

**PIZZA PIZZA ROYALTY INCOME FUND
MANAGEMENT'S DISCUSSION AND ANALYSIS**

FINANCIAL HIGHLIGHTS

The following tables set out selected financial information and other data of the Pizza Pizza Royalty Income Fund (the "Fund") and should be read in conjunction with the consolidated financial statements of the Fund. Readers should note that the 2008 results are not directly comparable to the 2007 results due to the fact that there are 609 restaurants in the Royalty Pool for 2008 compared to 531 restaurants in the Royalty Pool for the first and second quarters of 2007 and 572 for the third and fourth quarters of 2007.

Equity income earned by the Fund through its interest in the Pizza Pizza Royalty Limited Partnership (the "Partnership") and interest income from the Pizza Pizza Limited Loan have been derived as shown in the table below:

	January 1, 2008 to December 31, 2008	January 1, 2007 to December 31, 2007	January 1, 2006 to December 31, 2006
(in thousands of dollars, except number of restaurants and per unit amounts)			
Restaurants in Royalty Pool ⁽¹⁾	609	572	501
Same store sales growth	1.7%	4.6%	4.5%
System sales reported by Pizza Pizza restaurants in the Royalty Pool	\$ 389,518	\$ 376,375	\$ 353,138
System sales reported by Pizza 73 restaurants in the Royalty Pool	81,105	33,124	-
	\$ 470,623	\$ 409,499	\$ 353,138
Royalty – 6% on Pizza Pizza system sales	\$ 23,371	\$ 22,583	\$ 21,188
Royalty – 9% on Pizza 73 system sales	7,299	2,981	-
Total Royalty on System Sales	30,670	25,564	21,188
Partnership expenses ⁽²⁾	(3,280)	(2,545)	(1,710)
Earnings available for distribution to the Fund and Pizza Pizza Limited ⁽³⁾	27,390	23,019	19,478
Pizza Pizza Limited's interest ⁽⁴⁾	(7,311)	(6,200)	(5,388)
Equity income before issuance costs ⁽³⁾	20,079	16,819	14,090
Interest income ⁽⁵⁾	1,800	1,849	1,800
Net earnings before non-cash future income tax expense & issuance costs ⁽⁷⁾	\$ 21,879	\$ 18,668	\$ 15,890
Share of Partnership issuance costs	-	169	-
Provision for (recovery of) future income taxes	(2,235)	8,208	-
Net earnings	\$ 24,114	\$ 10,291	\$ 15,890
Basic earnings per Fund unit excluding the impact of non-cash future income tax expense (recovery) and issuance costs ⁽⁷⁾	\$ 1.003	\$ 0.954	\$ 0.885
Basic earnings per Fund unit ⁽⁶⁾	\$ 1.105	\$ 0.526	\$ 0.885
Diluted earnings per Fund unit ⁽⁶⁾	\$ 1.065	\$ 0.526	\$ 0.865
Distributions declared	\$ 20,127	\$ 17,608	\$ 15,108
Distributions per Fund unit	\$ 0.923	\$ 0.888	\$ 0.842
Payout ratio	92%	94%	95%
	December 31, 2008	December 31, 2007	December 31, 2006
Positive working capital of Partnership	\$ 3,487	\$ 1,945	\$ 1,466
Total assets	\$ 220,336	\$ 212,643	\$ 171,796
Total liabilities	\$ 7,664	\$ 9,866	\$ 1,275

(1) The Pizza 73 Rights were acquired on July 24, 2007 and resulted in the addition of 41 restaurants to the Royalty Pool for the balance of 2007. Effective January 1, 2008, there were 50 Pizza 73 restaurants in the Royalty Pool.

PIZZA PIZZA ROYALTY INCOME FUND

Management's Discussion & Analysis

- (2) The Fund, indirectly through the Partnership, incurs administrative expenses and interest expense on the \$47,000 outstanding bank loan (2007 - \$47,000, 2006 - \$20,000). Interest expense on the bank loan for 2008 was \$2,667 (2007 - \$1,800, 2006 - \$1,100).
- (3) For December 31, 2007, earnings shown exclude issuance costs of \$207 paid from the proceeds raised to acquire the Pizza 73 trademarks and rights.
- (4) Represents the interest of Pizza Pizza Limited ("Pizza Pizza") in the earnings of the Partnership from Class B, Class C and Class D Partnership units. The Class B and D units are exchangeable into Fund units based on value of the Class B Exchange Multiplier and the Class D Exchange Multiplier at the time of exchange as defined in the Pizza Pizza Licence and Royalty Agreement and the Pizza 73 Licence and Royalty Agreement, respectively, and represents 21.5% of the fully diluted units of the Fund at December 31, 2008 (2007 - 18.4%, 2006 - 20.3%).
- (5) The Fund indirectly earns interest income on the \$30,000 loan to Pizza Pizza, with interest income accruing at 6% per annum, payable monthly.
- (6) Net earnings for the year ended December 31, 2008 reflect the non-cash future tax recovery of \$2,235 relating to the new tax legislation (2007 - expense \$8,208, 2006 - \$nil) and the Fund's share of the Partnership's issuance costs \$nil (2007 - \$169, 2006 - \$nil)
- (7) "Net earnings excluding the impact of non-cash future income tax and issuance costs" and "Basic earnings per Fund unit excluding non-cash future income tax and issuance costs" are not recognized measures under Canadian GAAP. References to net earnings, excluding the impact of non-cash future income tax and issuance costs, are to earnings determined in accordance with GAAP applicable to the financial statements before amounts for taxes and the Fund's share of issuance costs of the Partnership, as included in net earnings. The Fund believes that, in addition to net earnings, net earnings excluding the impact of non-cash future income tax expense and issuance costs is a useful supplemental measure in evaluating its performance as it provides investors with an indication of operating earnings. Investors are cautioned, however, that this should not be construed as an alternative to net earnings as a measure of profitability. The method of calculating net earnings excluding the impact of non-cash future income tax expense and issuance costs for the purposes of this report may differ from that used by other issuers and, accordingly, it may not be comparable to that used by other issuers.

	Q4 2008 (unaudited) ⁽¹⁾	Q3 2008 (unaudited) ⁽¹⁾	Q2 2008 (unaudited) ⁽¹⁾	Q1 2008 (unaudited) ⁽¹⁾
(in thousands of dollars, except number of restaurants, days in the Period and per unit amounts)				
Restaurants in Royalty Pool	609	609	609	609
Same store sales growth	-0.6%	2.2%	1.3%	3.7%
System sales reported by Pizza Pizza restaurants in Royalty Pool	\$ 101,464	\$ 99,894	\$ 94,190	\$ 93,970
System sales reported by Pizza 73 restaurants in Royalty Pool ⁽¹⁾	20,975	20,493	20,087	19,550
	\$ 122,439	\$ 120,387	\$ 114,277	\$ 113,520
Royalty – 6% on Pizza Pizza system sales	\$ 6,088	\$ 5,994	\$ 5,651	\$ 5,638
Royalty – 9% on Pizza 73 system sales	1,887	1,844	1,808	1,760
Royalty on System Sales of Royalty Pool Partnership expenses ⁽²⁾	\$ 7,975	\$ 7,838	\$ 7,459	\$ 7,398
	(791)	(810)	(854)	(825)
Earnings available for distribution to the Fund and Pizza Pizza Limited	7,184	7,028	6,605	6,573
Pizza Pizza Limited's interest ⁽³⁾	(1,899)	(1,867)	(1,776)	(1,769)
	5,285	5,161	4,829	4,804
Interest income ⁽⁴⁾	450	450	450	450
Net earnings excluding the impact of non-cash future income tax expense ⁽⁶⁾	\$ 5,735	\$ 5,611	\$ 5,279	\$ 5,254
Provision for (recovery of) future taxes	-	-	(3,091)	856
Net earnings	\$ 5,735	\$ 5,611	\$ 8,370	\$ 4,398
Basic earnings per Fund unit excluding the impact of non-cash future income tax expense ⁽⁶⁾	\$ 0.263	\$ 0.257	\$ 0.242	\$ 0.241
Basic earnings per Fund unit ⁽⁵⁾	\$ 0.263	\$ 0.257	\$ 0.384	\$ 0.202
Diluted earnings per Fund unit ⁽⁵⁾	\$ 0.258	\$ 0.253	\$ 0.349	\$ 0.202
Distributions declared	\$ 5,073	\$ 5,073	\$ 5,007	\$ 4,975
Distributions per Fund unit	\$ 0.233	\$ 0.233	\$ 0.230	\$ 0.228
Payout ratio	88%	90%	95%	95%

