Q1

KILLAM
PROPERTIES INC

2006 FIRST QUARTER REPORT

First Quarter 2006 Highlights

$35 million in acquisitions

84% increase in revenue over first quarter 2005

50% increase in funds from operations over first quarter 2005

$403 million in multifamily apartments in four provinces

$89 million in manufactured home communities in five provinces

President's Message to Shareholders

On behalf of the Board of Directors, I am pleased to present Killam's first quarter 2006 results and discussion of operations. Killam continues to grow with the acquisition of an additional 741 units in the first quarter, bringing our total units to 12,170 as at March 31, 2006. Throughout the quarter we expanded our apartment portfolio presence in a number of markets including St. John's, NL and Moncton, NB. In addition we continue grow our manufactured home community (MHC) line of business with the acquisition of an additional 163 units in the first quarter.

Strategic Priorities

We continue to view revenue enhancement as one of our strategic priorities through the following;

- Increasing below market rents to current rates on the renewal and roll-over of current leases.
- Acquire $100-150 million of new acquisition in 2006 to expand our portfolio.
- Continue to expand our MHC business by developing new sites. We are continuing to expand our Glen Aire Estates property and we have launched the expansion of Green Hill Estates which will also provide us revenue from the sale of new homes into this expanded community.
- Continue to move a number of our apartment sites through the planning and approval stages to determine the expansion capacity the surplus land will hold. Management believes that the surplus land on existing properties could contain up to 750 to 1,000 extra units. The surplus land could either be developed internally or sold to a third party.
- Finally, we are investing in our apartment portfolio through capital upgrades to reposition certain assets by improving their functionality and overall presentation.

Strong Financial Management

Our first quarter 2006 results were on target with our expectations. Our revenues grew by approximately 10% over the fourth quarter of 2005. More importantly Funds from Operations (FFO) were $2.1 million in the first quarter of 2006, an increase of $0.5 million from the same period in 2005. Our net loss of $1.2 million was negatively affected by $2.0 million of building amortization. We are required by generally accepted accounting principles to amortize our buildings even though they do not reduce in value over time.

Killam in the Community

During 2005 we launched our "Home Away From Home" community program with the donation of a furnished suite to Ronald McDonald House for patient families of the IWK Health Centre. During the last quarter we expanded the program by donating a furnished suite to Saint John and Moncton, New Brunswick hospitals. I would like to extend Killam's thanks to our staff who have worked hard to renovate and furnish these suites to allow us to "Welcome Home" the families of patients.

Looking Forward

We are excited about the acquisition opportunities that still exist in our core markets. We will continue to acquire quality assets that are accretive and effectively integrate the new properties into our portfolio.

I would like to thank our shareholders for their continued support and I look forward to our next quarterly report to update you on our progress.

Sincerely,

Philip Fraser
President & CEO

May 3, 2006

Management's Discussion and Analysis:

Overview of the Structure of the MD&A

The following management's discussion and analysis (MD&A) has been prepared by management and focuses on key statistics from the consolidated financial statements and pertains to known risks and uncertainties. To ensure that the reader is obtaining the best overall perspective, this MD&A should be read in conjunction with material contained in the Company's 2005 Annual Report and the Company's 2005 Annual Information Form. These documents are available on SEDAR at www.sedar.com. The discussions in this MD&A are based on information available at May 2, 2006. The MD&A will be presented in the following structure:

Corporate Overview provides an overview of the Company as well as a discussion of the significant developments of the first quarter of 2006.

Financial Performance Summary provides a high-level overview of the Company and its financial performance in the first quarter of 2006. Please note that a more detailed discussion of the results is provided in latter sections of the MD&A.

Financial Statement Analysis provides a detailed discussion and analysis of the Company's financial performance for the first quarter of 2006 and financial position as at March 31, 2006.

Liquidity and Capital Resources provides a discussion of the Company's financing needs and our plans to source these funds.

Risk Management provides a detailed look at the Company's significant risks and our management of these risks.

Accounting Estimates and Policies provides a brief discussion on the Company's critical accounting estimates and policies.

Future Objectives provides an overview of the Company's key performance targets for 2006.

Forward-looking Statements

Certain statements in this MD&A constitute "forward-looking statements". You can identify forward-looking statements by our use of the words "believe", "expect", "anticipate", "intend", "estimate", "assume", "project", and other similar terms that predict or indicate future events and trends that do not relate to historical matters. Such statements are based on Killam management's assumptions and beliefs in light of the information currently available to them. Readers are cautioned not to place undue reliance on forward-looking statements. A number of important factors could cause actual results to differ materially from those expressed in such forward-looking statements.

Non-GAAP Measures

There are measures included in this MD&A that do not have a standardized meaning under Generally Accepted Accounting Principles (GAAP) and therefore may not be comparable to similarly titled measures presented by other publicly traded companies. The Company includes these measures as a means of measuring financial performance.

- Earnings from property operations are calculated as revenue less property operating expenses.
- Funds from operations (FFO) are calculated as net income plus amortization, stock compensation, non-cash debenture interest, and future income taxes.
- Same store results are rental revenues and property operating expenses for properties the Company has owned for equivalent periods in 2005 and 2006.

Management's Discussion and Analysis:

Corporate Overview

Killam Properties Inc. ("Killam") is a publicly traded real estate company focused on the acquisition, re-development and management of multi-family apartments and manufactured home communities (MHCs). Killam's corporate strategy is based on the principles of bringing professional management to a fragmented industry coupled with a portfolio diversified by two asset classes operating in multiple regions.

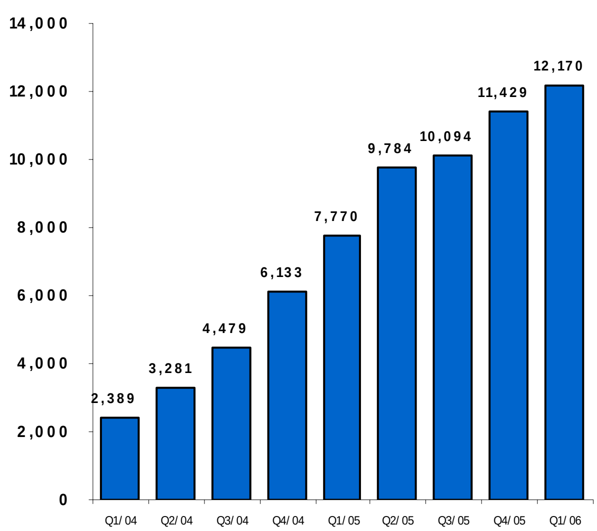
Killam continued to consolidate the rental market during the first quarter of 2006 with the acquisition of ten properties representing 741 units to bring the Company's total portfolio to 12,170 units.

