

ADVANTAGE

ENERGY INCOME FUND

2004 THIRD QUARTER REPORT

FINANCIAL AND OPERATING HIGHLIGHTS



(thousands of dollars except per Unit amounts)

	Three months ended Sept. 30, 2004	Three months ended Sept. 30, 2003	Nine months ended Sept. 30, 2004	Nine months ended Sept. 30, 2003
Financial				
Revenue before royalties	\$ 56,722	\$ 40,863	\$ 164,739	\$ 122,596
per Unit ⁽¹⁾	\$ 1.39	\$ 1.32	\$ 4.18	\$ 4.13
per boe	\$ 39.87	\$ 35.81	\$ 39.73	\$ 37.59
Cash flow from operations	\$ 32,860	\$ 24,567	\$ 97,213	\$ 73,918
per Unit ⁽¹⁾	\$ 0.80	\$ 0.79	\$ 2.47	\$ 2.49
per boe	\$ 22.16	\$ 21.53	\$ 22.70	\$ 22.67
Cash available for distribution ⁽³⁾	\$ 31,074	\$ 23,581	\$ 91,667	\$ 70,609
per Unit ⁽²⁾	\$ 0.75	\$ 0.76	\$ 2.30	\$ 2.38
per boe	\$ 20.95	\$ 20.67	\$ 21.40	\$ 21.65
Net income	\$ 7,102	\$ 9,560	\$ 25,836	\$ 45,890
per Unit ⁽¹⁾	\$ 0.13	\$ 0.28	\$ 0.51	\$ 1.44
Cash distributions	\$ 28,730	\$ 21,507	\$ 82,447	\$ 60,477
per Unit ⁽²⁾	\$ 0.69	\$ 0.69	\$ 2.07	\$ 2.02
Payout ratio	92%	91%	90%	86%
Working capital deficit	\$ 9,537	\$ 12,078	\$ 9,537	\$ 12,078
Bank debt	\$ 184,437	\$ 126,366	\$ 184,437	\$ 126,366
Convertible debentures	\$ 176,462	\$ 43,549	\$ 176,462	\$ 43,549
Operating				
Production				
Natural gas (mcf/d)	75,425	58,686	74,788	55,053
Light oil and NGLs (bbls/d)	3,550	2,623	3,167	2,770
boe (6:1)	16,121	12,404	15,632	11,945
Average prices (including hedging)				
Natural gas (\$/mcf)	\$ 5.76	\$ 5.96	\$ 6.08	\$ 6.20
Light oil & NGLs (\$/bbl)	\$ 51.20	\$ 36.04	\$ 46.24	\$ 38.95
Supplemental (000s)				
Trust Units outstanding - end of period	44,350	31,318	44,350	31,318
Trust Units issuable for				
Convertible Debentures	9,261	2,783	9,261	2,783
Trust Units outstanding and issuable for				
Convertible Debentures - end of period	53,611	34,101	53,611	34,101
Weighted average Units	40,887	31,069	39,403	29,676

⁽¹⁾ based on weighted average number of Trust Units outstanding

⁽²⁾ based on number of Trust Units outstanding at each cash distribution date

⁽³⁾ cash flow from operations less interest on convertible debentures

CASH DISTRIBUTIONS TO UNITHOLDERS

- ◆ The Fund declared three distributions during the quarter totalling \$0.69 per Unit. The distributions amounted to \$0.23 per Unit, payable on August 16, September 15 and October 15 to Unitholders of record on July 30, August 31 and September 30 respectively.
- ◆ Cash available for distribution for the third quarter was \$31.1 million or \$0.75 per Unit compared to the amount reported in the third quarter of 2003 of \$0.76 per Unit and represents a payout ratio of 92% of total cash available for distribution.
- ◆ As a result of the closing of the Anadarko asset acquisition and the recent strength in commodity prices the Fund increased its monthly distribution to \$0.25 per Unit commencing in October. The Fund has announced a further increase to the distribution to \$0.28 per Unit commencing in January, 2005 subject to the closing of the Defiant acquisition prior to year end. The increased monthly distribution represents a 22% increase from the \$0.23 per Unit paid in September.

OIL & NATURAL GAS PRODUCTION

NATURAL GAS

- ◆ Natural gas production for the third quarter of 2004 was 75.4 mmcf/d, a 28% increase over the 58.7 mmcf/d reported in the third quarter of 2003.
- ◆ The increase in production is attributed to the acquisition of MarkWest Resources which closed December 2, 2003 and additional volumes added through drilling at Medicine Hat, Bantry and Shouldice.
- ◆ During the third quarter of 2004 Advantage drilled 35.5 net (46 gross) natural gas wells.

CRUDE OIL & NGLS

- ◆ Crude oil and natural gas liquids production increased 35% and averaged 3,550 bbls/d compared to 2,623 bbls/d in the third quarter of 2003. Third quarter 2003 oil production included 240 bbls/d related to a minor property disposition that occurred in the fourth quarter of 2003.
- ◆ Production increases resulted from the acquisition of MarkWest Resources and a successful drilling program at Nevis, Alberta.
- ◆ During the third quarter the Fund drilled 6.5 net (8 gross) successful oil wells.

DEVELOPMENT ACTIVITY

NEVIS

- ◆ The Fund acquired 23 sections of land at Nevis, Alberta through the MarkWest acquisition in December 2003. Through crown sales, swaps and a farm-in arrangement the Fund has acquired an additional 18 sections of land in this area.
- ◆ Over the course of the past year Advantage has drilled a total of 10 horizontal wells, four vertical earning wells and one vertical natural gas well at Nevis all with a 100% working interest. Three of the vertical earning wells encountered oil and will be re-entered and drilled as horizontal wells in the fourth quarter.
- ◆ In the fourth quarter, in addition to the re-entries, the Fund expects to drill six horizontal wells to continue developing the field with up to 60 to 70 additional wells planned over the next 12 to 18 months.
- ◆ Currently eight of the ten horizontal wells have been completed and equipped as oil wells and have added an average of 130 to 140 boe/d per well of new production, stabilizing at 80 to 90 boe/d per well after approximately eight months.
- ◆ Also during the third quarter the Fund shot 36 square kilometres of three dimensional seismic. Substantially all of the area now has three dimensional seismic coverage.

