

ROYAL HOST REAL ESTATE INVESTMENT TRUST

Consolidated Interim Financial Statements

For the three months ended March 31, 2003 and March 31, 2002

(Unaudited)

ROYAL HOST REAL ESTATE INVESTMENT TRUST
Consolidated Interim Balance Sheets
\$000's (Unaudited)

	As At	
	March 31, 2003	December 31, 2002
	<u> </u>	<u> </u>
ASSETS		
Current Assets		
Cash and short-term investments	5,134	16,106
Accounts and notes receivable	8,302	9,430
Deposits and prepaid expenses	4,022	3,783
Inventories	3,812	3,885
Property under development	1,107	340
Future income taxes	2,487	195
	<u>24,864</u>	<u>33,739</u>
Restricted Cash (Note 3)	4,348	4,159
Deposits on Purchase of Capital Assets (Note 11)	12,778	-
Capital Assets (Note 5)	326,362	327,818
Long-term Notes Receivable and Other Assets	<u>5,611</u>	<u>5,012</u>
	<u>373,963</u>	<u>370,728</u>
LIABILITIES AND EQUITY		
Current Liabilities		
Accounts payable and accrued liabilities	18,811	18,366
Current portion of mortgages and other debt (Note 6)	39,305	36,307
Current portion of capital leases (Note 7)	1,100	1,208
Distributions payable	1,670	1,667
Other current liabilities	1,733	2,118
	<u>62,619</u>	<u>59,666</u>
Mortgages and Other Debt (Note 6)	112,563	104,933
Capital Leases (Note 7)	977	1,125
Future Income Taxes	635	792
Deferred Revenue	1,397	1,478
Equity (Note 8)	<u>195,772</u>	<u>202,734</u>
	<u>373,963</u>	<u>370,728</u>

See accompanying Notes to Consolidated Financial Statements

ROYAL HOST REAL ESTATE INVESTMENT TRUST
Consolidated Interim Statements of Net Loss
For the three months ended March 31, 2003 and March 31, 2002
\$000's (Unaudited)

	Three Months Ended	
	March 31,	March 31,
	2003	2002
Hospitality Revenues		
Rooms	20,372	18,154
Food and beverage	5,233	4,560
Other hospitality revenues	4,192	4,316
	29,797	27,030
Hospitality Expenses	24,867	21,304
Gross Margin	4,930	5,726
Other (Income) and Expenses		
Interest income	(83)	(83)
Interest on mortgages and other debt	3,142	3,305
Trust administration	460	397
Capital and other taxes	49	67
Future income taxes (recovery)	(2,449)	51
Amortization	4,696	4,352
	5,815	8,089
Net Loss (Note 4)	(885)	(2,363)
Per unit net loss		
- basic (Note 4)	(0.11)	(0.16)
- diluted (Note 4)	(0.12)	(0.16)

See accompanying Notes to Consolidated Financial Statements

ROYAL HOST REAL ESTATE INVESTMENT TRUST
Consolidated Interim Statements of Cash Flows
For the three months ended March 31, 2003 and March 31, 2002
\$000's (Unaudited)

	Three Months Ended	
	March 31, 2003	March 31, 2002
CASH PROVIDED BY (USED IN)		
Operating Activities		
Net loss	(885)	(2,363)
Items not affecting cash:		
Amortization of capital assets	4,512	4,024
Future income tax (recovery) expense	(2,449)	51
Funds from operations	<u>1,178</u>	<u>1,712</u>
Change in non-cash working capital:		
Decrease in accounts and notes receivable	1,128	2,023
Increase in deposits and prepaid expenses	(239)	(360)
Decrease in inventories	73	85
Increase in accounts payable and accrued liabilities	445	407
Decrease in other current liabilities and deferred revenue	(466)	(344)
Amortization of deferred finance costs	184	328
	<u>2,303</u>	<u>3,851</u>
Financing Activities		
Additions to mortgages and other debt	11,403	-
Principal repayments on mortgages and other debt and capital leases	(1,123)	(19,785)
Payments on trust units under employee unit purchase plan	37	-
Issuance of convertible debentures	-	40,000
Equity financing issue costs	-	(1,722)
Equity distributions (Note 8(b))	(6,111)	(5,582)
	<u>4,206</u>	<u>12,911</u>
Investing Activities		
Restricted cash (Note 3)	(189)	(103)
Deposits on purchase of capital assets (Note 11)	(12,778)	-
Capital expenditures	(2,964)	(1,079)
Property under development	(767)	-
Increase in long-term notes receivable and other assets	(783)	(379)
	<u>(17,481)</u>	<u>(1,561)</u>
Net Change in Cash and Short-term Investments	(10,972)	15,201
Cash and Short-term Investments, beginning of period	16,106	9,007
Cash and Short-term Investments, end of period	5,134	24,208