Portfolio Summary

By Unit Type and Location

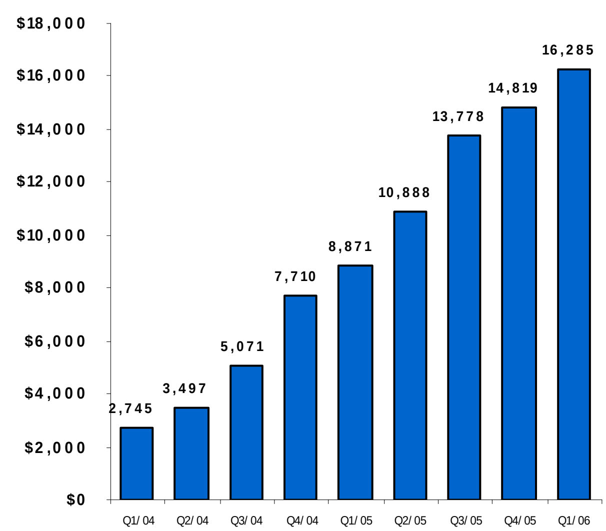
	Apartments	MHCs	Total
Halifax	3,472	291	3,763
Moncton	841	1,160	2,001
Saint John	1,062	100	1,162
Fredericton	248	176	424
St. Johns/Grand Falls	679	86	765
Sydney	156	217	373
PEI	588	-	588
Other NS	-	984	984
Other NB	-	86	86
Ontario	-	1,777	1,777
Saskatchewan	-	247	247
Total	7,046	5,124	12,170
Percentage by unit count	57.9%	42.1%	
Percentage by dollar value	82.6%	17.4%	

Unit Growth



Revenue Growth

(in $000's)



Management's Discussion and Analysis:

Financial Performance Summary

As at and for the three months ended,

	March 31, 2006	March 31, 2005	December 31, 2005
Total assets	**$513,193,382**	$283,750,702	$469,516,525
Mortgages payable	**327,030,503**	191,204,176	302,821,105
Shareholders' equity	**93,682,784**	77,914,113	94,843,668
Total revenue	**16,285,167**	8,870,567	14,820,759
Net operating income	**8,380,345**	4,639,634	8,287,979
Funds from operations	**2,057,690**	1,596,803	3,137,947
Net loss	**(1,205,266)**	(61,818)	(292,620)
Net loss per share - basic	**(0.0148)**	(0.00008)	(0.0036)
- diluted	**(0.0148)**	(0.00008)	(0.0036)

Total Assets increased to $513.2 million (3.3%) over December 31, 2005 as a result of completing the acquisition of ten properties during the first quarter of 2006. These acquisitions added 741 units to our rental portfolio.

Total Revenue for the first quarter of 2006 increased $7.4 million (83.6%) over 2005 driven by the unit growth during 2006.

Funds from Operations (FFO) increased by $0.5 million (28%) over the first quarter of 2005 as a result of the increase in the rental portfolio during 2006.

Net Loss of $1.2 million for the first quarter of 2006 is higher than 2005 as a result of a number of factors including higher energy costs and $2.0 million of depreciation related to the Company's building assets. In addition, the first quarter of 2006 included $1.2 million of additional interest related to Killam's convertible debenture interest ($0.7 million) and credit facility interest ($0.5 million). Please see a detailed discussion later in the MD&A.

Revenues per acquisition year
(In $000s)

	2005				**2006**
	Q1	**Q2**	**Q3**	**Q4**	**Q1**
Revenue from 2002 acquisitions	$ 632	$ 646	$ 652	$657	$665
Revenue from 2003acquisitions	1,683	1,690	1,690	1,647	1,645
Revenue from 2004 acquisitions	6,339	6,319	6,498	6,644	6,829
Revenue from 2005 acquisitions	200	2,114	4,917	5,761	6,393
Revenue from 2006 acquisitions	-	-	-	-	635
	$8,854	$10,796	$13,757	$14,709	$16,167

The above revenue excludes corporate revenues.

Management's Discussion and Analysis:

Financial Statement Analysis

Consolidated Statement of Income

Revenue

For the three months ended March 31	**2006**	2005	% change
Rental income	**$16,051,521**	$8,832,496	82%
Interest income	**17,372**	12,689	37%
Other income	**216,274**	25,382	752%
	$16,285,167	$8,870,567	84%

Rental revenue increased $7.2 million or 82% compared to the prior year. The increase is due primarily to the completion of accretive acquisitions over the past twelve months.

The annualized rental revenue of the properties the Company owned as at March 31, 2006 is approximately $64.1 million based on the rental and vacancy rates as at quarter-end. Killam, as with all real estate rental operators, is sensitive to vacancy rates. However, Killam believes its portfolio is quite defensive given our diversification in terms of multiple locations and two asset classes. Based on our current rents, a 1% change in vacancy rates would impact the annualized rental revenues by $0.68 million.

Other income for 2006 includes commissions on the Company's exclusivity agreement with Aliant Inc., a gain on debt settlement and other sundry revenue from tenants.

The following table presents our revenues by operating segment:

For the three months ended March 31	**2006**	2005	% change
Apartments	**$13,014,900**	$7,702,713	69%
Manufactured Home Communities	**3,151,576**	1,151,436	173%
Corporate	**118,691**	16,418	622%
	$16,285,167	$8,870,567	84%
Weighted average rent per unit			
Apartments	**$670**	$646	4%
Manufactured Home Communities	**$195**	$186	5%

Weighted average rent per unit increased for both apartments and MHCs in 2006 over 2005. Both of these increases are primarily the result of new acquisitions in the relatively more expensive sub-markets of Halifax for apartments and southwestern Ontario for MHCs.

