

**STERLING SHOES INCOME FUND
MANAGEMENT'S DISCUSSION AND ANALYSIS
November 16, 2009**

The following management's discussion and analysis ("MD&A") should be read in conjunction with the unaudited interim consolidated financial statements and accompanying notes ("Interim Financial Statements") of Sterling Shoes Income Fund (the "Fund") for the three-month and nine-month periods ended September 30, 2009. Results have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP" and reported in Canadian dollars unless otherwise indicated). The fiscal year-end of the Fund is December 31.

This MD&A contains forward-looking statements. Please see "Forward-Looking Statements" and "Risks and Uncertainties" for a discussion of the risks, uncertainties and assumptions relating to these statements. This MD&A also makes reference to certain non-GAAP measures to assist in assessing our financial performance. Non-GAAP measures do not have any standard meaning prescribed by GAAP and are therefore unlikely to be comparable to similar measures presented by other issuers. See "Non-GAAP Measures" and "Adjusted Distributable Cash".

OVERVIEW OF THE FUND

The Fund is an unincorporated, open-ended, limited-purpose trust established under the laws of the Province of British Columbia pursuant to the declaration of trust dated May 31, 2005. The Fund was established to acquire an 80% interest in Sterling Shoes Limited Partnership ("Sterling Shoes LP"), which had acquired the retail footwear business of SSI Investments Inc., previously named Sterling Shoes Inc. ("Inc"). Inc retained a 20% interest in Sterling Shoes LP.

As at November 16, 2009, there were 5,313,488 units ("Units") of the Fund issued and outstanding. In addition, to provide Inc with voting rights commensurate with Inc's retained interest in Sterling Shoes LP, Inc holds 1,328,372 special voting units of the Fund (equal to the number of Class D LP Units Inc holds in Sterling Shoes LP (the "Class D LP Units")), which entitle the holder to one vote per special voting unit at meetings of unitholders of the Fund ("Unitholders").

Distributions on the Class D LP Units were subordinated and the Class D LP Units themselves were not exchangeable for Units of the Fund until the Subordination End Date. As a result of the Fund achieving a specified EBITDA target for the year ended December 31, 2007 and distribution target for each of the fiscal years ended December 31, 2007 and 2006, the Subordination End Date occurred on March 31, 2008. Consequently, the Class D LP Units became freely exchangeable for Units on a one-for-one basis and were reclassified from non-controlling interest to unitholders' equity in 2008. The distributions on the Class D LP Units are no longer subordinated and are made monthly, instead of quarterly.

On October 3, 2007 the Fund closed an offering of \$25 million of convertible unsecured subordinated debentures (the "Debentures") at a price of \$1,000 per debenture. The Debentures bear interest at an annual rate of 6.5% payable semi-annually in arrears on October 31 and April 30 in each year commencing April 30, 2008. The maturity date for the Debentures is October 31, 2012.

The Units trade on the Toronto Stock Exchange under the symbol SSI.UN and the Debentures trade under the symbol SSI.DB.

OVERVIEW OF OUR BUSINESS

The Fund is a Vancouver-based, leading footwear retailer operating through six separate retail banners: Sterling, Joneve, Shoe Warehouse, Freedman Shoes, Gia and Sterling Outlet. These retail concepts were designed to effectively and profitably serve identified market segments. Since 1987 the Sterling Shoes business (formerly carried on by Sterling Shoes Inc.) has grown from five locations to 162 stores as at November 16, 2009. Our stores are located in leased premises primarily in high-traffic, high-visibility locations within enclosed shopping malls, on high streets and in strip malls.

Our products include dress and casual footwear ranging from sandals and athletic shoes to career footwear and special occasion shoes. We offer footwear products under both private label and national brands in each of our stores as well as a range of accessories, including handbags, shoe care products and hosiery.

Each of our banners targets a specific consumer group through different product, merchandising, location, pricing, service and advertising strategies.

Retail Banner	General Price Range	Products and Consumers	Key Private Label Brands	Key National Brands	
<i>Sterling</i>	\$50 to \$ 140	<ul style="list-style-type: none"> • mid-range women's fashion and comfort footwear • latest fashion trends, current looks • targeted to women 15 years of age & up 	<ul style="list-style-type: none"> • Roberto Gianni • Joy & Peace • Gianni Collections 	<ul style="list-style-type: none"> • Skechers • Puma • Franco Sarto • Steve Madden • Converse 	<ul style="list-style-type: none"> • Blowfish • DC Skate • Roxy • Kenneth Cole • Rocket Dog
<i>Joneve</i>	\$69 to \$180	<ul style="list-style-type: none"> • mid-high end women's fashion and comfort footwear • fashionable upscale career, comfort and dress shoes • dress, casual and fashion athletic shoes, boots and sandals • targeted to women 20 years of age & up 	<ul style="list-style-type: none"> • Roberto Gianni • Gianni Collections 	<ul style="list-style-type: none"> • Skechers • Puma • Nine West • Franco Sarto 	<ul style="list-style-type: none"> • Guess • Bebe Sport • Steve Madden • Kenneth Cole
<i>Shoe Warehouse</i>	\$19 to \$49 — kids \$39 to \$99 — ladies \$39 to \$99 — mens	<ul style="list-style-type: none"> • value-priced, family footwear products, including fashion, comfort, athletic footwear and work boots • leather and synthetic products representing good value to family-oriented or price-conscious consumers 	<ul style="list-style-type: none"> • Be Wild • Rinaldi • Blizzard • Workers • Urban XT • EC Collections 	<ul style="list-style-type: none"> • Bare Traps • Fila • Rockport • Nike • Kodiak • Sorel 	<ul style="list-style-type: none"> • Skechers • New Balance • Saucony • BOC by Børn
<i>Freedman Shoes</i>	\$90 to \$350	<ul style="list-style-type: none"> • high-end men's and women's fashion and comfort footwear • 95% of products are national brands • wide selection of fittings and sizes • targeted to men and women 25 years of age & up 	<ul style="list-style-type: none"> • Gianni Collections • Roberto Gianni 	<ul style="list-style-type: none"> • Amalfi • Stuart Weitzman • Donald J Pliner • Johnson & Murphy 	<ul style="list-style-type: none"> • Cole Haan • Rockport • DKNY • Franco Sarto
<i>Gia</i>	\$70 to \$360	<ul style="list-style-type: none"> • cutting-edge, funky women's street fashion • fashion-athletic footwear and accessories • 85% of products are national brands 	<ul style="list-style-type: none"> • Gianni Collections 	<ul style="list-style-type: none"> • Guess • Steve Madden • Jessica Simpson • Betsey Johnson • Rocket Dog 	<ul style="list-style-type: none"> • Puma • UGG • Blowfish • BCBG
<i>Sterling Outlet</i>	\$50 to \$ 140	<ul style="list-style-type: none"> • mid-range women's fashion and comfort footwear • latest fashion trends at clearance prices • dress, casual and fashion athletic shoes, boots and sandals • targeted to women 15 years of age & up 	<ul style="list-style-type: none"> • Roberto Gianni • Gianni Collections • Joy & Peace 	<ul style="list-style-type: none"> • Skechers • Puma • Franco Sarto • Steve Madden 	<ul style="list-style-type: none"> • Kenneth Cole • Converse • Rocket Dog

Sterling/Joneve, Shoe Warehouse, Freedman Shoes, Gia and Sterling Outlet compete with other local, regional and national footwear retailers. The fragmented nature of the Canadian retail footwear industry and our six distinct retail banners means that we compete against a wide variety of participants at various levels of the value chain. Examples of who we believe to be the principal competitors for our Sterling/Joneve/Gia, Shoe Warehouse and Freedman Shoes banners are provided below.

