



le château

QUARTERLY REPORT

FOR THE NINE MONTHS
ENDED OCTOBER 29, 2005

MESSAGE TO SHAREHOLDERS

On behalf of the Board of Directors, I am pleased to provide the results of Le Château Inc. for the third quarter ended October 29, 2005.

Sales increased 12.1% to \$69,231,000 for the third quarter ended October 29, 2005, compared with sales of \$61,776,000 for the third quarter ended October 30, 2004. Comparable store sales increased by 7.4% in the third quarter of 2005 compared with the same period a year ago.

Net earnings for the third quarter increased 25% to \$6,143,000 or \$1.03 per share from \$4,905,000 or \$0.92 per share last year.

Sales rose 17.7% to \$198,839,000 for the first nine months of the year, compared to \$168,981,000 last year. Net earnings for the nine-month period increased 56% to \$17,021,000 or \$2.87 per share from \$10,873,000 or \$2.05 per share the previous year. Comparable store sales increased 13.1% over the same period a year ago.

For the first five weeks ended December 3, 2005, total retail sales increased 10.1% and same store sales increased 5.9% compared to the same period last year.

At the Board of Directors meeting held of December 6, 2005, a quarterly cash dividend of \$0.25 was declared on the Class A Subordinate Voting and Class B Voting shares outstanding, representing an increase of 25% from the previous dividend rate of \$0.20 per share. This dividend is the 49th consecutive one declared by Le Château and is payable on February 6, 2005 to shareholders of record at the close of business on January 13, 2006.

I wish to thank our employees, customers, suppliers and our shareholders for their continued support.



Herschel H. Segal
Chairman of the Board and Chief Executive Officer
December 6, 2005

MANAGEMENT'S DISCUSSION AND ANALYSIS

Management's Discussion and Analysis (MD&A) should be read in conjunction with the unaudited interim consolidated financial statements for the nine months ended October 29, 2005 and the audited consolidated financial statements and MD&A for the year ended January 29, 2005. The risks and uncertainties faced by the Company are substantially the same as those outlined in the annual MD&A contained in the Company's 2004 Annual Report. The MD&A has been prepared as at December 6, 2005.

Results of Operations

Sales increased 12.1% to reach \$69.2 million for the third quarter ended October 29, 2005, due primarily to an increase of 7.4% in comparable store sales and an increase in square footage. On a year-to-date basis, sales increased 17.7% to \$198.8 million with comparable store sales growing 13.1%. Increased sales resulted from a combination of the strong appeal of the Company's selection of fall merchandise, as well as increased square footage in strategic locations. Year-to-date, the Company opened thirteen new stores, closed one store and expanded several existing locations, resulting in the addition of 80,000 square feet or 12% to the Le Château network.

As the Company executes its strategy of broadening its customer base, the Company expects that its business will become less seasonal. However, retail sales are traditionally higher in the third and fourth quarters due to the back-to-school period and the Christmas season, respectively. In addition, fourth quarter earnings results are usually reduced by post Christmas sale promotions.

	For the three months ended			For the nine months ended		
	October 29, 2005	October 30, 2004	% Var	October 29, 2005	October 30, 2004	% Var
TOTAL SALES BY DIVISION						
(in thousands of dollars)						
Ladies' Clothing	37,958	36,456	4.1%	110,151	99,442	10.8%
Men's Clothing	9,038	7,629	18.5%	25,303	20,851	21.4%
Junior Girl Clothing	2,908	3,537	-17.8%	8,237	10,350	-20.4%
Footwear	6,223	4,512	37.9%	18,155	13,455	34.9%
Accessories	13,104	9,642	35.9%	36,993	24,883	48.7%
	69,231	61,776	12.1%	198,839	168,981	17.7%
TOTAL SALES BY REGION						
(in thousands of dollars)						
Ontario	24,114	21,618	11.5%	69,968	59,195	18.2%
Quebec	19,493	16,840	15.8%	55,001	46,329	18.7%
Prairies	11,483	10,621	8.1%	33,980	29,429	15.5%
British Columbia	9,315	7,892	18.0%	25,278	20,763	21.7%
Maritimes	3,097	2,968	4.4%	9,060	7,540	20.2%
United States	1,729	1,837	-5.9%	5,552	5,725	-3.0%
	69,231	61,776	12.1%	198,839	168,981	17.7%

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

The Company continues to re-align existing real estate to maximize profitability by re-assigning space from the Junior Girl clothing division to other more profitable divisions. This profit optimization strategy commenced two years ago. As at October 29, 2005, the Junior Girl Division operated in approximately 45 stores, down from 60 stores as at January 29, 2005. The Company plans to completely phase out of this division by next spring.

