

Leon's Furniture Limited



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A N N U A L R E P O R T

Corporate Directory

Board of Directors

LEWIE LEON,
Port Colborne

ANTHONY T. LEON,
Toronto

EDWARD M. LEON,
Thornhill

JOSEPH M. LEON,
Doctor of Medicine, Welland

PETER B. EBY,
Vice-Chairman and Director,
Burns Fry Limited, Toronto

RICHARD E. SHIBLEY,
Barrister,
Partner in Shibley, Righton
& McCutcheon, Toronto

Officers

LEWIE LEON,
Chairman of the Board

ANTHONY T. LEON,
President

EDWARD M. LEON,
Vice-President

MARJORIE LEON,
Secretary-Treasurer

ALAN F. MATHESON,
Controller

Corporate Offices

88 Gordon Mackay Road,
P.O. Box 460
Weston, Ontario M9N 3N2

Auditors

CLARKSON GORDON
Chartered Accountants, Toronto

Registrar & Transfer Agent

NATIONAL TRUST COMPANY,
Toronto

Listing

Leon's shares are listed on
The Toronto Stock Exchange
Ticker Symbol is LNF

Annual Meeting of Shareholders

April 22nd, 1987
10:00 a.m.
Royal York Hotel
British Columbia Room
100 Front Street West,
Toronto, Ontario

Financial Highlights

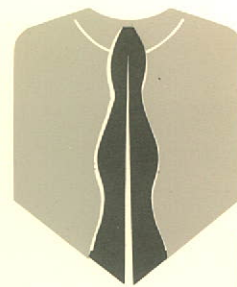
	1986	1985	% increase from 1985
Sales	\$193,942,000	\$158,960,000	22.0%
Income before income taxes and extraordinary item	23,201,000	13,739,000	68.9%
Income taxes	11,732,000	7,049,000	66.4%
Income before extraordinary item	11,469,000	6,690,000	71.4%
Extraordinary item		1,270,000	
Net income	11,469,000	7,960,000	44.1%
Number of shares outstanding (weighted average)	4,939,600	4,938,400	
Earnings per share:			
Income before extraordinary item	\$ 2.32	\$ 1.35	71.9%
Extraordinary item		.26	
Net income	2.32	1.61	44.1%
Dividends per share	.53	.225	135.6%
Shareholders' equity per share	9.70	7.93	22.3%
Share Price on The Toronto Stock Exchange			
High	25.00	11.50	
Low	11.50	6.00	
Close	21.50	11.50	
Total assets	\$ 91,930,000	\$ 77,637,000	18.4%
Number of employees	1,185	1,035	

The dividend record is as follows:

1978, 1979, 1980	18.75¢ per share
1981	22.50¢ per share
1982	8.75¢ per share
1983	18.75¢ per share
1984	22.50¢ per share
1985	22.50¢ per share
1986	53.00¢ per share

EARNINGS PER SHARE FOR EACH QUARTER

	MAR 31	JUNE 30	SEPT 30	DEC 31	TOTAL
From operations:					
1986	24¢	42¢	74¢	92¢	\$2.32
1985	3¢	22¢	51¢	59¢	\$1.35
1984	16¢	20¢	10¢	14¢	\$.60
From extraordinary item:					
1985			25¢		\$.25
1984			35¢		\$.35



*As your company grows,
the administrative process
becomes even more impor-
tant. New systems and proce-
dures are being developed
constantly to keep pace
with our anticipated growth.*

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Chairman's and President's Report

We are pleased to report the best year of sales and profits in our company's history.

Sales in 1986 were \$193,942,000, exceeding our 1985 record by 22%. Income before extraordinary item of \$11,469,000 represented a 71% increase over 1985.

Our outstanding success is attributed to the hard work of our dedicated and loyal staff as we did not open any new stores in 1986. To all employees, we say thank you.

The company once again carried out an aggressive marketing and merchandising campaign. We continued to place strong emphasis on building our image as Canada's leading furniture and appliance chain that gives outstanding value with first rate service. Advertising expenses as a percentage of sales, decreased to 6.7% from 7.9% in 1985.