<u>Sterling/Joneve/Gia</u>	<u>Shoe Warehouse/Sterling Outlet</u>	<u>Freedman Shoes</u>
<ul style="list-style-type: none"> ● ALDO ● Town Shoes ● Nine West ● Feet First ● Little Burgundy ● Mall-based specialty shoe stores ● Apparel stores selling mid-to-high range fashion and fashion-athletic footwear products 	<ul style="list-style-type: none"> ● Payless Shoe Source ● The Shoe Company ● Winners ● Softmoc ● The Bay ● Zellers ● National and regional comfort-oriented shoe stores ● Style Sense 	<ul style="list-style-type: none"> ● Browns ● Town Shoes ● Holt Renfrew ● Harry Rosen ● Feet First ● B2

We now operate 162 stores across Canada, a significant increase from the 100 stores at the time of our initial public offering in July 2005. In light of the current economic environment, we have slowed the pace of our expansion. We are cautious with opening new locations and we will only add to our store base if the locations meet strict criteria for expected sales, profitability and return on invested capital. We remain focused on our strategic objective: the right shoe, at the right price, at the right place, in the right quantity. We do so by managing the fundamentals that we control, including: managing purchasing, product mix and inventory, offering excellent customer service, tightening control over expenses and continually evaluating our planned capital expenditures. Additionally, we actively seek ways to improve the efficiency and profitability of our existing stores. One of the most important strategic initiatives we have undertaken recently is the investment in our information technology systems to better position our business.

RECENT EVENTS AND OUTLOOK

Economic Conditions and our Recent Performance

Over the past twelve months economic conditions deteriorated considerably in many countries and regions, including Canada. Volatility in financial markets, higher unemployment rates and recessionary conditions resulted in a low level of consumer confidence, increased promotional activity, reductions in consumer spending and weakness in a number of industries in the regions in which we operate.

Despite reports of economic recovery, the retail economy continues to deteriorate as shown by the August 2009 Statistics Canada retail sales survey, the most recently available data. During August 2009 Canadian retail sales in B.C., Ontario and Alberta, our three largest geographic markets, were down 7.6%, 5.9% and 10.3%, respectively, compared to August 2008. We experienced similar declines.

Our results for the three-month and nine-month periods ended September 30, 2009 reflected these issues:

- Overall sales for the third quarter of 2009 decreased 6.5% to \$31.7 million from \$33.9 million in to the same period in 2008;
- Overall sales for the nine-months of 2009 increased 2.0% to \$90.0 million from \$88.2 million in the same period in 2008;
- Same store sales fell by 12.8% and 5.7% for the three and nine-month periods ended September 30, 2009, respectively, compared to the same periods in 2008;
- The Fund has reduced the level of its inventory over the past few quarters. At September 30, 2009, on a units per store basis, we had 12.0% less inventory than at September 30, 2008.

The future economic uncertainty and the higher cost of capital assumptions in the valuation methodology led to a non-cash impairment of the Fund's goodwill and intangible assets at September 30, 2009.

Number of Stores

During the third quarter of 2009, we opened three new stores and closed two underperforming stores. Since October 1, 2008, the Fund has opened 9 stores, renovated 4 stores, relocated 2 stores and closed 4 stores. We do not intend to open any more stores during the remainder of 2009. We may close an additional two underperforming stores in the upcoming two quarters.

The normal course of business includes closing stores due to a number of factors such as the redevelopment of real estate in malls, high streets and strip malls, changes in the economic environment and lease terms. We are taking a cautious approach to additional store openings and expansion in light of uncertain economic conditions.

Our 162 stores operate under six retail banners in British Columbia, Alberta, Saskatchewan, Manitoba and Ontario as follows:

Number of Stores Operating												
16-Nov-09								Dec 31, 2008	Dec 31, 2007	Dec 31, 2006	Dec 31, 2005	July 12, 2005
Province	Shoe Warehouse	Sterling	Joneve	Freedman	Gia	Sterling Outlet	Total	Total	Total	Total	Total	Total
British Columbia	40	20	6	8	2	-	76	75	65	63	60	59
Alberta	15	9	2	-	-	1	27	26	25	25	24	24
Saskatchewan	2	2	-	-	-	-	4	4	3	3	4	4
Manitoba	9	3	-	-	-	-	12	12	12	11	11	11
Ontario	12	23	6	2	-	-	43	43	36	25	5	2
Total	78	57	14	10	2	1	162	160	141	127	104	100

INTERNATIONAL FINANCIAL REPORTING STANDARDS (“IFRS”)

On February 13, 2008, the Canadian Accounting Standards Board confirmed that publicly accountable enterprises will be required to adopt IFRS in place of GAAP for interim and annual reporting purposes for fiscal years beginning on or after January 1, 2011.

Our conversion project is led by finance management and includes input from various areas of the organization. Using the changeover plan that we developed to map conversion to these new standards, we have identified and documented the areas of significant differences that apply to the Fund as well as the different options available under IFRS. This plan also assessed the impact of the changes to the Fund’s financial reporting, business processes and information systems.

The conversion project consists of three primary phases, which in certain cases will be in process concurrently as IFRS is applied to specific areas from start to finish:

- Scoping and diagnostic phase — This phase involves performing a detailed diagnostic comparing Canadian GAAP to IFRS and identifying key areas that may be impacted by the transition to IFRS.
- Impact analysis and design phase — In this phase, each area identified from the scoping and diagnostic phase will be addressed. This phase will determine the impact of the conversion on existing accounting policies, information systems, business processes and internal controls over financial reporting and disclosure. This phase will include an analysis of policy alternatives allowed under IFRS and development of draft IFRS financial statement content.
- Implementation and review phase — This phase will include execution of changes to information systems and business processes, completing formal authorization processes to approve recommended accounting policy changes and training programs across the Fund’s finance and other staff, as necessary. The ultimate objective being able to provide IFRS compliant financial information.

During the third quarter of 2009, we continued to work with our accounting system consultants and ERP developers to enable the Fund’s system to capture the necessary information for IFRS reporting. In many financial statement areas, IFRS requires more extensive disclosures than Canadian standards. Management is focused in the fourth quarter of 2009 on making the necessary estimates and draft disclosures for the transition date of January 1, 2010

At this time, the impact on our future financial position and results of operations is not reasonably determinable or estimatable.