See accompanying Notes to Consolidated Financial Statements

ROYAL HOST REAL ESTATE INVESTMENT TRUST
Notes to Consolidated Interim Financial Statements
As at March 31, 2003 and March 31, 2002
(Unaudited)

1. GENERAL INFORMATION

Royal Host Real Estate Investment Trust ("Royal Host") was created pursuant to the Declaration of Trust dated August 27, 1997. Royal Host is an unincorporated closed-end mutual fund trust established for the purpose of investing in hotel properties and hospitality businesses, under specified guidelines as defined under the Declaration of Trust.

These consolidated interim financial statements follow the same accounting policies and methods as the most recent annual financial statements. These financial statements include all adjustments necessary to present fairly the results for the interim period. Certain information and footnote disclosures normally included in the year-end consolidated financial statements have been condensed or omitted. In the opinion of Management, all adjustments (consisting of normal recurring accruals) considered necessary for fair presentation have been included. Operating results for the three months ended March 31, 2003 are not necessarily indicative of the results that may be expected for the year ending December 31, 2003 due to the seasonal nature of operations. These interim financial statements should be read in conjunction with the most recent annual financial statements and notes included in Royal Host's annual report for the year ended December 31, 2002.

2. NON-GAAP MEASURES REPORTING

Cash available for distribution is calculated as net earnings before amortization of capital assets, amortization of deferred financing fees and future income tax (recovery) expense less the capital replacement reserve. This amount is determined in accordance with the Declaration of Trust and is intended to approximate Royal Host's taxable income, which is distributed to unitholders. Special charges and the capital replacement reserve are determined at the discretion of the Board of Trustees. Readers are cautioned that cash available for distribution is not a defined measure of performance under Canadian generally accepted accounting principles ("GAAP"). Royal Host's calculation of cash available for distribution may be different than similar calculations used by other comparable entities.

3. RESTRICTED CASH

Restricted cash is \$4,348,000 (December 31, 2002 - \$4,159,000) representing funds on deposit with lenders for future planned capital expenditures within the next 12 months.

ROYAL HOST REAL ESTATE INVESTMENT TRUST
Notes to Consolidated Interim Financial Statements
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(Unaudited)

4. CASH AVAILABLE FOR DISTRIBUTION AND PER UNIT COMPUTATIONS

There were 24,674,687 trust units outstanding as at March 31, 2003 (2002 – 24,138,035). Per unit computations are based on the weighted average number of trust units outstanding for the period, after adjusting the net earnings and cash available for distribution for payments on the convertible debentures of \$1,346,000 (2002 - \$819,000) and payments on the redeemable partnership units of \$567,000 (2002 - \$567,000).

For the three months ended:

	March 31, 2003			March 31, 2002		
	(\$000's)	Weighted Average Units (000's)	Per Unit	(\$000's)	Weighted Average Units (000's)	Per Unit
Earnings						
Net loss	(885)			(2,363)		
Less:						
Distributions on redeemable partnership units	(567)			(567)		
Interest on 8% convertible debentures	(434)			(434)		
Interest on 9.25% convertible debentures	(912)			(385)		
Basic loss	(2,798)	24,648	(0.11)	(3,749)	24,123	(0.16)
Unit options		907			907	
Unit option repurchase		(1,544)			(1,396)	
Diluted loss	(2,798)	24,011	(0.12)	(3,749)	23,634	(0.16)
 Cash available for distribution						
Net loss	(885)			(2,363)		
Add (deduct):						
Amortization of capital assets	4,512			4,024		
Amortization of deferred financing fees	184			328		
Future income tax (recovery) expense	(2,449)			51		
Cash available for distribution	1,362			2,040		
 Distributions on redeemable partnership units						
	(567)			(567)		
Interest on 8% convertible debentures						
	(434)			(434)		
Interest on 9.25% convertible debentures						
	(912)			(385)		
Basic adjusted cash available for distribution	(551)	24,648	(0.02)	654	24,123	0.03
Adjustment for impact of:						
Unit options		907				
Unit option repurchase		(1,544)				
Diluted adjusted cash available for distribution	(551)	24,011	(0.02)	654	24,123	0.03

