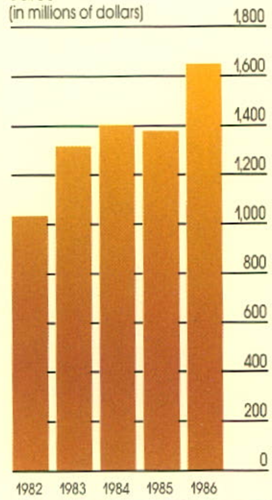
METRO-RICHELIEU

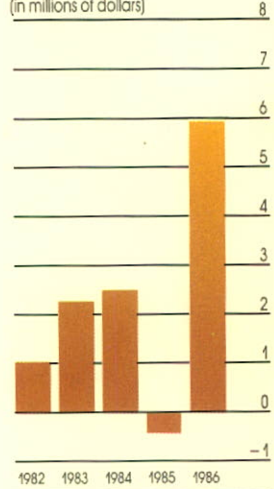
Annual Report 1986

Financial highlights

Sales
(in millions of dollars)

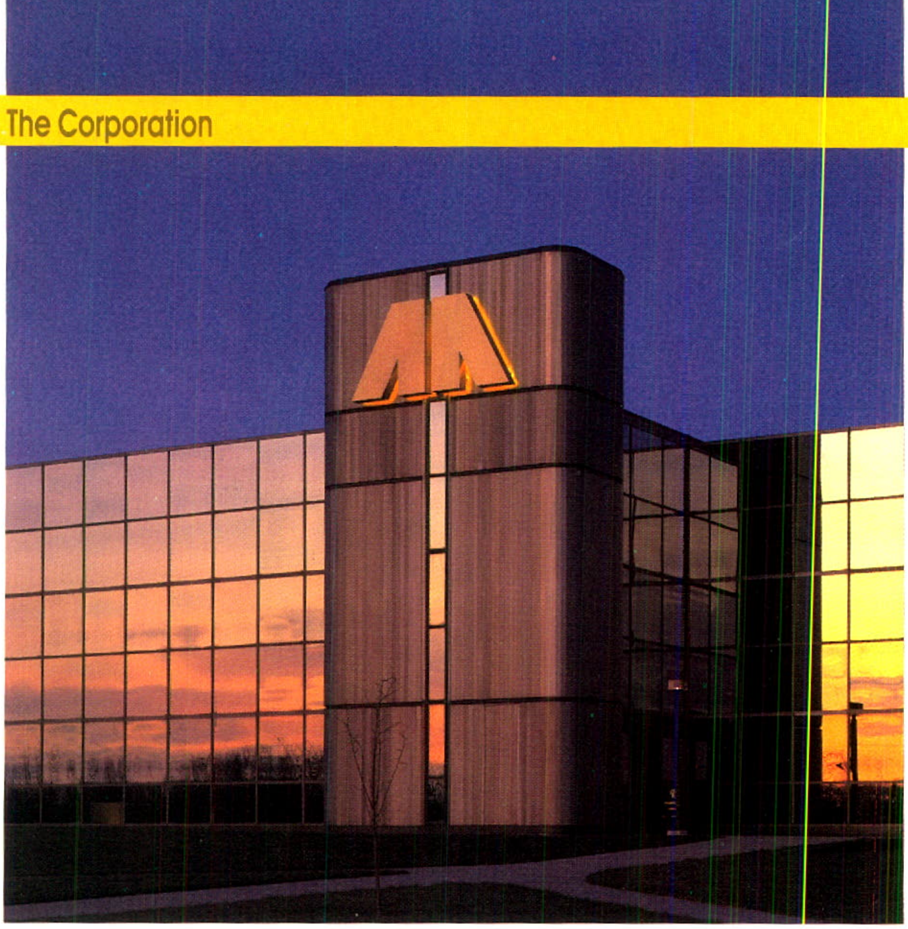


Net Earnings
(in millions of dollars)

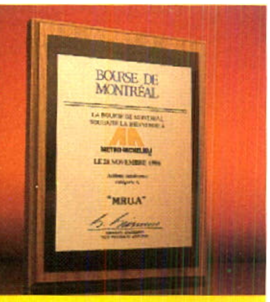


Year ended September 27, 1986
(in thousand of dollars)

		1986	1985	1984	1983	1982
Operations	Sales	**$ 1 659 413**	$ 1 389 704	$ 1 404 203	$ 1 325 307	$ 1 042 997
	Earnings from operations	**30 318**	19 870	26 103	15 608	11 556
	Financial expenses	**11 015**	13 873	14 278	7 548	6 621
	Depreciation and amortization	**9 409**	8 745	8 473	4 920	3 362
	Income taxes	**3 913**	(1 682)	824	837	683
	Earnings (loss) before extra-ordinary item	**5 981**	(1 066)	2 528	2 303	890
	Net earnings (net loss)	**5 981**	(417)	2 528	2 303	1 144
Financial position	Current assets	**153 686**	143 567	119 635	120 818	109 135
	Current liabilities	**133 903**	136 262	107 302	107 823	92 002
	Working capital	**19 783**	7 305	12 333	12 995	17 133
	Fixed assets	**91 404**	84 456	85 665	84 130	57 591
	Long term liabilities	**79 226**	64 949	88 219	87 791	65 779
	Shareholders equity	**44 404**	33 624	15 626	15 915	12 373
Ratios	Working capital	**1,15**	1,06	1,12	1,12	1,19
	Long term liabilities/ shareholders equity	**1,79**	1,94	5,65	5,52	5,32
	Interests coverage	**1,90**	,81	1,24	1,42	1,24



1928 Epiciers Unis Inc.
1940 Epiceries Richelieu Limitee
1947 Magasins LaSalle Stores Limitée
1952 Les Epiceries LaSalle Groceteria Limitée
1963 Les Marchés d'Aliments Metro-LaSalle Ltée
1972 Marchés d'Aliments Métro Limitée
1979 Groupe Métro-Richelieu Inc.
1982 Groupe des Épiciers Unis Métro-Richelieu Inc.
1986 MÉTRO-RICHELIEU INC.



Metro-Richelieu Inc., Canada's largest independently owned food distributor, ranks high among Canada's 500 largest companies and holds a predominant place among the most progressive companies in Quebec.

Metro-Richelieu serves both affiliated and non-affiliated retailers, independent buyers as well as many institutions throughout Quebec.

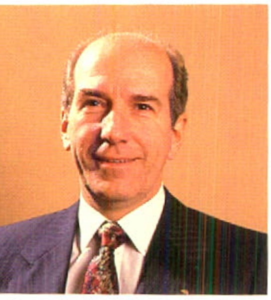
Through the combined operation of its sales outlets, central divisions, corporate divisions and head office, Métro-Richelieu has been able to penetrate all sectors of the food industry.

Métro-Richelieu employs some 2,400 people, while approximately 15,000 more work in affiliated stores. Its modern warehouses in Montreal, Quebec City and Mont-Joli, sophisticated data processing centre, and efficient communications system allow its retailers and clients to maximize the profitability of their operations and maintain their lead in an increasingly competitive market.