IFRS 1, “First-Time Adoption of International Financial Reporting Standards”, provides entities adopting IFRS for the first time with a number of optional exemptions and mandatory exceptions, in certain areas, to the general requirement for full retrospective application of IFRS. We are analyzing the various accounting policy choices available and will implement those determined to be most appropriate in the Fund’s circumstances.

Most adjustments required on transition to IFRS will be made, retrospectively, against opening retained earnings as of the date of the first comparative balance sheet presented based on standards applicable at that time.

SUMMARY FINANCIAL INFORMATION

Statement of Income Items (\$000's)	Three months ended September 30		Nine months ended September 30	
	2009	2008	2009	2008
Sales	\$ 31,685	33,895	89,975	88,248
Cost of Sales	(18,777)	(17,333)	(51,117)	(45,603)
Gross Margin	12,908	16,562	38,858	42,645
<i>As a percentage of sales</i>	40.7%	48.9%	43.2%	48.3%
Store and selling expenses	(11,502)	(12,112)	(34,122)	(33,400)
General and administrative expenses	(1,892)	(1,736)	(5,232)	(5,370)
EBITDA ⁽¹⁾	(486)	2,714	(496)	3,875
Adjusted EBITDA ⁽¹⁾	(587)	2,617	(1,035)	3,593
<i>As a percentage of sales</i>	-1.9%	7.7%	-1.2%	4.1%
Interest expense	(672)	(494)	(1,968)	(1,647)
(Loss) / Gain on disposal	(26)	0	(260)	(333)
Impairment of goodwill and intangible assets	(33,246)	0	(33,246)	0
Amortization	(1,002)	(818)	(2,538)	(2,348)
Income / (Loss) before taxes	(35,432)	1,402	(38,508)	(453)
Future income taxes	-	-	-	724
Net income / (loss)	(35,432)	1,402	(38,508)	271
Maintenance capital expenditures	708	330	1,836	2,339

Balance Sheet Items (\$000's)	September 30, 2009	December 31, 2008
Total assets	81,156	111,126
Long-term financial liabilities	27,343	26,847

Notes:

- (1) See definition of EBITDA, Adjusted EBITDA and Maintenance Capital Expenditures under "Non-GAAP Measures".

The table below summarizes the distributions declared during the three and nine-month periods ended September 30, 2009 and 2008 for Units of the Fund and to Inc on the Class D LP Units:

	Three-months ended September 30,		Nine-months ended September 30,	
	2009	2008	2009	2008
Trust Units and Class D LP Units	\$ 371	\$ 2,491	\$ 1,308	\$ 7,472

OPERATING RESULTS

Sales

Sales were \$31.7 million during the three-month period ended September 30, 2009, representing a decrease of 6.5% from the \$33.9 million in 2008. The Fund experienced same-store sales decline of 12.8% in those stores that were open at least three months leading up to October 1, 2008. The three-month period ended September 30, 2009 reflected an uncertain retail sales environment, characterized by significant promotional activity in response to slow consumer activity and traffic. Sales were also affected by unseasonable weather in our key markets during the quarter.

For the nine-month period ended September 30, 2009, sales increased to \$90.0 million or 2.0% over the same period in 2008. During the nine-month period ended September 30, 2009 same store sales declined by 5.7% in those stores that were open at least nine-months leading up to October 1, 2008 for the reasons discussed above.

Our ability to grow sales will depend on a number of factors including our ability to successfully identify and respond to changes in trends and customer tastes, our ability to hire, train, motivate, manage and retain qualified buyers, retail store management and personnel, as well as other factors further outlined in "Risks and Uncertainties".

Cost of sales and gross margin

Consumer confidence and the overall retail market continues to be weak. The Fund continued its promotional activity to generate sales, clear inventory and respond to competitive forces during the three-months ended September 30, 2009. More promotional activity took place during the three-month and nine-month periods of 2009 than the same periods of 2008. This contributed to weaker gross margins.

Cost of sales was also impacted by the deterioration of the Canadian dollar versus the U.S. dollar earlier in 2009. Substantially all footwear sold in Canada is manufactured outside of Canada. Consequently, the cost of substantially all of our purchases is exposed to currency fluctuations either directly or indirectly. During the three and nine-month periods ended September 30, 2009, approximately 54% and 47% of product purchases were denominated in U.S. dollars, respectively. During the quarter ended September 30, 2009 the Fund's U.S. dollar purchases were approximately 12% more costly in Canadian dollar terms than during the same period in 2008. This has increased purchase prices, inventory valuation and cost of sales.

Cost of sales as a percentage of sales, for the three and nine-month periods ended September 30, 2009 was 59.3% and 56.8%, compared to 51.1% and 51.7% respectively for the same periods during 2008.

Store and selling expenses

Store and selling expenses for the three and nine-months ended September 30, 2009 were 36.3% and 37.9% of sales, compared to 35.7% and 37.8% for the same periods during 2008, respectively. Store and selling expenses have a fixed underlying core with a large variable component, primarily consisting of expenses relating to occupancy and employee costs. The increase in store and selling expenses as a percentage of sales for the third quarter of 2009 compared to the same period in 2008 is a result of four more stores operating at September 30, 2009 compared to September 30, 2008.

Store and selling expenses for the nine months ended September 30, 2009 were slightly higher as a percentage of sales compared to the same period in 2008. Due to the declining sales environment, management's efforts to reduce costs in this area are not as evident when bench-marking against this lower sales base. Efforts to reduce store and selling expenses, particularly store payroll costs, as a percentage of sales continues to be a key area of focus in this current economic climate.

General and administrative expenses

General and administrative ("G&A") expenses for the three and nine-months ended September 30, 2009 were 6.0% and 5.8% of sales, compared to 5.1% and 6.1% during the same periods in 2008, respectively.

The Fund initiated the investment into a new inventory management system in 2009. However, until the new system is implemented, we will continue to support our legacy system to run our business. General and administrative expenses for the three-month period ended September 30, 2009 are higher than the same period in 2008 as it becomes more challenging and costly to upkeep the legacy system.

For the nine-months ended September 30, 2009, G&A expenses have been reduced in nearly all cost categories as a result of our comprehensive review of business processes to manage the business through the current economic volatility.

Adjusted EBITDA (see "Non-GAAP Measures")

Adjusted EBITDA for the three and nine-months ended September 30, 2009 was negative \$0.6 million and negative \$1.0 million, respectively, compared to \$2.6 million and \$3.4 million for the same periods during 2008.

Interest expense

Net interest expense with respect to funds utilized under the Fund's credit facilities for the three-months and nine-months ended September 30, 2009 was \$96 thousand and \$252 thousand, respectively. During the same periods in 2008 the Fund incurred interest expense of \$71 for the three-months ended September 30, 2008, but earned interest income of \$18 thousand for the nine-months ended September 30, 2008.

Interest expense with respect to the Debentures for the three-month and nine-month periods ended September 30, 2009 was \$578 thousand and \$1.7 million (2008 - \$559 thousand and \$1.7 million), respectively.

