the previous two reporting periods, this variance is primarily due to lower than expected demand in the GTA and Ottawa markets. Revenues also were affected by reduced travel due to the war in Iraq and concerns about SARS as noted above. Occupancy of 53.6% was 2.0% lower than the forecast of 54.7%. The ADR was \$0.65 or 0.8% below the forecast, while RevPAR was \$1.24 or 2.9% below the forecast.

There is typically a net loss in the first quarter reflecting the seasonality in the Canadian hotel industry. Net loss for the quarter was \$2.4 million or \$0.11 per unit, compared with the forecast loss of \$1.5 million or \$0.09 per unit. There is no comparable bottom line data for the first quarter of 2002. The shortfall from the forecast reflects lower operating income for reasons described above, partially offset by reduced interest and depreciation expenses and higher than forecast franchise business income.

Distributable income for the quarter was \$1.1 million, or \$0.03 per unit, compared with \$1.9 million or \$0.05 per unit for the forecast. During the quarter, \$11.6 million was distributed to the Unitholders, consistent with the forecast distributions.

## Outlook

We expect that the shortfall from forecast operating performance that InnVest experienced in the first quarter will continue in the second quarter of 2003. Results for the year will reflect a delay in the recovery of business activity, particularly in Toronto, as concerns about SARS continue to affect the travel and hotel industry.

Although these developments have created a more challenging business environment than we anticipated, our strong balance sheet combined with our diversified portfolio help us to work through these tough economic times. We are taking measures to maximize results in the current business environment, and are well positioned to benefit when business conditions improve.

(signed)

Kenneth Gibson  
President and Chief Executive Officer  
May 21, 2003

The following is a discussion of the results of operations and financial condition of InnVest Real Estate Investment Trust (“InnVest” or the “REIT”) for the three months ended March 31, 2003, with a comparison with (1) the results of operations of the acquired hotel properties and franchise business during the comparable period in 2002 and (2) the REIT’s forecast provided in its initial public offering (“IPO”) prospectus dated July 18, 2002.

The following management’s discussion and analysis should be read in conjunction with the unaudited consolidated financial statements of the REIT and the notes thereto as at and for the three months ended March 31, 2003, and with the audited consolidated financial statements and the notes thereto for the 159-day period from July 26, 2002 to December 31, 2002 and with the audited statements of net income of the acquired hotel portfolio and the forecast contained in the prospectus dated July 18, 2002.

The financial statements of InnVest are prepared in accordance with Canadian generally accepted accounting principles and are presented in Canadian dollars. Data in tabular form and in the text unless otherwise indicated are in thousands of dollars, except for per unit, Average Daily Rate (“ADR”), and Revenue per Available Room (“RevPAR”) amounts.

### Forward-looking information

The following discussion, as well as other sections within this quarterly report, contains forward looking or outlook information with respect to InnVest. Because forward-looking information addresses future events and conditions, it involves risk and uncertainties that could cause actual results to differ materially from those contemplated by the forward-looking information. These risks and uncertainties are discussed in the Management Discussion and Analysis contained in the 2002 annual report, which is filed with SEDAR and posted on InnVest’s Web site at [www.innvestreit.com](http://www.innvestreit.com).

InnVest disclaims any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, unless required to do so by applicable securities laws.

### Key Performance Indicators

The key measures that indicate the strength of the hotel industry throughout the economic cycle and the relative strength of participants in the industry are Occupancy, Average Daily Rates (“ADR”) and Revenue per Available Room (“RevPAR”). These key performance indicators for the REIT by geographic region in Canada for the three months ended March 31, 2003 are as follows:

	Ontario	Quebec	Atlantic	Western	Total
Occupancy	54.6%	58.1%	52.8%	44.6%	53.6%
Average Daily Rate	\$ 82.28	\$ 79.87	\$ 68.98	\$ 63.83	\$ 77.79
Revenue per Available Room	\$ 44.93	\$ 46.40	\$ 36.41	\$ 28.47	\$ 41.69

### Seasonality

Revenues earned from hotel operations fluctuate throughout the year, with the first quarter being the lowest as leisure travel tends to be lower and the third quarter being the highest due to the increased level of leisure travel in the summer months. As a result, the hotel portfolio typically incurs a loss in the first quarter and this is not indicative of results for the year.