The following table presents our revenues by operating segment as a percentage of total revenue

For the three months ended March 31	**2006**	2005
Apartments	**79.9%**	86.8%
Manufactured Home Communities	**19.4%**	13.0%
Corporate	**0.7%**	0.2%

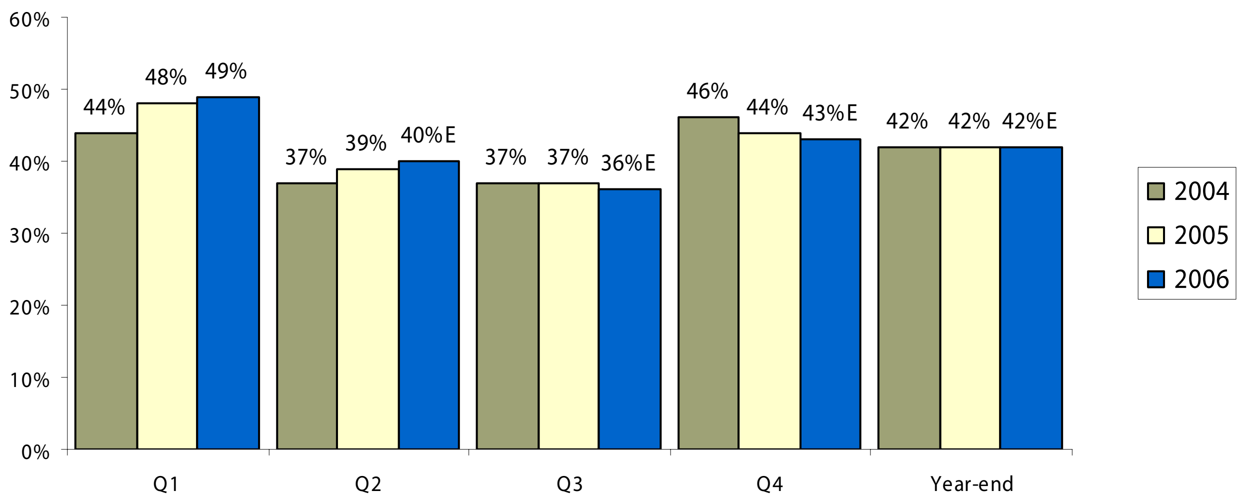
Management's Discussion and Analysis:

Property Operating Expenses

For the three months ended March 31	**2006**	2005	% change
Apartments	**$6,616,757**	$3,840,680	72%
Manufactured Home Communities	**1,288,065**	390,253	230%
	$7,904,822	$4,230,933	87%
As a Percentage of Rental Revenue	**49.2%**	47.9%	

Property operating expenses include property taxes, utilities, salaries and benefits for employees at the property level, repair and maintenance, insurance, advertising and other expenses directly associated with a property. Property operating expenses were higher on a gross dollar basis due primarily to the increase in the size of the portfolio.

Operating Costs as a Percentage of Rental Revenue



Property operating expenses as a percentage of rental revenue increased slightly to 49.2% in 2006 from 47.9% in 2005. This increase was minimized through effective cost management even with large increases in the following costs and other factors:

- Oil increased 27% in Q1-2006 versus Q1-2005 while natural gas prices increased 21% in the same period. The Company hedged approximately 75% of its oil consumption for the first quarter of 2006 which kept its oil prices to a 20% increase.
- In many of our markets, property taxes and water and sewer rates continue to rise by 5-15% over the previous quarter.
- Killam had not actively pursued rental increases to offset these rising operating costs as it continued to consolidate the marketplace. Increases in rent likely would have the effect of raising the cost of acquiring other buildings within those markets. However, during the third quarter of 2005 and into 2006 the Company has initiated rental increases in those markets where we have a significant presence.

The property operating expense percentage is a key performance indicator for Killam as it represents the Company's ability to effectively manage its portfolio. In addition, the Company compares the "same store" results for properties which we have owned since January 1, 2005. A comparison of these results is presented below.

Management's Discussion and Analysis:

Same Store Results

The following table sets out the results of operations for 58 properties (5,942 units) we have owned for equivalent periods in 2006 and 2005.

For the three months ended March 31	**2006**	2005	% change
Rental revenues	**$8,647,487**	$8,470,725	2%
Property operating expenses	**4,317,600**	4,053,739	6%
Earnings from property operations	**$4,329,887**	$4,416,986	(2)%
Operating expenses as a percentage of rental revenue	**49.9%**	47.9%	

Earnings from property operations decreased slightly ($87,099 or 2%) compared to the prior year. Rental revenues increased 2% as a result of beginning to lease units which had been undergoing renovations as well as increased rents at re-leasing. The 6% increase in property operating costs over the same quarter of 2005 is well below the general rate increases seen in utility costs, water and sewer rates and property taxes as the Company minimized these increases through effective cost management.

Mortgage and Loan Interest

Financing expenses were higher in 2006 on a gross dollar basis compared to the prior year due to the increase in the mortgage portfolio related to acquisitions. Mortgage and loan interest on a gross dollar basis is expected to continue to increase during the remainder of 2006 as the Company continues to expand its portfolio. However, Killam expects to continue to finance properties at favorable rates throughout 2006. Please see further discussion in the Mortgages Payable section of the MD&A.

Killam is sensitive to interest rate changes, however, the Company manages this risk by entering into fixed-rate mortgages and staggering the maturity dates of the mortgages. The reader should review the section on debt discussed later in the MD&A. An annualized 1% change in the interest rate on Killam's debt at March 31, 2006 would affect financing costs by $3.3 million per year were all of Killam's debt maturing within one year. However, as an example, only $66.5 million of Killam's mortgages are due within the next three years and that same interest rate change would only impact Killam by $0.67 million per annum.

Depreciation Expense

Depreciation expense increased $1.9 million compared to 2005. The increase in amortization is a result of the increased portfolio as well as Killam's capital improvement program.

General and Administrative Expenses

For the three months ended March 31	**2006**	2005	% change
Total	**$712,590**	$526,895	35%
As a Percentage of Rental Revenue	**4.4%**	6.0%	

General and administrative expenses include expenses which are not specific to an individual property. These expenses include TSX related costs, management salaries and benefits, office rent, communication costs, office equipment leases and other head office expenses. The percentage has decreased from 2005 as there is a relatively fixed component of these expenses which continues to be spread over increased revenue as Killam continues to grow its portfolio.

Management's Discussion and Analysis:

Provincial Large Corporation Tax (Capital Tax)

The Company is required to pay provincial capital tax in certain provinces based on the total taxable capital invested in those provinces at year-end. Total taxable capital invested includes share capital and mortgages on properties held outside the Company's internal trusts and is not a function of the time the capital is invested. These taxes are deductible for provincial and federal income tax purposes and the tax benefit of this deduction is included in Income Tax as discussed below. The increase in provincial capital tax from $49,086 in 2005 to $72,033 in 2006 is largely the result of the Company's private equity and debt placement in May 2005.