Income before extraordinary item rose to 5.9% of sales, also surpassing our previous 1985 record of 4.2%. Our gross margin rose to 37.06% of sales from 36.04% in 1985. For the first time our U.S. division in Tempe, Arizona achieved an operating profit. This along with a relatively stable fixed cost base were strong factors in obtaining the 1.7% increase.

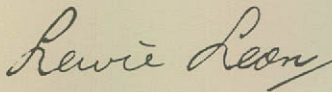
Our franchise division continued to grow in 1986. Franchises were opened in North Bay and Chatham, Ontario. We have grown to eight franchisees since this division's inception in 1983. In every case, our franchisees' sales and profits have increased dramatically since joining the Leon Family of Stores. For 1987, we plan to open eight to twelve new franchises.

Extensive renovations were completed in our 48,000 square foot store in Welland, Ontario, the community where our company commenced operations in 1909. Construction began on new company-owned warehouse and showrooms in Winnipeg, Manitoba and Windsor, Ontario. These locations should be opened by the summer of 1987.

Our objective for 1987 will be to maintain our excellence

in sales and service to the public. Our healthy balance sheet enables us to plan for new locations in Regina, Saskatchewan, Halifax, Nova Scotia and two additional locations in Montréal, Québec. We have a formidable task in increasing our sales and profits from our 1986 levels.

We look forward to the continuation of employee dedication, commitment, and desire to meet the challenges before us in 1987.