MEDICINE HAT

- ◆ A total of 66 natural gas wells (100% working interest) have been drilled during the first nine months of 2004 with a 100% success rate.
- ◆ An additional 32 natural gas wells (100% working interest) have been drilled in the early part of the fourth quarter.
- ◆ Current production from the Medicine Hat field is approximately 22 mmcf/d and expected to increase to approximately 24 mmcf/d by the end of the year with the completion and tie-in of the wells drilled in the fourth quarter.

ACQUISITION ACTIVITY

ANADARKO ASSETS

- ◆ On September 15, 2004 Advantage closed the acquisition of petroleum and natural gas properties located in central Alberta, southern Alberta and southeast Saskatchewan from Anadarko Canada Corporation for net consideration after adjustments of approximately \$175 million.
- ◆ Production acquired amounted to 6,250 boe/d weighted 49% light oil and NGLs, 40% natural gas and 11% heavy oil (23° API).
- ◆ Approximately 13.9 million boe of proven and probable reserves were acquired based on an independent engineering determination prepared by Sproule Associates Limited effective July 1, 2004.
- ◆ 60% of the production is operated with nine projects representing 87% of the total production.
- ◆ The acquisition was financed through the issuance of 3.5 million Advantage Trust Units at \$18.80 per Unit, \$75 million of 5 year 7.5% and \$50 million of 7 year 7.75% subordinated convertible debentures. The 7.5% debentures are convertible into Advantage Trust Units at \$20.25 per Unit and the 7.75% debentures are convertible into Advantage Units at \$21.00 per Unit. Total net proceeds of the offering amounted to \$182.5 million.

DEFIANT ENERGY CORPORATION

- ◆ On November 3, 2004 Advantage announced it had entered into an Arrangement Agreement to acquire all of the outstanding shares of Defiant Energy Corporation. The acquisition is expected to close prior to year end.
- ◆ Production to be acquired of 3,450 boe/d is weighted 72% towards natural gas and 28% to light oil and NGLs.
- ◆ Approximately 15.2 million boe of proven and probable reserves are to be acquired with a reserve life index in excess of 12 years.
- ◆ The asset base is highly concentrated consisting of three core areas located in central Alberta all of which are in close proximity to existing Advantage operations.
- ◆ approximately 90% of the production is operated, with four projects representing 85% of current production.

Consideration for the acquisition is as follows:

- ◆ Advantage will acquire all of the approximately 34.0 million fully diluted common shares of Defiant in exchange for 0.201373 of an Advantage Unit or \$4.40 per share in cash, subject to a maximum cash consideration of \$34 million. In lieu of Units, shareholders of Defiant may elect to receive exchangeable shares issued by Advantage Oil & Gas Ltd. subject to an aggregate limit of 1.5 million exchangeable shares. Advantage will assume Defiant's debt which was approximately \$41.3 million at October 31, 2004.
- ◆ For each share of Defiant, Defiant shareholders will also receive shares of a newly incorporated Explorecor, which will hold approximately 97,000 net acres of undeveloped land and the option to acquire approximately 120 boe/d of production from Advantage in the West Pembina area for \$5.6 million.

ACCRETION SUMMARY

Advantage estimates that, on a pro forma basis, these two acquisitions would have been accretive on the following key criteria at as August 31, 2004:

- | | |
|----------------------------|-------|
| ◆ Production per Unit: | 35.4% |
| ◆ Cash flow per Unit: | 36.9% |
| ◆ Reserves (P+P) per Unit: | 27.2% |

MANAGEMENT'S DISCUSSION & ANALYSIS

The following MD&A provides a detailed explanation of the financial and operating results of Advantage Energy Income Fund ("Advantage" or "the Fund") for the quarter ended September 30, 2004 and should be read in conjunction with the financial statements contained within this interim report and the audited financial statements and MD&A for the year ended December 31, 2003.

All per barrel of oil equivalent ("boe") numbers are stated at a 6:1 conversion rate for natural gas to oil.

CASH DISTRIBUTIONS

Cash distributions for the three months ended September 30, 2004 were \$0.69 per Unit, or \$28.7 million and \$2.07 per Unit, or \$82.4 million for the nine months ended September 30, 2004. The third quarter 2004 distributions were comprised of \$0.23 per month for each of July, August and September. The amount distributed for the quarter represents 92% of total cash available for distribution. Cash available for distribution is defined as cash flow from operations less interest on convertible debentures. The remaining cash withheld during the first nine months of 2004 of \$9.2 million was used to partially finance the Fund's ongoing capital expenditure program. Since its inception on May 23, 2001 the Fund has distributed \$216.3 million or \$7.96 per Unit. As a result of strengthening commodity prices and the closing of the Anadarko asset acquisition in September, Advantage has increased the monthly distribution from \$0.23 per Unit to \$0.25 per Unit commencing for the month of October. In addition, on November 3 Advantage announced that it had entered an Arrangement Agreement to acquire all of the outstanding shares of Defiant Energy Corp. Subject to successful closing of the acquisition, which is scheduled for mid December, Advantage will further increase its monthly distribution to \$0.28 per Unit commencing in the month of January 2005. This would represent a 22% increase in the monthly distribution rate from the month of September.

Cash distributions to Unitholders were paid as follows:

Period ended	Record date	Payment date	Distribution	Distribution per Unit
July 31, 2004	July 30, 2004	Aug. 16, 2004	\$ 9,219	\$ 0.23
Aug. 31, 2004	Aug. 31, 2004	Sept. 15, 2004	\$ 9,311	0.23
Sept. 30, 2004	Sept. 30, 2004	Oct. 15, 2004	\$ 10,200	0.23
			\$ 28,730	\$ 0.69

PRODUCTION

During the three months ended September 30, 2004 Advantage's natural gas production increased by 28% to 75.4 mmcf/d compared to 58.7 mmcf/d for the quarter ended September 30, 2003. Year to date, Advantage's natural gas production increased by 36% to 74.8 mmcf/d compared to 55.1 mmcf/d for the nine months ended September 30, 2003. The increase in natural gas production is primarily due to the acquisition of MarkWest Resources on December 2, 2003. In addition successful drilling at Medicine Hat, Shouldice and Bantry have added production to offset natural declines. On September 15, 2004 Advantage closed the acquisition of the Anadarko assets. Production related to the acquisition is included in the Funds financial statements from the date of closing and therefore did not have a material impact on third quarter production levels.