Income Tax

For the three months ended March 31	**2006**	2005	% change
Current	**$22,322**	$ 19,752	13%
Future	**(650,000)**	(25,783)	N/A%
	$(627,678)	$ (6,031)	N/A%

Current income tax expense represents federal large corporation's tax. The increase over 2005 is largely the result of the Company's May 2005 private equity and debt placement. In addition, the Company has booked a future income tax recovery representing the future tax benefit of Killam's 2006 net loss at an effective rate of approximately 35%.

Consolidated Balance Sheet

Capital Assets

As at	**March 31 2006**	December 31 2005	% change
Net book value	**$489,692,479**	$452,076,153	8.3%

Capital assets increased to $489.7 million from $452.1 million, as a result of ten property acquisitions totaling 741 units in the first quarter of 2006.

The following table is a summary of the Company's acquisitions for the first quarters ended March 31, 2006 and 2005. The acquisition value set out below excludes third party costs such as legal, environmental and other costs paid as part of the acquisition process.

For the three months ended March 31	**2006**	2005	% change
Apartment Acquisitions			
Value of acquisitions	**$31,632,000**	$12,315,000	157%
Units acquired	**578**	257	125%
Average price per unit	**$54,727**	$47,918	14%
MHC Acquisitions			
Value of acquisitions	**$3,525,000**	$26,350,000	(87)%
Units acquired	**163**	1,380	(88)%
Average price per unit	**$21,626**	$19,094	13%

Management's Discussion and Analysis:

During 2006, Killam continued to expand its geographic reach with the acquisition of an additional MHC in Ontario and an additional 243 units in St. John's, NL. Many of Killam's 2006 acquisitions are adjacent to Killam's existing buildings and MHCs which enable the Company to better control the neighborhood, provide a more consistent level of service and achieve efficiency cost savings.

Capital Improvements

In addition to property acquisitions, the Company has invested $5.0 million in property improvements during the first quarter of 2006 (Q1-2005 $1.8 million) as set out below:

	Q1 - 2006	Q1 - 2005
Project improvements	**$2,778,000**	$1,282,000
Suite improvements	**1,609,000**	412,000
Equipment	**396,000**	26,000
Appliances	**133,000**	45,000
Furniture & Fixtures	**33,000**	15,000
Parking Lots	**2,000**	2,000
Total	**$4,951,000**	$1,782,000

Of the $5 million invested in the first quarter of 2006, approximately $2.1 million relates to revenue enhancing suite and common area upgrades and the balance was invested in elevator, roof, window and heating plant upgrades which enhance revenue over the longer term.

Deferred Financing

As at	**March 31 2006**	December 31 2005	% change
Deferred financing costs	**$6,692,667**	$5,872,356	14%
Less: accumulated amortization	**(1,357,642)**	(1,104,360)	(23)%
	$5,335,025	$4,767,996	12%

Deferred financing costs (net of amortization) increased $0.6 million largely as a result of the January and March subordinated debt issuances with the remainder due to the increase in the portfolio. The costs related to mortgage assumption; application fees and legal costs are amortized over the term of the respective mortgage. CMHC insurance fees are amortized over the amortization period of the mortgage. The costs associated with the convertible and subordinated debentures are amortized over the terms of the debentures.

Other Assets

As at	**March 31 2006**	December 31 2005	% change
Prepaid property taxes	**$916,799**	$ 514,368	78%
Prepaid insurance	**768,410**	282,353	172%
Other	**390,548**	406,814	(4)%
Deferred charges	**415,751**	354,485	17%
Goodwill	**4,500,000**	4,500,000	- %
	$6,991,508	$6,058,020	15%

The increase in prepaids over the December 31, 2005 balance is due to the increased size of the portfolio as well as the timing of property tax payments in various provinces and the payment of insurance premiums for 2006.

Management's Discussion and Analysis:

Mortgages and Loans Payable

As at	**March 31 2006**	December 31 2005	% change
Mortgages	**$315,775,117**	$291,760,750	8%
Vendor financing	**11,255,386**	11,060,355	2%
	$327,030,503	$302,821,105	8%
Weighted average years to maturity	**5.4**	5.5	
Mortgage debt as a percentage of GBV	**64.5%**	65.0%	
Weighted average interest rate	**5.6%**	5.6%	

The Company's long-term debt consists largely of fixed-rate, long-term mortgage financing. In certain cases the Company will also utilize vendor-take-back mortgages as part of an acquisition. Mortgages are secured by a first or second charge against the individual properties and the vendor financing is secured by a general corporate guarantee. The increase in mortgages payable is due to the continued growth of the Company.

Killam's 2006 weighted average interest rate remained steady at 5.6%. It is anticipated that Killam will continue to benefit from the low interest rate environment throughout 2006. The Company's weighted average years to maturity fell slightly from December 31, 2005 to 5.4 years as a result of the assumption of mortgages during the first quarter of 2006 which have a shorter term to maturity than the Company's usual financing terms.

The Company continually reviews the maturity dates of its mortgages to reduce the overall interest rate risk. The following table sets out the maturity dates and average interest rates of debt by the year of maturity:

Fiscal Year	**Mortgage Balance 2006 *($000's)***	**Average Int. Rate %**
2006	13,165	6.13
2007	9,683	5.21
2008	43,620	6.11
2009	69,341	5.30
2010	50,066	5.26
2011	10,012	5.82
2012	4,771	6.17
2013	10,752	6.17
2014	34,423	5.85
2015	58,441	5.44
Thereafter	22,757	5.43

Management's Discussion and Analysis:

Convertible Debenture

As at	**March 31 2006**	December 31 2005
Convertible debentures	**$40,765,287**	$40,718,111

The convertible debentures bear interest at a rate of 6.5% payable semi-annually to their maturity at May 5, 2012. The debentures are convertible into common shares of the Company at a share price of $3.10 at any time after May 2007. At the time of issuance, the fair value of the Company's obligation to make principle and interest payments was $40.6 million and the fair value of the holder's conversion option was $1.6 million (which is reflected in "other paid-in capital"). The effective rate of interest on the liability component has been calculated at 7.2%.

Subordinated Debentures

As at	**March 31 2006**	December 31 2005
Subordinated debentures	**$10,000,000**	$Nil

On January 5 and March 17, 2006 the Company completed $5 million private placements of unsecured subordinated debentures and warrants. The debentures and warrants have terms of seven years. The debentures bear coupon rates of 5.92% and 6.06% respectively. The warrants are convertible into common shares of the Company at exercise prices of $3.60 and $3.80 per share respectively.