LEWIE LEON,
Chairman of the Board



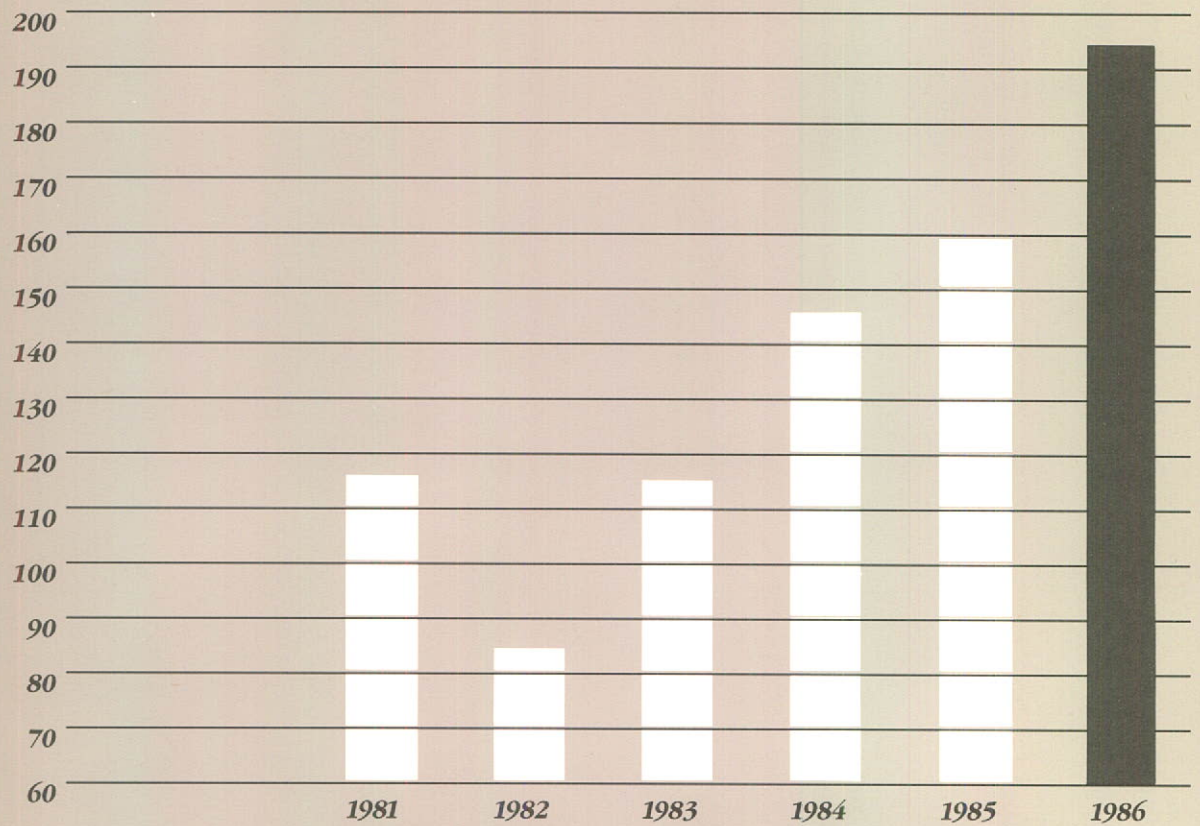
ANTHONY T. LEON,
President



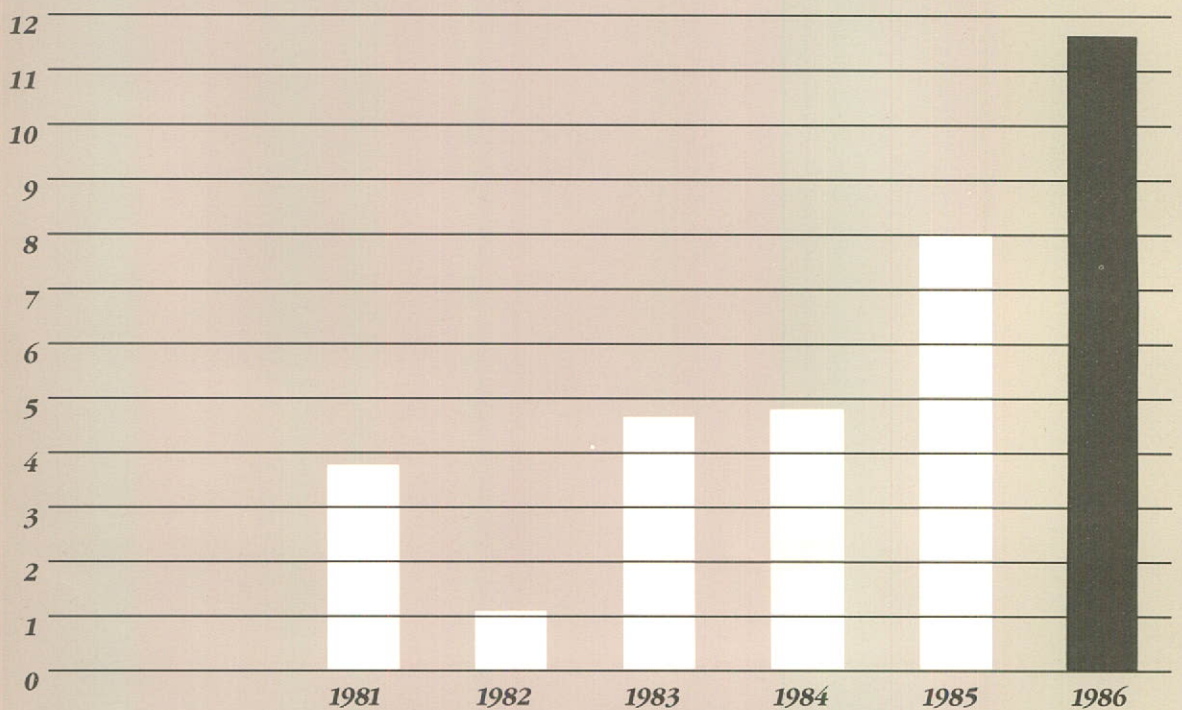
The leadership of the Board of Directors has resulted in your company following through with the strategic planning required for future growth and profitability.

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SALES IN MILLIONS



NET INCOME IN MILLIONS



Income Statistics (in thousands)