The Fund has allocated the proceeds of the Debentures between debt and equity based on the relative fair values of the debt and the conversion option, as determined by the residual valuation of the equity component. Under this approach, the liability component was valued first, and the difference between the proceeds of the Debentures and the fair value of the debt was assigned to the conversion option. The present value of the liability component was calculated using a discount rate of 9.2% (at the date of issuance), the estimated market interest rate for similar debentures having no conversion rights.

The conversion option was valued at \$2.657 million at the date of issuance. The liability portion of the Debentures is being accreted to its face value over the term of the debt. Included in interest expense for the three and nine-months ended September 30, 2009 was \$169 thousand and

\$496 thousand (2008 - \$17 thousand and \$446 thousand), respectively, relating to this interest accretion.

Impairment of goodwill and intangible assets

During 2008 and 2009, the global economic and financial crisis has significantly impacted the Canadian economy. This crisis has resulted in reduced liquidity in the financial markets, increased unemployment rates, decreased consumer confidence and adversely affected the retail industry. The erosion of the Fund's valuation, primarily as a result of these factors, future economic uncertainty and the higher cost of capital assumptions in the valuation methodology, contributed to the impairment charges against the Fund's goodwill and intangible asset balances at September 30, 2009.

The Fund undertook a detailed analysis in its determination of the fair value of its intangible assets. As a result of this analysis, the Fund incurred an impairment charge of \$33.2 million for the three-months ended September 30, 2009. This is a non-cash charge.

Inventory

The Fund has reduced the level of its inventory over the past few quarters. At September 30, 2009, on a units per store basis, we had 12% less inventory than at September 30, 2008. During Q4-2008, Q1-2009, Q2-2009, and Q3-2009 deterioration of the Canadian dollar meant that U.S. dollar purchases were 17%, 24%, 16% and 12% more expensive than in the respective periods one-year earlier. It is primarily purchases made during Q1-2009 and Q2-2009 that were brought into inventory and sold during the three-month period ended September 30, 2009. These factors have led to an increase in the per unit value of our inventory.

At September 30, 2009, we operated 162 stores, four more stores than at September 30, 2008. Inventory levels are likewise higher to reflect that growth.

We are currently working on enhancements to our information technology systems. We have made significant strides in the project and we are working diligently towards project completion. We believe that these changes will add to our ability to effectively manage our business.

SELECTED QUARTERLY FINANCIAL INFORMATION

in (\$000's) except per Unit amounts	Q3-2009	Q2-2009	Q1-2009	Q4-2008	Q3-2008	Q2-2008	Q1-2008	Q4-2007
Sales	\$ 31,685	\$ 30,618	\$ 27,672	\$ 42,520	\$ 33,895	\$ 29,405	\$ 24,948	\$ 36,083
(Loss) / Income before non-controlling interest and taxes ⁽¹⁾	\$ (35,432)	\$ (651)	\$ (2,428)	\$ 6,453	\$ 1,402	\$ 866	\$ (2,723)	\$ 5,228
Future income taxes	4,636	-	-	-	-	-	724	-
(Loss) / Income before non-controlling interest ⁽¹⁾	\$ (30,796)	\$ (651)	\$ (2,428)	\$ 6,453	\$ 1,402	\$ 866	\$ (1,999)	\$ 5,228
Net (Loss) / Income	\$ (30,796)	\$ (651)	\$ (2,428)	\$ 6,453	\$ 1,402	\$ 866	\$ (1,999)	\$ 4,153
Basic (loss) / income per Unit	\$ (4.637)	\$ (0.098)	\$ (0.366)	\$ 0.972	\$ 0.211	\$ 0.130	\$ (0.371)	\$ 0.787
Diluted (loss) / income per Unit	\$ (4.637)	\$ (0.098)	\$ (0.366)	\$ 0.897	\$ 0.211	\$ 0.130	\$ (0.371)	\$ 0.787
Cash distributions per Unit	\$ 0.056	\$ 0.056	\$ 0.085	\$ 0.192	\$ 0.375	\$ 0.375	\$ 0.375	\$ 0.780
Number of stores open at end of period	162	161	159	160	158	148	143	141

Notes:

- (1) During the quarter ended March 31, 2008, the non-controlling interest held by Inc, which retained a 20% in the business of Sterling Shoes LP was reclassified to unitholders' equity. For further information see "End of

Subordination”. As a result, (loss) / income before non-controlling interest and taxes is applicable to the quarters up to December 31, 2007 only.

Our sales are seasonal, primarily related to consumer spending patterns. The footwear and accessories sector of the Canadian retail market has two primary selling seasons during which new merchandise is introduced – Spring and Fall. Gross margins fluctuate over the course of these two primary selling seasons. Other factors include, and are not limited to, the timing of new store openings, merchandise mix and weather.

In any given period, weather can have a material impact on our business. As we become more geographically diversified, we expect weather-related effects will become less significant.

CASH FLOW AND LIQUIDITY

We assess liquidity in terms of the Fund’s ability to generate sufficient cash flow to fund its operations. Net cash flow is affected by the following items:

- operating activities, including the level of accounts receivable, inventory, prepaid expenses and deposits and accounts payable and accrued liabilities;
- investing activities, including capital expenditures; and
- external financing, including bank credit facilities and other capital market activities, providing both short and long-term financing. See “Capital Resources”.

Cash Flow from Operations

The table below reconciles net income to cash flow from operations for the three-month and nine-month periods ended September 30, 2009 and 2008.

Sterling Shoes Income Fund
Reconciliation of Net (Loss) / Income to Cash provided used in operations
September 30, 2009

in (\$000's)	Three-months ended Sept 30		Nine-months ended Sept 30	
	2009	2008	2009	2008
Net (loss) / income	\$ (30,796)	1,402	(33,872)	271
Add charges (deduct credits) to operations not requiring a cash payment:				
Impairment of goodwill and intangible assets	33,246	-	33,246	-
Future income tax recovery	(4,636)	-	(4,636)	(724)
Amortization of leaseholds and equipment	1,002	818	2,538	2,348
Accreted interest expense	169	17	496	446
Amortization of deferred leasehold inducements	(101)	(97)	(539)	(282)
Loss on disposal of leaseholds and equipment	26	-	260	333
	(1,090)	2,140	(2,507)	2,392
Net change in non-cash working capital balances related to operations:				
Accounts receivable	(336)	(295)	236	261
Inventory	(3,820)	(8,889)	(3,114)	(16,620)
Revaluation of inventory per CICA Handbook Section 3031	-	-	-	3,306
Prepaid expenses and deposits	36	231	84	207
Accounts payable and accrued liabilities	3,353	5,322	3,395	4,729
Cash used in operating activities	\$ (1,857)	(1,491)	(1,906)	(5,725)

For the three-month period ended September 30, 2009, cash used in operations was \$1.9 million compared to cash used in operations of \$1.5 million in the same period of 2008. While there still is an increase in cash used by operations during the period, given the current economic climate and the significantly lower net income in the third quarter of 2009, we conserved our cash position as best as possible by managing the timing of the investments in inventory and the payment of trade payables. Similarly, cash used in operations was only \$1.9 million for the nine-

month period ended September 30, 2009 as compared to \$5.7 million for the same period in 2008 reflecting inventory build-up to support our store expansion last year.

