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Silcorp Limited

Annual 1986 Report

Annual Report for the Year Ended December 28, 1986.

Contents

Shareholder Information
(as at December 28, 1986)

	number of shareholders	number of shares held
Class "A" Non-Voting Common		
— residents of Canada	1,628	1,902,066
— residents of U.S.A.	36	1,986
— other	8	264
Total Class "A" Non-Voting	1,672	1,904,316
Class "B" Common		
— residents of Canada	649	881,382
— residents of U.S.A.	20	1,042
Total Class "B"	669	882,424
Total Number of Shareholders	1,731	

Share Trading Summary*
(for the year 1986)

	High	Low	Close
For the 3-Months Ended:			
March 31, 1986			
Class "A" Non-Voting	17.25	12.50	17.25
Class "B"	16.75	12.88	16.75
June 30, 1986			
Class "A" Non-Voting	18.50	16.38	17.75
Class "B"	18.00	15.38	18.00
September 30, 1986			
Class "A" Non-Voting	18.50	16.50	16.50
Class "B"	17.50	15.88	15.88
December 31, 1986			
Class "A" Non-Voting	17.75	14.75	16.75
Class "B"	18.25	15.38	17.00

*Toronto Stock Exchange

Annual Meeting
The Annual Meeting of Shareholders will be held on Friday, April 24, 1987 at 11:00 a.m. in the Civic Ballroom of The Sheraton Centre, 123 Queen St. West, Toronto, Ontario.

En français
Si vous désirez recevoir le rapport annuel en français, veuillez écrire au secrétaire de la compagnie :

Le Secrétaire
Silcorp Limitée
6205 Airport Road
Mississauga, ON
L4V 1E1

Silcorp Limited

Silcorp Limited, headquartered in Mississauga, Canada, is a North American leader in the convenience and specialty retail store industry. At year-end, Silcorp operated 1053 convenience stores across Canada under the names Mac's and Mike's Mart and in four states of the United States as Hop-In and Pump 'N' Pantry, as well as 189 Baskin-Robbins ice cream stores in Canada.

Financial Highlights

($000's except per share data)

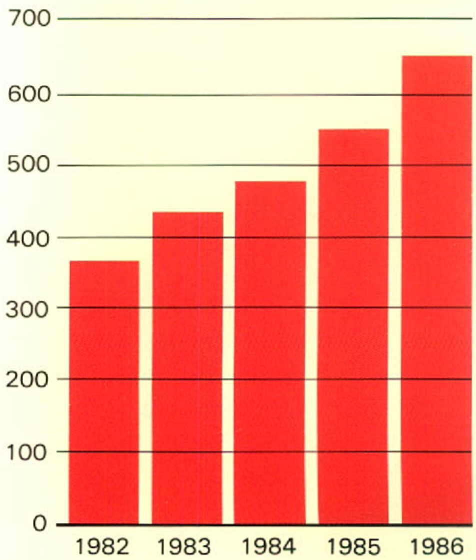
	1986	1985	1984
Operating Results			
Sales	**$651,534**	$551,184	$479,162
Net earnings	**$ 2,304**	$ 2,281	$ 2,715
Cash Flow			
Cash flow from operations	**$ 15,022**	$ 11,361	$ 9,184
Capital expenditures including goodwill	**$ 23,049**	$ 21,409	$ 17,106
Dividends	**$ 836**	$ 807	$ 807
Financial Position			
Working capital (deficit)	**$ 23,796**	$ (4,936)	$ 6,244
Total Assets	**$177,039**	$153,121	$121,406
*Senior debt — short-term	**$ 196**	$ 31,932	$ 4,978
— long-term	**$ 114**	$ 20,025	$ 24,847
Convertible subordinated debentures	**$ 60,000**		
Shareholders' equity	**$ 45,129**	$ 43,912	$ 40,018

*Senior debt includes bank borrowings, long-term debt and capital lease obligations

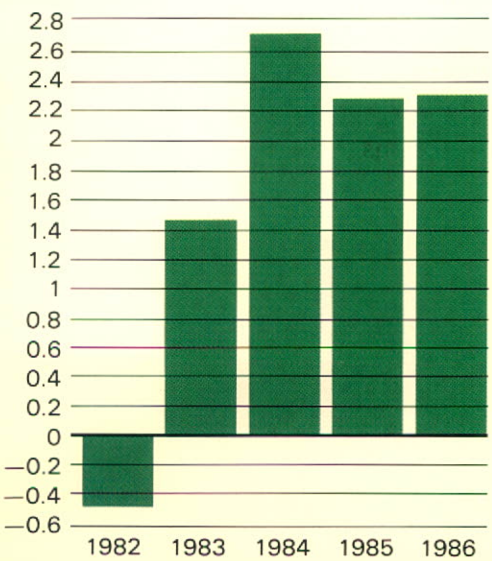
Per Share Data — for each Class "A" Non-Voting and Class "B" share (all information gives retroactive effect to the 2-for-1 subdivision of shares in May, 1985)

	1986	1985	1984
Net earnings — basic	**$ 0.83**	$ 0.85	$ 1.01
— fully diluted	**$ 0.81**		
Dividends paid			
— Class "A" Non-Voting and Class "B"	**$ 0.30**	$ 0.30	$ 0.30
Shareholders' equity	**$ 16.19**	$ 15.76	$ 14.88

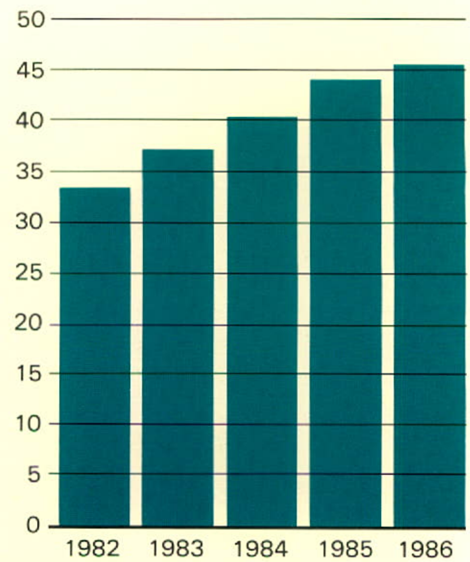
Consolidated Sales
($ Millions)



Net Earnings Before Extraordinary Items
($ Millions)



Shareholders' Equity
($ Millions)



To Our Shareholders

Fiscal 1986 was a year of both accomplishment and challenge for Silcorp Limited. We achieved sales growth targets, increasing profitability in four of our five divisions and additional strength in our balance sheet. However, our quest to achieve the stated net earnings and return on equity objectives remained unfulfilled.

Consolidated sales for the year ended December 28, 1986 increased 18.2% over 1985, consolidated operating income increased 43.4% and income before taxes increased by 66.2% while net earnings increased only 1%.

In 1986, sales of $651,534,000 increased by $100,350,000 or 18.2% over the prior year. Included in this total were sales of $52,085,000 arising from the acquisition of Mike's Mart convenience stores (Convenience Services Limited) on January 3, 1986.

Consolidated operating income increased 43.4% to $14,551,000 despite a higher operating loss in the U.S. business segment of $1,005,000 due to Hop-In division performance in the mid-Atlantic states. Canadian operations generated operating income of $17,424,000, a 45.0% increase over the $12,018,000 recorded in fiscal 1985.

Income before taxes grew by a substantial 66.2% to $6,642,000 in fiscal 1986.

However, the 1986 income tax provision of $4,338,000 reduced consolidated net earnings to $2,304,000, only 1.0% higher than the prior year. Earnings per basic share were $0.83 in 1986 compared with $0.85 in 1985. Net earnings were negatively impacted by approximately $788,000 because of our inability in 1986 to offset all losses incurred in the Hop-In Food Stores division, Roanoke, Virginia, against other taxable earnings in the United States. In Canada, the elimination of the tax benefit associated with the inventory tax credit further reduced net earnings by $497,000 for 1986. And, finally, the increase in Canadian corporate tax rates reduced net earnings by $122,000.

It was a year characterized by important milestones. We began 1986 with the announcement on January 3 that we had completed the acquisition of Convenience Services Limited of Barrie, Ontario, operating 78 Mike's Mart convenience stores and an integrated wholesale subsidiary. This acquisition has proven both strategically and financially beneficial, giving us a dominant market position in Central and Northern Ontario. This division achieved sales of $52,085,000 in 1986, exceeded our projections and made a positive contribution to Silcorp net earnings after allowance for all carrying costs and provision for annual goodwill amortization.

On June 26, 1986, Silcorp successfully issued $60,000,000 8% convertible subordinated debentures (unsecured and redeemable) which enabled us to retire all other secured bank borrowings and long-term debt from our balance sheet.