ROYAL HOST REAL ESTATE INVESTMENT TRUST
Notes to Consolidated Interim Financial Statements
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(Unaudited)

In computing the diluted loss per unit for the three months ended March 31, 2003 and 2002, the convertible debentures and redeemable partnership units had an anti-dilutive impact on earnings and therefore did not impact the calculation.

In computing the diluted adjusted cash available for distribution for the three months ended March 31, 2003 and 2002, the convertible debentures and redeemable partnership units had an anti-dilutive impact on cash available for distribution and therefore did not impact the calculation.

Under the Royal Host capital replacement reserve policy, 3% of total hotel revenue is deducted from cash available for distribution to allow for the upkeep and renovation of the hotel properties. This policy may be amended from time to time at the discretion of the Trustees. On this basis, the reserve provided for the three months ended March 31, 2003 would have been \$850,000 (2002 - \$590,000). As Royal Host spent \$2,964,000, excluding capital leases to March 31, 2003 (2002 - \$1,079,000) to renovate and reposition the hotel properties, the Trustees have determined that no reserve would be provided for the three months ended March 31, 2003 and 2002.

ROYAL HOST REAL ESTATE INVESTMENT TRUST
Notes to Consolidated Interim Financial Statements
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(Unaudited)

5. CAPITAL ASSETS

	<i>(in \$000's)</i>		
	Gross Book Value	Accumulated Amortization	Net Book Value
March 31, 2003			
Land	38,241	-	38,241
Buildings	294,976	44,211	250,765
Furniture, fixtures and equipment	36,081	27,142	8,939
Furniture, fixtures and equipment under capital leases	5,770	2,355	3,415
Paving and other	1,283	353	930
	376,351	74,061	302,290
Properties under development	5,663	-	5,663
Intangible assets			
Franchise rights and management contracts	27,622	10,817	16,805
Customer lists and intellectual and human capital	7,270	5,666	1,604
	416,906	90,544	326,362
December 31, 2002			
Land	38,233	-	38,233
Buildings	294,237	42,185	252,052
Furniture, fixtures and equipment	35,486	25,758	9,728
Furniture, fixtures and equipment under capital leases	5,679	2,062	3,617
Paving and other	1,239	333	906
	374,874	70,338	304,536
Properties under development	4,051	-	4,051
Intangible assets			
Franchise rights and management contracts	27,655	10,196	17,459
Customer lists and intellectual and human capital	7,270	5,498	1,772
	413,850	86,032	327,818

All hotel properties are wholly-owned by Royal Host, except one hotel property representing less than 5% of total capital assets, which is jointly owned by Royal Host and the vendor. Pursuant to the Exchange Agreement dated September 11, 1998, the vendor has an option to exchange its 50% ownership interest for units of Royal Host. The valuation of such exchange is to be determined based on a specified industry average historic capitalization rate and the units of Royal Host are to be priced based on a 20 day weighted average trading price per unit. This specified capitalization rate is not determined with reference to a base-lending rate such as prime rate. This calculation has been taken into consideration in the diluted per unit calculations in Note 4 and determined to be anti-dilutive.

For discussion of capital replacement reserves in 2003 and 2002, see Note 4.