Earnings before interest, income taxes, depreciation and amortization (EBITDA) increased 24.6% to \$12,484,000 as compared with \$10,020,000 last year. On a year-to-date basis, EBITDA increased 45.4% to \$35,067,000 as compared with \$24,109,000 last year.

Net earnings for the third quarter increased 25.2% to \$6,143,000 or \$1.03 per share from \$4,905,000 or \$0.92 per share last year. For the nine months ended October 29, 2005, net earnings increased 56.5% to \$17,021,000 or \$2.87 per share from \$10,873,000 or \$2.05 per share the previous year, resulting primarily from continued improvements in gross margins partially due to the strength in the Canadian dollar. The percentage increase in earnings per share was lower than the percentage increase in net earnings due to the dilutive impact of the share issuance in December 2004.

Net earnings attributable to Canadian operations amounted to \$6,388,000 or \$1.07 per share for the third quarter, compared to \$5,006,000 or \$0.94 per share the previous year. The U.S. operations reported a net loss \$245,000 Cdn or \$(0.04) Cdn per share for the period, compared to a net loss of \$101,000 Cdn or \$(0.02) Cdn per share for the same period a year ago.

During the third quarter, Le Château entered into a pilot licensing agreement with a retail developer in the Middle East regarding the opening of Le Château branded stores in the region. Construction is under way for a small number of test locations, which are expected to be launched over the next several months.

Dividends and Outstanding Share Data

On September 9, 2005, the Board of Directors declared a quarterly dividend of \$0.20 per Class A Subordinate Voting Share and Class B Voting Share, representing an increase of 14% from the previous dividend rate of \$0.175 per share. This dividend was paid on October 28, 2005 to shareholders of record at the close of business on October 7, 2005.

On December 6, 2005, the Board of Directors declared a quarterly dividend of \$0.25 per Class A Subordinate Voting Share and Class B Voting Share, representing an increase of 25% from the previous dividend rate of \$0.20 per share. This dividend is payable on February 6, 2006 to shareholders of record at the close of business on January 13, 2006.

These dividend payments represent the 48th and 49th consecutive quarterly dividends declared by Le Château.

As at December 6, 2005, there were 3,939,201 Class A subordinate and 2,040,000 Class B voting shares outstanding. On September 21, 2005, a shareholder converted 480,000 Class B shares into Class A shares. Further, there are 398,490 stock options outstanding with exercise prices ranging from \$3.75 to \$30.49, of which 113,590 are exercisable.

Liquidity and Capital Resources

Cash flow from operations rose to \$9.2 million for the third quarter of 2005, from \$7.4 million last year, mainly as a result of higher net earnings reported for the quarter. On a year-to-date basis, cash flow from operations increased to \$26.8 million from \$18.3 million the previous year.

Capital expenditures for the third quarter amounted to \$5.7 million, compared to \$3.0 million last year. Capital expenditures for the first nine months of 2005 totalled \$23.1 million compared to \$11.9 million the previous year and related primarily to the opening of thirteen new stores and the renovation of existing stores. Capital expenditures were financed from cash and cash equivalents and long-term debt financing of \$8.1 million obtained in the third quarter. Subsequent to quarter end, the Company borrowed \$4.9 million under various existing credit facilities. The borrowings are collateralized by the equipment and store fixtures financed as part of the credit facilities.

The projected capital expenditures for the fourth quarter of 2005 approximate \$4.0 million and relate primarily to the renovation and expansion of existing stores.

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

Financial Position

Working capital stood at \$52.3 million at the end of the third quarter of 2005, compared to \$35.0 million as at October 30, 2004 and \$47.8 million as at January 29, 2005.

Inventories increased to \$43.0 million at the end of the third quarter, from \$40.6 million a year earlier, due primarily to the additional 80,000 square feet added over the past year.

Long-term debt and capital lease obligations, including the current portions, increased to \$18.3 million from \$14.5 million as at October 30, 2004, after the additional long term financing of \$8.1 million obtained during the third quarter of 2005. The long-term debt to equity ratio decreased to 0.18:1 from 0.21:1 the previous year.

On September 21, 2005, a shareholder converted 480,000 Class B shares into Class A shares.

Accounting Policies

Critical Accounting Estimates:

The Company's critical accounting estimates are substantially the same as those disclosed in the Management's Discussion and Analysis section of its 2004 Annual Report.