### Historical Operating Results Comparison

InnVest has audited results for the 159 days from July 26, 2002 to December 31, 2002 and unaudited results for the three months ended March 31, 2003. The following is therefore a year over year comparison using unaudited first quarter figures for 2002, with adjusted first quarter figures for 1999-2001, which were included in the annual numbers reported in the IPO dated July 18, 2002. Management fees have been adjusted in the comparative amounts to reflect the current management fee arrangement with Westmont. Occupancy and RevPAR statistics have been adjusted to reflect that all rooms in the portfolio are available to rent each day, whereas previously reported figures, including those in the IPO, removed rooms under repair from total available rooms. These changes, which are not considered material, were made so that year over year RevPAR variances are more comparable.

## Historical Operating Results for the three months ended March 31<sup>(1)</sup>

	2003	2002	Var %	2001	2000	1999
Occupancy	53.6%	54.9%	(2.4%)	54.7%	54.4%	57.5%
Average daily rates	\$ 77.79	\$ 76.03	2.3%	\$ 78.04	\$ 75.86	\$ 70.37
Revenue per available room	\$ 41.69	\$ 41.74	(0.1%)	\$ 42.69	\$ 41.27	\$ 40.46
Room revenue	\$ 43,335	\$ 43,234	0.2%	\$ 43,914	\$ 42,879	\$ 41,634
Total revenue	\$ 47,305	\$ 47,275	0.1%	\$ 48,472	\$ 47,306	\$ 45,970
Gross operating profit <sup>(2)</sup>	\$ 17,899	\$ 18,675	(4.2%)	\$ 19,766	\$ 19,511	\$ 18,880
Gross operating profit margin	37.8%	39.5%	(4.3%)	40.8%	41.2%	41.1%
Hotel operating income	\$ 11,956	\$ 12,880	(7.2%)	\$ 14,324	\$ 14,648	\$ 13,772
Hotel operating income margin	25.3%	27.2%	(7.0%)	29.6%	31.0%	30.0%

(1) Unaudited data for the three months ended March 31, 2003 and unaudited data for the comparative periods, which were adjusted to reflect the current management fee arrangement.

(2) Gross operating profit is defined as hotel revenues less hotel operating expenses and management fees.

## Comparison to Previous Year

### Revenues

Hotel revenues consist primarily of revenue generated from room occupancy. Revenue from food and beverage services and other miscellaneous revenue streams associated with hotel operations such as space leases, vending commissions, movie rentals, parking and telephone are also included and account for approximately 8% of the total revenue of the hotel portfolio.

Room revenues for the three months ended March 31, 2003 were \$43.3 million, 0.2% higher than the \$43.2 million generated for the same period in 2002. In the first quarter of 2003, occupancy for the hotel portfolio decreased by 2.4% from 54.9% in the first quarter of 2002 to 53.6%, while average daily rate ("ADR") increased by 2.3% from \$76.03 to \$77.79 for a RevPAR decrease of 0.1% to \$41.69.

The 0.1% decrease in RevPAR for the REIT's hotel portfolio compares with a 1.1% increase in RevPAR for the limited service sector of the Canadian hotel industry. The overall Canadian hotel industry posted a RevPAR increase in the first quarter over 2002 of 1.9%. In the first quarter 2002 hotels now owned by InnVest had nearly \$1.2 million of one time crew business from an oil and gas project in Edmonton, Alberta. This crew business provided significant room revenue to InnVest's Edmonton hotels through the end of the third quarter in 2002. InnVest outperformed the market in Eastern Canada and Quebec, and Western Canada after adjusting for the one time crew business, and under performed the industry in Ontario. InnVest's portfolio demonstrated its stability and resiliency in room revenue and total revenue in a difficult operating environment.