ROYAL HOST REAL ESTATE INVESTMENT TRUST
Notes to Consolidated Interim Financial Statements
As at March 31, 2003 and March 31, 2002
(Unaudited)

6. MORTGAGES AND OTHER DEBT

	<i>(in \$000's)</i>	
	March 31, 2003	December 31, 2002
Mortgages and other debt secured by hotel properties	151,868	141,240
Less current portion	39,305	36,307
Long-term obligations	112,563	104,933
Years ending March 31 <i>(in 000's)</i>		
2004	39,305	
2005	2,818	
2006	29,372	
2007	2,974	
2008	20,053	
Subsequent	57,346	
	151,868	
Supplementary Information:	March 31, 2003	March 31, 2002
Cash interest paid in the periods ending	3,142	3,211

On July 3, 2002, Royal Host completed financing arrangements in the amount of \$5,000,000, the proceeds to be used to renovate certain hotel properties. The loan is interest bearing at the bank's floating base rate. The loan is secured by first mortgages on the land and general security registered against certain hotel properties. As at March 31, 2003, Royal Host had received advances of funds in the amount of \$2,303,000 related to the arranged financing.

On February 6, 2003, Royal Host completed financing in the amount of \$6.0 million, the proceeds to be used for general working capital purposes. This is a revolving operating loan, repayable on demand, available to the Trust at prime rate plus 2.0% payable monthly in arrears or as a First Bank Acceptance with a Stamping Fee of 3.0% per annum. The loan is secured by a certain hotel property. As at March 31, 2003, Royal Host had received advances of funds in the amount of \$3,000,000 related to the arranged financing.

On February 5, 2003, Royal Host completed financing in the amount of \$6.2 million, the proceeds to be used for working capital and corporate purposes. This is an operating loan, repayable on demand; bearing interest at prime plus 1% per annum, with interest payable monthly. The loan is secured by a certain hotel property. As at March 31, 2003, no funds have been advanced by the lender.

On March 27, 2003, Royal Host completed two financings with one lender in the amounts of \$2.4 and \$3.7 million, the proceeds to be used for working capital and corporate purposes. These are 20 year term mortgage loans, secured by certain hotel properties. The interest is adjusted semi-annually and is the greater of:

- a) 3.2% over the yield on the Government of Canada mortgage benchmark bond; and
- b) A floor of 7.9% per annum.

As at March 31, 2003, all funds were advanced by the lender.

Financing charges are deferred and amortized over the term of the related debt. In 2003, \$184,000 has been included in amortization (2002 - \$328,000).

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7. OBLIGATIONS UNDER CAPITAL LEASES

Royal Host has entered into various capital lease obligations to acquire computers and hotel furniture, fixtures and equipment. The present values of minimum lease payments under capital lease as of March 31, 2003 are as follows:

	<u>March, 31</u> <u>2003</u>	<u>December 31,</u> <u>2002</u>
Present value of future minimum lease payments	2,077	2,333
Less current portion	1,100	1,208
Long-term obligations	<u>977</u>	<u>1,125</u>
Years ending March 31 <i>(in 000's)</i>		
2004	1,257	
2005	626	
2006	309	
2007	127	
2008	<u>20</u>	
Future minimum lease payments	2,339	
Amounts representing interest	<u>262</u>	
Present value of future minimum lease payments	<u>2,077</u>	

8. EQUITY

	<i>(in \$000's)</i>	
	<u>March 31,</u> <u>2003</u>	<u>December 31,</u> <u>2002</u>
Balance, beginning of period	113,234	130,988
Net (loss) earnings	(885)	8,136
Issuance of trust units		
Distribution reinvestment plan	225	720
Employee unit purchase program <i>(Note 8(g))</i>	-	2,320
Employee loans pursuant to		
employee unit purchase program <i>(Note 8(g))</i>	-	(2,320)
Employee loan payments pursuant to		
employee unit purchase program <i>(Note 8(g))</i>	37	95
Equity financing issue costs	-	(1,892)
Equity distributions		
Trust units	(4,426)	(17,611)
Redeemable partnership units	(567)	(2,269)
Interest paid on convertible debentures	<u>(1,346)</u>	<u>(4,933)</u>
	<u>106,272</u>	<u>113,234</u>
Convertible Equity		
Redeemable partnership units	27,500	27,500
Convertible debentures	<u>62,000</u>	<u>62,000</u>
	<u>89,500</u>	<u>89,500</u>
Balance, end of period	<u>195,772</u>	<u>202,734</u>