Accounting Standards Implemented in 2005:

There were no new accounting standards implemented in the first nine months of 2005.

Supplementary Measures

In addition to discussing earnings measures in accordance with Canadian generally accepted accounting principles ("GAAP"), this MD&A provides earnings before interest, income taxes, depreciation and amortization ("EBITDA") as a supplementary earnings measure. EBITDA is provided to assist readers in determining the ability of the Company to generate cash from operations and to cover financial charges. It is also widely used for valuation purposes.

This MD&A also discloses cash flow from operations as a supplementary measure. Cash flow from operations is defined as cash flow from operating activities before the net change in non-cash working capital items related to operations. This measure provides an indication of the Company's ability to generate cash flows without considering certain timing and other factors causing variations in non-cash items.

The above measures do not have a standardized meaning prescribed by GAAP and may not be comparable to similar measures presented by other companies.

Forward-looking Statements

This "Management's Discussion and Analysis" may contain forward-looking statements relating to the Company and/or the environment in which it operates that are based on the Company's expectations, estimates and forecasts. These statements are not guarantees of future performance and involve risks and uncertainties that are difficult to predict and/or are beyond the Company's control. A number of factors may cause actual outcomes and results to differ materially from those expressed. These factors include those set forth in other public filings of the Company. Therefore, readers should not place undue reliance on these forward-looking statements. In addition, these forward-looking statements speak only as of the date made and the Company disavows any intention or obligation to update or revise any such statements as a result of any event, circumstance or otherwise.

Factors which could cause actual results or events to differ materially from current expectations include, among other things: the ability of the Company to successfully implement its strategic initiatives and whether such strategic initiatives will yield the expected benefits; competitive conditions in the businesses in which the Company participates; changes in consumer spending; general economic conditions and normal business uncertainty; customer preferences towards product offerings; seasonal weather patterns; fluctuations in foreign currency exchange rates; changes in the Company's relationship with its suppliers; interest rate fluctuations and other changes in borrowing costs; and changes in laws, rules and regulations applicable to the Company.

FINANCIAL HIGHLIGHTS

(Unaudited)

(In units except where otherwise stated)

	October 29, 2005	October 30, 2004
Working capital (\$,000)	\$ 52,282	\$ 35,046
Current ratio	2.53	2.41
Quick ratio	1.27	0.77
Long-term debt to equity *	0.18	0.21
Capital expenditures (\$,000)	\$ 23,068	\$ 11,942
Number of stores at end of quarter	186	172
Total number of square feet (,000)	766	689
Book value per share	\$ 16.68	\$ 13.13

* Including capital leases and current portion of debt. Excluding deferred lease inducements.

CONSOLIDATED BALANCE SHEETS

(Unaudited)

(In thousands of dollars)

	As at October 29, 2005	As at October 30, 2004	As at January 29, 2005
ASSETS			
Current			
Cash and cash equivalents	\$ 25,187	\$ 17,520	\$ 45,985
Short-term investments	14,894	–	–
Accounts receivable and prepaid expenses	3,343	1,707	2,089
Inventories	43,011	40,638	29,393
Total current assets	86,435	59,865	77,467
Fixed assets	65,342	49,335	50,731
	\$ 151,777	\$ 109,200	\$ 128,198
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current			
Accounts payable and accrued liabilities	\$ 24,960	\$ 18,224	\$ 22,397
Dividend payable	–	802	1,027
Income taxes payable	3,523	1,469	1,923
Current portion of capital lease obligations	1,466	1,427	1,399
Current portion of long-term debt	4,204	2,897	2,940
Total current liabilities	34,153	24,819	29,686
Capital lease obligations	1,221	2,687	2,329
Long-term debt	11,384	7,508	6,757
Future income taxes	1,695	1,758	1,695
Deferred lease inducements	3,595	2,261	2,487
Total liabilities	52,048	39,033	42,954
Shareholders' Equity			
Capital stock	26,886	15,302	26,393
Contributed surplus	251	–	–
Retained earnings	72,592	54,865	58,851
Total shareholders' equity	99,729	70,167	85,244
	\$ 151,777	\$ 109,200	\$ 128,198

CONSOLIDATED STATEMENTS OF RETAINED EARNINGS

<i>(Unaudited)</i> <i>(In thousands of dollars)</i>	For the three months ended		For the nine months ended	
	October 29, 2005	October 30, 2004	October 29, 2005	October 30, 2004
Balance, beginning of period	\$ 67,644	\$ 50,762	\$ 58,851	\$ 46,388
Net earnings	6,143	4,905	17,021	10,873
	73,787	55,667	75,872	57,261
Dividends	1,195	802	3,280	2,396
Balance, end of period	\$ 72,592	\$ 54,865	\$ 72,592	\$ 54,865