### Gross Operating Profit and Margin

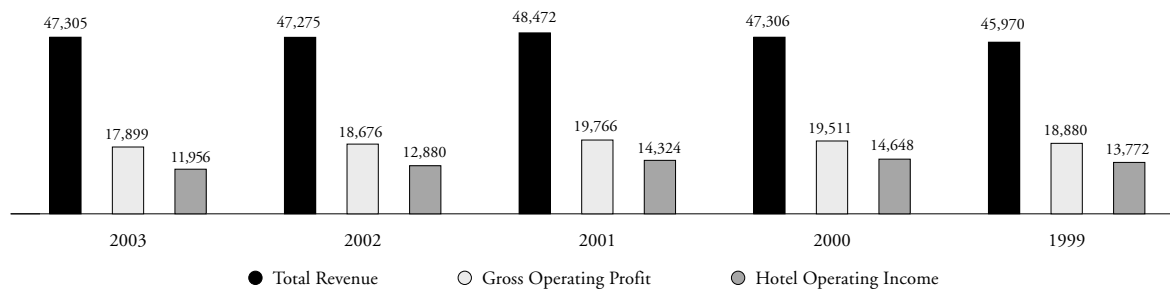
The gross operating profit for the first quarter decreased by 4.2% or \$776, from \$18.7 million in 2002 to \$17.9 million in 2003, primarily because of an increase in energy costs of \$651. There was an overall increase in electricity prices in Ontario and consumption increases in electricity and natural gas from the effects of the colder and longer than normal winter across the country. Direct room expense increases, particularly wages and benefits and repairs and maintenance, were substantially offset by a reduction in administrative and general expenses achieved through the continuation of cost control initiatives introduced in 2002. The gross operating profit margin decreased from to 39.5% to 37.8%, primarily reflecting increases in energy costs.

## Hotel Operating Income

Hotel operating income declined to \$12.0 million from \$12.9 million in the first quarter of 2002 despite slightly higher revenues mainly because of a \$651 increase in energy costs and a \$148 increase in property taxes and insurance net of decreases in operating lease expenses.

Historical revenues, gross operating profit, and hotel operating income, and accordingly the cash flow stream produced by the hotel portfolio, is demonstrated in the chart below.

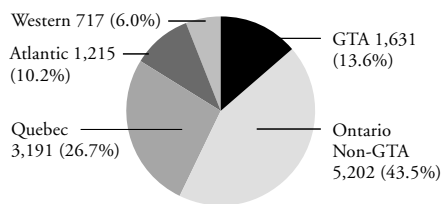
For the three months ended March 31



	2003	2002	2001	2000	1999
Revenue change	0.1%	(2.5%)	2.5%	2.9%	
Gross operating profit margin	37.8%	39.5%	40.8%	41.2%	41.1%
Hotel operating income margin	25.3%	27.2%	29.6%	31.0%	30.0%

Contributing to the hotel operating income margin decrease from 1999 to 2003, were increases in fixed costs such as property taxes and insurance, of \$670 or 14.9% and \$310 or 195% respectively, as well as an increase of \$900 or 36% in energy costs, over that period.

Hotel operating income generated by geographical region for the three months ended March 31, 2003 is shown in the chart below:



## Comparison to Forecast

The following table summarizes the actual results and the forecast provided in the IPO prospectus dated July 18, 2002 for the hotel portfolio and the franchise business for the three months ended March 31, 2003.

## Financial Highlights Summary

<i>For the three months ended March 31, 2003</i>	Actual		Forecast		Variance
Hotel revenues	\$	47,305	\$	48,647	\$ (1,342)
Hotel expenses		35,349		35,139	(210)
Hotel operating income		11,956		13,508	(1,552)
EBITDA <sup>(1),(2)</sup>		11,480		12,966	(1,486)
Net loss	\$	(2,354)	\$	(1,547)	\$ (807)
Net loss per unit					
– basic	\$	(0.11)	\$	(0.09)	\$ (0.02)
– diluted	\$	(0.11)	\$	(0.09)	\$ (0.02)
Net loss	\$	(2,354)	\$	(1,547)	\$ (807)
Add / (deduct)					
Depreciation and amortization		7,598		7,762	(164)
Future income tax recovery		(542)		(542)	–
Non-cash executive and trustee compensation		102		–	102
Funds from operations	\$	4,804	\$	5,673	\$ (869)
Funds from operations per unit					
– basic	\$	0.07	\$	0.09	\$ (0.02)
– diluted	\$	0.07	\$	0.09	\$ (0.02)
Funds from operations	\$	4,804	\$	5,673	\$ (869)
Amortization of fair value debt adjustment		(341)		(341)	–
Amortization of deferred financing costs		366		363	3
Reserve for replacement of furniture, fixtures and equipment and capital improvements		(1,892)		(1,946)	54
Convertible debenture interest		(1,828)		(1,828)	–
Distributable income <sup>(2)</sup>	\$	1,109	\$	1,921	\$ (812)
Distributable income per unit <sup>(3)</sup>					
– basic	\$	0.03	\$	0.05	\$ (0.02)
– diluted	\$	0.03	\$	0.05	\$ (0.02)
Distributions	\$	11,553	\$	11,553	\$ –
Distributions – per unit	\$	0.28	\$	0.28	\$ –

(1) EBITDA – Earnings before interest, income taxes, capital taxes and depreciation and amortization.