Year to date, Advantage's liquids production increased by 14% to 3,167 bbls/d compared to 2,770 bbls/d for the nine months ended September 30, 2003. Crude oil and natural gas liquids production averaged 3,550 bbls/d in the third quarter of 2004 compared to 2,623 bbls/d for the quarter ending September 30, 2003. The 35% increase in liquids production from the third quarter of 2003 is due to the acquisition of MarkWest on December 2, 2003 and additional light oil volumes added through the drill bit at Nevis, Alberta.

PRICES

During the nine months ended September 30, 2004, the Fund's natural gas price averaged \$6.35 per mcf (\$6.08 per mcf including hedging) compared to \$6.64 per mcf (\$6.20 per mcf including hedging) for the same period of 2003.

During the three months ended September 30, 2004 Advantage's natural gas price averaged \$6.11 per mcf (\$5.76 per mcf including hedging) compared to \$5.85 per mcf (\$5.96 per mcf including hedging) in the third quarter of 2003. For the three months ended September 30, 2004 AECO daily prices averaged \$6.49 per mcf compared to \$5.87 per mcf in the same period of 2003.

Natural gas prices have remained relatively strong during the third quarter of 2004 and have traded in a \$5 - \$7 per mcf range since the spring of 2003. Early in the fourth quarter of 2004 natural gas prices have increased above this band with winter 2004/

2005 prices currently trading at \$8.35 per mcf. The strengthening of natural gas has been attributed to (i) the strength of crude oil prices which has eliminated the economic advantage of fuel switching away from natural gas, (ii) the shut-in of production in the Gulf of Mexico which resulted from hurricane season and (iv) the approach of the winter heating season coupled with concerns over supply. Advantage continues to believe the pricing fundamentals for natural gas remain strong.

For the nine months ended September 30, 2004, crude oil and NGLs prices averaged \$46.24 per barrel (\$46.24 per barrel including hedging) compared to \$39.54 per barrel (\$38.95 per barrel including hedging) for the same period in 2003. Crude oil and NGLs prices averaged \$51.20 per barrel (\$51.20 per barrel including hedging) in the third quarter of 2004 compared to \$36.27 per barrel (\$36.04 per barrel including hedging) in the three months ended September 30, 2003. Advantage had no crude oil hedges in place in the third quarter of 2004. Third quarter 2004 prices for WTI crude oil averaged US\$43.88 per barrel, 45% higher than the US\$30.20 per barrel realized during the third quarter of 2003. Partially offsetting the increase in WTI prices was a stronger Canadian dollar which averaged \$US/\$Cdn \$0.77 in the third quarter of 2004 compared to \$0.73 in the third quarter of 2003.

Crude oil prices continued to be strong during the third quarter of 2004. Factors that affect the continued strength of crude oil include (i) continued conflict in the middle east, (ii) low global inventory levels and (iii) increasing world oil demand. All of these factors are expected to keep crude oil prices high for the remainder of the year and into 2005.

HEDGING

The Fund currently has the following hedge contracts in place:

Volume	Effective Period	Average Price
Natural gas - AECO		
50,350 mcf/d	April 1, 2004 - December 31, 2004	\$ 6.12/mcf
10,450 mcf/d	January 1, 2005 - March 31, 2005	\$ 6.30/mcf

During the third quarter of 2004 the Fund realized \$2.4 million (\$0.35/mcf) in hedging losses on natural gas. These realized losses are included within petroleum and natural gas sales on the statement of income. Advantage's current and future crude oil production is currently unhedged. At September 30, 2004, the mark-to-market valuation of Advantage's outstanding hedges was a loss of \$7.6 million. This amount has been included in the income statement as an unrealized hedging loss with a corresponding hedging liability recorded on the balance sheet. Advantage has not entered into any additional hedges for 2005 at this time. However, the Fund will continue to monitor commodity markets.

ROYALTIES

During the third quarter of 2004 Advantage's royalties amounted to \$11.1 million (18.8% of pre-hedged revenue) compared to \$6.4 million (15.8% of pre-hedged revenue) in the third quarter of 2003. For the nine months ended September 30, 2004, royalties have amounted to \$32.2 million (18.9% of pre-hedged revenue) compared to \$21.1 million (16.3% of pre-hedged revenue) for the nine months ended September 30, 2003. Total royalties in 2004 are higher as a result of higher revenues. The increase in the royalty rate in 2004 is the result of the acquisition of MarkWest Resources properties in December 2003 which attract higher royalty rates than other Advantage properties. In addition, the acquisition of the Anadarko properties is expected to increase the Fund's royalty rate to approximately 21% in the fourth quarter and into 2005.

OPERATING COSTS

Operating costs for the three months ended September 30, 2004 amounted to \$9.2 million or \$6.19 per boe compared to \$7.2 million or \$6.27 per boe in the third quarter of 2003. Operating costs for the nine months ended September 30, 2004 amounted to \$25.7 million or \$6.01 per boe compared to \$18.3 million or \$5.61 per boe for the nine months ended September 30, 2003. Operating costs have steadily increased over the past two years due to higher power costs and higher field costs associated with the shortage of supplies, services and materials that have occurred as a result of very high levels of industry activity. Advantage's increased operating costs over 2003 are in line with overall industry trends.

GENERAL AND ADMINISTRATIVE AND MANAGEMENT FEES

Year to date cash and general administrative (G&A) expenses have amounted to \$2.5 million or \$0.59 per boe compared to \$2.4 million or \$0.73 per boe for the nine months ended September 30, 2003. G&A expense in the third quarter of 2004 amounted to \$0.9 million or \$0.61 per boe compared to \$0.6 million or \$0.55 per boe in the third quarter of 2003. G&A expense in the third quarter of 2004 was slightly higher than the prior year due to increased staff levels that have resulted from the growth of the Fund.

A stock-based compensation expense of \$1.0 million was recorded in the second quarter of 2004 related to the issuance of Trust Unit rights to the independent directors of Advantage. This non-cash amount represents the fair value attributed to trust unit rights granted during the second quarter under the Trust Units Rights Incentive Plan. During the third quarter there were no further issuances of such unit rights.