Principal Subsidiaries

- Epiciers Unis Métro-Richelieu Inc.
- Soc. Immobilière Devimont Inc.
- Alimentation Dallaire St-Romuald Inc.
- McMahon-Essaim Inc.

Marcel Beaulieu
Chairman of the Board of Directors



Aimé Gagnon
Vice-Chairman

Jean-Claude Messier
Secretary

Bernard Belair
Treasurer

During the 1985-1986 fiscal year, Metro-Richelieu achieved a high rate of growth, enabling it, more than ever, to face the future with complete confidence. We can be proud of the results obtained by our revitalization program, at both wholesale and retail levels.

Despite stiff and relentless competition, Metro-Richelieu constantly increased its purchasing power and the quality of its services, thereby enabling it to maintain, and even increase, its market share.

The various commercial incentive programs introduced were extremely popular. The volume rebate program, for example, enabled the Company to significantly increase purchases in its divisions.

Our success has enabled us to plan major investments outside the food industry. With the diversification of its activities, Metro-Richelieu is supporting its development and acquiring the capacities and skills indispensable for achieving its goals.

First, the acquisition of a very large Quebec pharmaceutical products wholesaler, McMahon-Essaim, will give us a new opportunity to put our interests and experience to profitable use.

Second, the creation of Metro-Na, a company formed jointly with the RO-NA group, will enable us to take advantage of economies of scale by combining some of our services. Inspired by the symbiotic relationship between companies that characterized the Japanese miracle, the aim of this association is to improve the competitive positions of both companies.

By emphasizing the quality and quantity of services offered and committing ourselves to new endeavours, we shall ensure the success of the Company. The team spirit and confidence shown by our merchants encourage us to continue in this direction.

During the past two years, Metro-Richelieu has made considerable progress in reinforcing its financial structure and keeping pace with the other major food distributors in Quebec.

First, at a special general meeting held on June 26, 1985, the corporate shareholders unanimously agreed to convert their advances into capital stock.

Marcel Guertin
Director

Jean-Marie Vincent
Director

Benoit Gadoury
Director

Jean Dabate
Director

Roland Ferland
Director

Roger Lévesque
Director

This gesture, made during a period of uncertainty, clearly demonstrated the will of the merchants to restore their company to its full growth potential.

Second, they agreed, again unanimously, on September 24, 1986, to amend the by-laws so that Métro-Richelieu could tender a public offering in order to be truly adapted to the needs of the second half of the decade.

The offering of 5,060,000 class A subordinate shares priced at $6.00 a share was tendered on November 28, 1986 and, to our great satisfaction, public response was extremely favourable. The success of this initial offering, which was eligible for the QSSP, has been most encouraging.

As part of the public offering, the Company set up a financing program facilitating the purchase of shares by employees. It should be noted that 1,314 employees, i.e., more than half, took advantage of this opportunity. In our opinion, this is a unique and highly revealing development.

Maintaining the openness that has always characterized it, Metro-Richelieu marked its arrival on the stock market by welcoming two new outside directors, whose expertise and vision will assuredly be an asset to the Company.

Our change of status from a private to a public company will in no way affect the importance placed on communications with shareholder merchants. Métro-Richelieu will continue its policy of consultation through regional gatherings, advertising campaigns, conventions, etc.

During the past few months, our company officially adopted a new name: Métro-Richelieu Inc. A new corporate logo, composed of two distinct emblems, has also been created. It pays tribute to our origins and bears witness to the human resources that, from the beginning, have contributed to our success.

Our present outlook is most favourable. Our management team is young and aggressive; our board of directors, experienced and stable; our employees, highly motivated; and our shareholder merchants, solidly behind the team. They have been responsible for our success in the past and provide a strong base for our future development.

After some 20 years as a director, including three as Chairman of the Board, I have completed my mandate and am leaving with a feeling of satisfaction at having been able to serve you in this capacity.

The Chairman of the Board

Marcel Beaulieu

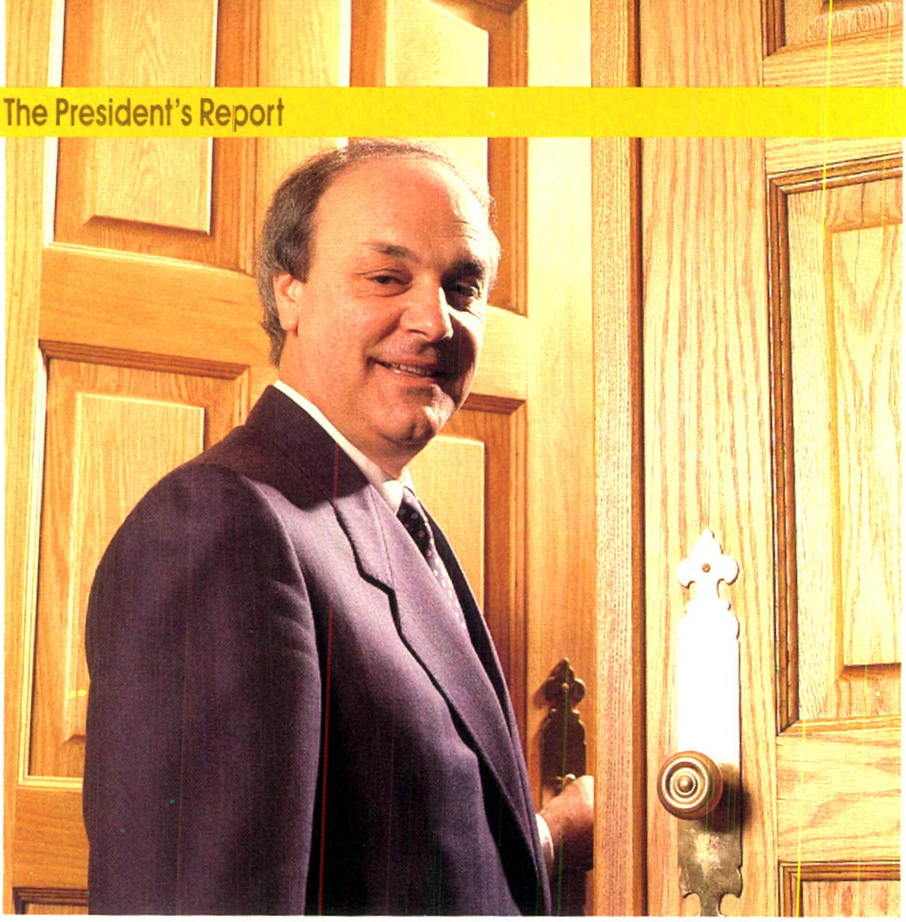
Marcel Beaulieu
December 19, 1986

Gaston Blackburn
Director

Jacques Laliberté
Director

Réal Brouillette
Director

The President's Report



Jacques L. Maltais
President and
Chief Executive Officer

Raymond Bachand
Vice-President
Planning and Development

André Roy
Vice-President
Administration

Rejean Bouchard
Assistant to the President

Fiscal 1985-1986 was a year of intense activity. Metro-Richelieu Inc. continued to rationalize its operations with a view to diversification.