PIZZA PIZZA ROYALTY INCOME FUND
Management's Discussion & Analysis

	Q4 2007 (unaudited) ⁽¹⁾	Q3 2007 (unaudited) ⁽¹⁾	Q2 2007 (unaudited)	Q1 2007 (unaudited)
(in thousands of dollars, except number of restaurants, days in the Period and per unit amounts)				
Restaurants in Royalty Pool	572	572	531	531
Same store sales growth	4.9%	5.1%	4.3%	5.5%
System sales reported by Pizza Pizza restaurants in Royalty Pool	\$ 99,654	\$ 95,041	\$ 92,162	\$ 89,518
System sales reported by Pizza 73 restaurants in Royalty Pool ⁽¹⁾	19,230	13,894	-	-
	\$ 118,884	\$ 108,935	\$ 92,162	\$ 89,518
Royalty – 6% on Pizza Pizza system sales	\$ 5,979	\$ 5,703	\$ 5,530	\$ 5,371
Royalty – 9% on Pizza 73 system sales	1,731	1,250	-	-
Royalty on System Sales of Royalty Pool	7,710	6,953	5,530	5,371
Partnership expenses ⁽²⁾	(896)	(813)	(498)	(338)
Earnings available for distribution to the Fund and Pizza Pizza Limited	6,814	6,140	5,032	5,033
Pizza Pizza Limited's interest ⁽³⁾	(1,619)	(1,564)	(1,508)	(1,509)
	5,195	4,576	3,524	3,524
Interest income ⁽⁴⁾	450	499	450	450
Net earnings before non-cash future income tax expense and issuance costs ⁽⁶⁾	\$ 5,645	\$ 5,075	\$ 3,974	\$ 3,974
Share of Partnership issuance costs	-	169	-	-
Provision for future taxes	(4,690)	4,198	8,700	-
Net earnings (loss)	\$ 10,335	\$ 708	\$ (4,726)	\$ 3,974
Basic earnings per Fund unit excluding the impact of non-cash future income tax expense and issuance costs ⁽⁶⁾	\$ 0.259	\$ 0.248	\$ 0.211	\$ 0.221
Basic earnings (loss) per Fund unit ⁽⁵⁾	\$ 0.474	\$ 0.035	\$ (0.263)	\$ 0.221
Diluted earnings (loss) per Fund unit ⁽⁵⁾	\$ 0.430	\$ 0.035	\$ (0.263)	\$ 0.215
Distributions declared	\$ 4,974	\$ 4,772	\$ 3,931	\$ 3,931
Distributions per Fund unit	\$ 0.228	\$ 0.222	\$ 0.219	\$ 0.219
Payout ratio	88%	94%	99%	99%

- (1) The Pizza 73 Rights were acquired on July 24, 2007 and resulted in the addition of 41 restaurants to the Royalty Pool for the balance of 2007. Effective January 1, 2008, there are 50 Pizza 73 restaurants in the Royalty Pool.
- (2) The Fund, indirectly through the Partnership, incurs administrative expenses and interest expense on the \$47,000 outstanding bank loan (2007 - \$47,000).
- (3) Represents the interest of Pizza Pizza in the earnings of the Partnership from Class B, Class C and Class D Partnership units. The Class B and D units are exchangeable into Fund units based on value of the Class B Exchange Multiplier and Class D Exchange Multiplier at the time of exchange as defined in the Pizza Pizza Licence and Royalty Agreement and the Pizza 73 Licence and Royalty Agreement, respectively, and represents 21.5% of the fully diluted units of the Fund at December 31, 2008.
- (4) The Fund indirectly earns interest income on the \$30,000 loan to Pizza Pizza, with interest income accruing at 6% per annum, payable monthly.
- (5) Net earnings (loss) for the quarters ended September 30, 2008, June 30, 2008, March 31, 2008, December 31, 2007, September 30, 2007 and June 30, 2007 reflect the effect of the non-cash, future tax expense, and for the quarter ended September 30, 2007 also reflect the Fund's share of the Partnership's issuance costs of \$169.
- (6) "Net earnings excluding the impact of non-cash future income tax expense", "Net earning excluding the impact of non-cash future income tax expense and issuance costs" and "Basic earnings per Fund unit excluding non-cash future income tax and issuance costs" are not recognized measures under Canadian GAAP. References to net earnings, excluding the impact of non-cash future income tax expense and issuance costs, are to earnings determined in accordance with GAAP applicable to the financial statements before amounts for taxes and the Fund's share of issuance costs of the Partnership as included in net earnings. The Fund believes that, in addition to net earnings, net earnings excluding the impact of non-cash future income tax expense, and net earnings excluding the impact of non-cash future income tax expense and issuance costs are useful supplemental measures in evaluating its performance as they provide investors with an indication of operating earnings. Investors are cautioned, however, that these figures should not be construed as an alternative to net earnings as a measure of profitability. The method of calculating net earnings excluding the impact of non-cash future income tax expense and issuance costs for the purposes of this report may differ from that used by other issuers and, accordingly, it may not be comparable to that used by other issuers.

PIZZA PIZZA ROYALTY INCOME FUND

Management's Discussion & Analysis

OVERVIEW AND BUSINESS OF THE FUND

The following Management's Discussion and Analysis (the "MD&A") is a discussion of the results of operations and financial condition of the Fund for the quarter (the "Quarter") and year (the "Year") ended December 31, 2008. The consolidated financial statements of the Fund are prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). The MD&A has been prepared as of March 18, 2009.

The Fund is a limited purpose, open-ended trust established under the laws of Ontario to indirectly, through the Partnership, acquire the trademarks and trade names used by Pizza Pizza Limited ("Pizza Pizza") in its Pizza Pizza and Pizza 73 restaurants. The Pizza Pizza trademarks and other intellectual property (the "Pizza Pizza Rights") were licenced to Pizza Pizza in 2005 for 99 years, for which Pizza Pizza pays the Fund a royalty equal to 6% of the system sales of its Pizza Pizza restaurants in the Royalty Pool. On July 24, 2007, the Partnership acquired the trademarks and other intellectual property of Pizza 73 (the "Pizza 73 Rights") from Pizza 73, Inc. and licenced them to Pizza Pizza for 99 years, for which Pizza Pizza pays the Fund a royalty equal to 9% of the system sales of the Pizza 73 restaurants in the Royalty Pool. For the year 2008, the Royalty Pool consisted of 559 Pizza Pizza restaurants and 50 Pizza 73 restaurants.

A key attribute of the Fund is that revenues are based on top-line, system sales of the Royalty Pool restaurants and not on the profitability of either Pizza Pizza or the restaurants in the Royalty Pool. Moreover, the Fund is not subject to the variability of earnings or expenses of the operating companies. The Fund's only expenses are administration expenses and the interest on debt. Thus, the success of the Fund depends primarily on the ability of Pizza Pizza to maintain and increase system sales of the Royalty Pool and to meet its royalty obligations.

Increases in system sales are derived from both the development of new Pizza Pizza and Pizza 73 restaurants and same store sales growth ("SSSG"). The key metric for yield growth of the Fund is SSSG, which is dependent on maintaining operational excellence within each restaurant, general market conditions, pricing, and marketing programs undertaken by Pizza Pizza. One of Pizza Pizza's competitive strengths in increasing SSSG is that over 99% of its Pizza Pizza restaurants are new or renovated and have been expanded to accommodate customer seating. The seating offers franchisees the ability to increase "walk-in" sales, thereby, potentially increasing same store sales. Restaurant closures also affect system sales. Pizza Pizza has historically maintained a low closure rate throughout its chain.

From inception, the Fund adopted the guideline of Canadian Institute of Chartered Accountants referred to as "AcG-15", Consolidation of Variable Interest Entities. As a result, the Fund's subsidiary, the Partnership which owns the Pizza Pizza and Pizza 73 Rights, is accounted for on the equity basis. Pizza Pizza, the private operating company that pays royalties to the Partnership, consolidates the Partnership based on this same guideline.

ROYALTY POOL ADJUSTMENTS

Annually, on January 1 (the "Adjustment Date"), an adjustment is made to the Royalty Pool to include the forecasted system sales from new Pizza Pizza restaurants opened on or before December 31 of the prior year, less system sales from any Pizza Pizza restaurants that have been permanently closed during the year. The change in the amount of the Royalty due to the Partnership as a result of changes in the system sales of the Royalty Pool will affect Pizza Pizza's retained interest through an adjustment to the rate at which the Class B Partnership units may ultimately be exchanged for units of the Fund. On the Adjustment Date, the adjustment to the Class B Exchange Multiplier (as defined in the Pizza Pizza Licence and Royalty Agreement) involves first calculating the "Determined Amount", which is defined as 92.5% of the royalty revenue added to the Royalty Pool, divided by the prevailing yield of the Fund units. The Determined Amount is multiplied by 80%, then divided by the current market price of the units, and then further divided by the number of Class B Partnership units outstanding. This fraction is added to the Class B Exchange Multiplier from the preceding year, which was "one" on the closing of the initial public offering. On the following Adjustment Date, a second adjustment to the Class B Exchange Multiplier will be made in the same manner once the system sales for new restaurants are known with certainty. The adjustment for new restaurants rolled into the Royalty Pool is designed to be accretive for current unitholders.