Interim period working capital requirements typically reflect the seasonality of the business. In order to ensure that we have adequate inventory in advance of in-season demand, inventory levels increase in the periods immediately preceding peak seasons throughout the year. Accordingly, inventory levels typically increase in the first and third quarters and decline in the second and fourth quarter as sales pick up. Operating results in the three-month and nine-month periods ended September 30, 2009 generally reflected these expectations compared to prior years.

Capital Expenditures

We invested in capital expenditures of \$0.9 million and \$2.9 million (net of leasehold inducements) during the three-month and nine-month periods ended September 30, 2009 (2008 - \$1.8 million and \$5.4 million) respectively. Of this amount, \$0.3 million and \$1.1 million was invested in leaseholds and equipment to furnish new stores during the three-month and nine-month periods ended September 30, 2009 respectively (2008 - \$1.2 million and \$3.1 million). We incurred maintenance capital expenditures of \$0.7 million and \$1.8 million during the three-month and nine-month periods ended September 30, 2009 (2008 - \$0.3 million and \$2.3 million), which were related to upgrades to information technology (“IT”) infrastructure, store renovations and store relocations. New store capital expenditures and maintenance capital expenditures were funded by cash from operations and the Fund’s available credit facilities.

CAPITAL RESOURCES

Cash flow from operations and bank borrowings have been the primary funding sources for working capital requirements and capital expenditures over the last several years. During October 2007 the Fund raised \$25 million through the offering of the Debentures.

A portion of the net proceeds from the offering was used to repay existing bank indebtedness of approximately \$13 million. The balance of the net proceeds was used for existing expansion and corporate commitments during 2008.

A Canadian chartered bank has provided us with a revolving credit facility of up to \$15 million (the “Operating Loan”), which is available for working capital requirements, capital expenditures and for general corporate purposes and is repayable on October 31, 2010, subject to extension provisions. As at September 30, 2009, we have utilized \$6.8 million of the Operating Loan.

We have utilized our \$5 million revolving credit facility (the “Term Loan”) for general funding of capital expenditures, including new store facilities. The Term Loan matures on October 31, 2010 with no scheduled repayments of principal required prior to maturity.

Loans under these facilities are prepayable without any penalties and bear interest at a floating rate based on the Canadian dollar prime rate or on the bankers' acceptance rates plus, in each case, an applicable margin to those rates. The facilities are secured by a first-priority security interest in our property, subject to certain permitted encumbrances.

The facilities are subject to customary terms and conditions, including limits on incurring additional indebtedness, granting liens or selling assets without the consent of the lender, and to customary financial covenants, including the maintenance of a minimum senior fixed charge coverage ratio. The facilities may in certain circumstances restrict our ability to pay distributions, including limiting

distributions unless sufficient funds are available for the repayment of indebtedness and the payment of interest expenses. At September 30, 2009, we were in compliance with all covenants of these credit facilities.

OFF-BALANCE SHEET FINANCING

We enter into standby letters of credit to facilitate the international purchase of merchandise and to secure certain of our obligations, including insurance programs and duties related to import purchases. As of September 30, 2009, letters of credit totaling \$1.679 million have been issued. The Fund has no other off-balance sheet arrangements.

CONTRACTUAL OBLIGATIONS

We have the following inventory purchase, long-term debt and minimum rental commitments for premises, for the remainder of the current fiscal year and over the next four fiscal periods, in thousands of dollars:

<u>in \$000's</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>
Inventory purchase commitments	679				
Long-term debt				25,000	
Operating and Term Loans		11,781			
Minimum rental commitments ⁽¹⁾	<u>3,948</u>	<u>15,037</u>	<u>13,817</u>	<u>13,220</u>	<u>11,945</u>
	<u>4,627</u>	<u>26,818</u>	<u>13,817</u>	<u>38,220</u>	<u>11,945</u>

Note:

- (1) Excludes percentage rent adjustments and operating expense adjustments.

DISTRIBUTABLE CASH AND DISTRIBUTIONS

In any fiscal year Sterling Shoes LP and the Fund intend to make distributions of available cash to the maximum extent possible to the Unitholders and the non-controlling interest. This includes the distribution of all available cash from operations after cash required for maintenance capital expenditures, and after consideration of changes in non-cash working capital balances and other reserves considered advisable.

The Fund may make additional distributions in excess of monthly distributions. Distributions declared in respect of the month ended December 31 of each year may include such amounts as are necessary to ensure that the Fund will not be liable for income taxes under Part I of the Tax Act.

The Fund reviews its historic and expected results on a regular basis. This review includes consideration of economic conditions, including seasonality, and the competitive environment. Distributions made may not equal Adjusted Distributable Cash generated in any one period. The Fund's policy is to make stable monthly distributions to Unitholders based on estimated Adjusted Distributable Cash for the year.

ADJUSTED DISTRIBUTABLE CASH

On July 6, 2007 the Canadian Securities Administrators ("CSA") amended National Policy 41-201 "Income Trusts and Other Indirect Offerings" (the "CSA Guidance"). The Fund has calculated Standardized Distributable Cash based on the CSA Guidance as cash flows from operating activities, including the effects of changes in non-cash working capital, less sustaining

(maintenance) capital expenditures. The Fund has also retained the Fund's historical Non-GAAP measure of Adjusted Distributable Cash (formerly Distributable Cash) by further adjusting Standardized Distributable Cash to exclude the effect of changes in non-cash working capital. The table below is a summary of Standardized Distributable Cash and Adjusted Distributable Cash and per Unit and Ratio disclosures for the three-month and nine-month periods ended September 30, 2009.

in \$000's except per unit amounts and payout ratios	Three-months ended Sept 30		Nine-months ended Sept 30	
	2009	2008	2009	2008
Standardized Distributable Cash				
Cash used in operating activities	\$ (1,857)	\$ (1,491)	\$ (1,906)	\$ (5,725)
Less: Maintenance Capital Expenditures	(708)	(330)	(1,836)	(2,339)
Standardized distributable cash generated	\$ (2,565)	\$ (1,821)	\$ (3,742)	\$ (8,064)
Less: Changes in non-cash working capital balances related to operations	(767)	(3,631)	601	(11,423)
Adjusted distributable cash generated	\$ (1,798)	\$ 1,810	\$ (4,343)	\$ 3,359
Adjusted Distributable Cash available for distribution to Unitholders	\$ (1,798)	\$ 1,810	\$ (4,343)	\$ 3,359
Adjusted Distributable Cash generated per Unit	\$ (0.271)	\$ 0.273	\$ (0.654)	\$ 0.506
Distributions declared per Unit	\$ 0.056	\$ 0.375	\$ 0.197	\$ 1.125
Adjusted Payout Ratio	-20.6%	137.6%	-30.1%	222.4%
Number of units outstanding:	6,641,860	6,641,860	6,641,860	6,641,860

Management believes that the Standardized Distributable Cash calculation introduces significant volatility to the Fund's quarter-to-quarter distributable cash and payout ratios, as our non-cash working capital fluctuates significantly as a result of the seasonality of our business, changes in the timing of the payment of payable transactions and the investment in working capital required to open new stores. As a result, management believes our historical measure of Adjusted Distributable Cash, which excludes the impact of changes in non-cash working capital, is a better measure for determining our operating performance.