In 1986, the food industry achieved little or no real growth, due to economic deflation. Nevertheless, Métro-Richelieu managed to consolidate its market share and then increasing it considerably.

Sales gained 19.4% over the previous fiscal year, going from $1,389,704,000 to $1,659,413,000. This increase enabled our company to show an operating profit of $30,318,000, i.e., a gain of 52.6%.

Earnings for the 1985-1986 fiscal year, before income taxes and extraordinary items, were $12,642,000 higher than in the previous year. Net earnings increased to $5,981,000, compared with a net loss of $417,000 in the previous year.

A major effort was made to find the best way to respond to the needs of our members, clients and consumers. The concrete results achieved, both inside and outside the Company, confirm the effectiveness of our approach.

Métro-Richelieu's current financial health enables it to look to the future with confidence.

The Company's organizational structure makes it possible to serve a range of business sectors, both in the retail and the institutional markets. It also enables us to manage our central and corporate divisions, the foundation of Metro-Richelieu's operation, more efficiently.

In order to accelerate the storage and retrieval of information and make our services more efficient, we invested heavily in the upgrading of our data processing system. As a result, our capacity to store information has increased significantly.

Métro-Richelieu's current package of commercial incentive programs has been extremely popular with our retailer-shareholders. The renovation program encourages the modernization of retail outlets in a context where improvements must follow market trends.

Jacques Obry
Vice-President, Groce
Fruits and Vegetables

Gaetan Frigon
Vice-President,
Marketing and Head
of Retail Operations

The volume rebate program encourages dealers to concentrate their purchases within the divisions of the Company. The discount program for featured products responds to the needs of consumers, thereby contributing to customer satisfaction.

The success of each banner confirms the effectiveness of the measures we have taken in both marketing and distribution. The Métro banner continued its recovery, which started in 1985 when the chain made a commitment to satisfy the current needs of consumers. As for the Richelieu banner, becoming Marché Richelieu was a step in the right direction and should increase this banner's share of the market.

The corporate divisions also saw a significant increase in sales. Because of the increasing activity in this sector, a new vice-president was appointed to co-ordinate development.

The diversification of Métro-Richelieu's clientele in recent years has had a considerable effect on the Company's operations. In 1981, 95% of sales were made to Métro and Richelieu retailers. Today, just five years later, sales to other customers account for 25% of our business.

In November 1986, Métro-Richelieu took a giant step in its development by tendering a public stock offering. Diversification into sectors other than food is a must for a large organization such as ours; it will enable us to innovate and move towards new areas of operation.

It is important to mention here the excellent working environment at Métro-Richelieu. During the 1985-1986 fiscal year, no conflict disrupted our operations and the collective agreements that expired were renewed to the satisfaction of all parties.

We could not end this brief overview without a word of appreciation for all Métro-Richelieu employees. Their talents and motivation made a vital contribution to the success of the Company. As well, our management team showed great solidarity in their approach to decision-making.

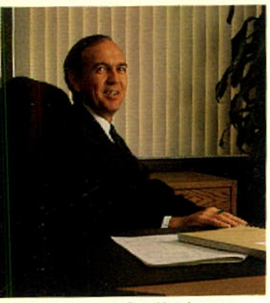
We would especially like to emphasize the personal contribution of our Chairman of the Board, Mr. Marcel Beaulieu. Métro-Richelieu has benefited greatly from his abilities as a director and a retailer. His term as Chairman of the Board ends on a note of prosperity with excellent prospects for the future.

At the beginning of 1987, we are more than ever convinced that Métro-Richelieu will remain an indisputed leader in the food industry in Quebec, while pursuing a policy of diversification that will further strengthen our company's operational base.

The President and Chief Executive Officer

Jacques L. Maltais

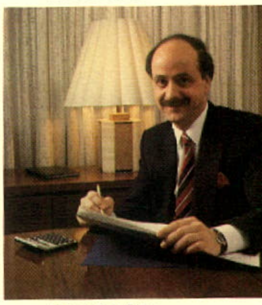
Jacques L. Maltais
December 19, 1986



L.G. Serge Gadbois, c.a.
Vice-President
Finance

Denise Martin
Vice-President
Information Systems

Paul Laporte
Vice-President
Distribution



Charles Roy
Vice-President
Corporate Divisions

Lawrence Timmons
Vice-President
Meats and frozen foods

Guy Piuze
Vice-President
Human Resources

METRO-RICHELIEU

Financial Report 1986

Report from Senior Management

The consolidated financial statements

Métro-Richelieu's consolidated financial statements, as well as the financial information contained in this report, are the responsibility of senior management. The consolidated financial statements have been prepared in accordance with generally accepted accounting principles, and have been approved by the Board of Directors.

Métro-Richelieu maintains a system of accounting and administrative controls which, in the view of senior management, reasonably assures exact financial information. These controls also contribute to the efficient, well-ordered management of the company.

The Board of Directors is responsible for approving the consolidated financial statements contained in this annual report, principally through its Audit Committee. This committee, which holds regular meetings with members of the senior management team, as well as the internal and external auditors, has reviewed Métro-Richelieu's consolidated financial statements, and recommended their approval by the Board of Directors.

The consolidated financial statements have been audited by the chartered accounting firm Mallette, Benoit, Boulanger, Rondeau & Associés. The report they have prepared indicates the extent of their audit and their opinion on the following consolidated financial statements.

President
and Chief Executive Officer

Jacques L. Maltais

Jacques L. Maltais

Vice-President,
Finance

L.G. Serge Gadbois

L.G. Serge Gadbois, c.a.

Auditors' report

To the Shareholders of
Métro-Richelieu Inc.
(formerly Groupe des Épiciers Unis Métro-Richelieu Inc.)

We have examined the consolidated balance sheet of MÉTRO-RICHELIEU INC. as at September 27, 1986 and the consolidated statements of earnings, retained earnings and changes in financial position for the year ended September 27, 1986. 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 company as at September 27, 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.