(2) EBITDA and distributable income are measures of earnings and cash flow that are not required under Canadian generally accepted accounting principles, and accordingly, may not be comparable to similar measures used by other organizations.

(3) Distributable income per unit has been calculated on a basis consistent with that prescribed by Canadian generally accepted accounting principles for calculating earnings per unit.

## Hotel Revenues

For the three months ended March 31, 2003, revenues were \$47.3 million, which is \$1.3 million or 2.8% less than the forecast. The shortfall can be attributed to the continued delay in the predicted economic recovery, the deterioration in the geopolitical situation related to Iraq and, in the Greater Toronto Area, concerns in March about the outbreak of SARS.

## Hotel Expenses

For the reporting period, hotel expenses of \$35.3 million were \$210 or 0.6% higher than the forecast. This increase was entirely attributable to higher energy costs related to electricity prices in Ontario and increased energy consumption as the result of the colder and longer than normal winter across the country, partially offset by the continued cost management initiatives implemented in 2002.

## Hotel Operating Income

Hotel operating income for the reporting period was \$12.0 million, compared with the forecast of \$13.5 million. Of the \$1.5 million shortfall from the forecast, 33% was accounted for in January, 19% in February and 48% in March.

## Other Income and Expenses

Other income and expenses consist of interest on mortgages, corporate and administrative costs, capital tax, franchise business income, other income and depreciation and amortization.

The net amount of other income and expenses for the reporting period was \$14.5 million of expenses, \$745 less than the forecast. This improvement from the forecast reflects interest costs that were \$518 below forecast and franchise business income that was \$57 above forecast. Depreciation and amortization was below the forecast by \$161, the cumulative result of less refurbishment work completed in 2002 than was forecast.

The savings in interest expense are expected to continue through June 30, 2003 for a total savings to the forecast of approximately \$1.6 million. The savings are being achieved by the locking in of \$211.0 million of mortgage debt for an average term of 5.1 years at base rates of 0.74% less than forecast in the IPO.

## Income Taxes

Income tax recovery for the period was \$225. This includes the future income tax recovery recorded as a result of the difference between depreciation for accounting purposes and the lesser amount allotted as capital cost allowance for income tax purposes for the reporting period, and large corporations tax.

Current income taxes and the draw down on future income taxes are consistent with the forecast. The REIT estimates that approximately 21% of the planned level of distributions made in 2003 will not be currently taxable to Unitholders.

## Net Loss

Net loss for the reporting period was \$2.4 million or \$0.11 per unit – basic (diluted – \$0.11) versus the forecast a net loss of \$1.5 million or \$0.09 per unit – basic (diluted – \$0.09).

## Distributable Income

Distributable income for the reporting period was \$1.1 million or \$0.03 per unit – basic (diluted – \$0.03), compared with the forecast of \$1.9 million or \$0.05 per unit – basic (diluted – \$0.05). Cash distributions for the reporting period were \$11.6 million or \$0.28 per unit, consistent with the forecast distributions.

---

## Changes in Financial Condition

### Investing Activities

During the reporting period, hotel properties and licence contracts decreased by \$5.6 million, being the net of capital additions and depreciation.

In the reporting period, other investing activities were limited to capital expenditures as part of the regular refurbishment program and the setting aside of 4% of revenues for the furniture, fixture and equipment reserve ("FF&E reserve") shown as restricted cash in the financial statements. For the three months ended March 31, 2003 a total amount of \$2.0 million was spent on capital items, which was in line with the forecast. The FF&E reserve increased by \$1.9 million (before capital expenditures), or \$54 less than the amount included in the forecast.