PIZZA PIZZA ROYALTY INCOME FUND

Management's Discussion & Analysis

If, during a year, a Pizza Pizza restaurant is closed, the sales of the restaurant from the closing date would no longer be included in the calculation of the royalty payable to the Partnership by Pizza Pizza. To compensate for this, in certain circumstances, the Pizza Pizza Licence and Royalty Agreement and the Limited Partnership Agreement provide that an amount (the "Make-Whole Payment") reflecting the reduction in the royalty resulting from the restaurant closure will be paid by Pizza Pizza to the Partnership for the balance of the year in which the restaurant was closed, commencing from the closing date. The Make-Whole Payment will be the sales of the closed restaurant for the first 52-week period in which it was included in the Royalty Pool multiplied by the royalty rate, payable as to one-twelfth per month.

Similarly, on the Adjustment Date, a separate adjustment is made to the Royalty Pool for the Pizza 73 restaurants. The Royalty Pool is increased to include the forecasted system sales from new Pizza 73 restaurants opened on or before September 1 of the prior year, less system sales from any Pizza 73 restaurants that have been permanently closed during the year. On the Adjustment Date, the adjustment to the Class D Exchange Multiplier is calculated in a similar manner as the Class B Exchange Multiplier described above. At the time of acquisition of the Pizza 73 Rights, the Class D Exchange Multiplier was zero.

Readers should note that the number of restaurants added to the Royalty Pool each year may differ from the number of restaurant openings and closings reported by Pizza Pizza on an annual basis, as the periods for which they are reported differ slightly.

RESTAURANTS ADDED TO THE ROYALTY POOL

In early January 2008, adjustments to royalty payments and Pizza Pizza's Class B Exchange Multiplier were made based on the actual performance of the 35 restaurants added to the Royalty Pool on January 1, 2007. As a result of the adjustments, the Class B Exchange Multiplier effective for 2007 was 1.23525 and Pizza Pizza's exchangeable units increased by 122,427 to 5,031,342 Fund units, effective January 1, 2007.

On January 1, 2008, 28 net, new Pizza Pizza restaurants were added to the Royalty Pool as a result of 36 new restaurants opening and eight closings during 2007. The additional system sales from the 28 net, new restaurants were estimated at \$8.0 million annually. The total number of Pizza Pizza restaurants in the Royalty Pool for 2008 then increased to 559. The yield of the Fund units was determined to be 9.0% calculated using \$9.87 as a weighted average unit price. Weighted average unit price is calculated based on the market price of the units traded on the TSX during the period of 20 consecutive days ending on the fifth trading day before January 1, 2008. As a result of the contribution of the additional net sales to the Royalty Pool, Pizza Pizza's Class B Exchange Multiplier increased fractionally by 80% of the total adjustment or 0.09805; the new Class B Multiplier was 1.33330. This adjustment also increased the entitlement of the holders of the Class B units to distributions of cash and allocations of income from the Partnership. As a result of the adjusted Class B Exchange Multiplier, Pizza Pizza held Class B Partnership units exchangeable into 5,430,699 Fund units. The second adjustment to the Class B Exchange Multiplier has been made effective January 1, 2008, with the actual performance of the new restaurants known. See "Subsequent Event" for additional information surrounding the transaction.

On January 1, 2008, nine new Pizza 73 restaurants opened on or prior to September 1, 2007 were added to the Royalty Pool. The additional system sales from the nine new restaurants were estimated at \$7.5 million annually. The total number of Pizza 73 restaurants in the Royalty Pool for 2008 then increased to 50. The yield and weighted average unit price used in the calculation of the multiplier is the same as that of the Class B adjustment previously discussed of 9.0% and \$9.87, respectively. As a result of the contribution of the additional net sales to the Royalty Pool, Pizza Pizza's Class D Exchange Multiplier increased fractionally by 80% of the total adjustment or 5.58750; the new Class D Multiplier was 5.5875. This adjustment also increased the entitlement of the holders of the Class D Units to distributions of cash and allocations of income from the Partnership. As a result of the adjusted Class D Exchange Multiplier, Pizza Pizza held Class D Partnership units exchangeable into 558,750 Fund units. The second adjustment to the Class D Exchange Multiplier has been made effective January 1, 2008, with the actual performance of the new restaurants known. See "Subsequent Event" for additional information surrounding the transaction.

As a result of the January 1, 2008 vend-in, the number of Fund units for which Pizza Pizza's Class B and Class D Partnership units are exchangeable increased to 5,989,449 which, as at December 31, 2008, equates to 21.5% of

PIZZA PIZZA ROYALTY INCOME FUND

Management's Discussion & Analysis

the fully diluted units of the Fund. The Fund reported an increase in its investment in the Partnership and a contributed surplus of \$8.7 million to reflect the increase in value as a result of the vend-in of the new royalty stream on January 1, 2008.

On January 1, 2009, the Royalty Pool was increased to include the royalties from 18 new Pizza Pizza restaurants and 19 new Pizza 73 restaurants. The Royalty Pool will decrease by four traditional and five non-traditional Pizza Pizza restaurants which were closed during the year. Of the 18 new Pizza Pizza restaurants opened between January 1, 2008 and December 31, 2008, six are traditional restaurants and 12 are non-traditional locations. The 19 Pizza 73 restaurants are comprised of 13 traditional restaurants and six non-traditional locations, opened between September 2, 2007 and September 1, 2008. With the addition of the 28 net, new restaurants, royalties are now paid to the Fund on 637 restaurants in the Royalty Pool. See "Subsequent Event" for additional information surrounding the transaction.

OWNERSHIP OF THE FUND

Pizza Pizza's 21.5% interest in the earnings of the Partnership at December 31, 2008, consists of its ownership of Class B, Class C and Class D Partnership units. Each Class B and Class D unit can be exchanged indirectly for that number of units equal to the Class B Exchange Multiplier and Class D Exchange Multiplier, respectively, (as defined in the Licence and Royalty Agreements) applicable at the date of the exchange. Class C units can be exchanged by requiring the Fund to purchase those Class C Units in consideration of the assumption by the Fund of an amount of the indebtedness under the PPL Loan equal to \$10.00 per Class C Unit transferred.

Ownership of the Fund on a fully diluted basis is as follows:

	Issued & Outstanding units, and Exchangeable Equivalent units
Fund units outstanding on January 1, 2008	21,818,392
Class B exchangeable units held by Pizza Pizza	5,430,699
Class D exchangeable units held by Pizza Pizza	558,750
Fully diluted units on December 31, 2008	<u>27,807,841</u>

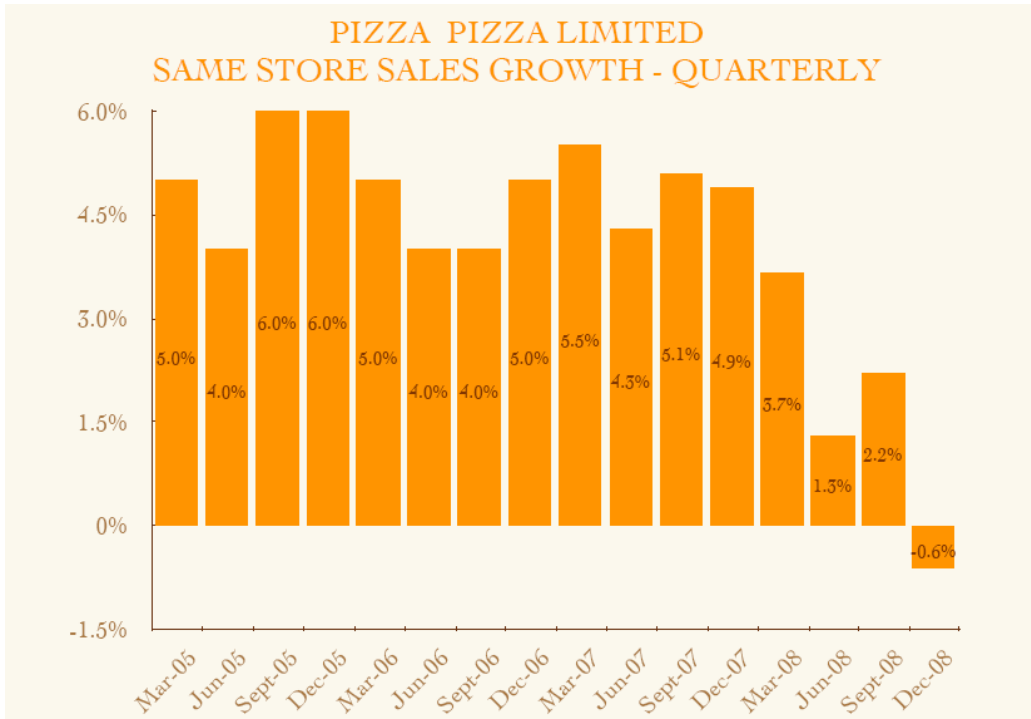
SAME STORE SALES GROWTH

Same Store Sales Growth, the key driver of yield growth for unitholders of the Fund, decreased by 0.6% (+4.9% -2007) for the quarter and increased 1.7% (+4.6% - 2007) for the year-ended December 31 2008 compared with the same period in 2007. For the quarter, SSSG for the Pizza Pizza restaurants was -1.3% and was 2.5% for Pizza 73 restaurants (2.6% and 18.1%, respectively - 2007). For the year, SSSG for the Pizza Pizza restaurants was 0.8% and was 6.0% for Pizza 73 restaurants (3.4% and 19.2%, respectively - 2007). During the year, the Pizza Pizza brand sales benefited from an increase in the average cheque, offset by a decrease in traffic counts; Pizza 73 sales benefited from an increase in both average cheque and traffic counts.