Mallette, Benoit, Boulanger, Rondeau & Associés
Chartered Accountants

Montreal,
November 14, 1986

Consolidated statement of earnings

year ended September 27, 1986

		1986	1985
		(in thousands of dollars)	
Sales		**$ 1 659 413**	$ 1 389 704
Cost of sales and operating expenses		**1 629 095**	1 369 834
Earnings from operations		**30 318**	19 870
Other expenses	Financial –		
	Short-term	**2 617**	3 271
	Long-term	**7 326**	7 476
	Loans from shareholders	**1 072**	3 126
	Depreciation and amortization (note 3)	**9 409**	8 745
		20 424	22 618
Earnings (loss) before income taxes and extraordinary item		**9 894**	(2 748)
Income taxes	Current	**330**	11
(note 4)	Deferred	**3 583**	(1 693)
		3 913	(1 682)
Earnings (loss) before extraordinary item		**5 981**	(1 066)
Extraordinary item (note 5)		**—**	649
Net earnings (net loss)		**$ 5 981**	$ (417)

Earnings per share
(note 16)

Consolidated statement of retained earnings

year ended September 27, 1986

		1986	1985
		(in thousands of dollars)	
Balance, at the beginning		$ 2 764	$ 4 268
Add:	Net earnings	5 981	—
	Transfer of the excess of the appraised value of fixed assets over cost	12	13
		8 757	4 281
Deduct:	Net loss	—	417
	Excess of the redemption price of shares over their stated value	566	417
	Dividends on preferred shares	106	683
		672	1 517
Balance, at the end		$ 8 085	$ 2 764

Consolidated statement of changes in financial position

year ended September 27, 1986

		1986	1985
		(in thousands of dollars)	
Operating activities	Earnings (loss) before extraordinary item	$ **5 981**	$ (1 066)
	Depreciation and amortization	**9 409**	8 745
	Loss (gain) on disposal of fixed assets and other assets	**573**	(130)
	Deferred income taxes	**3 583**	(1 693)
		19 546	5 856
	Net change in working capital, excluding cash	**21 465**	(14 355)
	Cash provided from (applied to) operating activities	**41 011**	(8 499)
Financing activities	Increase of long-term debt	**20 760**	3 458
	Repayment of long-term debt	**(5 003)**	(4 033)
	Increase of loans from shareholders	**2 270**	6 598
	Repayment of loans from shareholders	**(5 930)**	(27 188)
	Issuance of capital stock	**6 478**	20 349
	Redemption of capital stock	**(1 573)**	(1 250)
	Cash provided from financing activities	**17 002**	(2 066)
Investing activities	Purchase of fixed assets	**(16 566)**	(9 197)
	Disposal of fixed assets and other assets	**857**	3 634
	Net change in investments	**2 710**	(2 082)
	Net change in other assets	**(7 659)**	(1 387)
	Cash applied to investing activities	**(20 658)**	(9 032)
Dividends		**(106)**	(683)
Net increase (net decrease) in cash		**37 249**	(20 280)
Cash deficiency, at beginning of year		**(75 082)**	(54 802)
Cash deficiency, at end of year		**$ (37 833)**	$ (75 082)

Cash includes outstanding cheques and bank loans.

Assets

As of September 27, 1986

Assets		1986	1985
		(in thousands of dollars)	
Current assets	Accounts receivable	$ 71 354	$ 68 400
	Income taxes	459	702
	Inventories	77 306	69 224
	Prepaid expenses	3 989	2 760
	Current portion of investments (note 6)	578	2 481
		153 686	143 567
Investments (note 6)		895	1 702
Fixed assets (note 7)		91 404	84 456
Other assets (note 8)		11 548	5 110
		$ 257 533	$ 234 835

On behalf of the board

Marcel Beaulieu

Marcel Beaulieu
Chairman of the Board

Bernard Bélair

Bernard Bélair
Treasurer

Liabilities		1986	1985
		(in thousands of dollars)	
Current liabilities	Outstanding cheques	$ 34 226	$ 45 611
	Bank loans	3 607	29 471
	Accounts payable and accrued liabilities	88 204	54 717
	Current portion of long-term debt and loans from shareholders (notes 9 and 10)	7 866	6 463
		133 903	136 262
Long-term debt (note 9)		68 350	53 954
Deferred income taxes		5 281	1 698
Loans from shareholders (note 10)		5 595	9 297
Shareholders' equity	Capital stock (note 11)	35 540	30 051
	Retained earnings	8 085	2 764
	Contributed surplus (note 12)	193	211
	Excess of the appraised value of fixed assets over cost	586	598
		44 404	33 624
		$ 257 533	$ 234 835

1- Incorporation and change of name:

The company is governed by Part 1A of the Companies Act (Quebec). On September 25, 1986, the company obtained a certificate of amendment changing its name from United Grocers Métro-Richelieu Group Inc. to Métro-Richelieu Inc.

2- Summary of the principal accounting policies:

a) Consolidation
The consolidated financial statements include the accounts of the company and those of its wholly-owned subsidiaries.

b) Foreign currency translation
Monetary items expressed in foreign currencies are translated into Canadian dollars at current rates of exchange prevailing at year-end and non-monetary items are translated at historical rates. Items appearing in the consolidated statement of earnings are translated at historical rates. Foreign exchange gains or losses are included in the consolidated statement of earnings.

c) Inventory valuation
Inventories are valued at the lower of cost (generally determined on a first-in, first-out basis) and net realizable value.

d) Investments
Investments are accounted for at the lower of cost and net realizable value.

e) Fixed assets, fixed assets under capital leases and depreciation
Fixed assets and fixed assets under capital leases are accounted for at cost, except for land and a building which were appraised in 1968.

Depreciation of fixed assets and fixed assets under capital leases are recorded using the straight-line method at the following rates:

Land improvements	2½% to 5%
Buildings	2½%
Machinery, office furniture and equipment	2½% to 25%
Rolling stock	10% to 25%
Leasehold improvements	term of the leases

f) Other assets and amortization
Other assets are accounted for at cost and the amortization is recorded using the straight-line method at the following rates:

Goodwill	2½% to 5%
Amalgamation expenses, start-up costs and other	20% to 33⅓%

g) Excess of the appraised value of fixed assets over cost
The excess is transferred to retained earnings when realized through depreciation or sale of appraised fixed assets.

h) Income taxes
Income taxes are accounted for using the tax allocation method which takes into account timing differences between taxable income and accounting income.

i) Rebates and commercial incentive programs
Rebates and the cost of commercial incentive programs granted to shareholder customers are accounted for in the consolidated statement of earnings under the caption cost of sales and operating expenses.

j) Comparative figures
Certain figures for the preceding year have been reclassified to conform with the presentation used for the current year.

3- Earnings:

The consolidated statement of earnings includes the following items:

	1986	1985
	(in thousands of dollars)	
a) Depreciation and amortization:		
Fixed assets	**$ 8 553**	$ 7 772
Other assets	**856**	973
	$ 9 409	$ 8 745
b) Rebates	**$ 2 825**	

4- Income taxes:

The actual income tax rates of the company are as follows:

	1986	1985
Statutory income tax rates	**42.71 %**	(41.50)%
Inventory allowance	**(3.71)**	(25.40)
Other	**0.55**	5.66
	39.55 %	(61.24)%

5- Extraordinary Item:

The extraordinary item for the year ended September 28, 1985 represents a gain on insurance indemnity of $649 000, after a deduction for related income taxes of $222 000, and represents the excess of insurance proceeds over the net book value of the fixed assets which were destroyed.