The normal reserve for replacement of furniture, fixtures and equipment and capital improvements is managed over the longer term. This reserve is maintained to ensure that the properties remain competitive in their markets. During the balance of 2003, approximately \$6 million will be spent as part of the refurbishment program.

The REIT intends to follow a program of completing a significant amount of its property refurbishing work in the fourth and first quarters in order to minimize the revenue reduction caused by having rooms out of service.

### Financing Activities

Total regular scheduled principal payments during the reporting period were \$1.9 million.

### Liquidity and Capital Resources

Liquidity was generated from cash flow from hotel operations, an available bank operating line and by the ability to finance certain unencumbered or under-leveraged assets. Funds from operations before changes in working capital were \$4.8 million compared with the forecast of \$5.7 million.

During the reporting period, the REIT distributed \$11.6 million or \$0.28125 per unit and a regular monthly distribution of \$0.09375 per unit for the month of March 2003 was paid in April 2003.

The REIT has an unused operating loan facility of \$25 million and four hotel properties that remain unencumbered that could generate approximately \$6.3 million in mortgage proceeds based on 50% loan to value. The REIT also has an unused acquisition facility of \$40 million available to acquire hotel properties and an unused loan facility of \$24 million to fund 50% of capital expenditures incurred.

The REIT has a \$100 million mortgage loan facility with its main mortgage lender available to repay mortgage debts held by its various other lenders as they mature. Consequently, the REIT has minimal refinancing risk until 2006.

### Outlook

The same factors that affected revenues in the second half of 2002 continued in the first quarter of 2003 and were intensified by travel concerns related to the war in Iraq and to the SARS outbreak late in the quarter, which severely impacted tourism and business primarily in the Greater Toronto Area.

With the end of the war in Iraq, the anticipated containment of the SARS outbreak and promotional support for tourism by various levels of government, we are cautiously optimistic that business will return to normal levels this year. We continue to expect a shortfall from our IPO forecast for the second quarter of 2003, but expect to have sufficient cash flow to maintain forecast cash distributions. In order to safeguard cash flow, we continue to intensify our sales and marketing efforts and to closely monitor expenses.

Prior to the unusual pressures on the hotel industry in the first quarter, we were seeing a number of positive factors, including strong leisure travel and an improving supply/demand balance of hotel rooms in major markets. When the effects of the geopolitical and health related developments abate and the economy strengthens, we expect to see improving operating results. Our current priority continues to be to maximize revenues through sales and marketing initiatives and to continue to control operating costs.

CONSOLIDATED BALANCE SHEET

<i>(in thousands of dollars)</i>	March 31, 2003	December 31, 2002
	<i>(unaudited)</i>	
<b>Assets</b>		
<b>Current Assets</b>		
Cash	\$ 11,337	\$ 26,730
Accounts receivable	8,266	7,499
Prepaid expenses and other assets	4,152	3,865
	23,755	38,094
Restricted cash	11,947	12,075
Hotel properties (Note 2)	845,065	850,314
Licence contracts	25,420	25,749
Deferred financing costs	6,314	6,680
	\$ 912,501	\$ 932,912
<b>Liabilities</b>		
<b>Current Liabilities</b>		
Accounts payable and accrued liabilities	\$ 21,838	\$ 18,558
Distributions payable	3,851	3,851
Acquisition related liabilities	4,017	9,275
Current portion of long-term debt (Note 3)	8,633	8,976
	38,339	40,660
Long-term debt (Note 3)	308,590	310,486
Future income tax liability	121,191	121,733
	468,120	472,879
<b>Equity</b>		
Unitholders' equity	369,225	385,033
Convertible debentures (Note 5)	75,156	75,000
	444,381	460,033
	\$ 912,501	\$ 932,912

The accompanying notes are an integral part of these consolidated financial statements.



CONSOLIDATED STATEMENT OF NET INCOME

*For the three months ended March 31, 2003 (in thousands of dollars, except per unit amounts) (Unaudited)*

Hotel revenues	\$	47,305
Hotel expenses		
Operating expenses		27,805
Property taxes, rent and insurance		5,943
Management fees		1,601
		35,349
Hotel operating income		11,956
Other (income) and expenses		
Interest on mortgages		5,600
Corporate and administrative		746
Capital tax		495
Franchise business income		(217)
Other income		(53)
Depreciation and amortization		7,964
		14,535
Loss before income tax expense		(2,579)
Income tax expense (recovery)		
Current		317
Future		(542)
		(225)
Net loss	\$	(2,354)
Net loss per unit – basic (Note 6)	\$	(0.11)
– diluted (Note 6)	\$	(0.11)

The accompanying notes are an integral part of these consolidated financial statements.