The Fund's Board looks beyond quarter-to-quarter fluctuations in working capital when making decisions regarding monthly distributions. As mentioned earlier, the Fund's policy has been to make distributions to its Unitholders necessary to pay out its taxable income. The adjusted payout ratio for the trailing twelve months ended September 30, 2009 was 113.5%, as compared to 139.3% for the twelve months ended September 30, 2008.

Cash distributions have been made as follows:

Distribution History	Distributions	Distribution History	Distributions	Distribution History	Distributions
Year / Month	per Unit	Year / Month	per Unit	Year / Month	per Unit
2005		2006		2007	
		January	\$ 0.08958	January	\$ 0.12000
		February	0.08958	February	0.12000
		March	0.08958	March	0.12000
		April	0.08958	April	0.12000
		May ⁽³⁾	0.10500	May	0.12000
		June	0.10500	June	0.12000
		July	0.10500	July	0.12000
		August	0.10500	August	0.12000
July / August ⁽¹⁾	\$ 0.14737	September	0.10500	September	0.12000
September	0.08958	October	0.10500	October	0.12000
October	0.08958	November ⁽⁴⁾	0.12000	November	0.12000
November	0.08958	December	0.12000	December	0.12000
December	0.08958	December ⁽⁵⁾	0.32000	December ⁽⁷⁾	0.36000
December ⁽²⁾	0.16000	December ⁽⁶⁾	0.15000	December ⁽⁸⁾	0.06000
Total 2005	\$ 0.66569	Total 2006	\$ 1.69832	Total 2007	\$ 1.86000
2008		2009			
January ⁽⁹⁾	\$ 0.12500	January	\$ 0.03333		
February	0.12500	February	0.03333		
March	0.12500	March ⁽¹¹⁾	0.01862		
April	0.12500	April	0.01862		
May	0.12500	May	0.01862		
June	0.12500	June	0.01862		
July	0.12500	July	0.01862		
August	0.12500	August	0.01862		
September	0.12500	September	0.01862		
October	0.12500	October	0.01862		
November ⁽¹⁰⁾	0.03333				
December	0.03333				
Total 2008	\$ 1.31667	Total year-to-date 2009	\$ 0.21562		

Notes:

- (1) The Fund made its initial distribution of \$0.14737 per Unit for the 51-day period from July 12, 2005 to August 31, 2005.
- (2) On December 13, 2005 the Fund announced a special distribution of \$0.16 per Unit to Unitholders of record on December 30, 2005, representing the Fund's estimate of the distribution required to ensure the Fund was not liable for income taxes under Part I of the Tax Act for fiscal 2005. \$0.16 per Unit, the Fund's estimate of this amount, was paid on January 16, 2006 to Unitholders of record on December 30, 2005.
- (3) Effective May 1, 2006 the Fund raised its monthly distribution by 17.2% from \$0.08958 per Unit to \$0.105 per Unit.
- (4) Effective November 1, 2006 the Fund raised its monthly distribution by 14.3% from \$0.105 per Unit to \$0.12 per Unit.
- (5) On December 18, 2006 the Fund announced a special distribution of \$0.32 per Unit to Unitholders of record on December 29, 2006, representing the Fund's estimate of the distribution required to ensure the Fund was not

liable for income taxes under Part I of the Tax Act for fiscal 2006. This amount was paid on January 15, 2007 to Unitholders of record on December 29, 2006.

- (6) On March 22, 2007 the Fund announced a supplementary special distribution of \$0.15 per Unit to Unitholders of record on December 29, 2006, representing the Fund's remaining distribution required to ensure the Fund was not liable for income taxes under Part I of the Tax Act for fiscal 2006. The \$0.15 per Unit supplementary special is in addition to the \$0.32 per Unit that was estimated at December 18, 2006 and paid on January 15, 2007. The \$0.15 per Unit was paid on March 30, 2007 to Unitholders of record on December 29, 2006.
- (7) On December 17, 2007 the Fund announced a special distribution of \$0.36 per Unit to Unitholders of record on December 31, 2007, representing the Fund's estimate of the distribution required to ensure the Fund was not liable for income taxes under Part I of the Tax Act for fiscal 2007. This amount was paid on January 15, 2008 to Unitholders of record on December 31, 2007.
- (8) On March 26, 2008 the Fund announced a supplementary special distribution of \$0.06 per Unit to Unitholders of record on December 31, 2007, representing the Fund's remaining distribution required to ensure the Fund was not liable for income taxes under Part I of the Tax Act for fiscal 2007. The \$0.06 per Unit supplementary special is in addition to the \$0.36 per Unit that was estimated at December 17, 2007 and paid on January 15, 2008. The \$0.06 Unit was paid on March 31, 2008 to Unitholders of record on December 31, 2007.
- (9) Effective January 1, 2008 the Fund raised its monthly distribution by 4.2% from \$0.12 per Unit to \$0.125 per Unit.
- (10) Effective November 1, 2008 the Fund reduced its monthly distribution by 73% from \$0.125 per Unit to \$0.03333 per Unit.
- (11) Effective March 1, 2009 the Fund reduced its monthly distribution by 44% from \$0.03333 per Unit to \$0.01862 per Unit.

Distributions are paid on the 15th of each month, or the next following business day, to Unitholders of record on the last business day of the preceding month. Unitholders who are non-residents of Canada are required to pay all withholding taxes payable on any distributions by the Fund. Effective April 1, 2008, distributions to the non-controlling interest have been made monthly and are no longer subordinated. These distributions were subject to subordination until December 31, 2007 pending the Fund achieving specific EBITDA and distribution targets. For further information see "End of Subordination".

The Fund declared distributions to public Unitholders of \$371 thousand and \$1.3 million for the three-month and nine-month periods ended September 30, 2009 (2008 - \$2.5 million and \$7.5 million), respectively.

NON-GAAP MEASURES

References to "EBITDA" are to earnings before interest, income taxes, depreciation and amortization and references to "Adjusted EBITDA" are to EBITDA after adjusting for amortization of leasehold inducements. EBITDA is a measure used by many investors to compare issuers on the basis of ability to generate cash flow from operations. Adjusted EBITDA is a measure our management believes facilitates the comparability and analysis of our financial performance. EBITDA and Adjusted EBITDA are not earnings measures recognized by GAAP and do not have standardized meanings prescribed by GAAP and are therefore unlikely to be comparable to similar measures presented by other issuers. We intend to distribute substantially all of our cash on an on-going basis (after providing for certain amounts described elsewhere in this MD&A) and, accordingly, our management believes that EBITDA and Adjusted EBITDA are important

supplemental measures in evaluating our performance and in determining whether to invest in Units.