	1981	1982	1983	1984	1985	1986
Sales	\$116,188	\$ 83,908	\$115,212	\$146,099	\$158,960	\$193,942
Cost of sales	73,739	52,425	72,279	95,479	101,669	122,063
Gross profit	42,449	31,483	42,933	50,620	57,291	71,879
Operating expenses (net of interest and sundry income)	30,189	24,760	29,102	38,725	38,963	44,082
Rent and property taxes	1,395	1,621	1,681	1,869	1,897	1,883
Depreciation and amortization	1,823	1,715	1,758	1,787	1,804	1,898
Interest on long-term debt	1,290	1,052	949	941	888	815
	34,697	29,148	33,490	43,322	43,552	48,678
Income before items shown below	7,752	2,335	9,443	7,298	13,739	23,201
Income taxes	4,016	1,280	4,837	4,309	7,049	11,732
Income before extraordinary items	3,736	1,055	4,606	2,989	6,690	11,469
Extraordinary items: (net of tax)						
Gain on sale of Houston warehouse					1,270	
Sale of investment				1,720		
Net income	\$ 3,736	\$ 1,055	\$ 4,606	\$ 4,709	\$ 7,960	\$ 11,469
Shares outstanding (000's) (weighted average)	4,892	4,904	4,904	4,924	4,938	4,940
Earnings per share						
Income before extraordinary item	\$.77	\$.22	\$.94	.60	\$ 1.35	\$ 2.32
Net income	\$.77	\$.22	\$.94	.95	\$ 1.60	\$ 2.32
Percent annual increase (decrease) in sales	27.3%	(27.8%)	37.3%	26.8%	8.8%	22.0%
Income before extraordinary items as a percentage of sales	3.2%	1.3%	4.0%	2.0%	4.2%	5.9%
Dividends	\$ 1,103	\$ 429	\$ 919	\$ 1,110	\$ 1,111	\$ 2,618

Balance Sheet Statistics (in thousands)

Shareholders' equity	\$ 23,490	\$ 24,116	\$ 28,026	\$ 31,980	\$ 39,150	\$ 47,929
Total assets	50,371	49,367	61,680	59,479	77,637	91,930
Additions to fixed assets	872	438	1,055	2,203	1,249	5,412
Decrease in long-term debt-net	(368)	(241)	(350)	(220)	(761)	(964)
Working capital	8,058	9,685	13,684	17,038	25,340	29,531
Current ratio	1.5:1	1.6:1	1.6:1	1.9:1	1.8:1	1.8:1
Shareholders' equity per share	\$ 4.80	\$ 4.92	\$ 5.72	\$ 6.50	\$ 7.93	\$ 9.70
Share price range on the Toronto Stock Exchange						
High	\$ 5.00	\$ 4.38	\$ 5.69	\$ 7.00	\$ 11.50	\$ 25.00
Low	4.25	3.25	4.25	5.25	6.00	11.50



Never in your company's history has so much time and effort been devoted to the implementation of sales training. The professionalism and expertise of our sales staff has improved dramatically.

Leon's Furniture Limited – Meubles Leon Ltée*(Incorporated under the laws of Ontario)***Consolidated Balance Sheet****December 31, 1986***(with comparative figures at December 31, 1985)***ASSETS**

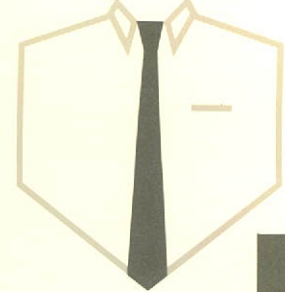
	<u>1986</u>	<u>1985</u>
Current assets:		
Deposit receipts	\$25,274,000	\$19,521,000
Accounts receivable	7,212,000	5,859,000
Inventory	33,606,000	30,043,000
Total current assets	66,092,000	55,423,000
Deferred income taxes	740,000	516,000
Fixed assets:		
Buildings and leasehold improvements	23,037,000	21,909,000
Vehicles	3,739,000	3,226,000
Equipment, signs and paving	4,976,000	4,900,000
	31,752,000	30,035,000
Less accumulated depreciation and amortization	18,085,000	16,430,000
Land	13,667,000	13,605,000
	11,431,000	8,093,000
Net fixed assets	25,098,000	21,698,000
	\$91,930,000	\$77,637,000

Auditors' Report

*To the Shareholders of Leon's Furniture Limited
– Meubles Leon Ltée:*

We have examined the consolidated balance sheet of Leon's Furniture Limited – Meubles Leon Ltée as at December 31, 1986 and the consolidated statements of income and retained earnings and cash flows for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

Toronto, Canada,
February 18, 1987.