There are no comparative figures as the REIT began operations on July 26, 2002.

CONSOLIDATED STATEMENT OF UNITHOLDERS' EQUITY

*For the three months ended March 31, 2003 (in thousands of dollars) (Unaudited)*

Balance at December 31, 2002	\$	385,033
Costs incurred regarding the Distribution Reinvestment Plan (Note 5)		(19)
Executive and trustee compensation (Note 5)		102
Net loss		(2,354)
Convertible debenture interest and accretion (Note 5)		(1,984)
Unit distributions		(11,553)
Closing unitholders' equity	\$	369,225

The accompanying notes are an integral part of these consolidated financial statements.

There are no comparative figures as the REIT began operations on July 26, 2002.



## CONSOLIDATED STATEMENT OF CASH FLOWS

For the three months ended March 31, 2003 (in thousands of dollars) (Unaudited)

### Operating Activities

Net loss	\$	(2,354)
Add (deduct) items not affecting funds from operations		
Depreciation and amortization		7,598
Future income tax recovery		(542)
Non-cash executive and trustee compensation		102
Funds from operations		4,804
Amortization of fair value debt adjustment		(341)
Amortization of deferred financing costs		366
Changes in non-cash working capital		(2,616)
		2,213

### Financing Activities

Repayment of long-term debt		(1,898)
Costs incurred regarding the Distribution Reinvestment Plan		(19)
Unit distributions		(11,553)
Changes in non-cash working capital related to financing activities		(416)
Convertible debenture interest		(1,828)
		(15,714)

### Investing Activities

Capital expenditures on hotel properties		(2,020)
Decrease in restricted cash		128
		(1,892)
Decrease in cash during the period		(15,393)
Cash, beginning of period		26,730
Cash, end of period	\$	11,337
Supplemental disclosure of cash flow information:		
Cash paid for interest	\$	5,930
Cash paid for income taxes (including capital tax)	\$	1,025

The accompanying notes are an integral part of these consolidated financial statements.

There are no comparative figures as the REIT began operations on July 26, 2002.

As at March 31, 2003 (unaudited) (all dollar amounts are in thousands, except per unit amounts)

## 1. Basis of Presentation

InnVest Real Estate Investment Trust (the "REIT") is an unincorporated open-ended real estate investment trust governed by the laws of Ontario. The REIT was established pursuant to a declaration of trust dated January 1, 2002. On July 25, 2002, the REIT raised \$300,000 (before issue costs) by issuing units on the Toronto Stock Exchange. These proceeds together with the issue of additional units and convertible debentures were utilized to acquire a portfolio of 114 Canadian hotels with 11,602 guest rooms operated under international brands. These consolidated financial statements represent operations for the three months ended March 31, 2003. The REIT began operations on July 26, 2002 therefore there are no comparatives.

The accompanying unaudited interim consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). These financial statements are consistent with those used in the annual consolidated financial statements. They do not include all the information and disclosure required by Canadian GAAP for annual financial statements, and should be read in conjunction with the annual consolidated financial statements.

Revenues earned from hotel operations fluctuate throughout the year, with the third quarter being the highest due to the increased level of leisure travel in the summer months, and the first quarter being the lowest as leisure travel tends to be lower at that time of the year.

## 2. Hotel Properties

	Cost	Accumulated Depreciation	Mar. 31, 2003 Net Book Value	Dec. 31, 2002 Net Book Value
Land	\$ 58,801	\$ —	\$ 58,801	\$ 58,801
Buildings	753,431	12,884	740,547	744,798
Furniture and equipment	52,567	6,850	45,717	46,715
	\$ 864,799	\$ 19,734	\$ 845,065	\$ 850,314

## 3. Long-term Debt

	Mar. 31, 2003	Dec. 31, 2002
Mortgages payable	\$ 317,223	\$ 319,462
Less: current portion	8,633	8,976
Total long-term debt	\$ 308,590	\$ 310,486

Substantially all of the REIT's assets have been pledged as security under various debt agreements. At March 31, 2003, long-term debt has a weighted average interest rate of 7.6% (December 31, 2002 – 7.6%). The long-term debt is repayable in blended monthly payments of principal and interest totalling \$2,610 (December 31, 2002 – \$2,610) per month, and matures at various dates from May 1, 2003 to October 1, 2018.