Deteriorating economic conditions in Pizza Pizza's core markets have impacted SSSG in 2008, and more notably in the fourth quarter. The majority of the Pizza Pizza restaurants operate in the province of Ontario which continues to experience a decline in manufacturing employment and tourism, both attributable to an economic slowdown in the United States and fears of weak global growth. For the Pizza 73 brand, the majority of the restaurants operate in Alberta, whose economy is beginning to be affected by the decline in the price of oil. The province reported lower retail sales and manufacturing shipments in November 2008 compared to the previous month. In addition to the economic impact, 17 traditional stores have opened in Alberta in the last 18 months, of which 15 have reduced territories of previously existing stores which negatively impacted SSSG. Adding restaurants in the Alberta market is part of Pizza Pizza's overall strategy to relieve capacity constraints at the

PIZZA PIZZA ROYALTY INCOME FUND
Management’s Discussion & Analysis

restaurant level and provide improved customer service, while growing and protecting the Pizza 73 brand. The Fund receives a monthly step-out payment, subject to store performance, for up to two years on sales adjustments which are a result of a territory reduction. (See “Step-Out Payments” and “Adjusted Restaurants” under “Licence and Royalty – Adjustments to the Royalty Pools and Payments Made Under the Licence and Royalty Agreements” in the Annual Information Form for the period ended December 31, 2008)



ROYALTY POOL SALES

The restaurants in the Royalty Pool increased to 609 on the January 1, 2008 adjustment date, to include the royalties from 37, net new restaurants. In the prior year, the Royalty Pool increased from 531 to 572 in July 2007, to include the royalties from 41 Pizza 73 restaurants added upon the purchase of the Pizza 73 Rights by the Partnership.

System sales from the 609 restaurants in the Royalty Pool for the quarter and year-ended December 31, 2008 were \$122.4 million and \$470.6 million respectively. Sales from the 50 Pizza 73 restaurants in the Pool were \$21.0 million for the quarter and \$81.1 million for the year, while sales from the 559 Pizza Pizza restaurants in the Pool were \$101.5 million and \$389.5 million, for the same periods. For the prior year comparative quarter and year, system sales for the 572 restaurants in the Royalty Pool were \$118.9 million and \$409.5 million, respectively. In 2007, sales from the 41 Pizza 73 restaurants in the Pool were \$19.2 million for the quarter and \$33.1 for the year, while sales from the 531 Pizza Pizza restaurants in the Pool were \$99.7 million for the quarter and \$376.4 million for the year. The increase in Royalty Pool sales, as compared to the prior year is the result of adding 37, net new restaurants on January 1, 2008, 41 new Pizza 73 restaurants in July 2007 and the positive same store sales growth for the year.

Pizza Pizza’s system sales for the quarter ended March 31 have generally been the softest and the December 31 quarter system sales have been the strongest due to seasonality of the business.

PIZZA PIZZA ROYALTY INCOME FUND
Management's Discussion & Analysis

An independent audited statement of Royalty Pool system sales is reported each year, the results of which follow:

System sales reported by Pizza Pizza Royalty Pool Restaurants
From January 1, 2008 to December 31, 2008

(in thousands of dollars)

Total Pizza Pizza retail sales	\$	391,171
New locations ⁽¹⁾		(2,248)
Closed locations		595
2008 Pizza Pizza Royalty Pool System Sales	<u>\$</u>	<u>389,518</u>

System sales reported by Pizza 73 Royalty Pool Restaurants
From January 1, 2008 to December 31, 2008

(in thousands of dollars)

Total Pizza 73 retail sales	\$	85,936
New locations ⁽¹⁾		(11,895)
Step-out payments		7,064
Closed locations		-
2008 Pizza 73 Royalty Pool System Sales	<u>\$</u>	<u>81,105</u>

System sales (as defined in the Licence and Royalty Agreements between Pizza Pizza and the Partnership) reported by Pizza Pizza and Pizza 73 restaurants include the gross sales of Pizza Pizza company-owned, jointly-controlled and franchised restaurants, excluding sales and goods and service tax or similar amounts levied by any governmental or administrative authority.

Total Pizza Pizza retail sales for the year ended December 31, 2008, include sales reported by franchisees and sales from Company-owned locations during the reporting period. Sales from new locations include sales from franchisee or Company-owned locations that were opened on or after January 1, 2008 and on or prior to December 31, 2008. Sales from closed locations include sales from restaurants that were closed on or after January 1, 2008 and on or prior to December 31, 2008, and for which Pizza Pizza is required to pay the Make Whole Payment.

Total Pizza 73 retail sales for the year ended December 31, 2008 include sales reported by the jointly-controlled locations during the reporting period. Sales from new locations include sales from jointly-controlled locations that were opened after September 1, 2007 and on or prior to December 31, 2008. Any amounts calculated as Step-Out Payments under the Pizza 73 Licence and Royalty Agreement, as defined below, are added back to system sales.

As new restaurants are opened within the Pizza 73 group of restaurants, it is expected that the territory assigned to certain of the existing Pizza 73 restaurants, already included in the Royalty Pool, may be reallocated between existing restaurants and new Pizza 73 restaurants that will be opened, among other reasons, to address capacity or market growth issues or increase market penetration. Pursuant to the Pizza 73 Licence and Royalty Agreement, Pizza Pizza will pay to the Partnership a monthly Step-Out Payment in respect of a Pizza 73 restaurant, the territory of which has been reduced, from the month in which the reduction occurs to the end of the next following calendar year. As a result, during this period, the opening of the new restaurant will not cause a reduction of the Pizza 73 royalty in respect of the affected restaurant from the average level paid in the previous year.

Systems sales reported by Pizza Pizza and Pizza 73 restaurants to the Company are self-assessed by each restaurant on a weekly reporting basis and are submitted without audit or other form of independent assurance. However, Pizza Pizza management has internal controls in place and monitors sales weekly, using loss prevention techniques.

¹ Reflects sales at newly opened restaurants not yet included in the applicable Royalty Pool.

PIZZA PIZZA ROYALTY INCOME FUND
Management's Discussion & Analysis

OPERATING RESULTS

From inception, the Fund adopted the guideline of Canadian Institute of Chartered Accountants referred to as "AcG-15", Consolidation of Variable Interest Entities (the "VIE rules"). As a result, the Fund's subsidiary, the Partnership, which owns the Pizza Pizza and Pizza 73 Rights, is accounted for on the equity basis and not on the consolidation basis. To provide further disclosure, the Fund has prepared the following table, that shows the non-GAAP combination of the Fund, as if the VIE rules were not applied to the Fund and the Partnership. Pizza Pizza believes that, in addition to the audited financial statements, the following combination is a useful supplemental measure of performance. The method of performing the combination may differ from that used by other issuers and, accordingly, it may not be comparable to that used by other issuers.