Our continuing confidence in the ability of this Corporation to achieve its goals is based not only on our strong positioning within the North American convenience and specialty retail sectors but also on the quality of the people of Silcorp and all of its operations. The divisions are managed by experienced, aggressive industry leaders. Throughout the organization they are building an exciting, involved and consumer-oriented team of store managers, dealers, and franchisees with their friendly, committed staffs. There is a pride of performance permeating the retailing staff in all divisions as people recognize their leading position within our industry and strive to maintain that leadership.

Booming commercial real estate markets have tended to increase retail occupancy costs and have slowed new store growth in Mac's Convenience Stores, Mike's Marts, and to a lesser degree Baskin-Robbins. Nonetheless, during 1986 Silcorp expanded its store network substantially. The acquisition of the Mike's Mart chain added 78 stores, while an additional 80 new retail stores were opened across all divisions. A total of 65 stores which no longer met operating criteria were disposed of, thus generating a net store expansion throughout the Corporation of 93 stores. At year-end 1986, the Silcorp store network totalled 1,242 . . . 789 Mac's Convenience Stores, 79 Mike's Marts and 189 Baskin-Robbins Ice Cream Stores in Canada; 128 Hop-In Food Stores in Virginia, North Carolina and Tennessee and 57 FarrView division outlets in Michigan.

Despite the diversity of economies across its marketplace and intense competition, the Mac's Convenience Stores division set new records for sales and operating income and continued its leadership of the Canadian convenience store marketplace. Mac's total sales increased 8.6% in 1986 while operating income increased 11.1%.

The ever-changing concept of consumer convenience needs is being met by Mac's as it continually modifies its consumer offering of product categories and services. The increasing focus on the fast food and premium coffee sector and services such as video movie rentals, lotteries and financial services typify this commitment to leadership.

This division continues its concentration on development of new prime site locations with increasing involvement

Eric F. Findlay and Robert S. Maich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in self-serve gasoline installations. This awareness of changing consumer trends brings about an increase in store disposals as Mac's ensures that its facilities are state-of-the-art and consumer-friendly, appealing to the customer of today *and* tomorrow.

The positive success of the Baskin-Robbins divison during 1986 within a slow growth ice cream market reflects a series of strategies undertaken by management commencing some three years ago.

In 1984, we described our investment in modernizing production facilities at Peterborough, Ontario, together with the development of a distinct change in store presentation, new location criteria and totally revised consumer marketing concepts. The comment was made then that "the effect of these changes will appear in sales and profit growth in the years ahead".

That expectation was further enhanced in 1986 as this division increased its store network by 14%, increased wholesale sales by 15% and system-wide franchisee retail sales by 20%, while more than doubling its 1985 operating income performance.

Attainment of Silcorp financial goals continued to be negatively affected by the loss performance of the Hop-In division operating in Virginia, North Carolina and Tennessee. Despite a concentrated effort by a strengthened management team, this division generated increased losses during 1986.

The start-up costs of new stores opened in 1986, combined with new stores opened in late 1984 and 1985 which were not at full profit potential, generated an increase in operating losses. However, the second half of 1986 produced a steadily growing number of customers and accelerating sales trends in both merchandise sales and gasoline gallonage that gained momentum as the effects of the programs instituted became more evident to existing and potential Hop-In customers. While the cost of implementing these programs precluded a reduction in the operating losses during the last half of the year, the sales momentum generated gives this division a strengthened opportunity for significant loss reductions in 1987.

Mention should be made of the approach by Crown Central Petroleum Inc. of Baltimore, Maryland to Silcorp regarding the purchase of the Hop-In Food Stores division. In view of our commitment to shareholders, it was concluded that we should enter into negotiations to ascertain whether an acceptable sale of assets could be achieved. On November 25, 1986, a letter of intent was signed with the objective of closing the transaction in late December, 1986. However, just prior to the finalization of a definitive agreement, Crown Central Petroleum declared that they were not in a position to comply with Virginia "petroleum divorcement laws" and thus they could not complete the purchase.

Our FarrView division in Michigan experienced an excellent and increasingly profitable year in 1986, while stabilizing its operations by fully completing the integration of the Pump 'N' Pantry acquisition. Sales of this division increased 9% and operating income increased 42% over the levels attained in 1985. With the current implementation of new marketing programs by this division's strengthened management team, we anticipate a continuing growth pattern to emerge over the coming years.

Despite the problems evident within the Hop-In divison, Silcorp management remains confident that, given time, this division can become profitable. Together with the profitable FarrView division in Michigan, we remain committed to developing a significant presence in the United States marketplace.

We record with regret the death of William P. Pigott of Hamilton, Ontario, on March 13, 1986. Bill Pigott had served as a director for seven years and had made an outstanding contribution on behalf of all shareholders. He was a man who understood the value of the free enterprise system to Canada — a man who practised it with every fibre in his body. He was a man of principle and a leader among Canadians.

On August 1, 1986, Gordon R. Carton, Q.C., Director, General Counsel, Secretary and Vice-President, Legal and Corporate Affairs, reached retirement age. Gordon joined the Silcorp (then Silverwood Industries) executive group in April, 1974 following retirement as Minister of Transportation and Communications in the Government of Ontario. He served the Corporation well over those twelve years and we will genuinely miss his counsel.

On October 1, 1986, William P. Thomas was appointed Vice-President, Secretary and General Counsel of Silcorp Limited. He has had extensive experience as General Counsel over the last fourteen years with two leading consumer and industrial marketing organizations headquartered in Ontario.

On August 19, 1986, Peter C. Maurice, Senior Executive Vice-President, Canada Trustco Mortgage Company, was appointed to our Board of Directors. Peter has been an executive with Canada Trust over the last 14 years. He brings great strength and knowledge in the financial field to your Board of Directors.

We reiterate the commitment of management to its primary strategic goal, first stated in 1984 . . . to achieve a minimum 15% return on beginning shareholders' equity per annum by fiscal year 1989. Appraising the return on equity performance over the past three years ranging from 7.3% in 1984, 5.7% in 1985 and 5.3% in 1986 would indicate little progress in accomplishment of this goal. However, deeper assessment and analysis of this corporation's progress during the same time period would indicate that this goal continues to be realistic and achievable. It is important to note that, apart from our current difficulties with the Hop-In Food Stores division, which we are determined to change, our return on equity in 1986 would have approximated the 15% minimum goal.

As we look to the longer term future, we remain confident of this Corporation's ability to meet the challenges and achieve the opportunities that face us in North America. Our leadership position in the Canadian convenience store and specialty retail industry provides us with a strong base for continued profitable growth and expansion in this country.

We are at the formative stage of our entry into the United States. During the past few years, the experiences gained in this market and the changes of strategy under consideration continue to indicate realistic opportunities for a profitable and tangible presence for Silcorp in a growing number of markets in the United States.

As a corporation committed to long term profitable growth in North America, we are truly on the move. Our people are dedicated to building the business through a North American network of stores.

Sales are expected to approximate $720,000,000 in 1987, with capital expenditures on the order of $24,000,000 for the year. In 1987, our plans call for a net increase in total store count of approximately 40 locations developed through the real estate process. In addition, we are committed to accelerating growth through acquisition.

We are most grateful for the support of our shareholders and the dedicated team of people that comprise the Silcorp organization. Working together, the future of this Corporation appears exciting.

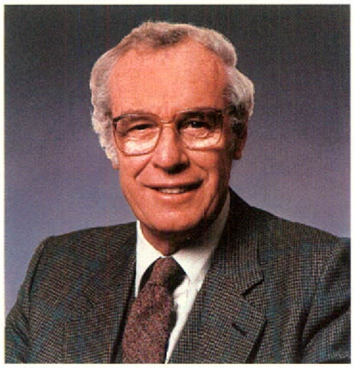
Eric F. Findlay
Chairman of the Board

Robert S. Maich
President

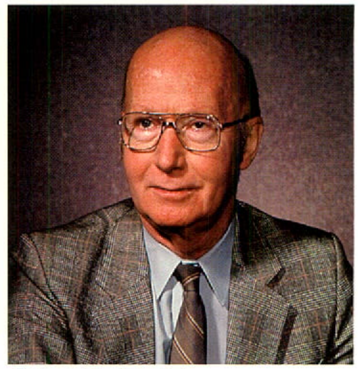
In November 1986, your President, Robert S. Maich, was named to serve as Chairman of the National Association of Convenience Stores headquartered in Washington, D.C. This appointment is not only a distinct personal achievement but one that reflects on and emanates from the position being achieved within the North American convenience store industry by your Corporation, led by Robert S. Maich as its President.