ROYAL HOST REAL ESTATE INVESTMENT TRUST
Notes to Consolidated Interim Financial Statements
As at March 31, 2003 and March 31, 2002
(Unaudited)

a) Unit Capital

	<u>Number of units</u>	<u>(in \$000's)</u>
Balance, December 31, 2001	24,115,846	219,868
Issuance of trust units		
Employee unit purchase program <i>(Note 8(g))</i>	400,000	2,320
Distribution reinvestment plan	119,130	720
Balance, December 31, 2002	24,634,976	222,908
Issuance of trust units		
Distribution reinvestment plan	39,711	225
Balance, March 31, 2003	24,674,687	223,133

As is common with REITs and other income trusts, Royal Host distributes cash in excess of the net earnings, and accordingly an accumulated deficit results, which at March 31, 2003 amounts to \$116,861,000 (December 31, 2002 - \$109,674,000).

b) Distributions to Unitholders

Cash available for distribution for the three months ended March 31, 2003 was \$1,362,000 (2002 - \$2,040,000) and distributions declared to Unitholders, excluding distributions on redeemable partnership units, aggregated \$4,426,000 (2002 - \$4,344,000) for the same period. The distributions to holders of redeemable partnership units for 2003 was \$567,000 (2002 - \$567,000) and interest on convertible debentures was \$1,346,000 (2002 - \$819,000).

On the consolidated statement of cash flows distributions paid are net of distribution reinvestment plan contributions of \$225,000 for the three months ended March 31, 2003 (2002 - \$147,000). Accordingly, gross distributions for the period were \$6,339,000 (2002 - \$5,730,000).

c) Distribution Reinvestment Plan

Royal Host has established a Distribution Reinvestment Plan ("DRIP") that is administered by its transfer agent and has reserved 500,000 units for issue under this Plan. For the period January 2001 to July 2001, the transfer agent purchased DRIP units on the open market. Subsequent to July 2001, Royal Host has issued new units for DRIP participants out of the previously authorized reserved units.

d) Unit Options

Royal Host has reserved 1,883,000 units under its unit option plan. As at March 31, 2003, Royal Host has unit options outstanding to certain directors, employees and consultants to purchase an aggregated total of 907,500 units (2002 - 907,500 units), ranging from \$10.00 to \$10.50 per unit. In 2003 and 2002, the weighted average exercise price is \$10.03. All unit options were issued prior to 1999 and were fully vested and exercisable at March 31, 2003 and December 31, 2002. These options expire on October 31, 2007 and on March 23, 2008. During 2003 and 2002, no options were issued or exercised and no options expired.

The adoption of Handbook Section 3870 - Stock Based Compensation Plans has no financial impact on the stock options under the existing stock option plan, which were issued prior to the date of adoption.

ROYAL HOST REAL ESTATE INVESTMENT TRUST
Notes to Consolidated Interim Financial Statements
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(Unaudited)

e) Redeemable Partnership Units

Holders of redeemable partnership units ("Holders") are entitled to receive distributions indirectly from Royal Host equivalent to the distributions paid by Royal Host to its Unitholders, commencing on January 1, 1999. Each partnership unit is redeemable by the Holders after January 1, 2000 at a cash price equal to the market value of a Royal Host unit, or at the option of Royal Host and subject to regulatory approval, one Royal Host unit or a combination thereof.

Under certain circumstances, including a change of control ("Trigger Event"), the Holders have the right to redeem the partnership units for cash proceeds of \$27.5 million. If the Trigger Event occurs after the issuance of redeemable units but prior to January 1, 2004, then the Holders may redeem the then outstanding redeemable partnership units for cash, at the greater of \$9.00 per unit or the market price of the Royal Host units. Change in control is defined as ownership by any one entity or a group of related entities of more than 20% of the outstanding units of Royal Host.

For accounting purposes, the redeemable partnership units have equity characteristics and accordingly, they are classified as equity instruments.

f) Convertible Debentures

i) 8.00% Convertible Secured Debentures

The convertible debentures of \$22,000,000 bear interest at 8% per annum and are payable monthly, at Royal Host's option, in either cash or Royal Host units of an equivalent value. In addition, upon maturity in 2003, Royal Host has the option to repay the debentures in either cash or in equivalent units of Royal Host on the basis that one unit has a value equal to the weighted average trading price of a unit on the Toronto Stock Exchange ("TSE") for the twenty (20) trading days immediately preceding the maturity date.