Management fees for the three months ended September 30, 2004 amounted to \$0.5 million or \$0.37 per boe compared to \$0.4 million or \$0.36 per boe in the third quarter of 2003. Year to date, management fees have amounted to \$1.6 million or \$0.37 per boe compared to \$1.2 million or \$0.38 per boe for the nine months ended September 30, 2003. Management fees are calculated based on 1.5% of operating cash flow which is defined as revenue less royalties and operating costs.

The Manager of the Fund is entitled to earn a performance incentive fee which is calculated at the end of each year based on the total return of the Fund. At September 30, 2004 no amount was paid to the Manager, nor is the Manager entitled to receive any payment related to the Fund's performance for the first nine months of 2004 as the actual amount is calculated and paid on an annual basis only. If the performance fee was paid at September 30, 2004, based on the performance of the Trust in the first nine months of the year, the total fee payable would be \$19.0 million. The Trust has accrued three quarters of this amount or \$14.2 million for the first nine months of 2004. There is no certainty that the fee accrued in the financial statements will be paid at year end. Any performance incentive fee paid to the Manager at year end is expected to be settled in Advantage Trust Units.

INTEREST

Year to date, interest expense has amounted to \$4.3 million (\$1.01 per boe) compared to \$4.9 million (\$1.51 per boe) for the nine months ended September 30, 2003. Interest expense for the three months ended September 30, 2004 amounted to \$1.6 million (\$1.11 per boe) compared to \$1.5 million (\$1.34 per boe) for the third quarter of 2003. Higher interest expense in the third quarter of 2004 is primarily the result of higher debt balances partially offset by lower interest rates.

TAXES

Current taxes are comprised primarily of capital tax, which amounted to \$0.5 million for the three months ended September 30, 2004 compared to \$0.2 million for the same period of 2003. Capital taxes are determined based on debt and equity levels at the end of the year and primarily increased due to property acquisitions during the third quarter. As a result of new legislation in 2003, capital taxes are to be gradually eliminated over the next five years.

For the three months ended September 30, 2004 a future income tax recovery of \$7.1 million was included in income compared to a \$3.5 million recovery for the comparable period in 2003. The Alberta government enacted a tax rate reduction of 1% in the first quarter of 2004, reducing the tax rate from 12.5% to 11.5% effective April 1, 2004. This resulted in an additional tax recovery during the first quarter of approximately \$2.2 million.

During the second quarter of 2003 the Fund recorded a non-recurring benefit of \$11.7 million resulting from changes to the Income Tax Act related to the resource sector. The changes included a change in the federal tax rate, deductibility of crown royalties and the elimination of resource allowance, to be phased in over the next five years.

CASH FLOW NETBACK

Breakdown of cash flow per boe	Three months ended		Nine months ended	
	Sept. 30		Sept. 30	
	2004	2003	2004	2003
Crude oil and natural gas sales	\$ 39.87	\$ 35.36	\$ 39.73	\$ 39.76
Hedging gains (losses)	(1.63)	0.45	(1.26)	(2.17)
Government and other royalties	(7.49)	(5.59)	(7.53)	(6.47)
Operating costs	(6.19)	(6.27)	(6.01)	(5.61)
Operating netback	24.56	23.95	24.93	25.51
General and administrative	(0.61)	(0.55)	(0.59)	(0.73)
Management fees	(0.37)	(0.36)	(0.37)	(0.38)
Interest and taxes	(1.42)	(1.51)	(1.27)	(1.74)
Cash flow from operations	\$ 22.16	\$ 21.53	\$ 22.70	\$ 22.66
Interest on convertible debentures	(1.21)	(0.86)	(1.30)	(1.01)
Cash available for distribution	\$ 20.95	\$ 20.67	\$ 21.40	\$ 21.65

DEPLETION, DEPRECIATION AND ACCRETION OF ASSET RETIREMENT OBLIGATION

The depletion, depreciation and accretion (“D,D&A”) rate for the third quarter of 2004 was \$16.27 per boe compared to \$11.56 per boe for the third quarter of 2003. The D,D&A rate per boe increased in 2004 compared to 2003 due the acquisition of MarkWest Resources and the Anadarko assets and revisions to the Fund’s total proven reserves pursuant to National Instrument 51-101. Included in third quarter D,D&A is \$0.7 million of accretion expense related to the asset retirement obligations. The retroactive application of the new accounting policy for asset retirement obligations requires restatement of prior periods, which resulted in the third quarter 2003 D,D&A rate to increase to \$11.56 per boe compared to the previously reported rate of \$11.50 per boe and D,D&A expense to increase by \$0.1 million.

FINANCIAL REPORTING UPDATE

Hedging Relationships

Effective in the Fund’s first quarter of 2004, the new CICA Accounting Guideline 13 “Hedging Relationships” requires that hedging relationships be identified, designated, documented and measured in order for the Fund to apply hedge accounting. Although the Fund believes that all of the hedges Advantage enters into are effective economic hedges, Advantage has elected to not use hedge accounting. The Fund will be using the fair value method to account for all of its hedge transactions. This method requires Advantage to mark-to-market at the balance sheet date the fair value of all outstanding hedges. At September 30, 2004 the mark-to-market valuation of Advantage’s outstanding hedges was a loss of \$7.6 million. This amount has been included in the income statement as an unrealized hedging loss with a corresponding hedging liability recorded on the balance sheet.

Asset Retirement Obligations

In March 2003 the CICA issued handbook section 3110 “Asset Retirement Obligations” which requires liability recognition for retirement obligations associated with the Fund’s property and equipment. The obligations are initially measured at fair value, which is the discounted future value of the liability. The fair value is capitalized as part of the cost of the related assets and depleted to earnings over the assets useful life. The liability accretes until the retirement obligations are settled. Advantage adopted the new standard in the first quarter of 2004. The impact to the Trust of the implementation of this policy is disclosed in note 1 (b) of the September 30, 2004 financial statements.

Full Cost Accounting

Effective January 1, 2004 the Trust adopted CICA accounting guideline 16 “Oil and Gas Accounting – Full Cost”. This accounting guideline replaced CICA accounting guideline 5, “Full cost accounting in the oil and gas industry”. Accounting guideline 16 modifies how the ceiling test calculation is performed. The recoverability of a cost centre is tested by comparing the carrying value of the cost centre to the sum of the undiscounted cash flows expected from the cost centre. If the carrying value is not recoverable the cost centre is written down to its fair value. Adopting accounting guideline 16 had no effect on the Trust’s financial results.