Board of Directors (indicating number of years as a Director)

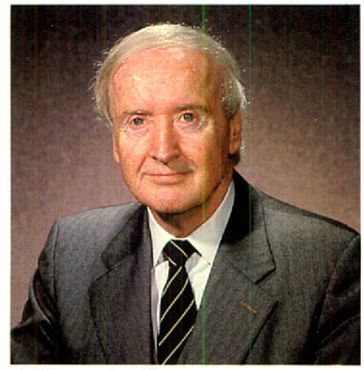
W.I. (Irv) Barton



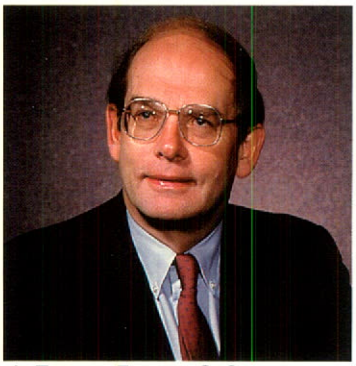
Robert J. Butler



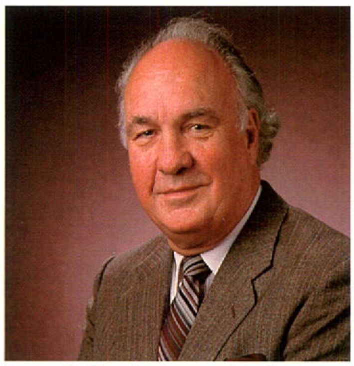
Grant M. Carlyle



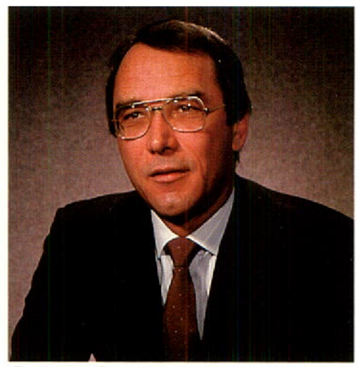
William A. Dimma



J. Trevor Eyton, O.C.

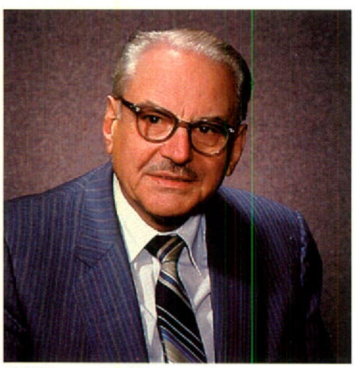


Eric F. Findlay



Robert S. Maich

Peter C. Maurice



William A. Stewart

J. Allyn Taylor, O.C.

Donald H. Thain

David B. Weldon

W.I. (Irv) Barton (17)
former Secretary-Treasurer of the Corporation, retired,
Victoria, B.C.

J. Trevor Eyton, O.C. (4)
President and Chief Executive Officer,
Brascan Limited,
Toronto, Ontario

William A. Stewart (9)
former Ontario Minister of Agriculture,
farmer,
London, Ontario

Robert J. Butler (2)
Chairman of the Board,
Urban Transportation Development Corporation Limited,
Bolton, Ontario

Eric F. Findlay (18)
Chairman of the Board and Chief Executive Officer of the Corporation,
Toronto, Ontario,

J. Allyn Taylor, O.C. (28)
retired Chairman,
Canada Trustco Mortgage Company,
London, Ontario

Grant M. Carlyle (21)
private investor,
Calgary, Alberta

Robert S. Maich (8)
President and Chief Operating Officer of the Corporation,
Oakville, Ontario

Donald H. Thain (17)
Professor, School of Business Administration,
University of Western Ontario,
London, Ontario

William A. Dimma (4)
Deputy Chairman,
Royal LePage Limited,
Toronto, Ontario

Peter C. Maurice (1)
Senior Executive Vice-President,
Canada Trustco Mortgage Company,
Toronto, Ontario

David B. Weldon (17)
Chairman of the Board,
Midland Doherty Financial Corporation,
Toronto, Ontario

Committees of the Board of Directors (Page 32)

Segmented Information

Year ended December 28, 1986
(with comparative amounts for the years ended December 29, 1985 and December 30, 1984)
($000's)

	1986	1985	1984
Total revenue:			
Canada	**$494,330**	$406,633	$382,970
U.S.A.	**157,204**	144,551	96,192
Consolidated	**$651,534**	$551,184	$479,162
Segment operating income (loss):			
Canada	**$ 17,424**	$ 12,018	$ 9,951
U.S.A.	**(2,873)**	(1,868)	(423)
Consolidated	**14,551**	10,150	9,528
General corporate expenses	**3,149**	2,581	2,514
Interest expense	**4,760**	3,572	2,252
	7,909	6,153	4,766
Income before taxes	**6,642**	3,997	4,762
Income taxes	**4,338**	1,716	2,047
Net earnings	**$ 2,304**	$ 2,281	$ 2,715
Total assets:			
Canada	**$125,372**	$ 91,272	$ 92,633
U.S.A.	**51,667**	61,849	28,773
Consolidated	**$177,039**	$153,121	$121,406
Depreciation and amortization:			
Canada	**$ 6,593**	$ 5,180	$ 4,209
U.S.A.	**3,805**	3,150	2,240
Consolidated	**$ 10,398**	$ 8,330	$ 6,449
Fixed asset additions:			
Canada	**$ 10,775**	$ 11,029	$ 12,293
U.S.A.	**5,449**	10,294	4,756
Consolidated	**$ 16,224**	$ 21,323	$ 17,049

Description of business
The Corporation operates in one industry segment and two geographic segments, deriving its revenue from sales of convenience items, ice cream, fast food and gasoline.

Mike's Mart

	1986	1985	1984
Sales ($000's)	**52,085**	—	—
Year End Store Count	**79**	—	—
Capital Expenditures ($000's)	**679**	—	—
Capital Employed ($000's)	**10,957**	—	—

Acquired by the Corporation January 3, 1986, Convenience Services Limited operated during the year as a separate and wholly-owned subsidiary of Silcorp Limited.

This division, which operates the Mike's Mart chain of convenience stores and Northmar Distributors, a wholesale operation, in Central and Northern Ontario, achieved consolidated sales of $52.1 million in fiscal 1986, significantly exceeding corporate plans. Operating income also exceeded corporate projections, and a very positive contribution to net earnings was achieved after fully accounting for all costs of the acquisition.

At year-end, Convenience Services Limited operated 79 convenience store outlets in Owen Sound, Barrie, Midland, Orillia, the Muskokas, Parry Sound, North Bay, Sault Ste. Marie and Thunder Bay. Seven outlets also provide self-serve gasoline, while a further five have adjacent gasoline operations. Two new locations were opened during the year and one eliminated.

Headquartered in Barrie, Ontario, this division is the dominant convenience store chain in Central and Northern Ontario. Northmar, based in North Bay, is a confectionery, tobacco, grocery and sundry wholesale distribution centre serving primarily the Mike's Mart network.

During 1986, the existing stores were remerchandised and re-introduced to the consumer to reflect the products and services demanded by today's customers. With this achieved, virtually all of Mike's Mart stores were able to offer customers a new fast food/fountain drink program together with a quick and convenient video movie rental system. Both of these concepts were well received by customers and will be expanded further in 1987.

December, 1986 marks the 20th anniversary of Mike's Mart stores. The chain's profitable growth and dominant positioning in its marketplaces over these years reflects the commitment to service by management, staff and store operators and their intimate knowledge of the market needs of the communities which they serve. The outlook for this new Silcorp division is notably positive. Its people have participated in and have been intensely involved with their communities. They are attuned to the ever-changing lifestyles and demographics of their customers from many walks of life and to the competitive environment.

left to right: Bob Moffat, Dave Rodgers, Joe Lewis, Scott Findlay.

This pinpoint marketing approach by Convenience Services Limited ensures unique, friendly and convenient service to Mike's Mart customers, and profitable growth in 1987 and beyond.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Mac's Convenience Stores

	1986	1985	1984
Sales ($000's)	**427,118**	393,125	368,910
Year End Store Count	**789**	788	759
Capital Expenditures ($000's)	**9,537**	10,120	10,049
Capital Employed ($000's)	**45,610**	38,644	31,095

Total 1986 sales for this major operating division increased 8.6% over the prior year to $427.1 million. Division operating income increased 11.1% over the prior year indicating management's commitment to productivity increases throughout the organization.

This record was achieved despite an often adverse 1986 external environment typified by an increasingly competitive total food retail industry marketplace, depressed economic circumstances particularly in Alberta, Saskatchewan and British Columbia and unusually poor summer weather throughout much of Canada.

Mac's celebrated its 25th Anniversary with record levels of sales and profitability despite a challenging year. Non-gasoline sales increased 7.4% while gasoline sales revenue increased 40.4% and gasoline volume reached 113.5 million litres. A total of 789 Mac's outlets were in operation at year-end, a net increase of one over the prior year. Eighty convenience stores offered self-service gasoline at the end of 1986 compared with the previous year level of 67.

A significant portion of the $9.5 million of Mac's capital spending was utilized to secure and develop 39 new prime site locations from Quebec to Vancouver Island. The important process of eliminating marginal stores where an adequate return on investment is not available led to the disposal of 38 stores. Most of these outlets were older stores opened in the late 1960s and early 1970s.