Based on certain conditions, the debentures are convertible, at the holders' discretion, at \$11.00 per trust unit for the period from October 1, 2001 to maturity at September 30, 2003.

ii) 9.25% Convertible Unsecured Subordinated Debentures

The convertible debentures of \$40,000,000 bear interest at 9.25% per annum and are payable semi-annually in arrears on March 1 and September 1 in each year commencing September 1, 2002.

On redemption or at maturity on March 1, 2007, Royal Host has the option to repay the debentures in either cash or in equivalent units of Royal Host. The number of units to be issued will be determined by dividing the principal amount of the debentures by 95% of the current market price of the units. The term "current market price" is defined in the Indenture to mean the weighted average trading price of the units on the TSE for the twenty (20) consecutive trading days ending on the fifth (5) trading day preceding the date of maturity.

The debentures will not be redeemable on or before March 1, 2005. Thereafter, the debentures will be redeemable, in whole at any time or in part from time to time, at the option of Royal Host on at least 30 days prior notice at a price equal to the principal amount thereof, plus accrued and unpaid interest, provided that the current market price preceding the date upon which notice of redemption is given is at least 125% of the conversion price of \$7.00 per unit.

Based on certain conditions, the debentures are convertible, at the holders' discretion, at \$7.00 per trust unit from date of issue to maturity at March 1, 2007.

For accounting purposes, the convertible debentures have equity characteristics and accordingly, they are classified as equity instruments.

ROYAL HOST REAL ESTATE INVESTMENT TRUST
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g) Employee Unit Purchase Program

During 2000, the Trustees approved the issuance of up to 400,000 units from treasury for an employee unit purchase program. Under this program, certain approved Royal Host employees (excluding certain senior executives) were eligible to finance the purchase of units from treasury at \$5.80 per unit at that time.

On April 1, 2002, 400,000 units were issued under this plan. The employee unit purchase program represents a financing program for selected employees to purchase units of Royal Host. Royal Host has recorded employee loans receivable of \$2,320,000 in respect to this transaction, which bear interest at a fixed rate of 5.0%, a rate established based on consideration of existing institutional rates and Canadian

Customs and Revenue Agency ("CCRA") guidelines for employee loan rates at that time. This plan structure does not meet the definition of stock based compensation plans, and therefore does not fall under the Handbook Section 3870 – Stock Based Compensation Plans.

In accordance with EIC ("Emerging Issues Committee") 44, for accounting purposes, these employee loans receivable have been offset against the corresponding trust units equity.

9. CONTINGENT LIABILITIES

Effective December 18, 2001, Royal Host management, acting in its capacity as manager of an unincorporated, independent vacation club society ("Society") entered into a lease agreement with a party to secure, on behalf of the Society, the right to use a vacation property. The Society is not owned or controlled by Royal Host. The lease agreement temporarily obligates a Royal Host subsidiary to lease the particular vacation property for three successive 15-year terms followed by a final 5-year term. The renewal terms are automatic and substantially obligate the lessee to renew the lease for a full term of 50 years.

Management intends to fully transfer the entitlements and obligations associated with this lease agreement to the Society, and the Society has agreed to accept the entitlements and obligations associated with the lease agreement pending finalization of legal and contractual documentation pertaining to the transfer of the lease entitlements and obligations to the Society.

It is anticipated that the finalization of such transfer of lease entitlements and obligations will occur in the near future. Should matters arise that result, for whatever reason, in the entitlements and obligations of the lease agreement not transferring to the Society, Royal Host may record such entitlements and obligations in its consolidated financial statements at that time. The current estimated fair value of each of the future entitlements and of the obligations at March 31, 2003 is approximately \$3.0 million.

10. COMPARATIVE FIGURES

Certain prior year's figures have been reclassified to conform with the presentation adopted for 2003. Commencing December 31, 2002, Royal Host has adopted the practice of classifying restricted cash held by lenders (see Note 3) as a non-current item. This classification has been applied on a comparative basis.

11. SUBSEQUENT EVENTS

Royal Host has purchased the Calgary Best Western Village Park Inn, adding 160 guestrooms, for a purchase price of \$12.7 million. As at March 31, 2003, all funds related to the purchase were held in trust by Royal Host's legal counsel. This transaction closed on April 1, 2003.