CONTRACTUAL OBLIGATIONS AND COMMITMENTS

The Trust has contractual obligations in the normal course of operations including purchase of assets and services, operating agreements, transportation commitments and sales contracts. These obligations are of a recurring and consistent nature and impact cash flow in an ongoing manner. The following is a summary of the Fund's contractual obligations and commitments:

(\$millions)	Total	Payments due by period			
		2004	2005-2006	2007-2008	2009 & thereafter
Building lease	\$ 4.9	\$ 0.2	\$ 2.8	\$ 1.9	-
Capital lease	\$ 2.4	\$ 0.1	\$ 0.9	\$ 1.4	-
Pipeline/transportation	\$ 2.8	\$ 0.4	\$ 2.1	\$ 0.2	\$ 0.1
Total contractual obligations	\$ 10.1	\$ 0.7	\$ 5.8	\$ 3.5	\$ 0.1

QUARTERLY PERFORMANCE

(\$thousands, except per Unit amounts)	2004				2003			2002
	Q3	Q2	Q1	Q4	Q3	Q2	Q1	Q4
Net revenues	\$ 48,255	\$ 44,436	\$ 32,227	\$ 36,074	\$ 34,483	\$ 33,144	\$ 33,883	\$ 29,641
Net income (loss)	\$ 7,102	\$ 11,762	\$ 6,972	\$ (1,866)	\$ 9,559	\$ 20,752	\$ 15,578	\$ 2,892
Net income (loss) per Unit, basic	\$ 0.13	\$ 0.26	\$ 0.13	\$ (0.18)	\$ 0.28	\$ 0.67	\$ 0.50	\$ 0.07
Net income (loss) per Unit, diluted	\$ 0.13	\$ 0.26	\$ 0.13	\$ (0.18)	\$ 0.28	\$ 0.64	\$ 0.48	\$ 0.07

The table above highlights the Trust's performance for the third quarter of 2004 and also for the preceding seven quarters through 2003 and 2002. Net revenues are primarily impacted by commodity prices, production volumes and royalties.

LIQUIDITY AND CAPITAL RESOURCES

Advantage's capital expenditures on development activities for the quarter ending September 30, 2004 were \$25.5 million. Expenditures were focused on drilling, completions, pipelines and compression at Medicine Hat, Bantry, Nevis and Shouldice. The Fund's Board of Directors approved an increase in the capital expenditures budget to \$100 million during the second quarter. The additional funds will be primarily expended developing the Nevis oil discovery and at Medicine Hat where an additional 32 natural gas well program commenced late in the third quarter.

Sources and Uses of Funds (\$ thousands)

	Nine months ended Sept. 30, 2004
Sources of funds	
Cash flow from operations	\$ 97,213
Units issued, net of costs	62,617
Convertible debentures issued, net of costs	119,567
Increase in bank debt	81,469
Property dispositions	791
	<u>\$ 361,657</u>
Uses of funds	
Capital expenditures	\$ 78,710
Property acquisitions	176,300
Distributions paid to Unitholders	80,692
Interest paid to debenture holders	5,546
Increase in working capital	19,769
Other	640
	<u>\$ 361,657</u>

Currently, Advantage has 44,349,704 Trust Units outstanding and 9,261,303 Trust Units are issuable for the \$176,462,000 convertible debentures still outstanding.

On September 15, 2004 Advantage issued 3,500,000 Trust Units and \$75 million aggregate principal amount of 7.50% convertible unsecured subordinated debentures and \$50 million aggregate principal amount of 7.75% convertible unsecured subordinated debentures to partially finance the acquisition of certain petroleum and natural gas properties and related assets from Anadarko.

Total bank debt outstanding at September 30, 2004 was \$184.4 million. Advantage has an agreement with a syndicate of four Canadian chartered banks that provides for a \$270 million facility consisting of \$260 million extendible revolving loan facility and a \$10 million operating loan facility both of which mature on May 28, 2005. The credit facilities are secured by a \$500 million floating charge demand debenture, a general security agreement and a subordination agreement for the Trust covering all assets and cash flows. At September 30, 2004 Advantage also had a working capital deficit of \$9.5 million.

Forward Looking Information

The information in this report contains certain forward-looking statements that involve substantial known and unknown risks and uncertainties, certain of which are beyond Advantage's control, including: the impact of general economic conditions, industry conditions, changes in laws and regulations including the adoption of new environmental laws and regulations and changes in how they are interpreted and enforced, increased competition, fluctuations in commodity prices and foreign exchange and interest rates, stock market volatility and obtaining required approvals of regulatory authorities. Advantage's actual results, performance or achievement could differ materially from those expressed in, or implied by, such forward-looking statements and, accordingly, no assurances can be given that any of the events anticipated by the forward-looking statements will transpire or occur or, if any of them do, what benefits that Advantage will derive from them.

Non-GAAP Measures

Cash flow from operations and per Unit and cash available for distribution and per Unit are not recognized measures under the Canadian generally accepted accounting principles (GAAP). Management believes that cash flow and cash available for distribution are useful supplemental measures to analyse operating performance and provide an indication of the results generated by the Trust's principal business activities prior to the consideration of how those activities are financed or how the results are taxed. Investors should be cautioned, however, that these measures should not be construed as an alternative to net income determined in accordance with GAAP as an indication of Advantage's performance. Advantage's method of calculating these measures may differ from other companies, and accordingly, they may not be comparable to measures used by other companies.