Thirteen of the newly-opened Mac's stores include a self-service gasoline facility. This continued emphasis on combining self-service gasoline with new convenience stores serves two prime strategic objectives: the attainment of high quality, high traffic prime site corner locations; and the combining of a compatible traffic-building product category, gasoline, with the range of products and services offered within the store. The division is staffing its management group with additional experienced oil industry personnel to accelerate Mac's strategic commitment to aggressive gasoline marketing.

Mac's continues to focus its consumer-driven marketing effort on providing customers with superior service. At the same time, management recognizes the reality of low retail price inflation and increasing competition and, accordingly, continues to

left to right: Don Cameron, Derek Ridout, Bob Scott, John Fraser.

concentrate day-to-day emphasis on achieving productivity improvements.

Combined with running the current business more effectively is the ongoing requirement to develop, test and roll out new products and services which appeal to the ever-changing needs and wants of the consuming public. Superior customer service requires a dedicated effort to upgrade the ambience of each individual store for both in-store staff comfort and efficiency and for the consuming public. Emphasis on the recruitment, training, motivation and reward of highly qualified independent store dealers, franchisees and employees who operate our individual outlets is a cornerstone of the business.

New products and services within the Mac's store network are a fast growing,

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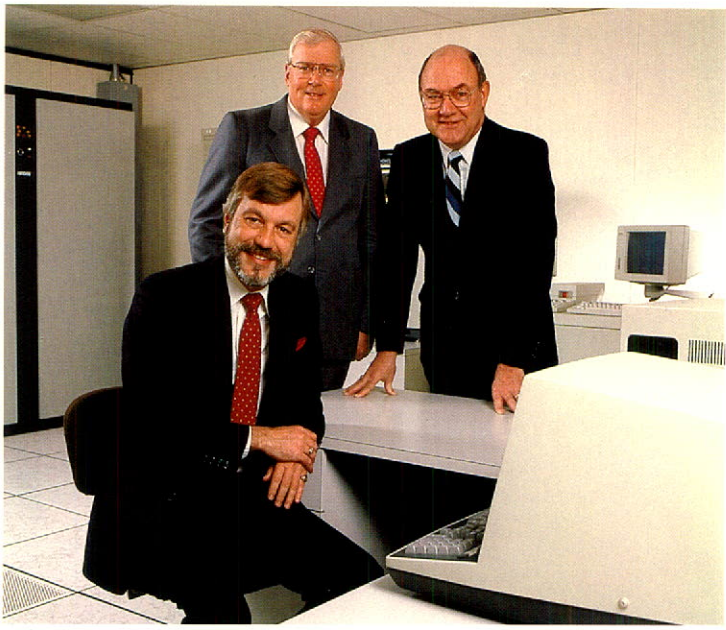
high profit margin sector of the business. During 1986, a number of important developments were initiated which will contribute to the performance of the division in future years. Foremost among these was the successful introduction of a video movie rental program in place in more than 450 stores at year-end 1986. Customer acceptance of this new service has been exceptional. The Mac's division projects that it will be the largest single retailer of video movie rentals in Canada during 1987.



left to right: Rick Broadhead, Bern Harrington, Russ Egerdie.

Other important developments during the year included: the introduction of a new premium blend coffee tested as the finest product available in the food service industry; an accelerated program to install additional fountain and frozen carbonated beverage machines; and, following successful test marketing, complete refurbishing and revitalization of the confectionery and soft drink store sections to further increase sales and profitability of leading national brands.

Mac's also tested successfully a number of store remodel and upgrade concepts in selected markets during 1986. The benefits of these tests will begin to be realized in 1987 as the division rolls out these improved store designs to more than 250 existing locations across the country.

Mac's range of store formats continues to focus on a blend of newer, larger outlets offering various combinations of fresh baked goods, delicatessen products and upgraded sandwich items as well as self-serve gasoline. Although newer units will be somewhat larger than the conventional Mac's store, the conventional store format will continue for some time to be the basic foundation of the existing store network. For 1987, it is planned that sales will continue to grow substantially and that Mac's record of continuing profitability increases will be sustained.

The Mac's division has an enviable record of accomplishment over its 25 year history. As Canada's leading convenience store chain, this division continues to work intensively with its regional and national suppliers to ensure that the best possible marketing programs are available to its customers who visit Mac's more than 220 million times each year.

Baskin-Robbins Ice Cream

	1986	1985	1984
Sales ($000's)	**15,127**	13,106	11,073
Year End Store Count	**189**	166	151
Capital Expenditures ($000's)	**220**	667	1,613
Capital Employed ($000's)	**4,315**	4,415	5,067

The responsiveness of Baskin-Robbins to changing Canadian consumer demographics, lifestyles and demands over the past three years has culminated in a very successful year for this division. Total sales increased more than 15% to $15.1 million, while systemwide retail sales of the total store network increased to $31.3 million.

Operating income more than doubled over 1985, reflecting the fruition of a variety of strategies which commenced in 1984. The Peterborough, Ontario ice cream plant was modernized and streamlined for plant efficiencies in 1984, the management team was strengthened and new real estate facility and marketing strategies tested, then expanded throughout the store network.

In 1986, the division opened 30 new high traffic, high volume locations, 24 in enclosed malls, and closed 7 locations which no longer met corporate criteria. A total of 189 primarily franchised stores were in operation in five provinces of Canada at year-end. In addition, 16 "A La Carte" mobile scooping units provided additional seasonal and promotional availability to customers' demands where full facility year-round stores were not warranted.

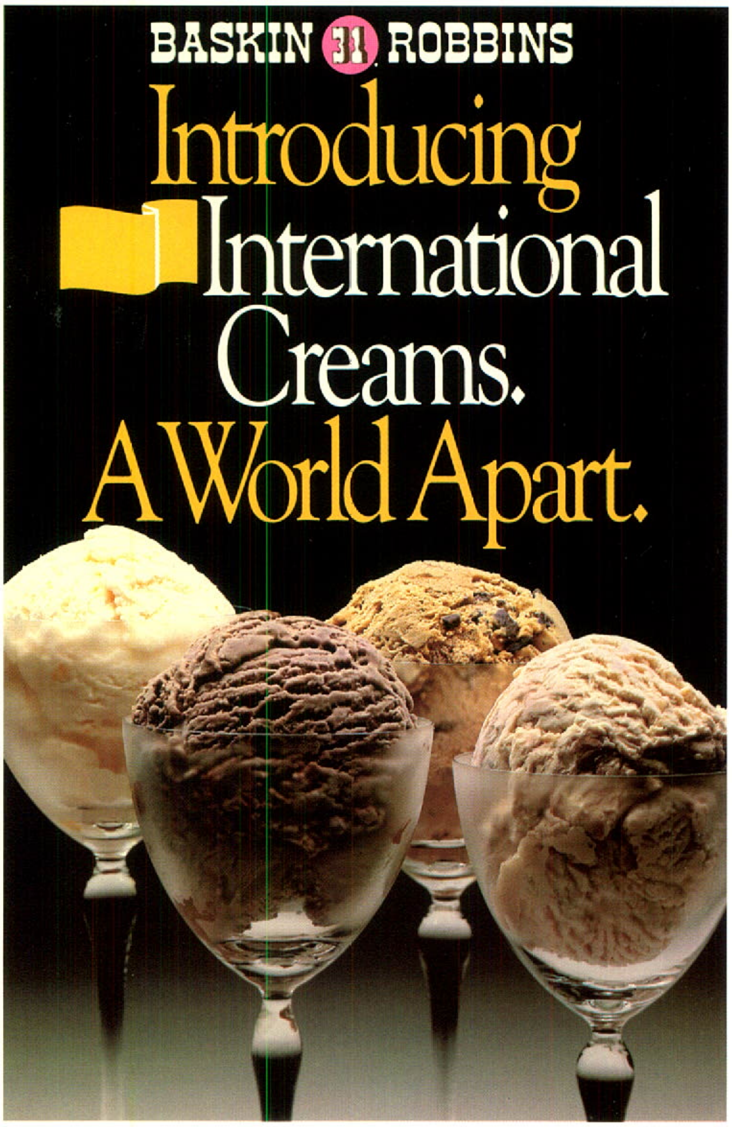
The 1986 entry of Baskin-Robbins into the Manitoba market met with outstanding success and provided a strengthening of our presence in Western Canada, adding to the base already being developed in the provinces of Alberta and British Columbia.

left to right: Henry Hudel, Craig Findlay, Stan White.

Total production of Baskin-Robbins ice cream gallonage increased by more than 11%, substantially exceeding the growth rate of the total market for hard ice cream across Canada. Production and distribution facilities headquartered in Peterborough, Ontario, continue to improve upon the efficiencies experienced in

previous years, and upon the superior quality standards achieved in 1985. This plant maintained its position as a leading ice cream manufacturing facility in the Baskin-Robbins worldwide network.