Scheduled repayment of long-term debt is as follows:

2003 remainder	\$ 6,737
2004	6,277
2005	4,983
2006	141,213
2007	8,061
2008 and thereafter	149,952
	\$ 317,223

The current portion of long-term debt on the balance sheet is based on the twelve months ended March 31, 2003, whereas the repayment schedule above reflects the fiscal year.

The estimated fair value of the REIT's long-term debt at March 31, 2003 is approximately \$315,009 (December 31, 2002 – \$319,119). This estimate was determined by discounting expected cash flows at the interest rates currently being offered to the REIT for debt of the same remaining maturities.

Long-term debt includes \$5,950 of mortgages payable, which are subject to floating interest rates. Interest expense will increase by \$60 for every 1% increase in the base Bankers' Acceptance rate.

The REIT has a \$100,000 mortgage loan facility with its main mortgage lender available to repay mortgage debts held by its various other lenders, as they mature.

#### 4. Guarantees

Effective January 1, 2003, the Company is required to disclose its obligations undertaken in issuing certain guarantees on the date the guarantee is issued or modified. Where the company expects to make a payment in respect of the guarantee, a liability will be recognized to the extent that one has not yet been recognized.

InnVest has not provided to third parties any significant guarantees other than the following:

##### Trustee and officer indemnification agreements

InnVest has entered into indemnification agreements with its trustees and officers to indemnify them, to the extent permitted by law, against any and all charges, costs, expenses, amounts paid in settlement and damages incurred by the trustees and officers as a result of any lawsuit or any other judicial, administrative proceeding in which the trustees and officers are sued as a result of their service. These indemnification claims will be subject to any statutory or other legal limitation period. The nature of the indemnification agreements prevents InnVest from making a reasonable estimate of the maximum potential amount it could be required to pay to counter parties. InnVest has purchased trustees' and officers' liability insurance. No amount has been recorded in the financial statements with respect to these indemnification agreements.

#### 5. Unitholders' Equity

The REIT was established pursuant to a declaration of trust dated January 1, 2002 when one unit was issued for ten dollars. The REIT is authorized to issue an unlimited number of units, each of which represents an equal undivided beneficial interest in any distributions from the REIT. All units are of the same class with equal rights and privileges.

	Units		Amount
Balance at December 31, 2002	41,075,910	\$	387,744
Units issued to trustees of the REIT	6,810		60
Balance at March 31, 2003	41,082,720	\$	387,804

##### Trustee Compensation Plan

The members of the Board of Trustees receive 50% of their annual retainer in units (based on the then current market price of the units). The REIT has set aside 100,000 units in reserve for this purpose.

##### Executive Compensation Plan

The senior executives participate in the executive compensation plan under which units are granted by the Board of Trustees from time to time. The REIT has reserved a maximum of 1,000,000 units for issuance under the plan. A unit granted through the plan entitles the holder to receive on the vesting date the then current fair market value of the unit plus the value of the cash distributions that would have been paid on the unit if it had been issued on the date of grant assuming the reinvestment of the distribution into REIT units. The payment will be satisfied through the issuance of units.

On July 17, 2002, the Board of Trustees approved the granting of 49,500 units to the senior executives for services rendered. The units granted on July 17, 2002 vest equally over a three year period on each annual anniversary date of grant.

The following table summarizes the status of the executive compensation plan at March 31, 2003:

Date of Grant	Executive Units Declared	Units Accumulated from Distributions	Total Units
July 17, 2002	49,500	3,721	53,221

---

## Convertible Debentures

The convertible debentures bear interest at the rate of 9.75% per annum payable semi-annually in arrears and mature on June 30, 2007. Each \$1 principal amount of convertible debentures is convertible at the option of the holder into 93.0233 units (representing a conversion price of \$10.75 per unit). The convertible debentures are redeemable, in whole or from time to time in part, on and after July 1, 2005 at the option of the REIT, provided that the volume-weighted average trading price of the units for a stipulated period prior to the date on which the notice of redemption is given exceeds 115% of the conversion price. The REIT has the option to satisfy its obligation to pay the principal amount of the convertible debentures due at maturity or upon redemption, in whole or in part, by issuing the number of units equal to the principal amount of convertible debentures then outstanding divided by 95% of the volume-weighted average trading price of the units for a stipulated period prior to the date of redemption or maturity, as applicable.