6- Investments:

	1986	1985
	(in thousands of dollars)	
Loans and advances to shareholders, repayable over a two to five year period, bearing interest at variable rates	**$ 1 198**	$ 2 203
Loans to companies related to two Directors of the company	**–**	1 746
Other	**275**	234
	1 473	4 183
Current portion	**578**	2 481
	$ 895	$ 1 702

7- Fixed Assets:

	1986			1985
	Cost	Accumulated depreciation	Net value	Net value
	(in thousands of dollars)			
Land and land improvements	$ 4 859	$ 221	$ 4 638	$ 4 117
Buildings	53 578	6 727	46 851	44 407
Machinery, office furniture and equipment	39 801	15 024	24 777	23 146
Rolling stock	15 521	9 861	5 660	5 532
Leasehold improvements	1 782	652	1 130	506
	115 541	32 485	83 056	77 708
Fixed assets under capital leases	12 678	4 330	8 348	6 748
	$128 219	$ 36 815	$ 91 404	$ 84 456

8- Other assets:

	1986	1985
	(in thousands of dollars)	
Goodwill – amortized cost	$ 9 933	$ 2 765
Amalgamation expenses, start-up costs and other – amortized cost	1 615	2 345
	$11 548	$ 5 110

9- Long-term debt:

	1986	1985
	(in thousands of dollars)	
Loans, secured by first mortgages, bearing interest at rates ranging from ¼% over prime rate to 13.5%, maturing up to 1995	**$37 599**	$38 137
Loan, secured by a collateral second mortgage and by a commercial pledge, bearing interest at the rate of 13.395%, maturing in 1993	**7 500**	8 500
Loans, secured by liens on equipment, bearing interest at rates ranging from 11.50% to 17.75%, maturing on various dates up to 1990	**3 872**	5 059
Notes, bearing interest at rates ranging from 10.6% to 1½% over prime rate, maturing up to 1991	**16 772**	–
Series A Sinking Fund Bonds, 9½%, secured by a first mortgage, maturing October 1, 1986	**150**	150
	65 893	51 846
Obligations under capital leases, bearing interest at rates ranging from 9.6% to 14.75%, maturing from 1987 to 1991	**8 652**	6 942
	74 545	58 788
Current portion	**6 195**	4 834
	$68 350	$53 954

Capital repayments of the long-term debt, payable during the next five years, and minimum payments under capital leases are as follows:

Long-term debt

1987	–	$ 3 483
1988	–	$31 233
1989	–	$ 3 777
1990	–	$ 2 414
1991	–	$ 5 031

Capital leases

1987	–	$ 3 570
1988	–	3 232
1989	–	2 605
1990	–	698
1991	–	470
		10 575
Less interest included in instalments		1 923
		$ 8 652

10- Loans from shareholders:

	1986	1985
	(in thousands of dollars)	
Loans redeemable in three or after five and ten years of their respective instalments, bearing interest at rates ranging from 1% below to 1½% above the average prime rate	$ 5 230	$ 9 163
Notes, without interest, convertible into Class C subordinate shares within 20 days of the year-end	853	443
Demand notes, without repayment conditions, bearing interest payable semi-annually at the rate of 1½% below average prime rate	1 183	1 320
	7 266	10 926
Current portion	1 671	1 629
	$ 5 595	$ 9 297

Capital repayments of loans from shareholders over the next five years are as follows:

1987 – $1 671
1988 – $1 649
1989 – $ 932
1990 – $ 114
1991 – $ 165

The shareholders of the company have subordinated their past and future loans to the rights of the lending institutions which have agreed to finance Centre Mérite I and have also subordinated their loans to the rights of lenders which granted or will grant loans to the company or its subsidiaries.

11- Capital stock:

Authorized:
- Unlimited number of first preferred non-voting, non-participating shares, cumulative dividend of 75% of the sum of the bank prime rate increased by 1½%, redeemable at their par value of $ 100
- Unlimited number of Class A common shares, without par value
  - Unlimited number of Class B subordinate non-voting shares, without par value
  - Unlimited number of Class C subordinate non-voting shares, without par value

	1986	1985
	(in thousands of dollars)	
Issued:		
11 219 first preferred shares (1985 – 12 472)	$ 1 122	$ 1 247
76 741 Class A common shares (1985 – 80 633)	3 713	3 785
10 536 Class B subordinate shares (1985 – 10 131)	881	843
368 351 Class C subordinate shares (1985 – 303 791)	29 824	24 303
Deduct:		
Shares held by wholly-owned subsidiaries	–	(127)
	$35 540	$30 051

The change in capital stock is summarized as follows:

	1986		1985	
	Number of shares	Stated value	Number of shares	Stated value
		(in thousands of dollars)		
Issuance of capital stock:				
First preferred shares	–	$ –	320	$ 32
Class A common shares	3 240	$269	5 130	$563
Class B subordinate shares	1 485	$128	2 430	$257
Class C subordinate shares (including, for the year ended September 28, 1985, the conversion of second preferred shares, Series 1981 and 1982, into 60 074 shares for a total amount of $4 806 000)	71 571	$ 6 081	304 071	$24 325
		Price paid		Price paid
Redemption of shares:				
First preferred shares	1 253	$125	510	$ 51
Second preferred shares, 1981 Series	–	$ –	150 813	$151
Second preferred shares, 1982 Series	–	$ –	160 279	$160
Class A common shares	7 132	$876	5 162	$645
Class B subordinate shares	1 080	$108	1 080	$135
Class C surbordinate shares	7 011	$591	280	$ 22

As a result of the July 1, 1985 capital stock reorganization, the majority of the shareholders converted their loans made to the company during previous years, repayable after 5 and 10 years, into Class C subordinate shares. On this date, all the second preferred shares have been also converted into Class C subordinate shares.

12- Contributed Surplus:

The contributed surplus has been reduced by an amount of $18 000, which represent part of the excess of the redemption price of shares over their stated value.

13- Contingent liabilities:

a) Endorsements
The company assumes a contingent liability for certain of its shareholders as endorser of lease contracts extending over a twenty year period and maturing from 1994 to 2001. The annual minimum lease payments excluding escalator clauses are in the order of $480 000. The amount of contingent liability in virtue of these endorsements as of September 27, 1986 is $6 459 200.

b) Guarantees
The company has a limited contingent liability as guarantor of conditional sales contracts. As at September 27, 1986, the outstanding contracts amounted to $12 749 300, including capital and interest up to the date of maturity of the contracts.

c) Income tax assessments
The company received notices of assessment from Revenue Canada, Taxation totalling $286 000 following refusal of inventory allowance deductions claimed for the year ended September 27, 1980.

The company is contesting these assessments and, accordingly, no provision has been accounted for. Amounts which could become payable by the company will be accounted for as a prior years' adjustment.