"International Creams" . . . an innovative new line of super premium liqueur-based ice cream products was introduced at mid-year by division management as a marketing response to changing consumer preferences and lifestyles. Its reception was simply outstanding. Such programmed success strengthens this division's commitment to the objective of innovative leadership within the specialty ice cream retail sector in Canada. The development and expansion of additional premium quality products will continue in the years ahead.



The combined commitment by Baskin-Robbins division management and its franchisee team has been instrumental in the profitable growth of the division this past year. The outlook for 1987 is one of continued store expansion and strong sales growth combined with solid and growing profit improvements for both the division and individual franchisees.


ELLE
31
ONTARIO
BR 31
YOURS TO DISCOVER

	1986	1985	1984
Sales (U.S.$000's)	**41,797**	38,268	12,585
Year End Store Count	**57**	60	37
Capital Expenditures (U.S.$000's)	**581**	3,074	584
Capital Employed (U.S.$000's)	**5,599**	5,736	2,047

The FarrView division continued its strong sales and profitability trends during 1986. Total sales of U.S.$41.8 million increased 9.2% over the prior year despite a slightly reduced store base and significantly lower gasoline retail prices.

The store network includes 34 conventional convenience stores plus 2 stores with self-serve gasoline operating under the "Hop-In" banner. In addition, there are 21 Pump 'N' Pantry self-serve gasoline and convenience stores which were fully integrated into the FarrView division for the full year 1986. The division ended 1986 with 57 stores in operation, 3 fewer than the prior year as the Michigan store network was further rationalized.

A consequent realignment of the division organization and the addition of three seasoned convenience store professionals to the management group was accomplished during the year. The functions of operations, merchandising and information services were considerably strengthened.

Gasoline volume increased to 19.7 million U.S. gallons in the highly competitive Michigan market. Although lower retail prices cut deeply into dollar sales, margins were sufficiently strong to allow the gasoline category to contribute substantially to overall profits for the year. Non-gasoline sales totalled U.S.$24.4 million, an 18.5% increase over the prior year. Operating Income increased by a significant 42%.

Michigan's improved economic environment challenged FarrView to maintain and gain market share and to recruit store personnel in an increasingly competitive labour marketplace. Aggressive market-by-market consumer promotions increased customer count and average customer transaction size.

Late in fiscal 1986, new programs and services began to be added to the overall FarrView store network as the integration of the acquired stores was largely completed. This division entered 1987 with a comprehensive video movie rental program being launched throughout its store network, a prototype test underway in joint tenancy with a major pizza operator, expansion of on-line lottery terminals to additional stores and the installation of automatic banking machines at selected stores. These new initiatives are expected to benefit this division during 1987 and beyond.

left to right: John DeWit, Tom Becker.

Division management's dedication to customer service, the aggressive pursuit of an increasingly dominant position within the Michigan marketplace and the development of the potentials of all FarrView employees will ensure continued profitable growth in 1987.


MICHIGAN
MICHIGAN STATE SPARTANS
HOPIN
MICHIGAN
THE BIG BUNNY
FOR A BIG DRINK

Hop-In Food Stores

	1986	1985	1984
Sales (U.S.$000's)	**71,353**	67,494	61,478
Year End Store Count	**128**	135	126
Capital Expenditures (U.S.$000's)	**3,341**	4,465	3,045
Capital Employed (U.S.$000's)	**17,784**	16,765	14,291

The restructuring and strengthening of the Hop-In division organization, commenced in 1985, was completed in the first quarter 1986. By mid-year, an intensive review of both business opportunities and operating problems had been completed and action plans developed.

The actual implementation of these action plans in the second half of 1986 began to generate dramatic improvements in sales revenue performance and gasoline gallonage. The rebuilding process indicates continued momentum through 1987 as all of the various programs are fully implemented and the consuming public becomes fully aware of the changes.

In 1986, Hop-In opened 9 new stores in prime locations, while 16 unproductive units were eliminated. Three new sites are scheduled to open in early 1987.

Thus, at year-end, this mid-Atlantic state division was operating 128 stores, 7 fewer than the prior year.

Total sales for 1986 increased to U.S.$71.4 million representing 5.7% growth. Non-gasoline sales increased 7.8%. Gasoline sales revenue increased 2.2% despite generally lower retail selling prices due to declining world oil prices. Total gasoline volume increased to approximately 39 million U.S. gallons in 1986, reflecting a 30.1% increase over the prior year. The very significant increases in both non-gasoline sales and in gasoline gallonage from fewer stores reflects the early results of the action plans now underway.

Increased operating loss performance in fiscal 1986 was disappointing. The costs of developing and then implementing new action plans, further exacerbated the short-term loss during the year. Compounding short-term performance was the fact that by year-end some 29 of the 128 stores in operation had been opened for approximately 24 months or less and have not yet achieved their full sales and contribution to profit potential.

The addition of new products and services at the end of 1986 and through the first half of 1987 is expected to continue to accelerate growth in customer store traffic, non-gasoline sales and gasoline volume. A video movie rental program was introduced into 30 Hop-In stores in December 1986, with immediate customer acceptance. Most stores will offer this program by mid-1987.

left to right: Peter Surprenant, Ron Adams, Glenn LiFonti.

Management is committed to developing a clear ongoing focus on operating fundamentals and consumer-driven promotions aimed at accelerating the momentum generated in customer store traffic, sales revenue and gasoline volume during the past year.

A significant reduction in this division's operating loss is the goal for 1987.

HOP-IN
SELF SERVICE
No Smoking · Stop Motor
HOP-IN
FREE Glazed DONUT LARGE COFFEE... 65¢
ICE CREAM BAR 25¢
89¢
REGULAR

Five Year Comparative Summary

($000's except per share data and store count)

	1986	1985	1984	1983	1982**
Operating Results					
Sales	**$651,534**	$551,184	$479,162	$437,167	$365,820
Earnings (loss) before extraordinary item	**$ 2,304**	$ 2,281	$ 2,715	$ 1,465	$ (476)
Net earnings (loss)	**$ 2,304**	$ 2,281	$ 2,715	$ 4,890	$ (291)
Cash Flows					
Cash flow from operations	**$ 15,022**	$ 11,361	$ 9,184	$ 10,257	$ 7,818
Capital expenditures including goodwill	**$ 23,049**	$ 21,409	$ 17,106	$ 12,235	$ 7,707
Dividends	**$ 836**	$ 807	$ 807	$ 1,008	$ 427
Financial Position					
Cash and short-term investments	**$ 13,455**	$ 11,182	$ 9,608	$ 23,528	$ 750
Working capital (deficit)	**$ 23,976**	$ (4,936)	$ 6,244	$ 14,636	$ 3,990
Fixed assets (net)	**$ 67,977**	$ 60,956	$ 50,391	$ 42,794	$ 41,606
Total assets	**$177,039**	$153,121	$121,406	$117,881	$129,746
*Senior debt — short-term	**$ 196**	$ 31,932	$ 4,978	$ 2,945	$ 13,772
— long-term	**$ 114**	$ 20,025	$ 24,847	$ 29,542	$ 47,763
Convertible subordinated debentures	**$ 60,000**				
Shareholders' equity	**$ 45,129**	$ 43,912	$ 40,018	$ 37,176	$ 33,297

*Senior debt includes bank borrowings, long-term debt and capital lease obligations.

Per Share Data — for each Class "A" Non-Voting and Class "B" share (all information gives retroactive effect to the 2-for-1 subdivision of shares in May, 1985)

	1986	1985	1984	1983	1982**
Earnings (loss) before extraordinary item					
— basic	**$ 0.83**	$ 0.85	$ 1.01	$ 0.55	$ (0.18)
— fully diluted	**$ 0.81**				
Net earnings (loss)					
— basic	**$ 0.83**	$ 0.85	$ 1.01	$ 1.82	$ (0.11)
— fully diluted	**$ 0.81**				
Dividends paid — Class "A" Non-Voting	**$ 0.30**	$ 0.30	$ 0.30	$ 0.30	$ 0.30
— Class "B"	**$ 0.30**	$ 0.30	$ 0.30	$ 0.30	$ 0.175
Shareholders' equity	**$ 16.19**	$ 15.76	$ 14.88	$ 13.82	$ 12.38
Shares outstanding at year-end					
Class "A" Non-Voting	**1,904,316**	1,904,316	1,806,316	1,806,316	1,806,316
Class "B"	**882,424**	882,424	882,424	882,424	882,424
Store Count					
Convenience stores open at year-end	**1,053**	983	922	906	869
Ice cream stores open at year-end	**189**	166	151	151	146
Restaurants open at year-end			1	2	2
Total units open at year-end	**1,242**	1,149	1,074	1,059	1,017
Convenience stores selling gasoline included in year-end totals	**223**	205	150	135	131

**1982 is as restated and reported in the 1983 and subsequent financial statements after giving effect to the disposal of Silverwood Dairies division.