In accordance with Canadian GAAP, the holder conversion option was valued separately from the Convertible Debentures at \$2,850, being the estimated fair market value of the option on the date the security was issued. The debenture discount equal to the value of the option is being accreted to Unitholders' equity over the term of the Convertible Debentures.

The convertible debenture balance has been recorded as equity as the REIT has the ability to satisfy its obligations (principal and interest) under the terms of such instrument through the issue of units.

## Distribution Reinvestment Plan (DRIP)

The REIT has a DRIP whereby eligible Canadian unitholders may elect to have their distributions of income from the REIT automatically reinvested in additional units. Unitholders who so elect will receive a further bonus distribution of units equal in value to 3% of each distribution that was reinvested.

## 6. Per Unit Information

Net loss per unit calculations are based on the following:

		Weighted Average Units
Net loss	\$ (2,354)	41,082,720
Convertible debenture interest and accretion	(1,984)	–
Net loss – basic	(4,338)	41,082,720
Dilutive effect of executive compensation plan	–	7,268
Net loss – diluted	\$ (4,338)	41,089,988

Distributable income per unit calculations are based on the following (Note 7):

		Weighted Average Units
Distributable income – basic	\$ 1,109	41,082,720
Dilutive effect of executive compensation plan	–	7,268
Distributable income – diluted	\$ 1,109	41,089,988

Funds from operations per unit calculations are based on the following:

		Weighted Average Units
Funds from operations	\$ 4,804	41,082,720
Convertible debenture interest	(1,828)	–
Funds from operations – basic	2,976	41,082,720
Dilutive effect of executive compensation plan	–	7,268
Funds from operations – diluted	\$ 2,976	41,089,988
Funds from operations per unit – basic	\$ 0.07	
– diluted	\$ 0.07	

The convertible debentures have been excluded from all diluted calculations because the impact of this conversion would not be dilutive.



In addition, salaries of REIT employees paid by Westmont and reimbursed by the REIT, were \$81. Included in accounts payable and accrued liabilities are amounts payable to Westmont at March 31, 2003 totalling \$916 (December 31, 2002 – \$722).

## 9. Segmented Financial Information

The REIT operates hotel properties throughout Canada. Information related to these properties by geographic segment is presented below. The accounting policies used in the preparation of the segmented information are the same as those described for the REIT in the annual consolidated financial statements. The REIT primarily evaluates operating performance based on hotel operating income. All key financing, investing and capital allocation decisions are centrally managed.

<i>Three months ended March 31, 2003</i>	Western	Ontario	Quebec	Atlantic	Total
Hotel revenues	\$ 5,110	\$ 26,165	\$ 11,507	\$ 4,523	\$ 47,305
Hotel expenses	4,393	19,332	8,316	3,308	35,349
Hotel operating income	\$ 717	\$ 6,833	\$ 3,191	\$ 1,215	\$ 11,956
Capital expenditures	\$ 267	\$ 1,313	\$ 432	\$ 8	\$ 2,020
Hotel properties					
March 31, 2003	\$ 67,251	\$ 480,826	\$ 194,232	\$ 102,756	\$ 845,065
December 31, 2002	\$ 67,686	\$ 483,537	\$ 195,492	\$ 103,599	\$ 850,314

EXECUTIVE OFFICE

5090 Explorer Drive  
7th Floor  
Mississauga, Ontario  
L4W 4T9  
Phone: 905-206-7100  
Fax: 905-206-7114  
Web: [www.innvestreit.com](http://www.innvestreit.com)

TRANSFER AGENT AND REGISTRAR

Computershare Trust Company of Canada  
100 University Avenue  
Toronto, Ontario  
M5J 2Y1  
Toll: 1-800-663-9097

STOCK EXCHANGE LISTING

Toronto Stock Exchange  
Trading Symbol: INN.UN