LIABILITIES AND SHAREHOLDERS' EQUITY

	1986	1985
Current liabilities:		
Bank indebtedness	\$ 2,780,000	\$ 3,280,000
Accounts payable and accrued liabilities	26,033,000	21,628,000
Customers' deposits	1,392,000	1,372,000
Current portion of long-term debt (note 2)	925,000	397,000
Dividend payable	889,000	556,000
Income taxes payable	4,542,000	2,850,000
Total current liabilities	36,561,000	30,083,000
Long-term debt (note 2)	7,440,000	8,404,000
Shareholders' equity:		
Capital stock (note 3) –		
Authorized:		
10,000,000 shares		
Issued:		
4,939,600 (1985 – 4,939,600) shares	3,554,000	3,554,000
Retained earnings	43,660,000	34,809,000
Foreign currency translation equity adjustment (note 1)	715,000	787,000
Total shareholders' equity	47,929,000	39,150,000
	\$91,930,000	\$77,637,000

(See accompanying notes)

In our opinion, these consolidated financial statements present fairly the financial position of the company as at December 31, 1986 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Clarkson Gordon
Chartered Accountants

On behalf of the Board:

Richard Leon
Director

Edward Leon
Director

Your company has always
believed that the procure-
ment of saleable products
is vital to the organization.
The skills of our organiza-
tion, in regard to purchas-
ing, as well as supplier rela-
tions, play a dominant role
in our success.

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Leon's Furniture Limited – Meubles Leon Ltée
Consolidated Statement of Income and Retained Earnings
For the Year Ended December 31, 1986
(with comparative figures for the year ended December 31, 1985)

	1986	1985
Sales	\$193,942,000	\$158,960,000
Cost of sales	122,063,000	101,669,000
Gross profit	71,879,000	57,291,000
Operating expenses (income):		
Salaries and commissions	24,990,000	21,425,000
Employee deferred profit-sharing plan (note 6)	879,000	672,000
Advertising	12,950,000	12,573,000
Rent and property taxes	1,883,000	1,897,000
Depreciation and amortization	1,898,000	1,804,000
Interest on bank indebtedness		55,000
Interest on long-term debt	815,000	888,000
Interest income on deposit receipts	(1,723,000)	(823,000)
Other operating expenses and income (net)	6,986,000	5,061,000
	48,678,000	43,552,000
Income before items shown below	23,201,000	13,739,000
Income taxes (note 4)	11,732,000	7,049,000
Income before extraordinary item	11,469,000	6,690,000
Extraordinary item (note 7):		
Gain on sale of Houston warehouse		1,270,000
Net income	11,469,000	7,960,000
Retained earnings, beginning of year	34,809,000	27,960,000
Dividends	(2,618,000)	(1,111,000)
Retained earnings, end of year	\$ 43,660,000	\$ 34,809,000
Shares outstanding (weighted average)	4,939,600	4,938,400
Earnings per share (note 7):		
Income before extraordinary item		\$1.35
Net income	\$2.32	\$1.61

(See accompanying notes)

Leon's Furniture Limited – Meubles Leon Ltée

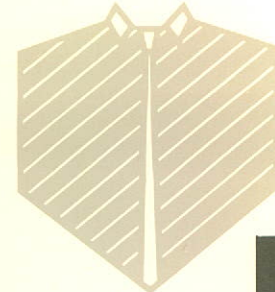
Consolidated Statement of Cash Flows

For the Year Ended December 31, 1986

(with comparative figures for the year ended December 31, 1985)

	1986	1985
Cash from (used in):		
Operations –		
Income before extraordinary item	\$11,469,000	\$ 6,690,000
Add (deduct) items not involving cash movements:		
Depreciation and amortization	1,898,000	1,804,000
Deferred income taxes	(224,000)	(186,000)
Gain on sale of fixed assets	(70,000)	(13,000)
Change in non-cash working capital relating to operations –		
Accounts receivable	(1,355,000)	(2,415,000)
Inventory	(3,592,000)	(5,911,000)
Income taxes	1,692,000	3,663,000
Accounts payable and accrued liabilities	3,452,000	6,889,000
Customers' deposits	20,000	316,000
Cash from operations	13,290,000	10,837,000
Investing activities –		
Proceeds on sale of fixed assets	146,000	83,000
Purchase of fixed assets	(4,450,000)	(1,062,000)
Proceeds on sale of Houston warehouse		2,700,000
Gain (loss) on translation of foreign investment	(52,000)	302,000
Cash from (used in) investing activities	(4,356,000)	2,023,000
Financing activities –		
Repayment of long-term debt	(396,000)	(1,015,000)
Share capital issued:		
Stock options exercised		20,000
Dividends paid	(2,285,000)	(1,110,000)
Cash used in financing activities	(2,681,000)	(2,105,000)
Net increase in cash during the year	6,253,000	10,755,000
Cash, beginning of year	16,241,000	5,486,000
Cash, end of year	\$22,494,000	\$16,241,000
Cash is composed of:		
Deposit receipts	\$25,274,000	\$19,521,000
Bank indebtedness	(2,780,000)	(3,280,000)
	\$22,494,000	\$16,241,000