You are cautioned that EBITDA and Adjusted EBITDA should not be construed as an alternative to net income or loss determined in accordance with GAAP as indicators of our performance or to cash flows from operating, investing and financing activities as measures of our liquidity and cash flows.

“Maintenance Capital Expenditures” is not a recognized measure under GAAP. Maintenance Capital Expenditures include those required to upgrade existing stores and to maintain information systems and equipment and our warehouse.

FUTURE INCOME TAXES

On October 31, 2006, the Minister of Finance announced proposed changes to the income tax treatment of “flow-through entities”, including income trusts. On June 22, 2007 the Government of Canada enacted new legislation imposing a tax on distributions paid by publicly traded income trusts in Canada, commencing in 2011. Unitholders will be treated as if they have received an eligible dividend from a Canadian public corporation equal to the taxable portion of their distributions and will be taxed accordingly.

Prior to June 22, 2007, the Fund calculated its future income tax on certain temporary differences between amounts recorded on its balance sheet for book and tax purposes at a nil tax rate. Under the newly enacted legislation, the tax rate on the post-2010 reversal of these temporary differences is estimated to be 28.5%. Temporary differences reversing prior to December 31, 2010 will still give rise to nil future income taxes. Based on its assets and liabilities as at December 31, 2007, the Fund has estimated the amount of its temporary differences which were previously not subject to tax and the period in which these differences will reverse.

As a result of this new legislation, Canadian accounting guidance requires that the Fund record a future tax liability and a corresponding, one-time, non-cash charge to net income. The Fund’s identifiable intangible assets, recorded on the balance sheet at \$49.0 million, (but which have nil basis for tax purposes), are treated as a temporary difference that will reverse after January 1, 2011.

The result of this treatment was a future income tax liability of \$7.7 million created during the second quarter of 2007. This future income tax liability was based on the expected tax rate of 31.5% and the assumption that the Fund will be a taxable entity in 2011. Based on the currently enacted tax rate of 28.5%, and the same assumptions, the Fund revised this future income tax liability during the first quarter of 2008 to \$7.0 million. As at September 30, 2009 the impairment of intangible assets further reduced the Fund’s expected future income tax liability. The future income tax recovery for the three-month and nine-month periods ended September 30, 2009 was \$4.6 million (2008 - \$nil) with the remaining future income tax liability estimated at \$2.4 million based on the temporary differences between the accounting and tax basis of the Fund’s assets and liabilities expected to reverse after January 1, 2011.

In future periods, adjustments to this future tax liability may be required based on changes in the differences between the tax basis and financial statement basis of the Fund’s assets and liabilities. These adjustments could be material. Consistent with the initial recognition, any future adjustments will be non-cash in nature and will be either a charge or an addition to net income of the period.

Since this tax will not be in effect until 2011, any changes to the tax legislation or to the legal structure of the Fund prior to that time could have a material effect on the level of the future income taxes recorded by the Fund.

TRANSACTIONS WITH RELATED PARTIES

- (a) The Fund paid rent to a company in which Jeremy Horwitz and Mannie Druker, trustees and officers of the Fund, have an interest, amounting to \$71 thousand and \$213 thousand for the three-month and nine-month periods ended September 30, 2009 (2008 – \$71 thousand and \$213 thousand), respectively.
- (b) The Fund purchased equipment from a company in which Mannie Druker, a trustee and officer of the Fund, has an interest, for \$48 thousand and \$163 thousand during the three-month and nine-month periods ended September 30, 2009 (2008 – \$190 thousand and \$413 thousand), respectively.

These transactions arose during the normal course of business and have been recorded at the exchange amount, which is the amount agreed upon by the parties.

CRITICAL ACCOUNTING ESTIMATES

The preparation of our financial statements requires us to estimate the effect of several variables that are inherently uncertain. These estimates and assumptions can affect the reported amounts of assets, liabilities, sales and expenses. Management bases its estimates on historical experience and other assumptions, which it believes to be reasonable under the circumstances. Management also evaluates its estimates on an ongoing basis. Our significant accounting policies are described in Note 2 of the Fund's financial statements for the three and twelve-month periods ended December 31, 2008. Management believes that the following items represent the Fund's critical accounting estimates.

Inventory Valuation

Effective January 1, 2008, the Fund adopted CICA Handbook Section 3031, Inventories ("Section 3031"). Section 3031 requires inventories to be measured at the lower of cost and net realizable value. The Fund determines inventory cost based on a weighted average cost formula and values inventory at the lower of cost and net realizable value.

Intangible assets and Goodwill

Identifiable intangible assets, including store banners and private label brand names, are carried at cost. These assets have been determined by management to have indefinite lives and are therefore not being amortized. These assets are reviewed at least annually for impairment or whenever events or changes in circumstances indicate that the carrying amount of an asset may be impaired.

If such assets are considered to be impaired, the impairment to be recognized is measured as the amount by which the carrying amount of the assets exceeds fair value.

At September 30, 2009 the Fund determined that the fair value of the intangible assets was less than the book value, resulting in a non-cash impairment charge of \$32.4 million for the three-months ended September 30, 2009. The impairment arose primarily due to future economic uncertainty and the higher cost of capital assumptions in the valuation methodology

Goodwill is recorded at cost and is not amortized. Goodwill is reviewed for impairment at least annually, or whenever events or changes in circumstances indicate that the carrying amount may be impaired. If goodwill is considered to be impaired, the impairment to be recognized is measured as the estimated amount by which the carrying amount of the goodwill exceeds fair value.

In view of the current economic and market conditions, management reviewed the Fund's goodwill for impairment. At September 30, 2009 the Fund determined that the fair value of the goodwill was less than the book value primarily due to future economic uncertainty and the higher cost of capital assumptions in the valuation methodology. As a result, the Fund has recorded a non-cash impairment charge of \$0.8 million for the three-months ended September 30, 2009.

Future income taxes

Future income tax assets and liabilities are determined based on the difference between the tax basis of the Fund's assets and liabilities and the amounts reported in the financial statements. Future tax assets or liabilities are calculated using the tax rates for the periods in which the differences are expected to be settled. Future tax assets are recognized to the extent that they are considered more likely than not to be realized.

Convertible Debentures

The Fund has allocated the proceeds of the Debentures between debt and equity based on the relative fair values of the debt and the conversion option, as determined by the residual valuation of the equity component. Under this approach, the liability component was valued first, and the difference between the proceeds of the Debentures and the fair value of the debt was assigned to the conversion option. The present value of the liability component was calculated using a discount rate of 9.2%, the estimated market interest rate at the date of issuance for similar debentures having no conversion rights.