Shareholders' Equity

	March 31 2006	December 31 2005	% change
Capital stock	**$92,889,608**	$92,900,223	- %
Contributed surplus	**460,417**	405,420	14%
Other paid-in capital	**1,601,693**	1,601,693	- %
Deficit	**(1,268,934)**	(63,668)	N/A%
	$93,682,784	$94,843,668	1%

Other paid-in capital represents the fair value of the holder's conversion option of the Company's May 2005 issuance of convertible subordinated dentures. The change in the contributed surplus account is as result of the expensing of stock options which have vested during 2006.

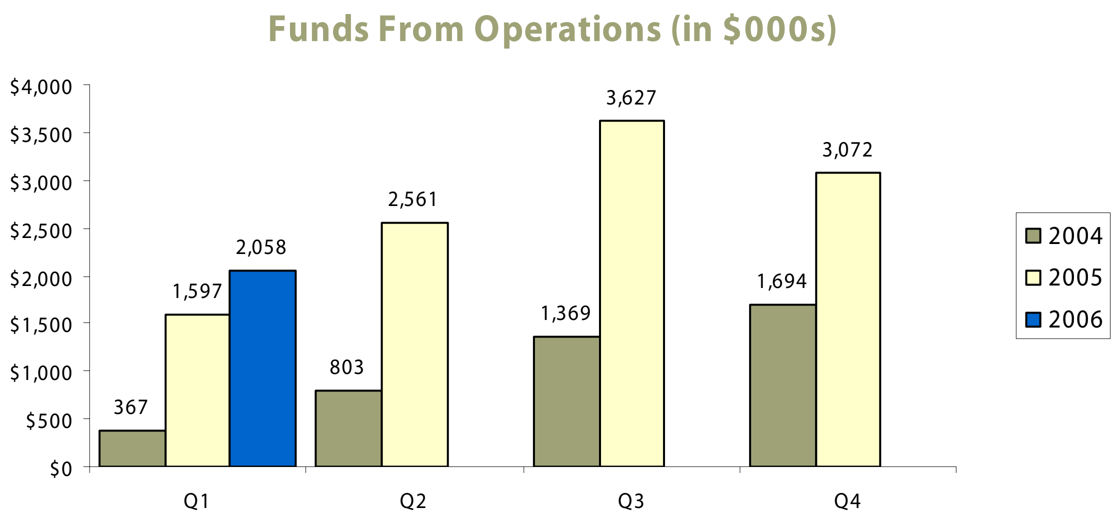
Management's Discussion and Analysis:

Consolidated Statement of Cash Flows

Operating Activities

For the three months ended	**2006**	2005	% change
Funds from operations	**$2,057,690**	$1,596,803	29%
FFO/share	**$0.03**	$0.02	50%

The Company's funds from operations continued to grow on a total dollar and per share basis during 2006 largely as a result of the expanded portfolio during 2005 and 2006.



Financing Activities

Issuance of Subordinated Debentures

As discussed earlier in the MD&A, during the first quarter of 2006, the Company completed the private placement of two $5 million subordinated debentures.

Deferred Financing

Deferred financing costs are costs incurred when mortgage debt is obtained as well as the costs of issuing the subordinated debentures and drawing on Killam's credit facilities. These costs are amortized over the term of the associated debt.

Credit Facility

During the first quarter of 2006 Killam has drawn an additional $6.85 million on its Credit Facility associated with its continued acquisitions.

Financing of Capital Assets

During the first quarter of 2006 the financing of new acquisitions and the re-financing of existing properties totaled $16.7 million compared to $31.5 million during the same period of 2005. These amounts exclude mortgages assumed on acquisition. See the section on Mortgages Payable elsewhere in the MD&A for a further discussion of financing.

Management's Discussion and Analysis:

Investing Activities

As discussed earlier in the MD&A, the Company completed the acquisition of ten properties representing 741 units during the first quarter of 2006. The purchase of capital assets amount in the cash flow statement is shown net of any debt assumed. In addition the Company completed approximately $5.0 million of capital improvements to its properties during the first quarter of 2006.

Liquidity and Capital Resources

The Company intends to meet its short-term liquidity requirements (defined as monthly mortgage payments of principal and interest and ongoing operating costs) through net cash flow provided by operating activities.

Killam's business plan requires an ample supply of capital resources. Capital resources are defined as mortgage debt, vendor mortgages and share capital equity. As at March 31, 2006 the Company had available $4.0 million of cash. In addition, the Company has credit facilities totaling $40 million of which the Company has drawn $23.8 million on these facilities as at March 31, 2006. The cash on hand and credit facilities provide the Company with sufficient capital to continue its acquisitions in the short term. Killam will continue to finance new properties at 75% of their value through new mortgages or placing second mortgages where available. The Company continuously reviews existing mortgages to ensure the properties are appropriately leveraged to maximize access to historically low mortgage rates.

Risk Management

Killam, like most real estate companies, is exposed to a variety of risk areas. These are described in detail in the Management's Discussion and Analysis found in Killam's 2005 Annual Report. These factors still exist at the end of this interim period and remain relatively unchanged.

Critical Accounting Estimates

The Company's accounting policies are described in Note 2 of the consolidated financial statements. The preparation of financial statements in conformity with Canadian Generally Accepted Accounting Principles requires management to make estimates and assumptions. The Company's critical accounting estimates remain unchanged from those set out in Killam's 2005 Annual Report

Future Objectives

Killam is well positioned to continue its accretive growth and effectively manage its portfolio.

2006 Goals and Objectives

- Continue to grow our portfolio through accretive acquisitions.
- Increase rental incomes from existing properties at tenant turnover and renewal.
- Lower costs through operational efficiencies.
- Maximize potential in our current portfolio through increases in occupancy rates.
- Grow our MHC business through community expansions utilizing our existing vacant land in the communities.
- Crystallize the value of our apartment surplus land through development agreements or sales.