	Pizza Pizza Royalty Income Fund (per GAAP) ⁽¹⁾	Pizza Pizza Royalty Limited Partnership	Eliminating Entries	Pizza Pizza Royalty Income Fund (non-GAAP) ⁽²⁾
Balance Sheet				
As at December 31, 2008				
Current Assets	\$ 1,691	\$ 5,379	\$ (1,541) (3)	\$ 5,529
Loan Receivable from Pizza Pizza	30,000	-	-	30,000
Investment in Pizza Pizza Royalty Limited Partnership	188,635	-	(188,635) (4)	-
Rights and Marks		305,899	-	305,899
Total Assets	220,326	311,278	(190,176)	341,428
Current Liabilities	1,691	1,893	(1,541) (3)	2,043
Long-term Debt	-	46,899	-	46,899
Cash Flow Hedge	-	4,033	-	4,033
Future Income Taxes	5,973	-	-	5,973
Non-controlling Interest	-	-	74,476 (5)	74,476
Equity	212,662	258,453	(263,111) (4)(5)	208,004
Total Liabilities and Equity	\$ 220,326	\$ 311,278	\$ (190,176)	\$ 341,428
Statement of Earnings				
For the Year ended December 31, 2008				
Royalty Income	\$ -	\$ 30,670	\$ -	\$ 30,670
Equity Income	20,079	-	(20,079) (4)	-
Interest Income	1,800	55	-	1,855
Total Revenue	21,879	30,725	(20,079)	32,525
General and Administrative expenses	-	634	-	634
Interest on long-term debt	-	2,701	-	2,701
Earnings before non-controlling interest and taxes	21,879	27,390	(20,079)	29,190
Non-controlling interest	-	-	7,311 (5)	7,311
Future tax recovery	(2,235)	-	-	(2,235)
Net Earnings for the Year	\$ 24,114	\$ 27,390	\$ (27,390)	\$ 24,114

(1) As publicly filed and audited.

(2) Represents the Fund combined with the Partnership, as it would appear if the VIE rules were not applied.

(3) Eliminate receivable/payable balance.

(4) Eliminate investment in the Partnership and distributions from Partnership.

(5) Establish Pizza Pizza's interest in the Partnership.

PIZZA PIZZA ROYALTY INCOME FUND

Management's Discussion & Analysis

The operations of the Fund and Partnership are separately analyzed in the following information to provide a better appreciation of the financial condition and results of the Fund and should be read in conjunction with the Fund's audited consolidated financial statements and the accompanying notes.

Partnership Operations

The Partnership earns royalty income from restaurants in the Royalty Pool. The Fund earns equity income from its investment in the Partnership. The Fund's equity income from the Partnership is calculated as the royalty income less the Partnership's operating expenses less earnings attributable to Pizza Pizza.

The following provides information on the Partnership's performance for the quarter and year ended December 31, 2008.

Revenues

Royalty income earned by the Partnership was \$8.0 million for the quarter and \$30.7 million for the year ended December 31, 2008. A 6% royalty was earned on the Royalty Pool of 559 Pizza Pizza restaurants reporting \$101.5 million in sales for the quarter and \$389.5 million for the year. A 9% royalty was earned on the Royalty Pool of 50 Pizza 73 restaurants reporting \$21.0 million in system sales for the quarter and \$81.1 million in sales for the year.

Royalty income earned by the Partnership for the comparative quarter and year was \$7.7 million and \$25.6 million, respectively, and the 531 Pizza Pizza restaurants in the Royalty Pool reported system sales of \$99.7 million and \$376.4 million, respectively, while the 41 Pizza 73 restaurants reported system sales of \$19.2 million in system sales for the quarter and \$33.1 million for the period from July 24, 2007 to December 31, 2007.

The period over period increase is due to the addition of 37, net new restaurants to the Royalty Pool on January 1, 2008, 41 Pizza 73 restaurants added to the Royalty Pool in July 2007, and the period-over-period SSSG.

Expenses

The Partnership's operating expenses include administrative expenses, amortization of deferred financing fees and interest paid on a \$47 million bank term loan (2007 - \$47 million). See "Liquidity and Capital Resources-Term Loan".

Operating expenses for the quarter were \$791,000, including \$605,000 of interest expense and \$7,000 of amortization of deferred financing fees on the \$47 million term loan and \$179,000 of administrative expenses. Operating expenses for the year were \$3.3 million, including \$2.7 million of interest expense and amortization of financing fees on the \$47 million term loan and \$634,000 of administrative expenses.

Operating expenses for the comparative quarter of 2007 were \$896,000, including \$697,000 of interest expense and \$10,000 of amortization of deferred financing fees on its \$47 million credit facility and \$189,000 of administrative expenses. Operating expenses for the 2007 year-end, excluding issuance costs of \$207,000, were \$2.5 million, including \$1.9 million of interest expense and amortization of deferred financing fees on its \$47 million credit facility and \$636,000 of administrative expenses.

The increase in the year-to-date interest expense is the result of the increase in the term loan from \$20 million to \$47 million in July 2007 in conjunction with the acquisition of the Pizza 73 Rights, offset by a decrease in the interest rate charged on the previously existing, \$20 million facility. See "Liquidity and Capital Resources-Term Loan".

The one time expense for issuance costs incurred in 2007 of \$207,000, which related to the Pizza 73 transaction, is not reflected in the financial highlights table of this Management's Discussion and Analysis. The issuance costs were deducted from the proceeds of the issuance. Therefore, there was no effect on

PIZZA PIZZA ROYALTY INCOME FUND

Management's Discussion & Analysis

the Partnership's cash from operations for the current period. The issuance costs were determined to be without future benefit and were expensed.

Net Earnings

The Partnership had net earnings for the quarter and year ended December 31, 2008 of \$7.2 million and \$27.4 million, respectively, which were allocated to the Fund and Pizza Pizza based on their respective interest in the Partnership, as compared to \$6.8 million and \$23.0 million in the comparable quarter and year ended December 31, 2007.

The increase in the net earnings reflects the increase in royalty income offset by an increase in interest expense, as previously discussed.

Selected Partnership Balance Sheet Information

	(in thousands of dollars)	
	<u>December 31, 2008</u>	<u>December 31, 2007</u>
Current Assets	\$ 5,379	\$ 4,317
Total Assets	311,278	299,532
Current Liabilities	1,893	2,373
Loan Payable	46,899	46,865
Total Liabilities & Equity	311,278	299,532

Fund Operations

Equity income is earned by the Fund through limited partnership holdings of LP units representing its effective 78.5% interest in the Partnership at December 31, 2008. Interest income is earned on a \$30 million loan to Pizza Pizza Limited (the "PPL Loan") and is calculated at 6% per annum, payable monthly.

Equity Income in the Partnership

Equity income earned by the Fund for the quarter and year ended December 31, 2008 was \$5.3 million and \$20.1 million, respectively. The equity income, including issuance costs earned for the comparable 2007 quarter and year, was \$5.2 million and \$16.7 million based on its 81.6% share of the Partnership at that time. The increase in equity income is the result of greater net income earned by the Partnership.

During 2008, the Fund's percentage ownership interest in the Partnership decreased to 78.5% from 81.6% in 2007, as a result of Pizza Pizza vending in restaurants into the Royalty Pool which increased Pizza Pizza's proportionate share of the Fund's fully-diluted units.

Interest Income

The interest income for the quarter and year ended December 31, 2008 was \$450,000 and \$1.8 million, earned on the \$30 million loan from the Fund to Pizza Pizza, with interest paid monthly at 6% per annum. In the comparative quarter and year interest income was \$450,000 and \$1.8 million, respectively. An additional \$49,000 in interest was earned during the third quarter of 2007 on the subscription receipt proceeds held during July pending the closing of the Pizza 73 transaction.

Net Earnings Before Income Taxes and Issuance Costs

Net earnings before income taxes and issuance costs for the quarter were \$5.7 million or \$0.263 per unit, as compared to \$5.6 million or \$0.259 per unit for the comparable quarter in 2007, which equates to a 1.6% increase per unit.

PIZZA PIZZA ROYALTY INCOME FUND

Management's Discussion & Analysis

Net earnings before income taxes and issuance costs for the year were \$21.9 million or \$1.003 per unit, as compared to \$18.7 million or \$0.954 per unit for the 2007 year, which equates to a 5.1% increase per unit.

Future Tax Expense (Recovery)

In the second quarter of 2007, the Canadian federal government enacted tax legislation which included a provision to eliminate the deduction of distributions from taxable income commencing generally in 2011 for certain forms of publicly traded income trusts and partnerships. Accordingly, the Fund gave accounting recognition to these new rules beginning in the second quarter of 2007.

The recovery in the year ended December 31, 2008 is a result of a tax planning strategy to conserve the discretionary deductions available to the Fund until years in which the Fund will become taxable. During the comparative year, the Fund increased its non-cash future tax expense by \$8.2 million to record its proportionate share of the difference between the accounting and tax basis of the Pizza Pizza and Pizza 73 Rights in the Partnership. The future income tax would only be paid if the Pizza Pizza and Pizza 73 Rights were to be sold by the Partnership.

Net Earnings

Net earnings for the fourth quarter were \$5.7 million or \$0.263 per unit, as compared to net earnings of \$10.3 million or \$0.474 per unit in the comparable quarter of 2007. The fourth quarter of 2008 did not contain a future tax adjustment; however, during the fourth quarter of 2007, the net earnings were increased by a non-cash future tax recovery of \$0.215 per unit. The non-cash future tax recovery of \$4.7 million was the result of the determination of the return of capital percentage for 2007. The decision surrounding the return of capital percentage for 2008 was made in the second quarter of 2008, thus the fourth quarter net earnings are not comparable to the same quarter in 2007.