(See accompanying notes)



The truly competitive nature of the home furnishing industry demands successful retailers to be both innovative and cost efficient in regard to advertising. We believe your company has fulfilled these requirements.

M A R K E T I N G

Leon's Furniture Limited – Meubles Leon Ltée
Notes to Consolidated Financial Statements
December 31, 1986

1. Summary of significant accounting policies

Principles of consolidation –

The consolidated financial statements include the accounts of the company and its subsidiaries, all of which are wholly-owned.

Foreign currency translation –

Merchandise imported from the United States is recorded at its equivalent Canadian dollar value upon receipt; United States dollar accounts payable are translated at the year-end exchange rate.

Assets and liabilities of United States operations, which are operationally self-sustaining, are translated into Canadian dollars at the year-end exchange rate. Revenues and expenses are translated at average quarterly rates. Gains or losses resulting from translation are deferred and included in shareholders' equity until realized.

Inventory –

Inventory is valued at the lower of cost on a first-in, first-out basis and net realizable value less normal profit margin.

Fixed assets –

Property and equipment are initially recorded at cost and normal maintenance and repair expenditures are charged to expense as incurred. Depreciation is provided over estimated service lives:

Buildings	– 5% per annum, straight line
Parking lots	– 4% per annum, straight line
Equipment and signs	– 20%-30% per annum, declining balance
Vehicles	– 30% per annum, declining balance
Leasehold improvements	– Over the terms of the leases to a maximum of 15 years

Store pre-opening costs –

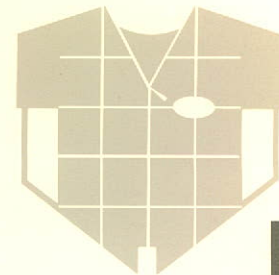
Store pre-opening costs are charged to expense as incurred.

Franchise revenue recognition –

Initial franchise fees are recorded as income when the store commences operations as a Leon's franchise. Expenses associated with the commencement of a specific franchise's operations are deferred and charged to expense when the related revenue is recognized. All other expenses associated with franchising are charged to expense when incurred. Continuing fees from franchised stores are recorded in income on an accrual basis. Franchise revenue has not been material to December 31, 1986 and is included in other operating expenses and income.

Income taxes –

The company follows the tax allocation method of providing for income taxes. Under this method, timing differences between reported and taxable income (which occur when revenues and expenses recognized in the accounts in one year are taxed or claimed for tax purposes in another year) result in deferred or prepaid taxes.



Our warehouse personnel expedited more merchandise than ever before. Through their efforts, our shipping and receiving productivity has been greatly increased.

2. Long-term debt

	1986	1985
Mortgages on land and buildings		
– payable in U.S. dollars		
(\$2,194,000 U.S. – 1986;		
\$2,238,000 U.S. – 1985)	\$3,029,000	\$3,129,000
– payable in Canadian dollars	4,736,000	4,972,000
8% Sinking Fund Debentures, due May 1, 1987		
– payable in Canadian dollars	600,000	700,000
	8,365,000	8,801,000
Less current portion of long-term debt	925,000	397,000
	\$7,440,000	\$8,404,000

The mortgage loans are secured by certain fixed assets, bear interest at rates varying from 9.25% to 10.75% per annum and mature at varying dates to 2009. The 8% Sinking Fund Debentures are secured by a specific charge on all the shares of Leon Holdings (1967) Limited, a subsidiary, and are held by shareholders.

The long-term debt matures as follows:

1988	–	\$ 357,000
1989	–	393,000
1990	–	432,000
1991	–	696,000
1992-1996	–	5,034,000
1997-2001	–	466,000
Subsequently	–	62,000
		\$7,440,000

3. Capital stock

During the year the company amended its Articles of Incorporation to:

- (a) increase the authorized share capital from 3,000,000 to 10,000,000 shares; and,
- (b) split the issued shares on a two for one basis.