Consolidated Balance Sheets

As at

	March 31 2006	December 31 2005
ASSETS		
Capital assets *(note 4)*	**$ 489,692,479**	$ 452,076,153
Cash and cash equivalents *(note 3)*	**8,203,610**	4,885,126
Accounts receivable	**670,400**	544,683
Other assets *(note 5)*	**6,991,508**	6,058,020
Deferred financing costs (net)	**5,335,025**	4,767,996
Future income taxes	**2,300,360**	1,184,547
	$ 513,193,382	$ 469,516,525
LIABILITIES AND SHAREHOLDERS' EQUITY		
Mortgages and loans payable *(note 6)*	**$ 327,030,503**	$ 302,821,105
Convertible debentures *(note 7)*	**40,765,287**	40,718,111
Subordinated debentures *(note 8)*	**10,000,000**	
Credit facility *(note 9)*	**23,788,000**	16,943,000
Accounts payable & accrued liabilities	**10,114,327**	7,057,797
Income tax payable	**267,504**	173,139
Security deposits	**1,475,163**	1,349,199
Future income taxes	**6,069,814**	5,610,506
	419,510,598	374,672,857
Shareholders' Equity		
Capital stock *(note 10)*	**92,889,608**	92,900,223
Contributed surplus *(note 10)*	**460,417**	405,420
Other paid-in capital *(note 7)*	**1,601,693**	1,601,693
Deficit	**(1,268,934)**	(63,668)
	93,682,784	94,843,668
	$ 513,193,382	$ 469,516,525

See accompanying notes

Consolidated Statements of Income and Deficit

For the 3 months ended March 31

	2006	2005
Revenue		
Rental income	**$ 16,051,521**	$ 8,832,496
Interest income	**17,372**	12,689
Other income	**216,274**	25,382
	16,285,167	8,870,567
Property expenses		
Property operating expenses	**7,904,822**	4,230,933
	8,380,345	4,639,634
Mortgage and loan interest	**4,249,874**	2,383,959
Convertible debenture interest	**732,926**	-
Subordinated debenture interest	**82,040**	-
Credit facility interest	**447,706**	15,690
Depreciation	**3,559,584**	1,612,918
Amortization of deferred financing	**251,199**	71,486
General and administrative	**712,590**	526,895
Professional fees	**65,554**	26,711
Provincial capital taxes	**72,033**	49,086
Interest and bank charges	**39,773**	20,738
	10,213,279	4,707,483
Loss before income taxes	**(1,832,934)**	(67,849)
(Provision for) recovery of income taxes		
- current	**(22,332)**	(19,752)
- future	**650,000**	25,783
Net loss	**(1,205,266)**	(61,818)
Deficit, beginning of period	**(63,668)**	(68,515)
Deficit, end of period	**$ (1,268,934)**	$ (130,333)
Net loss per share *(note 12)*		
- basic	**$ (0.0148)**	$ (0.0008)
- diluted	**$ (0.0148)**	$ (0.0008)

See accompanying notes

Consolidated Statements of Cash Flows

For the 3 months ended March 31

	2006	2005
OPERATING ACTIVITIES		
Net loss	**$ (1,205,266)**	$ (61,818)
Add items not affecting cash		
Depreciation and amortization	**3,810,783**	1,684,404
Non-cash debenture interest	**47,176**	-
Non-cash compensation expense	**54,997**	-
Future income taxes	**(650,000)**	(25,783)
Funds from operations	**2,057,690**	1,596,803
Net change in non-cash working capital items related to operations	**2,217,655**	777,610
Cash provided by operating activities	**4,275,345**	2,374,413
FINANCING ACTIVITIES		
Issue of common shares for cash (net of issue costs)	**(16,490)**	-
Issuance of subordinated debentures	**10,000,000**	-
Increase in deferred financing	**(818,228)**	(341,536)
Increase in credit facility	**6,845,000**	8,400,000
Issuance of long-term debt	**16,694,935**	31,525,087
Repayment of long term debt	**(1,961,325)**	(1,857,965)
Cash provided by financing activities	**30,743,892**	37,725,586
INVESTING ACTIVITIES		
Purchase of capital assets	**(31,700,753)**	(39,718,881)
Cash used in investing activities	**(31,700,753)**	(39,718,881)
Net increase in cash and cash equivalents	**3,318,484**	381,118
Cash and cash equivalents, beginning of period	**4,885,126**	4,168,071
Cash and cash equivalents, end of period	**$ 8,203,610**	$ 4,549,189

Notes to Consolidated Financial Statements

1. Incorporation

Killam Properties Inc. (the "Company") is a real estate corporation specializing in the acquisition and management of multi-residential apartment buildings and manufactured home communities. The Company is incorporated under the Canada Business Corporations Act.

2. Summary of Significant Accounting Policies

Basis of presentation

These financial statements are prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries.

Use of accounting estimates

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

Cash and cash equivalents

Cash and cash equivalents consist of cash, restricted cash and short-term investments. Short-term investments consist of short-term monetary investments with maturities not exceeding three months and are recorded at cost which approximates fair market value.

Revenue recognition

Revenue from rental properties is recognized when a tenant commences occupancy of a rental suite and rent is due. The Company retains all of the benefits and risks of ownership of its rental properties and therefore accounts for leases with its tenants as operating leases. Rental revenue includes rent, laundry, parking and other sundry revenues.

Income taxes

The Company follows the liability method of accounting for income taxes. Under this method future income tax assets and liabilities are determined based on the differences between the financial reporting and tax bases of assets and liabilities and are measured using substantively enacted tax rates and laws that are expected to be in effect in the periods in which the future tax assets and liabilities are expected to be realized or settled. The effect of a change in income tax rates on future income tax assets and liabilities is recognized in income in the period that the change occurs.

Capital assets

Revenue producing real estate properties held as ongoing investments are recorded at cost less accumulated amortization and net of any impairment loss. Cost includes all expenditures incurred in connection with the acquisition of real estate property including all direct costs. All costs associated with capital improvements, other than ordinary repairs and maintenance, are capitalized and amortized over terms appropriate to the expenditure.

2. Summary of Significant Accounting Policies (continued)

Amortization

Capital assets are amortized at rates designed to amortize the cost of the properties over their useful lives as follows:

Buildings	2% - 2.5%	straight-line, 40 - 50 years
Roads & driveways	4%	declining balance
Water & sewer	6%	declining balance
Suite renovations	20%	declining balance
Project improvements	10%	declining balance
Other assets	5% - 30%	declining balance

Deferred financing costs

Financing fees and other costs incurred in connection with debt financing are amortized on a straight-line basis over the term of such financing. Upon refinancing, any financing costs associated with previous mortgages are written off to income. Canadian Mortgage and Housing insurance premiums are amortized over the mortgage amortization period.

Stock-based compensation

The Company expenses the fair value of stock options. The Company determines the fair value of the options at the date of grant using the Black Scholes option pricing model and recognizes the fair value over the vesting period as compensation expense and contributed surplus. When stock options are exercised, the corresponding contributed surplus is transferred to capital stock.

Net income per share

Diluted net income per share is calculated using the treasury stock method which recognizes the use of proceeds that could be obtained upon exercise of stock options. This method assumes that any proceeds would be used to purchase common shares at the average market price during the period.