Net earnings for the year ended December 31, 2008 were \$24.1 million, or \$1.105 per unit, as compared to a net earnings of \$10.3 million or \$0.526 per unit for the same period in 2007. For that year, the net earnings per unit have been increased by the non-cash, future tax recovery of \$0.102 per unit, whereas the 2007 year included the initial recognition of the non-cash future tax expense of \$0.419 per unit.

Distributions

The Fund declared distributions of \$5.1 million or \$0.233 per unit for the quarter, equating to an 88% payout ratio; for the 2007 comparable quarter, the Fund declared distributions of \$5.0 million or \$0.228 per unit for a payout ratio of 88%. For the year ended December 31, 2008, the Fund declared distributions of \$20.1 million or \$0.923 per unit, equating to a 92% payout ratio; in 2007, the Fund declared distributions of \$17.6 million or \$0.888 per unit for a payout ratio of 94%.

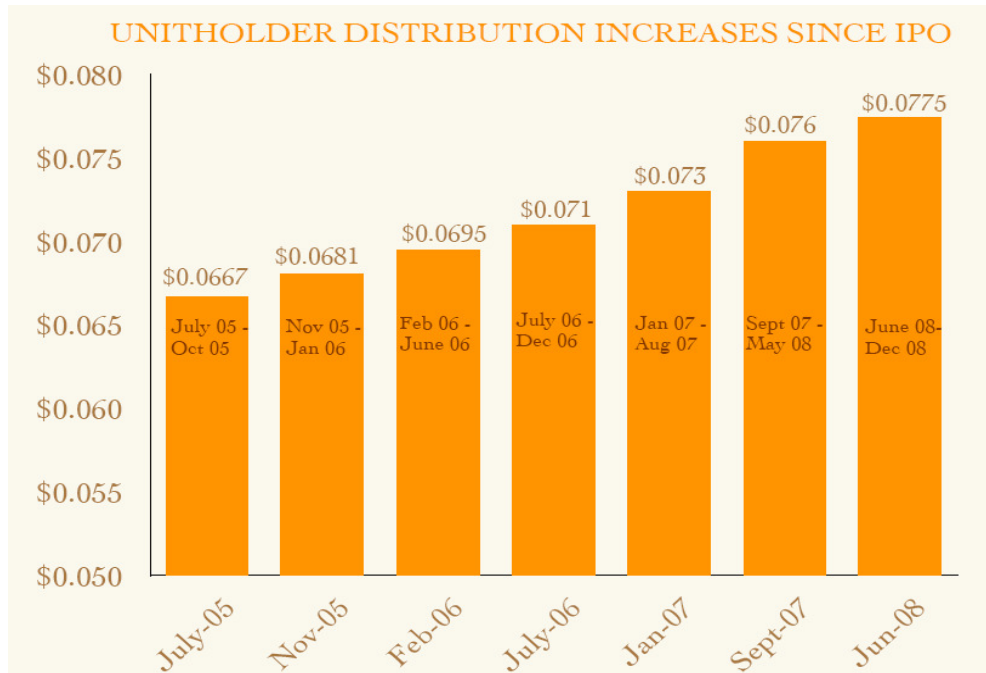
Distributions declared for 2008 are as follows:

<u>Period</u>	<u>Payment Date</u>	<u>Amount/unit</u>
January 1-31, 2008	February 15, 2008	7.6¢
February 1-29, 2008	March 14, 2008	7.6¢
March 1-31, 2008	April 15, 2008	7.6¢
April 1-30, 2008	May 15, 2008	7.6¢
May 1-31, 2008	June 13, 2008	7.6¢
June 1-30, 2008	July 15, 2008	7.75¢
July 1-31, 2008	August 15, 2008	7.75¢
August 1-31, 2008	September 12, 2008	7.75¢
September 1-30, 2008	October 15, 2008	7.75¢
October 1-31, 2008	November 14, 2008	7.75¢
November 1-30, 2008	December 15, 2008	7.75¢
December 1-31, 2008	January 15, 2009	7.75¢
Total		92.25¢

PIZZA PIZZA ROYALTY INCOME FUND
Management’s Discussion & Analysis

Distributions were funded entirely by cash flow from operations. No debt was incurred at any point during the quarter to fund distributions.

Since the initial public offering in July 2005, the Fund has increased distributions six times with the most recent being in June 2008, as depicted in the chart below:



LIQUIDITY & CAPITAL RESOURCES

The Fund’s distribution policy is to distribute all available cash in order to maximize returns to Unitholders over time, after allowing for reasonable reserves held at the Partnership level. In light of seasonal variations that are inherent to the restaurant industry, the Fund’s policy is to make equal distribution payments to Unitholders on a monthly basis in order to smooth out these fluctuations. Any further increase in distributions will be implemented with a view to maintain the continuity of uniform monthly distributions. It is expected that future distributions will continue to be funded entirely by cash flow from operations.

As of December 31, 2008, working capital of the Partnership was \$3.5 million (December 31, 2007 - \$1.9 million), accumulated as a reserve to cover seasonality and any unusual administrative expenditures.

Term Loan and Operating Loan

On July 24, 2007, the Partnership amended the, then, existing credit agreement with a Canadian chartered bank (the “Bank”) to increase the committed, non-revolving facility from \$20 million to \$47 million and to extend the term by five years to 2012. The initial \$20 million facility was arranged during the initial public offering to partially finance the purchase of the Pizza Pizza Rights from Pizza Pizza. To partially finance the Pizza 73 transaction, the facility was increased by \$27 million to \$47 million. As security for repayment of the facility, the Partnership has provided the Bank with a first ranking general security agreement charging all tangible and intangible assets of the Partnership, as well as an assignment of all security supporting the Licence and Royalty Agreements. In addition, Pizza Pizza granted to the Partnership a continuing, general security interest, subject to certain exceptions, in all present, and acquired property of Pizza Pizza. The facility bears interest at Prime plus 0% to 0.25% or the Bankers Acceptance rate plus 1.0% to 1.75%, depending on the level of debt-to-EBITDA, with EBITDA defined as annualized earnings before interest, taxes, depreciation and amortization. During 2007, the

PIZZA PIZZA ROYALTY INCOME FUND

Management's Discussion & Analysis

interest rate on the facility was fixed with one swap maturing in January 6, 2010 and two swaps maturing July 23, 2012.

The interest rate on the initial \$20 million facility decreased during the third quarter of 2007 from 3.55% plus 1.50% credit spread to 3.55% plus 1.25% credit spread. The remaining \$27 million is initially fixed with two swaps at 5.05% plus 1.25% credit spread. Interest rates may decrease should the debt-to-EBITDA ratio decrease to certain thresholds.

The Bank has also granted an extendable 364 day, committed, revolving operating facility for up to \$1 million; no funds have been drawn on this facility.

These facilities include affirmative and negative covenants customary for agreements of this nature. In particular, the Partnership has agreed to a financial covenant in which, on a four quarter rolling basis, Distributions may not exceed Distributable Cash Flow for such period *plus* the aggregate amount of Distributable Cash Flow for prior Distribution Periods not distributed, which as at December 31, 2008 was \$4.0 million (2007 - \$2.2 million). In addition, the Partnership is required to maintain a funded debt-to-EBITDA ratio not to exceed 2.5:1 on a four quarter rolling average. The debt-to-EBITDA ratio for the last four quarters rolling average is 1.56:1 (2007 – 1.89:1). The Partnership is presently making interest-only payments on the non-revolving credit facility. Should the debt-to-EBITDA ratio for the last four quarters rolling average drop below 1.5:1, then the interest rate on the credit facility will drop 25 basis points.

SUBSEQUENT EVENTS

Subsequent to the year ended December 31, 2008, the Fund declared distributions are as follows:

<u>Period</u>	<u>Payment Date</u>	<u>Amount/unit</u>
January 1-31, 2009	February 13, 2009	7.75¢
February 1-28, 2009	March 13, 2009	7.75¢
March 1-31, 2009	April 15, 2009	7.75¢

2008 Vend-in Adjustment

In early January 2009, adjustments to royalty payments and Pizza Pizza's Class B Exchange Multiplier were made based on the actual performance of the 28 net, restaurants added to the Royalty Pool on January 1, 2008. As a result of the adjustments, the Class B Exchange Multiplier effective for 2008 was 1.3737 and Pizza Pizza's Class B exchangeable units increased by 164,542 to 5,595,241. An adjustment was also made to the royalty payments and Pizza Pizza's Class D Exchange Multiplier based on the actual performance of the nine net, restaurants added to the Royalty Pool on January 1, 2008. As a result of the adjustments, the Class D Exchange Multiplier effective for 2008 was 7.9961 and Pizza Pizza's Class D exchangeable units increased by 240,860 to 799,610.