NEW ACCOUNTING STANDARDS ADOPTED

The Canadian Institute of Chartered Accountants ("CICA") issued a new accounting standard that became effective for the Fund on January 1, 2009: Handbook Section 3064, Goodwill and Intangibles ("Section 3064"). Section 3064 replaces Handbook Section 3062 of the same title and Handbook Section 3450, Research and Development Costs. Section 3064, effective for fiscal years beginning on or after October 1, 2008, establishes standards for the recognition, measurement and disclosure of goodwill and intangible assets. While the standards concerning goodwill are unchanged from the standards in the previous Section 3062, the provisions related to the definition and initial recognition of intangible assets are equivalent to the corresponding provisions of IFRS.

FUTURE CHANGES IN ACCOUNTING STANDARDS

(i) International Financial Reporting Standards ["IFRS"], as discussed above.

The Canadian Accounting Standards Board (AcSB) will require all public companies to adopt IFRS for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011. The Fund will be required to prepare both current and comparative financial information using IFRS.

While the conceptual framework for IFRS and Canadian GAAP are similar, there are significant differences in recognition, measurement and disclosure requirements. The Fund has developed a changeover plan to map its conversion from Canadian GAAP to IFRS by identifying and documenting the areas of significant differences that apply to the Fund, evaluating the different options available under IFRS, assessing the impact of the changes to the Fund's financial reporting, business processes and information systems, and anticipating the steps necessary for successful conversion on the date of transition. The Fund expects training and additional resources will be utilized to ensure timely conversion to IFRS.

The financial impact of the transition to IFRS cannot be reasonably estimated at this time. The Fund will continually review and adjust the changeover plan as necessary to properly address the key elements of the plan.

(ii) Handbook Section 1582, Business Combinations ("Section 1582")

Section 1582 replaces Handbook Section 1581 of the same title. It provides the Canadian equivalent to corresponding sections of IFRS.

Section 1582 applies prospectively to business combinations for which the acquisition date is on or after January 1, 2011 with early adoption permitted. This section improves the relevance, reliability, and comparability of the information that a reporting entity provides in its financial statements about a business combination. Adoption of this standard is not expected until January 1, 2011. The Fund has not yet determined the impact of the adoption of this new Section on the consolidated financial statements.

(iii) Handbook Section 1601, Consolidated Financial Statements ("Section 1601") and Handbook Section 1602, Non-controlling Interests ("Section 1602")

Sections 1601 and 1602 replace Handbook Section 1600, Consolidated Financial Statements and apply to fiscal years beginning on or after January 1, 2011, with early adoption permitted. Section 1601 establishes standards for the preparation of consolidated financial statements. Section 1602 establishes standards for accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination. An entity which adopts Section 1582, 1601, or 1602 early also adopts the other two sections at the same time. Adoption of this standard is not expected until January 1, 2011. The Fund has not yet determined the impact of the adoption of this new Section on the consolidated financial statements.

RISKS AND UNCERTAINTIES

BUSINESS RISK

A detailed discussion of our significant business risks is provided in the MD&A for the year ended December 31, 2009 and in the 2009 Annual Information Form, both of which can be found at www.sedar.com. There were no changes to our significant business risks during the nine months ended September 30, 2009.

CERTIFICATION OF DISCLOSURE CONTROLS AND PROCEDURES AND INTERNAL CONTROL OVER FINANCIAL REPORTING

Our management is responsible for designing disclosure controls and procedures that: (a) provide reasonable assurance that material information required to be disclosed by us is accumulated and

communicated to management to allow timely decisions regarding required disclosure; and (b) ensure that information required to be disclosed by us is recorded, processed, summarized, and reported within the time periods specified in applicable securities legislation. .

Our management is responsible for designing, establishing and maintaining an adequate system of internal control over financial reporting. Our internal control system was designed based on the Internal Control – Integrated Framework (“COSO Framework”) published by The Committee of Sponsoring Organizations of the Treadway Commission to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes, in accordance with Canadian generally accepted accounting principles (“Canadian GAAP”).

Our Chief Executive Officer and Chief Financial Officer certified the appropriateness of the financial disclosures in the interim MD&A and unaudited interim consolidated financial statements for the period ended September 30, 2009. These executives also certified that they are responsible for the design of disclosure controls and procedures and internal control over financial reporting. There have been no changes in internal control over financial reporting during the quarter ended September 30, 2009 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

The Fund’s Board of Trustees and Audit Committee reviewed and approved the September 30, 2009 unaudited interim consolidated financial statements and this management’s discussion and analysis prior to its release.

FORWARD-LOOKING STATEMENTS

This MD&A includes forward-looking statements. Forward-looking statements relate to, among other things, anticipated financial performance, business prospects, strategies, market forces, and commitments. Many of these statements can be identified by words such as “believe”, “expects”, “expected”, “will”, “intends”, “projects”, “anticipates”, “estimates”, “continues” or similar words. The Fund believes the expectations reflecting in such statements are reasonable but no assurance is given that such expectations will be correct. All forward-looking statements are based on the Fund’s beliefs and assumptions based on information available at the time the assumption was made and on management’s experience and perception of historical trends, current conditions and expected further developments as well as other factors deemed appropriate in the circumstances. In addition to other assumptions made in this MD&A, assumptions have been made in respect of factors such as, but not limited to, the following:

- industry activity levels;
- competitive conditions;
- consumer demand;
- access to capital;
- capital expenditure estimates, plans, schedules and activities;
- income tax considerations;
- operating risks; and
- cash distributions

By its nature, such forward-looking information is subject to various risks and uncertainties that are known and unknown, including general economic conditions and markets and, in particular, the potential impact of the current economic downturn, the cost and availability of capital, the possibility of deterioration in our working capital position, the impact on our liquidity if we were

to go offside of the covenants in our debt facilities, our ability to maintain profitability and manage growth, risks associated with leasing and expansion, competition, inventory and sourcing risk, ability to identify and respond to changing consumer fashion preferences, risks associated with international purchasing, reliance on key personnel, dependence on consumer spending, unseasonable weather conditions, uncertainties arising from world events, intellectual property risks, foreign exchange fluctuations on imported merchandise, labour relations, seasonality and fluctuations in cash distributions, fluctuations in distributable cash based on our performance, restrictions on potential growth, future issuances of Units by the Fund or future disposition of Units held by SSI Investments Inc., income tax matters, changes in accounting standards, including the transition to IFRS, and increases in interest rates. These risks are discussed in the Fund's most recent annual information form and in this management's discussion and analysis of the Fund and could cause actual results and experience to differ materially from the anticipated results or other expectations expressed. Readers are cautioned not to place undue reliance on this forward-looking information, which is given as of the date it is expressed in this annual information form or otherwise, and the Fund undertakes no obligation to update publicly or revise any forward-looking information to reflect new events or circumstances, except as explicitly required by securities laws.

ADDITIONAL INFORMATION

Additional information relating to the Fund, including the Fund's Annual Information Form and other public filings, are available on SEDAR (www.sedar.com) and on the Fund's website at www.SterlingShoesIncomeFund.com.

INVESTOR RELATIONS

Daniel S. Gumprich
Chief Financial Officer
2580 Viscount Way
Richmond, BC V6V 1N1
Phone: (604) 270-6114