CONSOLIDATED STATEMENTS OF EARNINGS

<i>(Unaudited)</i> <i>(In thousands of dollars, except per share data)</i>	For the three months ended		For the nine months ended	
	October 29, 2005	October 30, 2004	October 29, 2005	October 30, 2004
Sales	\$ 69,231	\$ 61,776	\$ 198,839	\$ 168,981
Cost of sales and expenses				
Cost of sales and selling, general and administrative	56,513	51,756	163,466	144,512
Depreciation and amortization	2,815	2,286	8,150	6,691
Interest	164	219	534	465
Write-off of fixed assets	234	–	306	360
	59,726	54,261	172,456	152,028
Earnings before income taxes	9,505	7,515	26,383	16,953
Provision for income taxes	3,362	2,610	9,362	6,080
Net earnings	\$ 6,143	\$ 4,905	\$ 17,021	\$ 10,873
Net earnings per share				
Basic	\$ 1.03	\$ 0.92	\$ 2.87	\$ 2.05
Diluted	0.99	0.88	2.77	1.97
Weighted average number of shares outstanding ('000)	5,977	5,334	5,937	5,297

CONSOLIDATED STATEMENTS OF CASH FLOWS

<i>(Unaudited)</i>	For the three months ended		For the nine months ended	
<i>(In thousands of dollars)</i>	October 29, 2005	October 30, 2004	October 29, 2005	October 30, 2004
OPERATING ACTIVITIES				
Net earnings	\$ 6,143	\$ 4,905	\$ 17,021	\$ 10,873
Adjustments to determine net cash from operating activities				
Depreciation and amortization	2,815	2,286	8,150	6,691
Write-off of fixed assets	234	-	306	360
Amortization of deferred lease inducements	(219)	(131)	(517)	(398)
Deferred lease inducements	94	370	1,625	728
Stock-based compensation	129	-	251	-
	9,196	7,430	26,836	18,254
Net change in non-cash working capital				
Items related to operations	(955)	(3,314)	(10,709)	(17,334)
Cash flows from operating activities	8,241	4,116	16,127	920
FINANCING ACTIVITIES				
Repayment of loan to director	-	-	-	566
Repayment of capital lease obligations	(352)	(386)	(1,041)	(1,139)
Proceeds of long-term debt	8,081	807	8,081	9,991
Repayment of long-term debt	(741)	(670)	(2,190)	(1,352)
Issue of capital stock	30	112	493	528
Dividends paid	(2,241)	(798)	(4,307)	(2,119)
Cash flows from financing activities	4,777	(935)	1,036	6,475
INVESTING ACTIVITIES				
Increase in short-term investments	(14,894)	-	(14,894)	-
Additions to fixed assets	(5,736)	(2,997)	(23,067)	(11,942)
Cash flows from investing activities	(20,630)	(2,997)	(37,961)	(11,942)
Increase (decrease) in cash and cash equivalents	(7,612)	184	(20,798)	(4,547)
Cash and cash equivalents, beginning of period	32,799	17,336	45,985	22,067
Cash and cash equivalents, end of period	\$ 25,187	\$ 17,520	\$ 25,187	\$ 17,520
Supplementary information:				
Interest paid during the period	\$ 164	\$ 219	\$ 534	\$ 465
Income taxes paid during the period, net	2,141	1,693	7,779	6,588

NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited – Tabular figures in thousands of dollars except share information)

1. Disclosure

These interim consolidated financial statements (the “financial statements”) do not include all disclosures required by Canadian generally accepted accounting principles for annual financial statements and accordingly, the financial statements should be read in conjunction with the most recently prepared annual financial statements for the 52-week period ended January 29, 2005.

As the Company executes its strategy of broadening its customer base, the Company expects that its business will become less seasonal. However, retail sales are traditionally higher in the third and fourth quarters due to the back-to-school period and the Christmas season, respectively. In addition, fourth quarter earnings results are usually reduced by post Christmas sale promotions.

2. Accounting Policies

These financial statements follow the same accounting policies and methods of their application as the most recent annual financial statements for the 52-week period ended January 29, 2005.