2009 Vend-in Adjustment – Class B Exchange Multiplier

On January 1, 2009, nine net, new Pizza Pizza restaurants were added to the Royalty Pool as a result of 18 new restaurants opening and nine closing during 2008. The additional system sales from the nine net, new restaurants are estimated at \$3.1 million annually. The total number of Pizza Pizza restaurants in the Royalty Pool has increased to 568. The yield of the Fund units was determined to be 15.3% calculated using \$6.04 as a weighted average unit price. Weighted average unit price is calculated based on the market price of the units traded on the TSX during the period of 20 consecutive days ending on the fifth trading day before January 1, 2009. As a result of the contribution of the additional net sales to the Royalty Pool, Pizza Pizza's Class B Exchange Multiplier increased fractionally by 80% of the total adjustment or 0.0365; the new Class B Multiplier is 1.4102. This adjustment will also increase the entitlement of the holders of the Class B Units to distributions of cash and allocations of income from the Partnership. The second adjustment to the Class B Exchange Multiplier will be adjusted to be effective January 1, 2010, once the actual performance of the new restaurants is determined in early 2010. As a result of the Adjusted Class B Exchange Multiplier, Pizza Pizza will hold Class B Partnership units exchangeable into 5,743,931 Fund units.

PIZZA PIZZA ROYALTY INCOME FUND

Management's Discussion & Analysis

2009 Vend-in Adjustment – Class D Exchange Multiplier

On January 1, 2009, 19 new Pizza 73 restaurants opened between September 2, 2007 and September 1, 2008 were added to the Royalty Pool. The additional system sales from the 19 new restaurants are estimated at \$14.1 million annually which was reduced by \$4.9 million in system sales attributable to certain of the restaurants now added to the Royalty Pool whose territory adjusted a previously existing restaurant. The total number of Pizza 73 restaurants in the Royalty Pool has increased to 69. The yield and weighted average unit price used in the calculation of the multiplier is the same as that of the Class B adjustment previously discussed of 15.3% and \$6.04, respectively. As a result of the contribution of the additional net sales to the Royalty Pool, Pizza Pizza's Class D Exchange Multiplier increased fractionally by 80% of the total adjustment or 6.6075; the new Class D Multiplier is 14.6036. This adjustment will also increase the entitlement of the holders of the Class D Units to distributions of cash and allocations of income from the Partnership. The second adjustment to the Class D Exchange Multiplier will be adjusted to be effective January 1, 2009, once the actual performance of the new restaurants is determined in early 2010. As a result of the Adjusted Class D Exchange Multiplier, Pizza Pizza will hold Class D Partnership units exchangeable into 1,460,355 Fund units.

Pizza Pizza's Ownership of the Fund

In exchange for adding the 28 net, new restaurants to the Royalty Pool, Pizza Pizza has received 148,690 additional Class B equivalent units and 660,745 Class D equivalent units. These units represent 80% of the full Class B and Class D entitlements (185,863 and 825,932 units, respectively, represent 100%), with the balance to be received when the 2009 sales performance is known with certainty.

Including the 809,435 exchangeable units described above, Pizza Pizza owns equivalent, exchangeable units equal to 24.8% of the Fund's fully diluted units.

		Issued & Outstanding units, and Exchangeable Equivalent units
Units outstanding & issuable on January 1, 2009		
Public float		21,818,392
Class B units held by Pizza Pizza	5,430,699	
Pizza Pizza additional Class B units - Holdback as of December 31, 2008	164,542	
Additional Pizza Pizza Class B equivalent units as of January 1, 2009	<u>148,690</u>	5,743,931
Class D units held by Pizza Pizza	558,750	
Pizza Pizza additional Class D units - Holdback as of December 31, 2008	240,860	
Additional Pizza Pizza Class D equivalent units as of January 1, 2009	<u>660,745</u>	1,460,355
Number of fully diluted units		<u>29,022,678</u>
Proportion of all units outstanding available for exchange by Pizza Pizza		24.8%

OUTLOOK

In 2009, Pizza Pizza management expects to grow the number of restaurants by 3% and to continue researching strategic acquisition opportunities. Organically, Pizza Pizza expects to grow outside its largely, Ontario markets by opening additional locations in Montreal, as well as in western provinces. In the Alberta marketplace, Pizza 73 traditional locations will continue to be added to better service the growing western Canadian customer base. Pizza 73's brand awareness will also be promoted using non-traditional locations with the addition of professional sports partnerships and event sponsorships. In 2008, Pizza Pizza opened a net, 24 restaurants increasing the overall number of restaurants by 3.9%.

PIZZA PIZZA ROYALTY INCOME FUND

Management's Discussion & Analysis

Deteriorating economic conditions in Pizza Pizza's core markets have impacted SSSG through 2008, and more notably in the fourth quarter. The majority of the Pizza Pizza restaurants operate in the province of Ontario which continues to experience a decline in manufacturing employment and tourism, both attributable to an economic slowdown in the United States and fears of weak global growth. For the Pizza 73 brand, the majority of the restaurants operate in Alberta, whose economy is beginning to be affected by the decline in the price of oil. The province reported lower retail sales and manufacturing shipments in November 2008 compared to the previous month. In addition to the economic impact, 14 traditional stores have opened in Alberta since October 1, 2007 of which 13 have reduced territories of previously existing stores which negatively impacted SSSG. Adding restaurants in the Alberta market is part of Pizza Pizza's overall strategy to relieve capacity constraints at the restaurant level and provide improved customer service, while growing and protecting the Pizza 73 brand.

Fourth quarter SSSG decreased slightly by 0.6% over the same period last year. This was a slight decrease from the results reported in the third quarter. As Ontario consumers continue to be price-sensitive, Pizza Pizza employed marketing strategies to meet this consumer trend by using competitive value initiatives. Year-to-date, the two brands reported a 1.7% SSSG.

Although SSSG of 1.7% year-to-date is below our historical sales growth experience, Pizza Pizza management is satisfied with the Company's performance in light of the economic challenges encountered in the Ontario market and new restaurants added at Pizza 73. Although the Company does not anticipate significant near-term improvement in the economy, our strategies will focus on reinforcing value-oriented menu offerings, launching new relevant products, and reinvesting in activities which drive sales growth.

Pizza Pizza's core strategy of driving long-term unitholder and restaurant value is supported by the Company's track record of innovation, especially in providing customer convenience and satisfaction. During the second quarter, we completed the successful roll-out of the wireless "debit-to-your-door" project for both Pizza Pizza and Pizza 73. In the third quarter, we took advantage of the wireless devices by introducing our enhanced loyalty card program not only for walk-in traffic, but also for consumers choosing to use our delivery system. Marketing initiatives and incentives will support the wireless introduction by encouraging consumers to use the loyalty/gift cards.

Additionally, in the last quarter of 2008, Pizza Pizza management completed a major technological investment of our on-line ordering option to improve this consumer contact experience. Pizza 73's on-line ordering was vastly improved last year and is the preferred method for over 20% of orders placed as it provides the consumer an efficient, convenient ordering method while reducing operating costs. We anticipate similar success with the Pizza Pizza on-line ordering enhancements. These innovations are examples of what drives Pizza Pizza's market share, which exceeds 50% in Ontario and over 30% in Alberta.

CONTROLS AND PROCEDURES

Internal controls and procedures are designed to provide reasonable assurance that relevant information is gathered and reported to senior management, including the Chief Executive Officer ("CEO") and the Chief Financial Officer ("CFO") of Pizza Pizza GP Inc., managing general partner of the Partnership and administrator of the Fund, on a timely basis so that the appropriate decisions can be made regarding public disclosure. Internal controls over financial reporting are designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of the financial statements in accordance with GAAP.

Management carried out an evaluation of the effectiveness of design and operation of the Company's disclosure controls and procedures and internal controls over financial reporting as of December 31, 2008. It was determined that the Company's disclosure controls and procedures and internal controls over financial reporting were effective.

During the quarter ending December 31, 2008, there were no material changes in the Company's internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

PIZZA PIZZA ROYALTY INCOME FUND

Management's Discussion & Analysis

CRITICAL ACCOUNTING ISSUES

The Fund's only critical accounting estimate is the valuation of its investment in the Partnership. As the Partnership's only significant assets are intangible assets consisting of the Pizza Pizza and Pizza 73 Rights, the valuation of the Fund's investment is based primarily upon the valuation of intangible assets in the Partnership. The Pizza Pizza and Pizza 73 Rights are not amortized as they have an indefinite life. Pizza Pizza GP Inc., as the general partner of the Partnership and administrator of the Fund, reviews the carrying values of the intangible assets in the Partnership and the Fund's investment at least annually, taking into consideration any events or circumstances which may have impaired the carrying values of these items. If permanent declines in the carrying amounts are determined, these items are written down to their estimated net recoverable amount. Pizza Pizza GP, Inc. believes that there have been no declines in either the carrying value of the intangible assets in the Partnership or in the carrying value of the Fund's investment in the Partnership as of December 31, 2008.