November 10, 2004

CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED BALANCE SHEETS

(thousands of dollars)	September 30, 2004 (unaudited)	December 31, 2003 (restated - note 1)
Assets		
Current assets		
Accounts receivable	\$ 38,707	\$ 34,181
Fixed assets		
Property and equipment	936,676	675,090
Accumulated depletion and depreciation	(219,594)	(155,155)
	717,082	519,935
Goodwill	27,773	27,773
	\$ 783,562	\$ 581,889
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities	\$ 38,044	\$ 53,287
Cash distributions payable to Unitholders	10,200	8,445
Hedging liability (note 6)	7,580	-
Bank indebtedness (note 2)	184,437	102,968
	240,261	164,700
Capital lease obligation	1,804	2,043
Asset retirement obligations (note 3)	21,554	13,892
Future income taxes	61,404	77,999
	325,023	258,634
Unitholders' equity		
Unitholders' capital (note 4i)	427,856	302,496
Convertible debentures (note 4ii)	176,462	99,984
Contributed surplus (note 4i)	1,036	-
Accumulated income	87,994	73,137
Accumulated cash distributions	(234,809)	(152,362)
	458,539	323,255
	\$ 783,562	\$ 581,889

Subsequent event (note 8)

CONSOLIDATED STATEMENTS OF INCOME AND ACCUMULATED INCOME

(thousands of dollars except for per Unit amounts) (unaudited)	Three months ended Sept. 30, 2004	Three months ended Sept. 30, 2003 (restated - note 1)	Nine months ended Sept. 30, 2004	Nine months ended Sept. 30, 2003 (restated - note 1)
Revenue				
Petroleum and natural gas	\$ 56,722	\$ 40,863	\$164,739	\$122,596
Unrealized hedging gain (loss) (note 6)	2,644	-	(7,580)	-
Royalties, net of Alberta Royalty Credit	(11,111)	(6,380)	(32,241)	(21,086)
	48,255	34,483	124,918	101,510
Expenses				
Operating	9,185	7,153	25,723	18,291
General and administrative	908	633	2,542	2,373
Stock-based compensation	-	-	1,036	-
Management fee	547	410	1,602	1,248
Non-cash performance incentive (note 7)	11,321	5,291	14,221	10,131
Interest	1,645	1,531	4,322	4,918
Depletion, depreciation and accretion	24,134	13,190	65,135	36,427
	47,740	28,208	114,581	73,388
Income before taxes	515	6,275	10,337	28,122
Future income tax recovery	(7,053)	(3,474)	(16,595)	(18,530)
Income and capital taxes	466	189	1,096	762
	(6,587)	(3,285)	(15,499)	(17,768)
Net income	7,102	9,560	25,836	45,890
Accumulated income, beginning of period as previously reported	88,044	70,640	72,022	36,581
Effect of change in accounting for asset retirement obligations (note 1)	-	1,150	1,115	1,255
Accumulated income, beginning of period as restated	88,044	71,790	73,137	37,836
Interest on convertible debentures	(1,786)	(986)	(5,546)	(3,309)
Costs on issuance of convertible debentures	(5,366)	(1,437)	(5,433)	(1,490)
Accumulated income, end of period	\$ 87,994	\$ 78,927	\$ 87,994	\$ 78,927
Net income per Trust Unit				
Basic	\$ 0.13	\$ 0.28	\$ 0.51	\$ 1.44
Diluted	\$ 0.13	\$ 0.28	\$ 0.51	\$ 1.40

CONSOLIDATED STATEMENTS OF CASH FLOWS

(thousands of dollars) (unaudited)	Three months ended Sept. 30, 2004	Three months ended Sept. 30, 2003 (restated - note 1)	Nine months ended Sept. 30, 2004	Nine months ended Sept. 30, 2003 (restated - note 1)
Operating Activities				
Net income	\$ 7,102	\$ 9,560	\$ 25,836	\$ 45,890
Add (deduct) items not requiring cash:				
Stock-based compensation	-	-	1,036	-
Non-cash performance incentive (note 7)	11,321	5,291	14,221	10,131
Future income taxes	(7,053)	(3,474)	(16,595)	(18,530)
Unrealized hedging loss (gain) (note 6)	(2,644)	-	7,580	-
Depletion, depreciation and accretion	24,134	13,190	65,135	36,427
Funds from operations	32,860	24,567	97,213	73,918
Expenditures on asset retirement (note 3)	(253)	(53)	(401)	(134)
Changes in non-cash working capital	(61)	397	(13,352)	742
Cash provided by operating activities	32,546	24,911	83,460	74,526
Financing Activities				
Units issued, net of costs (note 4)	62,389	52	62,617	(79)
Convertible debentures issued, net of costs (note 4)	119,567	28,510	119,567	28,510
Increase (decrease) in bank debt	22,730	(12,993)	81,469	12,144
Interest on convertible debentures	(1,786)	(167)	(5,546)	(3,228)
Reduction of capital lease obligation	(81)	-	(239)	-
Cash distributions to Unitholders	(27,718)	(21,420)	(80,692)	(58,152)
Cash provided by (used in) financing activities	175,101	(6,018)	177,176	(20,805)
Investing Activities				
Expenditures on property and equipment	(25,485)	(16,976)	(78,710)	(54,700)
Property dispositions	-	-	791	-
Property acquisitions	(176,300)	-	(176,300)	(894)
Changes in non-cash working capital	(5,862)	(1,917)	(6,417)	1,873
Cash used in investing activities	(207,647)	(18,893)	(260,636)	(53,721)
Net increase in cash	0	0	0	0
Cash, beginning of period	0	0	0	0
Cash, end of period	\$ 0	\$ 0	\$ 0	\$ 0
Taxes paid	\$ 368	\$ 468	\$ 999	\$ 858
Interest paid	\$ 954	\$ 880	\$ 4,275	\$ 5,201

NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

All tabular amounts in thousands, except for per Unit amounts (unaudited)

The interim consolidated financial statements of Advantage Energy Income Fund ("Advantage") have been prepared by management in accordance with Canadian generally accepted accounting principles using the same accounting policies as those set out in note 2 to the consolidated financial statements for the period ended December 31, 2003 except as described below. The interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements of Advantage for the year ended December 31, 2003 as set out in Advantage's Annual Report.

I. CHANGE IN ACCOUNTING POLICIES

(a) Petroleum and Natural Gas Properties and Related Equipment

Petroleum and natural gas assets are evaluated in each reporting period to determine that the carrying amount in a cost centre is recoverable and does not exceed the fair value of the properties in the cost centre.

The carrying amounts are assessed to be recoverable when the sum of the undiscounted cash flows expected from the production of proved reserves, the lower of cost and market of unproved properties and the cost of major development projects exceeds the carrying amount of the cost centre. When the carrying amount is not assessed to be recoverable, an impairment loss is recognized to the extent that the carrying amount of the cost centre exceeds the sum of the discounted cash flows expected from the production of proved and probable reserves, the lower of cost and market of unproved properties and the cost of major development projects of the cost centre. The cash flows are estimated using expected future product prices and costs and are discounted using a risk-free interest rate.