Convertible subordinated debentures

On issuance of subordinated debentures convertible into common shares of the Company, the fair value of the holders' conversion option is reflected as "Other paid-in capital". The Company's obligation to debenture holders for future interest and principal payments is reflected as a liability carried at amortized cost. If the holders exercise their conversion option, common shares issued on conversion will be recorded at an amount equal to the aggregate carrying value of the liability and conversion option extinguished, with no gain or loss recognized.

Derivative instruments

Periodically, the Company enters into oil futures contracts to hedge its exposure to rising oil prices. Hedge accounting is applied in accordance with CICA Accounting Guideline 13 "Hedging Relationships" and any realized gains or losses resulting from the settlement of these contracts are expensed in the period of settlement.

Notes to Consolidated Financial Statements

3. Cash and Cash Equivalents

	March 31, 2006	December 31, 2005
Cash	**$4,017,851**	$1,211,738
Tenant security deposits	**636,070**	539,589
Restricted cash	**3,549,689**	3,133,799
	$8,203,610	$4,885,126

Restricted cash includes deposits on real estate properties and property tax reserves.

4. Capital Assets

	March 31, 2006		December 31, 2005	
	Cost	**Accumulated Amortization**	Cost	Accumulated Amortization
Land	**$49,322,768**	**$ —**	$ 45,525,506	$ —
Buildings	**352,879,567**	**10,464,578**	319,637,430	8,499,728
Roads and driveways	**38,702,568**	**1,662,919**	36,924,444	1,303,561
Water and sewer	**38,727,945**	**2,477,516**	36,950,269	1,947,734
Suite renovations	**8,419,216**	**1,309,664**	6,819,881	1,003,152
Project improvements	**12,891,108**	**972,387**	14,690,865	714,438
Other assets	**6,254,241**	**617,870**	5,473,155	476,784
	$507,197,413	**$17,504,934**	466,021,550	$13,945,397
Less: accumulated amortization	**(17,504,934)**		(13,945,397)	
	$489,692,479		$452,076,153	

During the three months ended March 31, 2006, the Company capitalized indirect costs of $0.3 million (2005- $0.1 million) as part of its project improvement and suite renovation program. In addition, $116,000 of interest expense was capitalized as part of the Company's repositioning projects related to properties which were off-line (2005 - $2,000).

5. Other assets

	March 31, 2006	December 31, 2005
Prepaid	**$2,075,757**	$1,203,535
Deferred charges	**415,751**	354,485
Goodwill	**4,500,000**	4,500,000
	$6,991,508	$6,058,020

Goodwill presented above is the tax effect of the Company's acquisition of two properties though share purchase transactions. The offsetting liability is presented in future income taxes.

Notes to Consolidated Financial Statements

6. Mortgages and Loans payable

Mortgages payable bear interest at rates from 3.32% to 8.47% with maturity dates ranging from May 2006 to July 2019. Vendor mortgages and loans payable bear interest at fixed rates from 0.00% to 7.25% with maturity dates ranging from April 2006 to November 2015. Mortgages are secured by a first or second charge on the properties of the Company and vendor mortgages are secured by either a second charge on the property or a general corporate guarantee.

The weighted average mortgage rate at March 31, 2006 was 5.6% (December 31, 2005 – 5.6%).

Principal repayments of mortgages and loans are due as follows:

Year	
2006	$18,867,488
2007	16,378,808
2008	48,855,487
2009	67,173,794
2010	48,478,219
Thereafter	127,276,707
	$327,030,503

7. Convertible Subordinated Debentures

The Company's $42.2 million convertible subordinated debentures bear interest at a fixed rate of 6.5% payable semi-annually to their maturity at May 2012. The debentures are convertible into common shares of the Company at a share price of $3.10 at any time after May 2007. At the time of issuance, the fair value of the Company's obligation to make principal and interest payments was $40.6 million and the fair value of the holders' conversion option was $1.6 million (which is reflected in "other paid-in capital"). The effective rate of interest on the liability component is calculated at 7.2%.

8. Subordinated Debentures

The Company's unsecured subordinated debentures consist of two $5 million amounts and bear interest at fixed rates of 5.92% and 6.06% respectively, payable semi-annually to their maturity at January 2013. The debentures have attached warrants which are convertible into common shares of the Company at exercise prices of $3.60 and $3.80 per share respectively.

9. Credit Facilities

The Company has negotiated credit facilities set out as follows:

Operating Facility

Consists of a $500,000 revolving demand facility for general business purposes, bearing interest at the lender's prime plus 1%. As at March 31, 2006 the Company had a $Nil balance (December 31, 2005 - $Nil) related to this facility. The agreement includes certain restrictive covenants and undertakings of which the Company is in compliance.

9. Credit Facilities (continued)

Acquisition Bridge Facility

This agreement consists of two facilities:

(a) $20,000,000 senior revolving facility to fund asset acquisitions, bearing interest at the greater of prime plus 3.75% or 8.0%.. As at March 31, 2006 the Company had a $20,000,000 balance outstanding (December 31, 2005 - $16,943,000) related to this facility. The agreement includes certain restrictive covenants and undertakings of which the Company is in compliance.

(b) $20,000,000 revolving senior secured facility to fund asset acquisitions bearing interest at the greater of prime plus 5.0% or 9.25% plus a 0.6% fee on undrawn amounts (expensed monthly). As at March 31, 2006, the Company had a $3,788,000 balance outstanding (December 31, 2005 - $Nil) related to this facility. The agreement includes certain restrictive covenants and undertakings of which the Company is in compliance.

10. Capital Stock and Contributed Surplus

Capital Stock

Authorized:
Unlimited number of common shares.
Unlimited number of preferred shares, issuable in series.

Issued:
The following table summarizes the changes in issued common shares of the Company:

	2006		2005	
	Number of Shares	**Value**	Number of Shares	Value
Balance, beginning of year	**81,333,537**	**$92,900,223**	74,856,631	$77,809,075
Issued during the quarter				
Warrants issued [(i)]	—	**(17,120)**	—	—
Tax benefit of issuance costs	—	**6,505**	—	—
Balance, end of quarter	**81,333,537**	**$92,889,608**	74,856,631	$77,809,075

(i) Costs of issuing warrants attached to the subordinated dentures

Contributed Surplus

	2006	2005
Balance, beginning of year	**$405,420**	$233,984
Stock options expensed	**54,997**	1,387
Stock options exercised	—	—
Balance, end of quarter	**$460,417**	$235,371

11. Stock Options and Warrants

Under the terms of the stock option plan:

(i) the Company designates from time to time eligible participants to whom options will be granted, and the number of shares to be optioned to each;

(ii) eligible participants are persons who are employees, officers, directors and consultants of the Company;

(iii) shares to be optioned shall not exceed 5,500,000 (December 31, 2005 – 5,500,000) and the total number of shares to be optioned to any eligible participant shall not exceed 10% of the issued and outstanding shares of the class as at the date such option is granted;

(iv) the option price for the shares is determined at the time of granting of the option but cannot be less than the fair market value of the shares at the time the option is granted less any applicable discount permitted by the Toronto Stock Exchange; and

(v) the term during which any option granted may be exercised is determined by the Company at the time the option is granted but may not exceed the maximum period permitted from time to time by the Toronto Stock Exchange.