1984 — Fifty-three weeks ended December 30, 1984.
Other years — Fifty-two weeks ended approximately the end of December in each year.

Financial Review

Silcorp Limited

In 1986, Silcorp continued its positive sales growth. Net earnings, although slightly above 1985, did not meet expectations because of the increased operating loss incurred by the Hop-In division.

OPERATING RESULTS

In 1986, sales of $651.5 million increased by $100.4 million (18.2%), operating income of $14.6 million increased by $4.4 million (43.4%), whereas net earnings increased by $23,000 (1.0%) compared with 1985 results.

Sales

The 1986 sales increase of $100.4 million benefitted by $52.1 million in additional sales through the acquisition of Convenience Services Limited and by $7.8 million relating to the inclusion of the Pump 'N' Pantry acquisition (April 1, 1985) for a full year in 1986.

Gasoline sales continue to be a growing component of total sales. Because of fluctuating retail prices of gasoline, volumes are more representative of the growth trends.

Sales Summary
($000's)

	1986	1985	1984
Gasoline sales			
Retail sales	**$ 80,970**	$ 71,161	$ 33,670
Commission sales	**2,898**	2,083	1,271
	83,868	73,244	34,941
Merchandise and other	**567,666**	477,940	444,221
	$651,534	$551,184	$479,162

Gasoline Volume Summary
(000's — litres)

Canada	**124,233**	78,357	50,537
U.S.*	**222,870**	170,680	102,460
Total	**347,103**	249,037	152,997

*Conversion of U.S. gallons: 1 U.S. gal. = 3.78 litres

Operating income

Combined operating income increased by $4.4 to $14.6 million in 1986. This was adversely affected by the $2.9 million operating loss in our combined U.S. operations, an increase of $1.0 million over 1985. The increase in FarrView's operating income was more than offset by the increase in the operating loss of the Hop-In division. Combined operating income of the Canadian operations in 1986 was $17.4 million, $5.4 million more than in 1985. This increase significantly benefitted from the acquisition of Convenience Services Limited in 1986.

Interest

The increase in net interest expense of $1.2 million in 1986 reflects the borrowing cost associated with the Convenience Services Limited acquisition and the cost of increased borrowing to fund capital expenditures in excess of cash flows. The Corporation benefitted from the favourable 8% interest rate of the $60,000,000 convertible subordinated debentures which were issued June 26, 1986.

Interest coverage ratio for 1986 increased to 2.40 compared with 2.12 in 1985. This increase was moderated by the increase in the U.S. operating loss.

Interest expense is not expected to change significantly in 1987 and increased operating income is expected to improve the interest coverage ratio from the 1986 level.

Income taxes

The Corporation's income tax provision was $4.3 million for 1986 and was negatively impacted by $1.4 million due to the following factors:

- non-recognition of the tax benefit associated with U.S. tax loss — $0.8 million ($0.3 million in 1985)
- elimination of the inventory tax credit and increase in Federal and Provincial income tax rates — $0.6 million.

Net earnings

1986 net earnings of $2,304,000 increased by $23,000 over 1985 net earnings of $2,281,000.

Basic earnings per share decreased to $0.83 in 1986 from $0.85 in 1985, directly attributable to the higher number of shares outstanding during 1986 — 98,000 Class "A" Non-Voting shares were issued on December 3, 1985 under the Management Share Purchase Plan.

Quarterly earnings per share are set out in the following table:

Basic Earnings (Loss) Per Share

	1986	1985	1984
First quarter	**$(0.40)**	$(0.47)	$(0.43)
Second quarter	**0.30**	0.32	0.37
Third quarter	**0.82**	0.83	0.73
Fourth quarter	**0.11**	0.17	0.34
	$ 0.83	$ 0.85	$ 1.01

CASH FLOWS

Funds of $75 million generated from operating activities and the issue of the convertible subordinated debentures more than covered the $23 million requirement for capital expenditures and the Convenience Services Limited acquisition. The balance of the funds was used to retire $23 million of long-term debt and capital lease obligations and repay $17 million of current bank borrowings. The Corporation had a $13.5 million cash surplus at the end of the year.

FINANCIAL POSITION

Silcorp's financial position at December 28, 1986 remains strong. Total assets increased by $23,918,000 during 1986. This represents an increase of $34,100,000 in assets in Canada less a decrease of $10,182,000 in U.S. assets.

The increase in Canadian assets is mainly attributable to the Convenience Services Limited acquisition and the cash surplus at the end of 1986.

The decrease in U.S. assets relates to the use of the short-term investments in the U.S., on hand at the end of 1985, to repay current bank borrowings in the U.S.

The financial position of the Corporation was strengthened during 1986 with the $60,000,000 8% convertible subordinated debenture issue. The successful issue of this unsecured obligation provides the Corporation with greater financial flexibility to invest in growth opportunities for the future and provides for potential future increase in shareholders' equity through conversion.

Working capital increased by $28.7 million from a deficit position of $4.9 million at the end of 1985 to a positive working capital position of $23.9 million at the end of 1986. This was a direct result of the convertible subordinated debenture issue. Inventory is the principal working capital component of our business and represents a sizeable controllable asset of $46 million which is financed entirely by trade payables.

The Corporation's fixed asset base has been markedly improved in the last three years as indicated by the $54 million three year capital expenditures in relation to the net fixed asset base of $68 million at the end of the year.

The capital structure of any corporation reflects the combination of its funding from both external and internal sources. External funding affects the leverage factor and can lead to increased exposure to variable financing costs. The issue of the convertible subordinated debentures has, in addition to providing increased financial flexibility, added a measure of stability to the interest cost factor.

Total assets (including $13.5 million cash and short-term investments and $14.6 million of store properties under development) at the end of 1986 were financed principally by shareholders' equity (26%), convertible subordinated debentures (34%) and trade payables (34%).

Shareholders' equity increased $1.2 million during the year to $45.1 million.

The financial data provided in the reports of each of the divisions includes the amount of capital employed by each division. The capital employed at the division level means the total assets (including goodwill but excluding store properties under development) less accounts payable and accrued liabilities.

CAPITAL EXPENDITURES

During 1986, the Corporation invested $23 million for new store equipment and leaseholds, upgrading of existing stores and equipment and for the Convenience Services Limited acquisition.

Goodwill of $6.8 million arising on this acquisition is being amortized on a straight line basis over 20 years.

This activity reflects the Corporation's continued commitment to increase those areas of the business with the best return for the long run. Those areas of the business that do not offer satisfactory potential are continuously reviewed. These strategies will result in long-term growth and improve returns for shareholders.

FOREIGN CURRENCY TRANSLATION

United States operations are included in the Consolidated Financial Statements at the following translation rates:

	1986	1985	1984
Translation of Foreign Operations — Assets & Liabilities year-end, $1.00 Cdn. =	**U.S.$0.73**	U.S.$0.72	U.S.$0.76
— Revenues & Expenses average, $1.00 Cdn. =	**U.S.$0.72**	U.S.$0.73	U.S.$0.77

Management's Responsibility for Consolidated Financial Statements

The preparation of the consolidated financial statements of Silcorp Limited is the responsibility of management in consultation with the Auditors. This responsibility includes the selection of appropriate accounting principles and the exercise of careful judgement in establishing reasonable and accurate estimates in accordance with generally accepted accounting principles applied on a consistent basis and as appropriate in the circumstances. Financial information shown elsewhere in this annual report is consistent with that contained in the consolidated financial statements.

Management of Silcorp Limited and its operating divisions has developed and maintains accounting systems and internal controls designed to provide reasonable assurance that assets are safeguarded from loss or unauthorized use and that the financial records are reliable.

The Board of Directors approves these financial statements and carries out its responsibility in this regard principally through the Audit Committee of the Board, a majority of whose members are outside directors. The Audit Committee regularly reviews the results of audit examinations performed by the internal auditors and independent external auditors with respect to the Corporation's accounting principles, practices and systems of internal control.

The financial statements have been examined by Clarkson Gordon, Chartered Accountants. Their report stating the extent of their audit examination and their opinion on the consolidated financial statements is presented below.

Chairman of the Board and
Chief Executive Officer

Eric F. Findlay

Eric F. Findlay

Vice-President and
Treasurer

Dale A Pettit

Dale A. Pettit

Auditors' Report

To the Shareholders
of Silcorp Limited

We have examined the consolidated balance sheet of Silcorp Limited as at December 28, 1986, and the consolidated statements of earnings, 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.

In our opinion, these consolidated financial statements present fairly the financial position of the Corporation as at December 28, 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.
Toronto, Canada
February 12, 1987.