MANAGEMENT DISCUSSION AND ANALYSIS

Financial results for the three months ended March 31st 2003

HOSPITALITY REVENUES

Total hospitality revenues in the first quarter of 2003 increased by \$2.8 million or 10.2% compared to the same quarter in 2002. The increase was due to the inclusion of the Belleville, Trenton and Yellowknife hotels' operating results in the first quarter of 2003.

ROOM REVENUES

Room revenues increased by \$2.2 million due to the addition of rooms to the hotel portfolio resulting from new acquisitions, the take-over of operations for Yellowknife and a general overall revenue per available room ("RevPAR") increase. RevPAR increased by 4.2% on a consolidated basis for the first quarter of 2003 compared to the first quarter of 2002.

FOOD AND BEVERAGE

Food and beverage revenues increased by \$673,000, predominantly due to the addition of food and beverage operations at the new Belleville and Trenton properties and the take-over of operations for Yellowknife.

OTHER HOSPITALITY REVENUES

Other hospitality revenues decreased slightly to \$4.2 million in the first quarter of 2003 compared to \$4.3 million in the same quarter of 2002. The decrease was due to a one-time revenue item of \$253,000, related to sales for a managed property located in La Paz, Mexico, which was recognized in the first quarter of 2002 and not repeated in 2003. In addition, during the first quarter of 2002, Royal Host recognized \$0.5 million in lease revenue associated with the Yellowknife hotel, which was not recognized in the first quarter of 2003 due to the lease termination on October 31, 2002. For the first quarter of 2003, the Yellowknife hotel's actual operations were included in Royal Host's consolidated financial results. This change at the Yellowknife hotel had a significant negative impact on Royal Host's 2003 gross margin as the lease revenue in 2002 had no associated costs. Furthermore, the lease revenue was recognized evenly throughout the year and did not reflect the seasonal nature of the hotel's operation, as we see reflected in the first quarter 2003.

Approximately 50% of other hospitality revenues is generated through the ownership and operation of hotel properties, with the remaining portion generated by other hospitality-related activities.

HOSPITALITY EXPENSES

Consolidating the operations of the three above-mentioned hotels into the Royal Host portfolio contributed significantly to a \$3.6 million increase in hospitality expenses during the first quarter of 2003. In addition, a general increase in energy and utility costs across the country further contributed to higher operating costs, as did an increase in labour costs.

GROSS MARGIN

Gross margin decreased to 16.6% in the first quarter of 2003 from 21.2% in the same period of 2002. However, increased hospitality expenses were only partially responsible for the decrease in margins. The three additional hotel operations are more cyclical than Royal Host's previous portfolio and operate at much lower margins in the first quarter of the year. As was previously noted, termination of the Yellowknife lease which was in place for most of fiscal 2002, also had a negative impact on the gross margin in the first quarter of 2003.

OTHER (INCOME) AND EXPENSES

Total other (income) and expenses decreased by \$2.3 million in first quarter 2003 compared to first quarter 2002. The significant factors in this decline are as follows:

- ◆ Royal Host's interest on mortgages and other debt was \$163,000 lower in the first quarter of 2003, than in 2002, reflecting a lower cost of debt.
- ◆ Trust administration increased slightly due to additional compliance costs.
- ◆ Amortization was higher by \$344,000 due to new asset additions in the last three quarters of 2002 and in the first quarter of 2003, which resulted in greater amortization in 2003.
- ◆ Future income taxes, which are a non-cash item and an estimate, had a substantial recovery in the first quarter of 2003 compared to 2002. The recovery was primarily due to operating losses in the first quarter, which are anticipated to reverse during the course of the year due to seasonality.

NET LOSS

As a result of the large recovery in future income taxes, the first quarter loss was \$885,000 in 2003, compared to a loss of \$2.4 million during the same period in 2002.

CASH AVAILABLE FOR DISTRIBUTION

Cash available for distribution was \$1.4 million for the first quarter of 2003, which represents a \$678,000 decline in comparison to the same period in 2002.