3. Short-term Investments

Short-term investments include investments with original maturity terms of 90 days or more. Short-term investments are carried at the lower of cost and market value. All short-term investments are denominated in Canadian dollars. The fair value of the short-term investments approximates the carrying value.

As at October 29, 2005, the weighted average effective interest rate was 3.10% and the maturity dates vary over the period ending April 17, 2006.

4. Long-Term Debt and Capital Lease Obligations

Under various existing credit facilities, the Company borrowed \$8.1 million in the third quarter of 2005 at an interest rate of 6.05% and an additional \$4.9 million at 5.60% subsequent to the quarter end, both repayable over a 48 month period. The borrowings are collateralized by the equipment and store fixtures financed as part of the credit facilities.

5. Capital Stock

As at December 6, 2005, there were 3,939,201 Class A subordinate and 2,040,000 Class B voting shares outstanding. On September 21, 2005, a shareholder converted 480,000 Class B shares into Class A shares. Further, there are 398,490 stock options outstanding with exercise prices ranging from \$3.75 to \$30.49, of which 113,590 are exercisable. Further details are provided in note 9 of the consolidated financial statements contained in the 2004 Annual Report.

4,300 shares (2004 – 21,200 shares) were issued pursuant to the exercising of stock options for cash consideration of \$30,000 (2004 - \$112,000) for the three months ended October 29, 2005. For the nine months ended October 29, 2005, there were 111,900 shares (2004 – 97,510 shares) issued for cash consideration of \$493,000 (2004 - \$528,000).

On June 29, 2005, the Company's shareholders approved an amendment to the stock option plan (the “Plan”) in order to change the maximum number of Class A Subordinate Voting Shares issuable from time to time under the Plan from the current fixed maximum number of 1,500,000 Class A Subordinate Voting Shares to a fixed maximum percentage of 12% of the aggregate number of Class A Subordinate Voting Shares and Class B Shares issued and outstanding from time to time.

NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS (continued)

5. Capital Stock (continued)

For the nine-month period ended October 29, 2005, the Company granted 203,500 options to purchase Class A subordinate voting shares (There were no options granted during for the three month period ended October 29, 2005). The fair value of each option grant was established on the date of the grant using the Black-Scholes option pricing model with the following weighted average assumptions used for options granted in the period.

	<u>Assumptions</u>
Expected dividends	\$0.70
Expected volatility	37%
Risk-free interest rate	3.32%
Expected life	3.3 years

The weighted average fair value per option for the nine month ended October 29, 2005 amounted to \$6.85 per option. The compensation cost related to stock options granted after January 25, 2003 is recorded in the unaudited interim consolidated statements of earnings. For the three- and nine-month periods ended October 29, 2005, the stock-based compensation cost amounted to \$129,000 and \$251,000, respectively (Nil for the same periods last year) and is recorded in operating expenses in the Company's unaudited interim consolidated statements of earnings and credited to contributed surplus on the Company's unaudited interim consolidated balance sheets.

For stock options granted from January 27, 2002 to January 25, 2003, if the Company had used the fair market value method of accounting for its option plan, the Company's net earnings and the basic and diluted earnings per share, on a pro forma basis, would not have been materially different.

6. Earnings per Share

The numbers of shares used in the earnings per share calculation is as follows:

	<u>For the three months ended</u>		<u>For the nine months ended</u>	
	October 29, 2005	October 30, 2004	October 29, 2005	October 30, 2004
Weighted average number of shares outstanding - basic	5,977,346	5,334,201	5,936,953	5,296,800
Dilutive effect of stock options	245,148	226,598	211,734	226,299
Weighted average number of shares outstanding - diluted	6,222,494	5,560,799	6,148,687	5,523,099

7. Segmented Information

	<u>For the three months ended</u>		<u>For the nine months ended</u>	
	October 29, 2005	October 30, 2004	October 29, 2005	October 30, 2004
Sales				
Canada	\$ 67,502	\$ 59,939	\$ 193,287	\$ 163,256
United States	1,729	1,837	5,552	5,725
	\$ 69,231	\$ 61,776	\$ 198,839	\$ 168,981
Net earnings (loss)				
Canada	\$ 6,388	\$ 5,006	\$ 17,466	\$ 11,165
United States	(245)	(101)	(445)	(292)
	\$ 6,143	\$ 4,905	\$ 17,021	\$ 10,873
Identifiable assets				
Canada	\$ 146,292	\$ 104,643	\$ 146,292	\$ 104,643
United States	5,485	4,557	5,485	4,557
	\$ 151,777	\$ 109,200	\$ 151,777	\$ 109,200