Consolidated Statement of Earnings

Year ended December 28, 1986
(with comparative amounts for the years ended December 29, 1985 and December 30, 1984)
($000's)

	1986	1985	1984
Sales	**$651,534**	$551,184	$479,162
Less:			
Cost of sales	**459,247**	391,497	339,397
Divisional administrative and operating expenses	**167,338**	141,207	123,788
Depreciation and amortization (note 8(a))	**10,398**	8,330	6,449
	636,983	541,034	469,634
Operating income	**14,551**	10,150	9,528
General corporate expenses	**3,149**	2,581	2,514
Interest expense (note 8(b))	**4,760**	3,572	2,252
	7,909	6,153	4,766
Income before taxes	**6,642**	3,997	4,762
Income taxes (note 7)	**4,338**	1,716	2,047
Net earnings	**$ 2,304**	$ 2,281	$ 2,715
Earnings per Class "A" Non-Voting and "B" share (note 5):			
Net earnings — basic	**$ 0.83**	$ 0.85	$ 1.01
— fully diluted	**$ 0.81**		

Consolidated Statement of Retained Earnings

Year ended December 28, 1986
(with comparative amounts for the years ended December 29, 1985 and December 30, 1984)
($000's)

	1986	1985	1984
Balance, beginning of year	**$32,874**	$31,400	$29,492
Add net earnings	**2,304**	2,281	2,715
	35,178	33,681	32,207
Deduct dividends declared			
Class "A" Non-Voting	**571**	542	542
Class "B"	**265**	265	265
	836	807	807
Balance, end of year	**$34,342**	$32,874	$31,400

Consolidated Balance Sheet

December 28, 1986
(with comparative amounts at December 29, 1985 and December 30, 1984)
($000's)

	1986	1985	1984
ASSETS			
Current assets:			
Cash and short-term investments	$ 13,455	$ 11,182	$ 9,608
Accounts receivable	11,180	11,609	7,982
Inventories	45,886	41,604	36,005
Prepaid expenses	2,742	2,378	2,249
Store properties under development	14,557	12,138	3,326
Income taxes receivable			217
	87,820	78,911	59,387
Fixed assets (note 1)	67,977	60,956	50,391
Other assets (note 2)	21,242	13,254	11,628
	$177,039	$153,121	$121,406
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current liabilities:			
Bank indebtedness		$ 28,584	$ 3,831
Accounts payable and accrued charges	$ 61,045	51,793	48,165
Income taxes payable	2,783	122	
Current portion of long-term debt and capital lease obligations (note 3)	196	3,348	1,147
	64,024	83,847	53,143
Deferred revenue	1,908	1,877	688
Deferred income taxes	5,864	3,460	2,710
Long-term debt and capital lease obligations (note 3)	114	20,025	24,847
	71,910	109,209	81,388
Convertible subordinated debentures (note 4)	60,000		
	131,910	109,209	81,388
Shareholders' equity:			
Capital stock (note 5)	8,728	8,728	7,341
Retained earnings	34,342	32,874	31,400
Deferred foreign currency translation gain	2,059	2,310	1,277
	45,129	43,912	40,018
	$177,039	$153,121	$121,406

On behalf of the Board

Eric L. Findlay

Director

Director

Consolidated Statement of Cash Flows

Year ended December 28, 1986
(with comparative amounts for the years ended December 29, 1985 and December 30, 1984)
($000's)

	1986	1985	1984
Cash provided by (used in) operating activities:			
Net earnings	**$ 2,304**	$ 2,281	$ 2,715
Charges to net earnings which do not affect cash:			
Depreciation and amortization	**10,398**	8,330	6,449
Deferred income taxes	**2,320**	750	20
Cash flow from operations	**15,022**	11,361	9,184
Net change in non-cash working capital	**2,031**	(14,200)	(7,561)
Other	**75**	(258)	1,250
Cash provided by (used in) operating activities	**17,128**	(3,097)	2,873
Cash provided by (used in) investment activities:			
Additions to fixed assets	**(16,224)**	(21,323)	(17,049)
Acquisition of Convenience Services Limited	**(6,825)**		
Purchase of goodwill		(86)	(57)
Net proceeds from disposal of fixed assets	**3,087**	3,448	4,028
Cash provided by (used in) investment activities	**(19,962)**	(17,961)	(13,078)
Cash provided by (used in) financing activities:			
Issue of convertible subordinated debentures	**57,837**		
Issue of capital stock		1,387	
Net change in long-term debt	**(19,687)**	(2,012)	(4,632)
Net change in capital lease obligations	**(3,623)**	(689)	(722)
Dividends to shareholders	**(836)**	(807)	(807)
Cash provided by (used in) financing activities	**33,691**	(2,121)	(6,161)
Net increase (decrease) in cash during the year	**30,857**	(23,179)	(16,366)
Cash position, beginning of year	**(17,402)**	5,777	22,143
Cash position, end of year	**$ 13,455**	$ (17,402)	$ 5,777
Represented by:			
Cash and short-term investments	**$ 13,455**	$ 11,182	$ 9,608
Bank indebtedness		(28,584)	(3,831)
	$ 13,455	$ (17,402)	$ 5,777

Summary of Significant Accounting Policies

Year ended December 28, 1986

The consolidated financial statements present the financial position, results of operations and cash flows of the company in accordance with generally accepted accounting principles applied on a consistent basis. The significant accounting policies are summarized as follows:

Principles of consolidation
The consolidated financial statements include the accounts of all subsidiary companies. Intercompany accounts and transactions have been eliminated.

The results of operations of all subsidiaries are included only from the dates of their respective acquisitions.

Definition of fiscal year
The fiscal year of Silcorp Limited for 1986 ended on December 28, 1986 and for 1985 and 1984, on December 29 and 30 respectively. The 1986 and 1985 fiscal years comprised fifty-two weeks each and 1984 fiscal year comprised fifty-three weeks.

Short-term investments
Short-term investments are stated at cost which equals market value.

Inventories
Inventories are valued at the lower of cost and estimated net realizable value. Cost is determined by the retail method (retail price less normal margin) for convenience stores' inventories and the first-in, first-out method for other inventories.

Store properties under development
Store properties under development consist of land and buildings which are to be sold for cash and leased back.

Fixed assets
Fixed assets are carried at cost. Depreciation and amortization are provided on a straight-line basis over the estimated useful lives of the assets, generally at rates of 2 1/2% for buildings, 10% for machinery and merchandising equipment, and term of the lease for leasehold improvements.

Leases
Leases are classified as capital or operating leases. A lease that transfers substantially all of the benefits and risks incident to the ownership of property is classified as a capital lease. All other leases are accounted for as operating leases wherein rental payments are expensed as incurred. Assets recorded under capital leases are amortized on the same straight-line method described above.

Goodwill
Goodwill includes amounts arising from the excess of the purchase price of subsidiaries over the fair market value of the underlying assets and purchased goodwill.

Goodwill acquired prior to January 1, 1974 is carried at cost, less net proceeds from any disposals.

Goodwill acquired after December 31, 1973 is being amortized on a straight-line basis over periods of five to twenty years.

Debenture issue expense
Expenses associated with the issue of convertible subordinated debentures are amortized over twenty years, the term of the issue.

Deferred revenue
Deferred revenue consists substantially of the non-current portion of prepaid rentals arising from distributor arrangements relative to the sale of gasoline.

Income taxes
The Corporation follows the deferral method of tax allocation accounting. The deferrals arise substantially from claiming capital cost allowance for income tax purposes in excess of depreciation and amortization charged to consolidated earnings. Future income tax recoveries relating to losses are provided for only when it is virtually certain, in the loss year, that earnings in future years will be sufficient to make such recoveries possible.

Translation of foreign operations
At December 28, 1986 all assets and liabilities of USSIL Corporation, FarrView Limited and Hop-In Food Stores, Inc., wholly-owned subsidiaries, are translated at the year-end rate of U.S.$0.73 (U.S.$0.72 — 1985, U.S.$0.76 — 1984) = $1.00 Cdn. Revenue and expenses are translated at the average rates of exchange for the year. Gains or losses which result from translation are deferred and included in shareholders' equity on the consolidated balance sheet. These gains or losses will be included in consolidated earnings when realized.

Year ended December 28, 1986
(Tabular amounts in $000's except for Notes 5. and 7.)

1. Fixed assets

	1986	1985	1984
Land	**$ 879**	$ 988	$ 1,692
Buildings	**5,058**	4,943	6,221
Machinery and equipment	**9,732**	7,603	7,764
Merchandising equipment	**73,801**	63,229	49,834
Leasehold improvements	**24,479**	21,635	15,982
	113,949	98,398	81,493
Less accumulated depreciation and amortization	**45,972**	37,442	31,102
Net book value	**$67,977**	$60,956	$50,391

Included in the net book value of Fixed assets are assets under capital lease amounting to $232,000 for 1986, $3,149,000 for 1985, and $3,830,000 for 1984.