The Trust adopted the new accounting standard relating to full cost accounting effective January 1, 2004 and as at January 1, 2004 and September 30, 2004 no write-down to the carrying value of petroleum and natural gas assets was required. Prior to January 1, 2004 the ceiling test amount was the sum of the undiscounted cash flows expected from the production of proved reserves, the lower of cost or market of unproved properties and the cost of major development projects less estimated future costs for administration, financing, site restoration and income taxes. The cash flows were estimated using period end prices and costs.

(b) Asset Retirement Obligations

The Trust has adopted the asset retirement obligation method of recording the future cost associated with removal, site restoration and asset retirement costs. The fair value of the liability for the Trust's asset retirement obligation is recorded in the period in which it is incurred, discounted to its present value using the Trust's credit adjusted risk-free interest rate and the corresponding amount recognized by increasing the carrying amount of property, plant and equipment. The asset recorded is depleted on a unit of production basis over the life of the reserves. The liability amount is increased each reporting period due to the passage of time and the amount of accretion is charged to earnings in the period. Revisions to the estimated timing of cash flows or to the original estimated undiscounted cost could also result in an increase or decrease to the obligation. Actual costs incurred upon settlement of the retirement obligation are charged against the obligation to the extent of the liability recorded.

Previously, the Trust recognized a provision for estimated future removal and site restoration costs calculated on the unit-of-production method over the remaining proved reserves.

The effect of this change in accounting policy has been recorded retroactively with restatement of prior periods. The effect of the adoption is presented below as increases (decreases):

Balance Sheets	December 31, 2003	December 31, 2002
Asset retirement costs, included in property and equipment	\$ 7,137	\$ 3,856
Asset retirement obligations	\$ 13,892	\$ 7,351
Provision for future site restoration	\$ (8,451)	\$ (5,396)
Future income taxes	\$ 581	\$ 646
Accumulated income	\$ 1,115	\$ 1,255

Statements of Income	Three months ended Sept. 30, 2003	Nine months ended Sept. 30, 2003	Year ended December 31, 2003
Accretion expense	\$ 129	\$ 386	\$ 515
Depletion and depreciation on asset retirement costs	\$ 252	\$ 721	\$ 997
Amortization of estimated future removal and site restoration liability	\$ (309)	\$ (881)	\$ (1,307)
Future taxes	\$ (23)	\$ (72)	\$ (65)
Net income (loss) impact	\$ (49)	\$ (154)	\$ (140)
Basic net income (loss) per Unit	\$ (0.00)	\$ (0.00)	\$ (0.00)
Diluted net income (loss) per Unit	\$ (0.00)	\$ (0.00)	\$ (0.00)

(c) Hedging Relationships

Effective January 1, 2004, CICA Accounting Guideline 13 "Hedging Relationships" requires that hedging relationships be identified, designated, documented and measured in order for the Fund to apply hedge accounting. Advantage has chosen not to apply hedge accounting and will instead use the fair value method. This method requires the fair value of the derivative financial instruments be recorded at each balance sheet date. In accordance with this method, the Fund has recorded an unrealized hedging loss of \$7.6 million at September 30, 2004. Realized gains and losses on settlement of hedges has been included within petroleum and natural gas revenue.

2. BANK DEBT

Advantage has an agreement with a syndicate of four Canadian chartered banks to increase its extendible revolving loan facility from \$210 million to \$260 million and the renewal of a \$10 million operating loan facility with a maturity date of May 28, 2005. The loan's interest rate is based on either prime or bankers acceptances' rates at the Fund's option subject to certain basis point or stamping fee adjustments ranging from 0% to 2% depending on the Fund's debt to cash flow ratio. The credit facilities are secured by a \$500 million floating charge demand debenture, a general security agreement and a subordination agreement from the Trust covering all assets and cash flows. For the purpose of the cash flow statement the bank overdraft amount is considered cash equivalent.

3. ASSET RETIREMENT OBLIGATIONS

The Trust's asset retirement obligations result from net ownership interests in petroleum and natural gas assets including well sites, gathering systems and processing facilities. The Trust estimates the total undiscounted and inflated amount of cash flows required to settle its asset retirement obligations is approximately \$55.6 million which will be incurred between 2004 to 2054. A credit-adjusted risk-free rate of 7.0 percent was used to calculate the fair value of the asset retirement obligations.

A reconciliation of the asset retirement obligations is provided below:

	Nine month period ended Sept. 30, 2004	Year ended December 31, 2003
Balance, beginning of period	\$ 13,892	\$ 7,351
Accretion expense	695	515
Liabilities incurred	7,368	6,362
Liabilities settled	(401)	(336)
Balance, end of period	\$ 21,554	\$ 13,892

4. UNITHOLDERS' EQUITY

(i) Unitholders' Capital

(a) Authorized

(i) Unlimited number of voting Trust Units

(b) Issued

	Number of Units	Amount
Balance at December 31, 2003	36,717,206	\$ 282,904
2003 non-cash performance incentive	1,099,104	19,592
Issued for cash, net of costs	3,500,000	62,322
Issued on conversion of debentures	2,978,394	48,522
Issued on exercise of options, net of costs	55,000	295
Non-cash performance incentive estimated (see note 7)	-	14,221
Balance at Sept. 30, 2004	44,349,704	\$ 427,856

On January 27, 2004 Advantage issued 1,099,104 Trust Units to satisfy the obligation related to the 2003 year end performance incentive fee.

On September 15, 2004 Advantage issued 3,500,000 Trust Units to partially finance the acquisition of certain petroleum and natural gas properties and related assets.

(c) Trust Units Rights Incentive Plan

	Series A		Series B	
	Number	Price	Number	Price
Balance at December 31, 2003	140,000	\$ 7.87	-	-
Exercised	(55,000)	-	-	-
Issued	-	-	225,000	\$ 18.42
Reduction of exercise price	-	(2.07)	-	(0.92)
Balance at Sept. 30, 2004	85,000	\$ 5.80	225,000	\$ 17.50

On June 17, 2004 the Fund issued 225,000 Series B Trust Unit Rights to the independent directors of Advantage at a price of \$18.42 per Right. At the option of the Rights holder the exercise price can be adjusted downwards over time based on distributions made by the Trust to Unitholders. During the second quarter the Fund recorded a non-cash stock-based compensation expense of \$1.0 million to recognize the fair value of the Rights granted. As the Rights vested immediately no further expense will be recognized related to the Rights issuance. Based on a September 30, 2004 unit price of \$21.50, the increase in the intrinsic value of the Trust Unit Rights during third quarter of 2004 is approximately \$1.1 million.