14- Contractual obligations:

a) In virtue of lease agreements having terms varying from five to twenty-five years and extending up to the year 2006, the company has undertaken to lease premises and vehicles for annual minimum payments totalling $2 401 700. The total commitments excluding escalator clauses are in the order of $43 771 000. The balance of these commitments, as at September 27, 1986, amounts to $34 957 400.

b) Under lease agreements and lease offers with terms varying from twelve to twenty-five years extending until 2010, the company has undertaken to lease premises for minimum annual payments totalling $7 940 700. The total commitments excluding escalator clauses are in the order of $158 935 000. The balance of these commitments, as at September 27, 1986, amounts to $136 223 200.

In return, the company sublets these premises under the same terms and conditions and for the same considerations as in the above-mentioned lease agreements and lease offers.

15- Related party transactions:

The major portion of sales of the company and its subsidiaries results from transactions concluded with its shareholders.

16- Earnings per share:

	1986	1985
Basic earnings per share – Earnings (loss) before extraordinary item	**$0.73**	$(0.53)
Net earnings (net loss)	**$0.73**	$(0.34)
Pro-forma earnings per share – Basic	**$0.58**	
Fully diluted	**$0.56**	

The calculation of the basic earnings per share gives effect to the capital stock reorganization described in note 17 b).

In addition, the pro-forma earnings per share give effect to the public issue mentioned in note 17 e) and the potential exercise of stock options assuming a return, after income taxes, of 5.7% on the proceed of the potential issuances.

17- Subsequent Events:

a) Acquisition of McMahon – Essaim
The company acquired on September 29, 1986 from L'Essaim No. 2 du Québec Inc. ("Essaim") and its wholly-owned subsidiary, 151166 Canada Inc., which held all outstanding shares of the capital stock of McMahon-Essaim Inc. ("McMahon"), 50.3% of the voting shares of the capital stock of McMahon. On September 22, 1986, the company made an offer to all the shareholders of Essaim to purchase all the outstanding common shares of the capital stock of Essaim in other to become the owner, directly and indirectly of all the outstanding shares of McMahon. This offer has been accepted by all the shareholders of Essaim and since October 2, 1986 the company owns all the outstanding common shares of the capital stock of Essaim. The company has also purchased from all the shareholders of Essaim all the preferred shares of Essaim held by such shareholders. The purchase price of the preferred shares of the capital stock of Essaim is payable over a three year period upon certain conditions and the total cost of the transaction could amount to $6 418 000 over the three year period.

b) Reorganization of share capital:
Following the closing of the public issue, described hereafter, the capital stock of the company will be reorganized as follows:

i) the limitation to 12 000 of the authorized number of existing first preferred shares and the redesignation of such shares as "non voting non participating cumulative redeemable second preferred shares of the par value of $100 each" (the "second preferred shares");

ii) the creation of an unlimited number of first preferred shares without par value issuable in series (the "first preferred shares");

iii) the subdivision of each Class A common share into 20 and the redesignation of such shares as "Class B Shares without par value" (the "Class B Shares");

iv) the subdivision of each Class B subordinate share into 20 and the conversion of such shares into Class B Shares, on a one-for-one basis; and

v) the subdivision of each Class C subordinate share into 20 and the redesignation of such shares as "Class A Subordinate Shares without par value" (the "Class A Subordinate Shares");

so that the authorized capital stock of the company shall consist of:

i) an unlimited number of first preferred shares;
ii) 12 000 second preferred shares;
iii) an unlimited number of Class A Subordinate Shares; and
iv) an unlimited number of Class B Shares.

c) Redemption of shares
i) On October 7, 1986, the company has redeemed the shares held by shareholders who disqualified during the period from July 1, 1985 to September 28, 1985. The shares redeemed are as follows:

– 2 623 Class A common shares for an amount of $215 243;
– 1 Class B subordinate share for an amount of $82;
– 4 919 Class C subordinate shares for an amount of $403 653.

ii) Also, on October 7, 1986, the company authorized the redemption of the shares held by shareholders who disqualified during the period from September 29, 1985 to September 27, 1986. The shares redeemed are as follows:

– 972 first preferred shares for an amount of $97 200;
– 11 616 Class A common shares for an amount of $1 080 288;
– 810 Class B subordinate shares for an amount of $75 330;
– 21 680 Class C subordinate shares for an amount of $2 016 240.

Since the Class A common shares, Class B subordinate shares and Class C subordinate shares are redeemable at a price equal to the book value of such shares appearing in the financial statements for the fiscal year during which the shareholders have ceased to qualify and since the audited financial statements for the fiscal year ended September 27, 1986 were not available at the time the redemption was authorized, the company has authorized the redemption of these shares at book value, has paid $93 per share and has set aside $125 000 to pay the balance of the redemption price when the book value will be known.

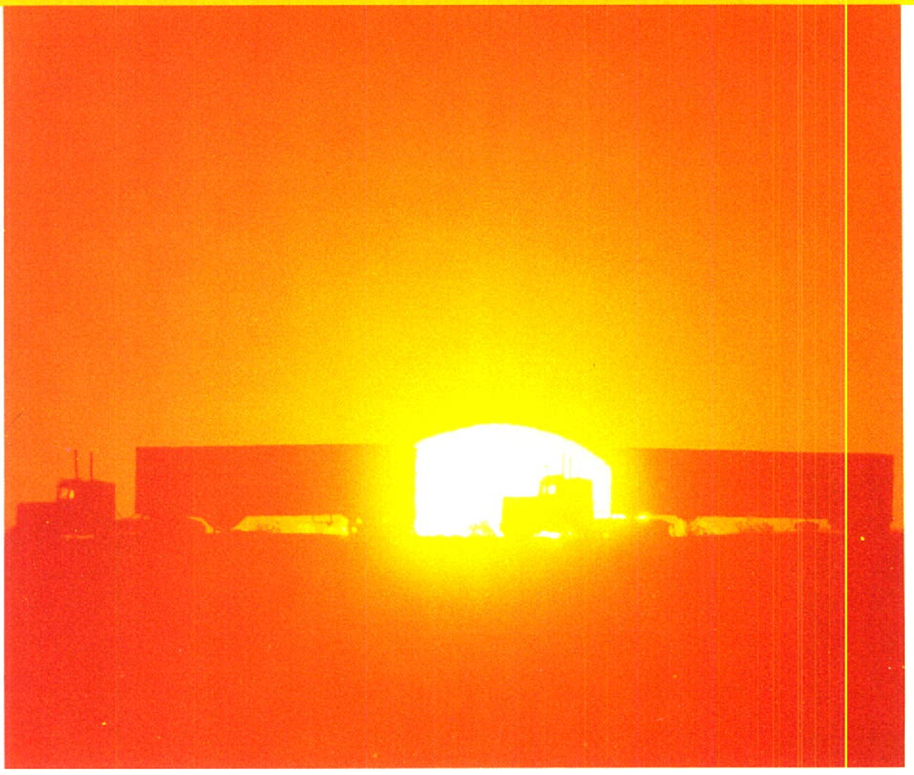
d) Issuance of shares
Since September 27, 1986, the company has issued the following shares

– 540 Class A common shares for an amount of $49 561;
– 270 Class B subordinate shares for an amount of $24 780;
– 560 Class C subordinate shares for an amount of $47 891.

e) Public issue
Pursuant to an underwriting agreement dated November 11, 1986, the company has agreed to sell to the public 4 600 000 Class A Subordinate Shares for estimated net proceeds of $25 390 000 net of the estimated expenses of issue and the underwriters' fee. Of these shares, 300 000 are reserved to be offered to employees of the company and its subsidiaries. Pursuant to a financing program, the company has undertaken to pay the interests on the loans granted to employees by a designated lender and which are repayable over a period of 12 months.