2. Other assets

	1986	1985	1984
Goodwill	**$15,665**	$ 9,698	$ 9,750
Debenture issue expense, at amortized cost	**2,105**	192	247
Other assets	**3,472**	3,364	1,631
	$21,242	$13,254	$11,628

3. Long-term debt and capital lease obligations

	1986	1985	1984
Long-term debt			
Floating rate redeemable debentures	**$**	$16,500	$16,500
Sinking fund debentures Series A		2,779	3,110
Mortgages payable	**88**		971
Term notes payable		232	919
Lease deposits		10	9
	88	19,521	21,509
Less portion due within one year included in current liabilities	**88**	2,811	508
		16,710	21,001
Capital lease obligations	**222**	3,852	4,485
Less portion due within one year included in current liabilities	**108**	537	639
	114	3,315	3,846
Long-term debt and capital lease obligations	**$ 114**	$20,025	$24,847

4. 8% Convertible Subordinated Debentures — due June 30, 2006

The $60,000,000 8% convertible debentures, issued June 26, 1986, are unsecured obligations and subordinated to all other indebtedness of the Corporation.

The debentures pay interest semi-annually on June 30 and December 31 and are convertible at the holder's option at any time prior to June 30, 1993 at a conversion price of $20.75 per Class "A" Non-Voting share.

The debentures are redeemable between January 1, 1989 and June 30, 1993 if the market value of the Class "A" Non-Voting shares exceeds 125% of the conversion price. After June 30, 1993, the debentures will be redeemable at any time at the option of the Corporation.

5. Capital stock

(a) Details at December 28, 1986 are set out below:

— Class "A" Non-Voting shares without par value, non-voting except in restricted circumstances, entitled to cumulative, preferential dividends of $.30 per share per annum payable quarterly and, after the Class "B" shares have received $.30 per share in any one year, to further participation rateably with Class "B" shares; entitled in liquidation to a priority of $7.50 per share.

— Class "B" shares without par value.

	CLASS "A" NON-VOTING SHARES	CLASS "B" SHARES	PAID UP CAPITAL
Authorized	6,000,000	1,000,000	
Issued	1,904,316	882,424	$8,728,000

The authorized and issued capital stock did not change during fiscal year 1986.

(b) In 1985, 190,000 Class "A" Non-Voting shares were originally set aside for issuance pursuant to the employee Management Share Purchase Plan and Management Share Option Plan. To date, 98,000 shares have been issued under the Management Share Purchase Plan. Loans, repayable over 10 years, to finance these purchases amounted to $1,364,650 at December 28, 1986 ($1,386,700 at December 29, 1985) and are included in Other assets.

(c) Earnings per share have been calculated using the weighted daily average number of shares outstanding during the year.

Fully diluted earnings per share have been calculated as if all of the convertible debentures which were issued on June 26, 1986 had been converted into 2,891,566 Class "A" Non-Voting shares at the time of issue.

The number of shares used in calculating earnings per share is as follows:

	1986	1985	1984
Basic	**2,786,740**	2,696,009	2,688,740
Fully diluted	**4,264,330**		

6. Operating lease agreements and commitments

(a) Operating lease agreements
Silcorp Limited and its subsidiary companies have entered into agreements to lease equipment and properties for various periods up to 2005. Certain of the leases provide for additional rent based on sales. Minimum annual net rental commitments for non-cancellable leases in effect at December 28, 1986 are as follows:

Year ended	Amount
December 27, 1987	$33,203
December 25, 1988	31,643
December 24, 1989	29,253
December 23, 1990	26,538
December 29, 1991	22,179

Net lease comitments to year 2005 aggregating $205.9 million have been reduced by payments totalling $22.4 million for which the Corporation is to be reimbursed by franchisees who are subtenants of the Corporation.

(b) Pension plans
The actuaries have advised the Corporation that in the aggregate there is no unfunded liability at December 28, 1986. Current service costs are funded and charged to operations as they accrue.

7. Income taxes

A reconciliation of the basic income tax rate to the effective rate for the Corporation is as follows:

	1986	1985	1984
Basic rate	**52.9%**	51.3%	50.0%
Inventory allowance	**(1.0)**	(11.6)	(9.0)
Non-recognition of losses in subsidiaries	**14.2**	6.7	8.0
Other permanent differences	**(0.8)**	(3.4)	(6.0)
	65.3%	43.0%	43.0%

No accounting recognition has been given to approximately $1,745,000 of future tax savings which may result from the carry-forward of cumulative losses by certain of the Corporation's subsidiaries.

8. Other information

(a) Depreciation and amortization includes charges to earnings for the following:

	1986	1985	1984
Fixed assets —			
Owned	**$ 8,866**	$7,210	$5,323
Leased	**465**	664	687
Debenture issue expense	**284**	55	54
Goodwill	**783**	401	385
	$10,398	$8,330	$6,449

(b) Interest expense includes the following charges (credits) to earnings:

	1986	1985	1984
Long-term debt	**$3,525**	$2,113	$2,999
Capital lease obligations	**380**	638	755
Short-term debt	**2,523**	3,286	441
Interest income from deposits and investments	**(1,668)**	(2,465)	(1,943)
	$4,760	$3,572	$2,252

9. Legal proceedings

In the ordinary course of business, a number of legal suits are outstanding, the resolution of which, in the opinion of management, will not have a material effect on the Corporation's financial position.

10. Acquisition

On January 3, 1986, Silcorp Limited acquired all the outstanding shares of Convenience Services Limited for $6,825,000 cash. Details of the acquisition were as follows:

Fair value of tangible assets	$8,515
Fair value of liabilities	8,515
Excess of fair value of tangible assets over liabilities	nil
Goodwill	6,825
Total purchase price	$6,825

Goodwill arising on this transaction will be amortized over 20 years commencing in 1986.

11. Comparative figures

Certain of the comparative amounts in the accompanying financial statements have been restated to reflect the presentation adopted in the current year.

12. Segmented Information

The Statement of Segmented Information appears in detail on page 7.

Corporate Information

OPERATING DIVISIONS:

Mike's Mart
Barrie, Ontario

Joseph E. Lewis
President

David R. Rodgers
Director of Store Operations

Scott F. Findlay
Director of Merchandising

Robert K. Moffat
Controller

Mac's Convenience Stores
Scarborough, Ontario

Derek M. Ridout
President

Russell F. Egerdie
Executive Vice-President, Finance and Administration

Robert E. Scott
Vice-President, Operations

Richard C. Broadhead
Vice-President, Marketing

Bernard J. Harrington
Vice-President, Real Estate

John I. Fraser
General Manager, Eastern Region

Donald A. Cameron
General Manager, Western Region

Kenneth J. Barnett
Treasurer and Chief Financial Officer

Baskin-Robbins Ice Cream
Toronto, Ontario

Craig F. Findlay
Canadian Director

H. Stanley White
Director, Marketing and Operations

Henry G. Hudel
Director, Franchising and Real Estate

Ninian W. Sanderson
Manager, Administration

Peter D. Hopps
Director of Plant Operations

Kevin M. Hammond
Controller

FarrView
Milford, Michigan

John DeWit
President

Charles A. Androsky
Vice-President, and Chief Financial Officer

Thomas H. Becker
Manager, Operations

Barbara J. Barrett
Manager, Marketing and Merchandising

Roger D. Nash
Controller

Hop-In Food Stores
Roanoke, Virginia

N. Ronald Adams
President

Glenn J. LiFonti
Vice-President, Operations

Peter L. Surprenant
Vice-President, Real Estate

Douglas M. Doane
Personnel Director

SILCORP LIMITED:

Officers

Eric F. Findlay
Chairman of the Board and Chief Executive Officer

Robert S. Maich
President and Chief Operating Officer

Dale A. Pettit
Vice-President and Treasurer

A. Clifford Denny
Vice-President, Corporate Planning and Management Information

William P. Thomas
Vice-President, Secretary and General Counsel

Robert C. Ferguson
Controller

Larry M. Hurst
Assistant Treasurer

Betty-Ann Lipke
Assistant Secretary

Head Office
6205 Airport Road
Mississauga, Ontario
L4V 1E1
(416) 678-9700

Listed — SIL
"A" Non-Voting and "B" Shares
Toronto Stock Exchange
Montreal Exchange

Transfer Agents
The Canada Trust Company
Toronto, Calgary and Vancouver

Auditors
Clarkson Gordon
Chartered Accountants
Toronto, Ontario

Committees of the Board of Directors

Executive Committee
Eric F. Findlay*
William A. Dimma
Robert S. Maich
William A. Stewart
J. Allyn Taylor
Donald H. Thain
David B. Weldon

Audit Committee
J. Allyn Taylor*
W.I. (Irv) Barton
Eric F. Findlay
Donald H. Thain
David B. Weldon

Compensation Committee
William A. Dimma*
Robert J. Butler
J. Trevor Eyton
Eric F. Findlay
David B. Weldon

Pension Committee
David B. Weldon*
William A. Dimma
Eric F. Findlay
Donald H. Thain

*Committee Chairman

Silcorp Limited

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