Options granted and exercised during the quarter are as follows:

	2006		2005	
	Number of Shares	**Weighted Average Exercise Price**	Number of Shares	Weighted Average Exercise Price
Outstanding, beginning of year	**3,108,500**	**$1.40**	1,732,000	$0.47
Expired/cancelled	**(4,500)**	**2.05**	—	—
Outstanding, end of quarter	**3,104,000**	**$1.40**	1,732,000	$0.47

11. Stock Options and Warrants (continued)

The following table summarizes the stock options outstanding at:

	March 31, 2006		December 31, 2005	
Exercise prices	**Number of Options Outstanding**	**Remaining Contractual Life**	Number of Options Outstanding	Remaining Contractual Life
$0.30	**471,000**	**1.15 years**	471,000	1.40 years
$0.30	**10,000**	**1.19 years**	10,000	1.44 years
$0.56	**200,000**	**2.19 years**	200,000	2.44 years
$0.65	**608,500**	**2.19 years**	608,500	2.44 years
$1.30	**10,000**	**2.67 years**	10,000	2.92 years
$1.69	**29,500**	**2.71 years**	29,500	2.96 years
$2.00	**10,000**	**3.67 years**	10,000	3.92 years
$2.05	**1,765,000**	**4.17 years**	1,769,500	4.42 years
	3,104,000		3,108,500	

Included in the above figures are 1,439,677 options at an average exercise price of $2.05, that were not exercisable at March 31, 2006, as they had not vested (December 31, 2005 – 1,528,052 options at an average exercise price of $2.04).

Warrants

The Company has issued warrants as part of certain financing and equity arrangements as follows:

	March 31, 2006		December 31, 2005	
Exercise price	**Number of Warrants Outstanding**	**Remaining Contractual Life**	Number of Warrants Outstanding	Remaining Contractual Life
$0.95	**500,000**	**2.41 years**	500,000	2.66 years
$3.60	**1,388,889**	**6.76 years**	—	—
$3.80	**1,315,789**	**6.76 years**	—	—
	3,204,678		500,000	

The 500,000 warrants at $0.95 were issued upon obtaining the credit facility and expire August 27, 2008. The warrants priced at $3.60 and $3.80 are the warrants attached to the subordinated debentures issued by the Company in the first quarter of 2006 (see note 8).

Notes to Consolidated Financial Statements

12. Per Share Information

Net income per share has been calculated based on the weighted average number of shares outstanding for the quarter as follows:

	2006	2005
Basic	**81,333,537**	74,856,631
Fully diluted	**84,089,252**	76,539,616

The diluted share amounts presented above exclude the convertible debentures as the effect would have been anti-dilutive.

13. Segmented Information

The Company operates in two segments of the multi-family residential industry; multi-family apartments and manufactured home communities.

The accounting policies of these segments are the same as those described in the summary of significant accounting policies. The segments are analyzed based on earnings from property operations before amortization. The operating results and capital assets of the segments as at and for the three months ended March 31, 2006 and 2005 are set out as follows:

As at and for the three months ended March 31, 2006

	Multi-family Apartments	Manufactured Home Communities	Corporate	Total
Revenue	**$13,014,900**	**$3,151,576**	**$118,691**	**$16,285,167**
Property operating expenses	**6,616,757**	**1,288,065**	**—**	**7,904,822**
Earnings from property operations	**$6,398,143**	**$1,863,511**	**$118,691**	**$8,380,345**
Capital assets (net)	**$404,065,379**	**$84,614,859**	**$1,012,241**	**$489,692,479**

As at and for the three months ended March 31, 2005

	Multi-family Apartments	Manufactured Home Communities	Corporate	Total
Revenue	$7,702,713	$1,151,436	$16,418	$8,870,567
Property operating expenses	3,840,680	390,253	—	4,230,933
Earnings from property operations	$3,862,033	$761,183	$16,418	$4,639,634
Capital assets (net)	$221,721,397	$52,784,304	$437,126	$274,942,828

Notes to Consolidated Financial Statements

14. Financial Instruments

The Company is exposed to financial risk that arises from, among other factors, fluctuation in interest rates and the credit quality of its tenants. These risks are managed as follows:

(i) ***Interest rate risk***
Interest rate risk is minimized through management's periodic review of its mortgage portfolio. If market conditions warrant, the Company will renegotiate its existing debt to take advantage of lower interest rates. The Company will also structure its debt so as to stagger the debt maturities, thereby minimizing the Company's exposure to interest rate fluctuations.

(ii) ***Credit risk***
Credit risk arises from the possibility that tenants may experience financial difficulty and be unable to fulfill their lease term commitments. The Company mitigates the risk of credit loss through the diversification of its existing portfolio and limiting its exposure to any one tenant. Credit assessments are conducted with respect to all new leasing and the Company also obtains a security deposit to assist in potential recovery requirements.

Fair Value

Financial instruments are defined as a contractual right to receive or deliver cash or another financial asset. The fair values of the Company's financial instruments, except for long-term debt, approximate their recorded values at December 31, 2005 and December 31, 2004 due to their short-term nature and or the credit terms of those instruments.

The fair value of the mortgages payable has been determined by discounting the cash flows using current market rates of similar investments. These estimates are subjective in nature and therefore cannot be determined with precision. The fair value of long-term debt as compared to book value has remained relatively consistent with the December 31, 2005 values.

As at March 31, 2006, the Company had $27,975 worth of oil futures contracts outstanding (December 31, 2005 - $167,729).

15. Related Party Transactions

During the first quarter of 2006 the Company paid real estate commissions of $17,698 to a company controlled by a director. The commission was based on market rates and there is no continuing contractual obligation to use the service of the related party.

16. Comparative Figures

Certain comparative figures have been reclassified to conform to the presentation adopted for 2006.

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