460 000 Class A Subordinate Shares are reserved for the purposes of the option granted to underwriters to cover overallotments.

15 166 Class C subordinate shares (to be subdivided on the basis of 20 for one and to be redesignated as "Class A Subordinate Shares") are reserved for the exercise of options granted to senior executives of the company.



Corporate Divisions

Besides its central divisions, Métro-Richelieu operates a certain number of corporate divisions in order to diversify and increase the Company's clientele both at the wholesale and retail levels as well as at the service level.

The largest of these divisions is Econogros. From warehouses in Quebec and Montreal, it serves more than 2,300 clients including hospitals, schools, restaurants and other institutions.

The particularly attractive potential of smaller retail outlets makes Econogros a promising division. Its contribution to the Company's earnings in the 1986-1987 fiscal year should be considerable.

The Buanderie Mérite division purchases, rents and maintains uniforms for the employees of Métro-Richelieu and its affiliated merchants. It also serves as an industrial laundry for many outside clients.

The Equipement Mérite division sells equipment to retailers and negotiates service contracts for this equipment.

In addition, Métro-Richelieu occasionally acquires retail stores which it operates and resells, while retaining ownership of the site or rights to the site under the lease. Over the last two years, the Corporate Stores Division has purchased 23 businesses and 11 of them have been resold to merchants.

Corporate stores have markedly improved their performances by constantly tightening their management.

With a view to improving productivity, an overall reorganization of the corporate divisions was carried out in December 1986. All these divisions now report to the same vice-president.

Sales for the corporate divisions represented 13% of Métro-Richelieu's total sales for the 1985-1986 fiscal year.

EPICERIE MERITE

The Épicerie Mérite division operates three distribution warehouses with a total area of ¾ of a million sq. ft.

Montreal has 525,000 sq. ft., Quebec City 180,000 sq. ft. and Mont-Joli 50,000 sq. ft.

During the 1985-1986 fiscal year, this division greatly improved its services to retailers by introducing new ways of estimating sales of advertised products and of co-ordinating deliveries from suppliers.

Sales for this division reached $943 million, which is equivalent to the sale of 34,862,000 cases, i.e., a weekly average of 670,423 cases involving 7,000 products, 700 of which were private brands.

As of September 27, 1986, Epicerie Mérite's sales represented 57% of Métro-Richelieu's total sales.

BOEUF MERITE

The Boeuf Mérite division operates two distribution centres for meat and frozen foods. One, in Montreal-North, has an area of 155,000 sq. ft.; the other, in Ville Vanier, has an area of 50,000 sq. ft. The Montreal-North operation also processes meats.

The Boeuf Mérite division buys from approximately 150 suppliers and serves retail outlets on the outskirts of large municipal centres as well as in outlying areas. This division has earned a solid reputation across Canada for the quality of its products.

Currently, Boeuf Mérite is upgrading its warehousing and distribution system for packaged meats. The new system will better respond to the needs of its clients, since they will no longer have to order directly from the various suppliers.

As of September 27, 1986, Boeuf Mérite's sales represented about 21% of Métro-Richelieu's total sales.

JARDIN MERITE

The Jardin Merite Division operates two distribution centres for fruits and vegetables. The Montreal centre is integrated with the grocery operation while the other centre at Beauport occupies 100,000 sq. ft.

During the year, this division completely reorganized its operation methods. It has also benefited from a more creative marketing approach, especially with regard to exotic fruits.

In addition, the volume rebate program had a spectacular impact on sales for this division, enabling it to consolidate the prominent position it holds among the fruit and vegetable wholesalers of Quebec.

Its sales totaled to 10,022,000 cases or about 9% of Métro-Richelieu's overall sales.

Specially for you!
METRO
LE SPÉCIALISTE
par excellence

MÉTRO

Métro, the Company's flagship, is pursuing its revitalization program based on promoting the specialization of its outlets.

Retailers displaying the Métro banner operate large-area food stores, offering consumers a wide variety of products at prices comparable to those in the other large food chains. They have counters specializing in fresh fish, delicatessen items, baked goods, fine cheeses, bulk goods and health and beauty aids.

The production and distribution of weekly circulars have become the major advertising medium in the industry and large sums have been allocated to enable Métro retailers to take full advantage of this marketing tool.

As of September 27, 1986, 342 stores were operating under the Métro banner. These represented a combined sales area of about 2,420,000 sq. ft.

The Métro banner is well-established throughout Quebec.

MARCHÉ RICHELIEU

In a highly specialized marketplace, Richelieu has become Marché Richelieu. The major restructuration that has given this banner its new identity should help to ensure future success.

Marché Richelieu's new approach consists of setting up specialized counters, providing high-quality meats, improving check-out service and offering home delivery.

The quantity and variety of the products sold in Richelieu outlets is considerable, although more limited than in Métro outlets.

As of September 27, 1986, there were 211 Marché Richelieu stores, representing a total sales area of 510,000 sq. ft.

The Marché Richelieu banner is well-known in the major centres in Quebec.

MARCHÉ
RICHELIEU

Other Banners

Through its Ami, Dépanneur 7 Jours and Gem banners, Métro-Richelieu is assured significant market penetration in Quebec.

AMI
The Ami banner is for small stores offering a limited choice of products. Most of the Ami outlets are located on the outskirts of Montreal and Quebec City and in the Abitibi region.

As of September 27, 1986, 59 stores were operating under the Ami banner. They represented a total sales space of approximately 84,000 sq. ft.

DÉPANNEUR 7 JOURS
The Dépanneur 7 Jours banner, which is found primarily in outlying areas of Montreal and Quebec City, is intended for independent convenience store owners who wish to operate a food store under a banner regulated by a strict operating code.

These stores are usually open seven days a week, including evenings, and offer a limited selection of products.

As of September 27, 1986, there were 83 Dépanneur 7 Jours stores with a total sales area of 130,000 square feet.

GEM
The Gem banner, launched in November 1986, is intended for operators of small convenience stores who wish to benefit from Métro-Richelieu's buying power. Gem merchants remain completely independent with respect to the management of their stores.

Ami, Dépanneur 7 Jours and Gem stores are supplied mainly by the Econogros Division.