Basic adjusted cash available for distribution was \$1.2 million lower in the first quarter of 2003. Increased equity distributions of \$527,000 in 2003 related to the \$40 million 9.25% convertible debentures issued in March 2002, and the slightly increased number of issued units (24.6 million units in first quarter 2003 compared to 24.1 million units in 2002), resulted in a reduction in basic adjusted cash available for distribution per unit to (\$0.02) in 2003 compared to \$0.03 in 2002. The full benefits of the 9.25% convertible debentures have not been realized to-date, since some of the proceeds have yet to be invested. However, a portion of the proceeds was utilized subsequent to March 31, 2003, as Royal Host purchased the Calgary Best Western Village Park Inn.

BALANCE SHEET

Assets

Current Assets

Cash and short-term investments decreased from \$16.1 million at December 31, 2002 to \$5.1 million at March 31, 2003. A portion of this reduction relates to funds paid and held in trust by legal counsel for the pending purchase of the Calgary Best Western Village Park Inn hotel. The purchase of this hotel was completed on April 1st, 2003.

At March 31, 2003, total current assets decreased by \$8.9 million from December 31, 2002, consisting of the aforementioned decrease in total cash, decrease in accounts and notes receivable (\$1.1 million), offset by increases in property under development (\$0.8 million) and future income taxes (\$2.3 million). The decrease in accounts and notes receivable is due to normal business activities. The increase in property under development relates to the construction of the Royal Private Residence Club ("PRC") at the Grand Okanagan Lakefront Resort and Conference Center in Kelowna. The increase in the future income taxes asset represents operating losses available to reduce future taxable income.

Royal Host intends to proceed with the PRC project in Kelowna. Management has received a commitment to finance the project, but did not recognize any revenue from the project during the first quarter of 2003. Royal Host's investment in the project is identified on the balance sheet in Property under Development.

Restricted Cash

For the first quarter 2003, Royal Host adopted the practice of classifying restricted cash held by lenders as a non-current item. At March 31, 2003 restricted cash of \$4.3 million (December 31, 2002 - \$4.2 million) represents a substantial portion of the year's capital expenditure requirements on certain hotels.

Deposits on Purchase of Capital Assets

On April 1, 2003, Royal Host purchased the Calgary Best Western Village Park Inn, adding 160 guestrooms, for a purchase price of \$12.7 million. As at March 31, 2003, all funds related to the purchase were held in trust by Royal Host's legal counsel.

Capital Assets

Throughout the first quarter of 2003, Royal Host continued to make substantial investments to its properties. Total spending on capital additions was approximately \$3.0 million in the first quarter of 2003 versus \$1.1 million in the same quarter of 2002.

Liabilities and Equity

Current Liabilities

The current portion of mortgages and other debt increased to \$39.3 million at March 31, 2003 from \$36.3 million at December 31, 2002.

Mortgages and Other Debt

During the first quarter of 2003, Royal Host's long-term portion of debt increased by \$7.6 million to \$112.5 million from \$104.9 million at December 31, 2002.

Total mortgages and other debt increased by \$10.6 million to \$151.8 million at March 31, 2003 compared to \$141.2 million at December 31, 2002. During the first quarter of 2003, Royal Host obtained debt financing totaling \$18.3 million, with funds advanced of \$9.1 million to March 31, 2003.

Equity

During the first quarter of 2003, Royal Host's equity decreased by \$6.9 million to \$195.8 million at March 31, 2003 from \$202.7 million at December 31, 2002. This decrease was mainly due to the issuance of additional units and the payment of interest and equity distributions.

LIQUIDITY AND CAPITAL RESOURCES

Royal Host continues to maintain a strong level of liquidity, with a \$5.1 million cash balance and \$11.9 million in undrawn bank lines at the end of March 31, 2003. The REIT also has additional borrowing capacity as the debt to gross book value stood at 32.7% at quarter end compared to a maximum allowable of 45%.

OUTLOOK

The short term outlook for the hospitality industry remains challenging at best due to economic turmoil, the impact of "SARS" and political uncertainties. Despite these increased risks, Royal Host performed reasonably well when compared against the industry as a whole in the first quarter of 2003. As we move forward into the future, Royal Host's objective is to continue to look for accretive hotel acquisitions, renovation and repositioning opportunities and complimentary businesses, which leverage management's expertise. Management remains optimistic about Royal Host's long term prospects.