4. Provision for income taxes

The company's income tax provision is made up as follows:

	1986		1985	
Provision for taxes based on combined basic Canadian federal and provincial income tax rate	\$12,041,000	51.9%	\$6,938,000	50.5%
Increase (decrease) in taxes resulting from –				
Inventory allowance	(67,000)	(0.3)	(328,000)	(2.4)
Tax benefit of U.S. losses not reflected in earnings			445,000	3.2
Utilization of prior years' U.S. tax losses	(230,000)	(1.0)		
Miscellaneous	(12,000)		(6,000)	
Actual provision for income taxes	\$11,732,000	50.6%	\$7,049,000	51.3%

The company's U.S. subsidiaries have incurred losses aggregating U.S. \$4,180,000 which may be carried forward and applied against such taxable income as may be earned by the companies in future years to 1999. The potential tax benefits of carrying forward these costs will not be reflected in earnings until they are actually recovered.

5. Commitments

The company is obligated, under leases expiring at varying dates to the year 2000, to minimum annual rentals for land and buildings from December 31, 1986 as follows:

1987	–	\$214,000
1988	–	209,000
1989	–	209,000
1990	–	205,000
1991	–	196,000
1992-1996	–	806,000
1997-2000	–	364,000

Annual rental income from leases to others will be approximately \$401,000 in 1987. The company may, at its option, renew most of the leases expiring in the next five years.

6. Employee deferred profit-sharing plan

Under the company's registered employee deferred profit-sharing plan, \$879,000 was set aside in 1986 (1985 – \$672,000). The plan provides that the directors are to determine annually the amount of the contribution, and that it may be a maximum of 10% and a minimum of 1% of the income before income taxes, excluding any unusual items, plus the deferred profit-sharing plan contribution.

7. Extraordinary item

During the third quarter of 1985 the Houston warehouse was sold resulting in a gain of \$1,270,000 (25¢ per share). No tax was payable because of U.S. losses being carried forward.

8. Reclassification of prior year

Certain of the prior year's figures have been reclassified to conform with the presentation adopted in the current year.

Company Facilities

CANADA		Gross Space
		(sq. ft.)
Alberta		
Calgary*	Leon's Furniture	60,000
Edmonton	Leon's Furniture Warehouse and Showroom	150,000
Ontario		
Burlington	Leon's Furniture Warehouse and Showroom	150,000
Kitchener	Leon's Furniture	50,000
London	Leon's Furniture	50,000
Ottawa	Leon's Furniture	75,000
St. Catharines	Carriage House Fine Furniture	15,000
Toronto	Leon's Furniture / Carpet / Appliance Warehouse and Showroom	226,000
Toronto*	New Era Furniture and Appliances	55,000
Toronto*	New Era Furniture and Appliances	26,000
Toronto*	Carriage House Fine Furniture	50,000
Toronto	Head Offices	25,000
Toronto	Leon's Furniture / Carpet / Appliance Warehouse Showroom and Distribution Centre	230,000
Welland	Leon's Furniture	48,000
Quebec		
Montreal	Leon's Furniture Warehouse and Showroom	150,000
U.S.A.		
Arizona		
Tempe	Leon's Furniture Warehouse and Showroom	126,000
		1,486,000

FRANCHISES

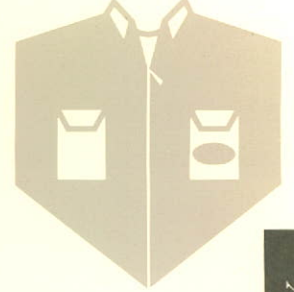
New Brunswick

Saint John Leon's Furniture

Ontario

Bracebridge Leon's Furniture
 Chatham Leon's Furniture
 Huntsville Leon's Furniture
 Kingston Leon's Furniture
 North Bay Leon's Furniture
 Peterborough Leon's Furniture
 Trenton Leon's Furniture
 Windsor Leon's Furniture

*Leased premises; all others are company-owned.



*Product availability is the
 lifeline of our business.
 Distribution of goods across
 the country and into custo-
 mer's homes continues to be
 the accumulative end result
 of all our efforts.*

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