CHANGES IN ACCOUNTING POLICIES, INCLUDING INITIAL ADOPTION

General Standards on Financial Statement Presentation

Commencing January 1, 2008, the Fund has adopted the new recommendations of the Canadian Institute of Chartered Accountants' ("CICA") Handbook Section 1400, General Standards on Financial Statement Presentation. Under these new recommendations, the Fund is required to assess and disclose its ability to continue as a going concern. The Fund's adoption of this standard did not have a material impact on disclosure in the Fund's financial statements.

Capital Disclosure

Commencing January 1, 2008, the Fund has adopted the new recommendations of the CICA Handbook Section 1535, Capital Disclosures. Under these new recommendations, the Fund is required to disclose its objectives, policies and processes for managing capital and whether the entity has complied with any capital requirements, and if it has not complied, the consequences of such non-compliance. The required disclosure is in note 8 of the Fund's annual consolidated financial statements.

Financial Instruments - Disclosures

Commencing January 1, 2008, the Fund has adopted the new recommendations of the CICA Handbook Section 3862, Financial Instruments – Disclosures. Under these new recommendations, the Fund is required to increase the disclosure to enable user to evaluate the significance of financial instruments for the Fund's financial position and performance, including disclosure about fair value. In addition, disclosure is required of qualitative and quantitative information about exposure to risks arising from financial instruments, including specified minimum disclosures about liquidity risk and market risk. The quantitative disclosures must also include a sensitivity analysis for each type of market risk to which an entity is exposed, showing how net earnings and other comprehensive income would have been affected by reasonably possible changes in the relevant risk variable. The required disclosure is in note 11 of the Fund's annual consolidated financial statements.

Financial Instrument Presentation

Commencing January 1, 2008, the Fund has adopted the new recommendations of the CICA Handbook Section 3863, Financial Instrument – Presentation, which replaces the existing requirements on presentation of financial instruments which have been carried forward unchanged to this new section. The Fund's adoption of this standard did not have a material impact on disclosure in the Fund's financial statements.

PIZZA PIZZA ROYALTY INCOME FUND

Management's Discussion & Analysis

RECENT ACCOUNTING PRONOUNCEMENTS

Recent accounting pronouncements issued and not yet effective:

Business Combinations

CICA Handbook Section 1582, Business Combinations, which replaces CICA Handbook Section 1581, Business Combinations, establishes standards for the accounting for a business combination. It is the Canadian equivalent to International Financial Reporting Standard IFRS 3, Business Combinations. This standard is effective for the Fund for interim and annual financial statements beginning on January 1, 2011. The Fund has not yet determined the impact of the adoption of this change on its financial statements.

Consolidated Financial Statements and Non-controlling Interests

CICA Handbook Sections 1601, Consolidated Financial Statements and 1602, Non-controlling Interests replace CICA Handbook Section 1600, Consolidated Financial Statements. 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. Section 1602 is equivalent to the corresponding provisions of International Financial Reporting Standard IAS 27, Consolidated and Separate Financial Statements. These standards are effective for the Fund for interim and annual financial statements beginning on January 1, 2011. The Fund has not yet determined the impact of the adoption of these changes on its financial statements.

International Financial Reporting Standards

The Canadian Accounting Standards Board announced in February 2008 that publicly accountable enterprises will be required to adopt IFRS in place of Canadian generally accepted accounting principles for interim and annual reporting purposes for fiscal years beginning on or after January 1, 2011. The Fund's first financial statement reported under IFRS will be the unaudited interim statements for the three months ended March 31, 2011. Prior year comparatives, restated under IFRS, will be included in these statements. At this time, the impact on the future financial position and results of operations is not reasonably determinable or estimable.

The IFRS project consists of four phases: diagnostic assessment, project planning and education, policy design and implementation. In 2008, the Fund, with the assistance of its external auditor, completed the diagnostic phase, which involved a high level review of the major differences between current Canadian GAAP and IFRS. The Fund is in the process of developing a detailed project plan for 2009 and 2010, which will include internal and external communications, and training. During 2009, the Fund will continue the process of evaluating available IFRS accounting policy alternatives and assess the potential impact on financial reporting, including systems and processes and other business areas.

As the IFRS transition plan progresses, the Fund will continue to report on the status of the plan, and will provide increased clarity into the anticipated consequences of accounting policy changes. The Fund's goal is to make policy changes that are compliant but also provide the most meaningful information to our unitholders.

RISKS & UNCERTAINTIES

The Fund continues to recognize certain risks and uncertainties associated with the ordinary course of business, including those associated with the business and operations of Pizza Pizza, upon which the Fund relies solely for its earnings.

The Restaurant Industry

The performance of the Fund is directly dependent upon the royalty and interest payments received from Pizza Pizza. The amount of royalty received from Pizza Pizza is dependent on various external factors that may affect

PIZZA PIZZA ROYALTY INCOME FUND

Management's Discussion & Analysis

the limited service sector of the restaurant industry. The restaurant industry, generally, is intensely competitive with respect to price, service, location and food quality. Competitors include national and regional chains, as well as independently owned restaurants and retailers of frozen pizza. If Pizza Pizza, Pizza Pizza franchisees and Pizza 73 operators are unable to successfully compete in the limited service sector, System Sales may be adversely affected, the amount of royalty reduced and the ability of Pizza Pizza to pay the royalty or interest on the PPL Loan may be impaired. Changes in demographic trends, traffic patterns, and the type, number, and location of competing restaurants also affect the restaurant industry. In addition, factors such as government regulations, smoking bylaws, inflation, publicity from any food borne illnesses, increased food, labour and benefits costs, and the availability of experienced management and hourly employees may adversely affect the restaurant industry in general and therefore, potentially, Pizza Pizza and Pizza 73 System Sales. Pizza Pizza's success also depends on numerous factors affecting discretionary spending, including economic conditions, disposable consumer income and consumer confidence. Adverse changes in these factors could reduce guest traffic or impose practical limits on pricing, either of which could reduce sales and operating income, which could adversely affect revenue, the royalty and the ability of Pizza Pizza to pay the royalty to the Fund or interest on the PPL Loan. For additional information concerning the performance of Pizza Pizza, please refer to the Pizza Pizza MD&A which is available at www.sedar.com and www.pizzapizzaroyaltyincomefund.com.

Litigation

In the fourth quarter of 2008, the Fund received an update from Pizza Pizza regarding a potential claim disclosed in the Fund's 2005 initial public offering prospectus and Pizza Pizza's subsequent financial statement filings.

The claim, which does not name the Fund or its subsidiaries, was formally served on Pizza Pizza and certain of its associates by Lawrence Austin, a former consultant to Pizza Pizza. In the claim, Mr. Austin asserts a right to \$45 million in damages and other amounts, including entitlements to a portion of the proceeds of the Fund's IPO that were directly or indirectly received by Pizza Pizza and its associates.

Pizza Pizza has advised the Fund that it believes the demand to be without merit and it will vigorously defend the claim. The parties have exchanged documents and examinations for discovery have been scheduled. The Fund notes that Michael Overs, the Chairman and CEO of Pizza Pizza, has agreed in an indemnity agreement to indemnify Pizza Pizza and the Fund against any liabilities that they may incur in this matter.

Other

For a more detailed list of risks and uncertainties please refer to the Fund's Annual Information Form which is available at www.sedar.com and www.pizzapizzaroyaltyincomefund.com.

FORWARD LOOKING STATEMENTS

Certain statements in this report including those concerning our plans and strategies described under "Outlook", may constitute "forward-looking" statements which involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by such forward looking statements. When used in this report, such statements include such words as "may", "will", "expect", "believe", "plan", and other similar terminology. These statements reflect management's current expectations regarding future events and operating performance and speak only as of the date of this report. These forward-looking statements involve a number of risks and uncertainties. The following are some factors that could cause actual results to differ materially from those expressed in or underlying such forward-looking statements: competition; changes in demographic trends; changing consumer preferences and discretionary spending patterns; changes in national and local business and economic conditions; legislation and governmental regulation; accounting policies and practices; and the results of operations and financial condition of Pizza Pizza. The foregoing list of factors is not exhaustive and should be considered in conjunction with the other risks and uncertainties described in the Fund's Annual Information Form. The Fund assumes no obligation to update these forward looking statements, except as required by applicable securities laws.

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ADDITIONAL INFORMATION

Additional information about the Fund including the Fund's most recent Annual Information Form is available on SEDAR at www.sedar.com or at the Fund's website www.pizzapizzaroyaltyincomefund.com.