(ii) Convertible Debentures

Interest Rate	Conversion Price per Unit	Balance at Dec. 31, 2003	Issued	Converted to Trust Units	Balance at Sept. 30, 2004
10.00%	\$ 13.30	\$ 10,214	\$ -	\$ (4,619)	\$ 5,595
9.00%	\$ 17.00	30,000	-	(7,334)	22,666
8.25%	\$ 16.50	59,770	-	(35,094)	24,676
7.75%	\$ 21.00	-	50,000	-	50,000
7.50%	\$ 20.25	-	75,000	(1,475)	73,525
		\$ 99,984	\$ 125,000	\$ (48,522)	\$ 176,462

On September 15, 2004 Advantage issued \$75 million aggregate principal amount of 7.50% convertible unsecured subordinated debentures and \$50 million aggregate principal amount of 7.75% convertible unsecured subordinated debentures to partially finance the acquisition of certain petroleum and natural gas properties and related assets.

The convertible debentures and the related interest obligations are classified as equity on the consolidated balance sheet as the Trust may elect to satisfy the debenture interest and principle obligations by the issuance of Trust Units. During the nine months ended September 30, 2004, \$48.5 million debentures were converted resulting in the issuance of 2,978,394 Advantage Units.

5. ASSET ACQUISITION

On September 15, 2004 Advantage closed the acquisition of certain petroleum and natural gas properties and related assets for net consideration of \$175.4 million. The asset retirement obligation assumed and recorded on this acquisition was \$6.6 million.

6. FINANCIAL INSTRUMENTS

As at September 30, 2004 the Fund has the following hedges in place:

Volume	Effective Period	Price
Natural gas - AECO		
50,350 mcf/d	April 1, 2004 - December 31, 2004	\$ 6.12/mcf
10,450 mcf/d	January 1, 2005 - March 31, 2005	\$ 6.30/mcf

As at September 30, 2004 the settlement value of the hedges outstanding was approximately \$7.6 million and has been charged to income as an unrealized hedging loss.

7. NON-CASH PERFORMANCE INCENTIVE

The Manager of the Fund is entitled to earn an annual performance incentive fee which is calculated based on the total return of the Fund. At September 30, 2004 no amount was paid to the Manager, nor is the Manager entitled to receive any payment related to the Fund's first nine months performance as the actual amount is only calculated and paid on an annual basis.

The Manager earns the performance incentive fee when the Fund's total annual return exceeds 8%. The total annual return is calculated at the end of each year by dividing the year over year change in Unit price plus cash distributions by the opening Unit price. The 2004 opening Unit price was \$17.83 per Unit. Ten percent of the amount of the total annual return in excess of 8% is multiplied by the market capitalization (defined as the opening Unit price multiplied by the average number of Units outstanding during the year) to determine the performance incentive. If the performance fee was paid at September 30, 2004 based on the performance of the Trust in the first nine months of the year the total fee payable would be \$19.0 million. The Trust has accrued three quarters of this amount or \$14.2 million for the first nine months of 2004. It is expected that any fee earned be paid to the Manager in Advantage Trust Units and therefore the accrued fee to September 30, 2004 has been classified as Unitholders' Capital. The Manager does not receive any form of compensation in respect of acquisition or divestiture activities.

8. SUBSEQUENT EVENT

On November 3, 2004 Advantage announced that it had entered into an Arrangement Agreement (the "Arrangement") to acquire all of the issued and outstanding shares of Defiant Energy Corporation ("Defiant"). Advantage will acquire all of the approximately 34.0 million fully diluted common shares of Defiant in exchange for 0.201373 of an Advantage Trust Unit or \$4.40 per share in cash, subject to a maximum cash consideration of \$34 million. In lieu of Advantage Trust Units, shareholders of Defiant may elect to receive exchangeable shares issued by Advantage Oil & Gas Ltd. subject to an aggregate limit of 1.5 million exchangeable shares. Advantage will assume Defiant's debt which was approximately \$41.3 million at October 31, 2004.

DIRECTORS

Gary F. Bourgeois
Kelly I. Drader
Ronald A. McIntosh
Roderick M. Myers
Carol D. Pennycook
Steven Sharpe
Lamont C. Tolley
Rodger A. Tourigny

OFFICERS

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President & CEO
Patrick J. Cairns
Senior Vice President
Gary F. Bourgeois
Vice President, Corporate Development
Peter A. Hanrahan
Vice President, Finance & CFO
Rick P. Mazurkewich
Vice President, Operations
Weldon M. Kary
Vice President, Exploitation

CORPORATE SECRETARY

Jay P. Reid
Partner, Burnet, Duckworth and Palmer LLP

OPERATING COMPANY

Advantage Oil & Gas Ltd.

AUDITORS

KPMG LLP

BANKERS

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National Bank of Canada
Bank of Montreal
Royal Bank of Canada

INDEPENDENT RESERVE EVALUATORS

Sproule Associates Limited

LEGAL COUNSEL

Burnet, Duckworth and Palmer LLP

ABBREVIATIONS

bbls - barrels
mbbls - thousand barrels
mmbbls - million barrels
bbls/d - barrels per day
boe - barrels of oil equivalent (6 mcf = 1 bbl)
mmboe - million barrels of oil equivalent
boe/d - barrels of oil equivalent per day
bcf - billion cubic feet
mcf - thousand cubic feet
mmcf - million cubic feet
mmcf/d - million cubic feet per day
gj - gigajoules
NGLs - natural gas liquids
WTI - West Texas Intermediate

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TORONTO STOCK EXCHANGE TRADING SYMBOLS

Trust Units: AVN.UN
10% Convertible Debentures: AVN.DB
9% Convertible Debentures: AVN.DBA
8.25% Convertible Debentures: AVN.DBB
7.75% Convertible Debentures: AVN.DBC
7.5% Convertible Debentures: AVN.DBD