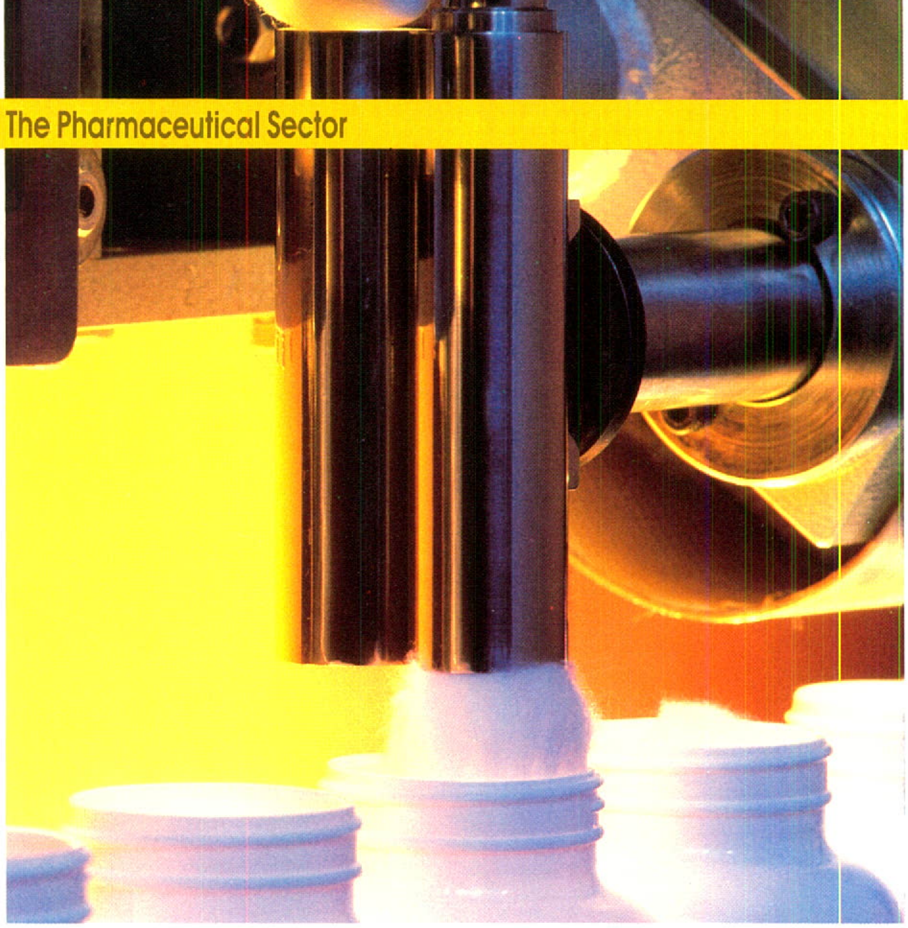
Services to Affiliates

Affiliated store owners have access to a wide range of services in order to maximize the profitability of their businesses and improve their competitive position.

These services include:

- a multi-faceted retail accounting system that provides, among other things, periodic statistics enabling merchants to compare their performance with that of other companies in the retail market.
- profitability studies for renovation, construction, acquisition or financing projects, etc., as well as studies of customer origins and buying habits.
- a general insurance program that is aimed at identifying, evaluating and controlling areas of risk and potential loss, as well as providing a group insurance package for merchants and their employees.
- a team of technicians trained in the various specialized areas of the food industry. They help members operate their businesses more efficiently and in accordance with the advertising programs and standards of the various banners.
- centralized advertising and marketing programs that maintain the specific positioning of each banner through print and electronic media.

The Pharmaceutical Sector



Guy Papillon
President
McMahon - Essaim

On September 29, 1986, Métro-Richelieu acquired McMahon-Essaim Inc., a large wholesaler of pharmaceutical products.

McMahon-Essaim was created in 1979 from the merger of M.F. McMahon, a pharmaceutical distributor and l'Essaim du Québec, a buying group. Since then, McMahon-Essaim has had a remarkable track record: in the past six years, it has had an annual growth rate of about 20%, with sales of $50,400,000 for the fiscal year ended April 30, 1986.

The Company serves some 300 pharmacies located throughout most of Quebec, 75 of which are Essaim outlets. The latter are located in the Trois-Rivieres, Montreal, Quebec City, Sherbrooke, Bois-Franc and Mauricie regions.

McMahon-Essaim's head office is in Sherbrooke where it owns a 36,000 sq. ft. building with both office and warehouse facilities. It also leases a warehouse with a total area of about 15,000 sq. ft. in Quebec City.

By virtue of this acquisition, Métro-Richelieu has entered a growing market. Indeed, many pharmacies today have not yet signed a franchise agreement with a wholesaler.

Annual retail sales of pharmaceutical products in Quebec amount to about $1.2 billion from almost 1,400 business outlets.

Métro-Richelieu intends to develop this sector quickly by aggressively recruiting pharmacies under the Essaim banner and penetrating every region of the province.

In making this major investment in the distribution of pharmaceutical products, Metro-Richelieu is banking on its strengths: well-trained personnel, reliable sources of supply, competitive prices, recognized service and customer-oriented marketing.

ESSAIM

Board of Directors:

○ **Marcel Beaulieu**
Chairman of the Board

○ **Aimé Gagnon**
Vice-Chairman

○ **Jean-Claude Messier**
Secretary

○ **Bernard Bélair**
Treasurer

□ **Gaston Blackburn**
Director

● **Réal Brouillette**
Director

● **Jean Dabate**
Director

● **Roland Ferland**
Director

■ **Benoît Gadoury**
Director

● **Marcel Guertin**
Director

□ **Jacques Laliberté**
Director

□ **Roger Lévesque**
Director

■ **Jean-Marie Vincent**
Director

○ Member of the Executive Committee
● Member of the Audit Committee
□ Member of the Human Resources Committee
■ Member of the Marketing Committee

Senior Officers:

Jacques L. Maltais
President and Chief Executive Officer

Raymond Bachand
Vice-President
Planning and Development

Gaétan Frigon
Vice-President, Marketing and
Head of Retail Operations

L.G. Serge Gadbois, c.a.
Vice-President
Finance

Paul Laporte
Vice-President
Distribution

Denise Martin
Vice-President
Information Systems

Jacques Obry
Vice-President
Groceries, Fruits and Vegetables

Guy Piuze
Vice-President
Human Resources

André Roy
Vice-President
Administration

Charles Roy
Vice-President
Corporate Divisions

Lawrence Timmons
Vice-President
Meats and frozen foods

Réjean Bouchard
Assistant to the President

Guy Papillon
President
McMahon-Essaim

Transfer Agent and Registrar:
Montreal Trust

Publicly-traded stocks:
Class A subordinated shares
Montreal Stock Exchange
Stock exchange symbol: MRU.A

Bankers:
National Bank of Canada
The Royal Bank of Canada
La Caisse centrale Desjardins
du Quebec

Auditors:
Mallette, Benoit, Boulanger,
Rondeau & Associes
Chartered Accountants

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Head Office: 11011 boulevard Maurice-Duplessis, Montreal, Quebec H1C 1V6 (514) 643-1000