C

ANNUAL
REPORT

1986

QUÉBEC-TÉLÉPHONE

60th
1927-87

CORPORATE PROFILE

Since its incorporation in 1927, Québec-Téléphone has provided dependable communication services within its territory and with the rest of the world. The Company employs the latest technologies to serve some 220,000 customers in areas south and west of Québec City and in the Lower St.Lawrence, Gaspé and North Shore regions.

The Company's 2,000 employees demonstrate their competence in the diversified fields of telephone services, computer communications, office automation, mobile radio and paging systems as well as in the transmission of data and television signals.

A corporate philosophy emphasizing a total commitment to excellence supports Québec-Téléphone's leadership in telecommunications. The Company makes every effort to meet the expectations and needs of the various groups affected by its operations – clients, shareholders and employees.

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On peut obtenir des exemplaires français de ce rapport à l'adresse suivante:

Le secrétaire
Québec-Téléphone
6, rue Jules-A.-Brillant
Rimouski (Québec)
G5L 7E4

HIGHLIGHTS

		1986	1985	Increase (Decrease)
Financial statements (thousands of dollars)	Revenues	**$ 182,667**	$ 176,525	3.5 %
	Expenses	**141,088**	130,794	7.9 %
	Net income	**19,927**	21,663	(8.0 %)
	Dividends on Common shares	**14,396**	13,908	3.5 %
	Gross capital expenditures	**43,787**	39,255	11.5 %
	Telecommunications property, at cost *	**511,935**	506,072	1.2 %
	Total assets *	**351,844**	336,633	4.5 %
Financial statistics	Earnings per Common share	**$ 1.21**	$ 1.32	(8.3 %)
	Dividends declared per Common share	**$ 0.91 ⅔**	$ 0.89 ⅔	2.2 %
	Common equity per share *	**$ 9.32**	$ 9.03	3.2 %
	Return on average Common share equity	**13.0 %**	15.0 %	(13.3 %)
	Return on average invested capital	**11.6 %**	12.6 %	(7.9 %)
Other statistics	Average number of Common shares (thousands)	**15,703**	15,509	1.3 %
	Number of Common shareholders *	**5,935**	5,806	2.2 %
	Subscriber lines in service *	**226,580**	221,471	2.3 %
	Terminals in service *	**285,231**	290,597	(1.8 %)
	Toll messages handled (thousands)	**34,553**	32,903	5.0 %
	Number of employees *	**1,978**	1,972	0.3 %

* At December 31

60th
1927-87

Honorable
Jules.-A. Brillant
1927-1962

Jacques Brillant
1962-1967

Basile A. Bénéteau
1967-1974

A TRADITION OF EXCELLENCE

The evolution of Québec-Téléphone since 1927 has followed the ambitious visions of its founder, the Honorable Jules-A. Brillant. He was a man dedicated to the advancement of rural development through the introduction of electricity, media, intercoastal transport and the consolidation of telephone networks.

Under the dynamic guidance of Mr. Brillant, the Compagnie de Téléphone Nationale, *acquired in 1927 from its founder Dr. Ferdinand Demers, expanded rapidly through mergers and acquisitions of numerous networks from Trois-Rivières to Matane. Under his impetus, the Company's head office located in Québec City was moved to Rimouski in 1937. The country's military effort during World War II increased communication needs which accelerated the development of the network around the Gaspé Peninsula.*

Jacques Brillant, son of Québec-Téléphone's founder, served as President of the Company from 1962 to 1967 at a time when technological innovation required ever-increasing capital investments. The need for greater financial resources prompted the Brillant family to divest its interests, with La Compagnie de Téléphone Anglo-Canadienne *becoming majority shareholder in 1966. The affiliation with the GTE group provided the necessary financial support for the extensive modernization of the Company's network.*

The extension of Québec-Téléphone's microwave network in the Middle and Lower North Shore of the Gulf of St.Lawrence and the automation of services highlighted Basile A. Bénéteau's presidency from 1967 to 1974. His successor is Raymond Sirois, whose rigorous management has enabled Québec-Téléphone to successfully integrate the latest technologies in the field of telecommunications.

The trend of deregulation which swept the traditionally stable world of telecommunications prompted demands for higher quality from those using our products and services. For our customers, courteous and personalized service has become just as important as the reliability of systems and equipment.

The changing market values which increasingly shape our activities lead us to develop our corporate strategies on our customers' diversified expectations of quality. Québec-Téléphone's service philosophy based on excellence places greater emphasis than ever on those qualities of diligence and innovation which have kept us strong and prosperous for almost sixty years.

Our success in maintaining the position of the leading provider of terminal equipment in our territory in the last three years is due to our firm determination to retain our customers through stringent asset management and continued rational investments in state-of-the-art technologies. To that effect, our emphasis on fiber optic facilities between digital switches strenghtens our ability to profitably integrate human voice, images and data in an increasingly computerized society.

MESSAGE TO OUR SHAREHOLDERS

In our relationship with our regulatory body, we strive to obtain recognition for excellence rather than penalty for success. As a result, we hope to be granted in the near future a rate of return which is more in line with our efforts and business risk. We also strive to have the non-regulated portion of our activities excluded from the regulatory process so we can effectively compete under the same rules in the free market environment.

By carefully planning our markets, we attempt to secure new sources of revenue. The particular attention we pay to growth sectors such as data transmission shows our intention to maintain our leading position as supplier of total telecommunication services at competitive rates. This determination is also evidenced by our participation in the research and development field. We are now in the process of defining, with appropriate R&D partners, the priority sectors for profitable investments.

To maximize the benefits of our expertise, we have entered new markets. In 1986, we have initiated training and technical support programs in the renovation of long-distance telephone networks in Africa. The venture represents a significant breakthrough for our Company in the international market.

Our present success is largely attributable to the talent, dedication and day-to-day efforts of our employees. We extend them our gratitude. We are especially indebted to Charles Mercier, our Vice President - Marketing and Customer Service, who has taken a well-deserved retirement after three decades of loyal service with the Company.

Raymond Sirois,
Chairman of the Board,
President and Chief Executive Officer

The Chairman of the Board,
President and
Chief Executive Officer

Raymond Sirois

Raymond Sirois
February 4, 1987

FAMILIAR VOICES AND FACES

Today's possibility of direct dialing to most localities in North America shows the progress we have accomplished since 1927 when all telephone calls were routed through the ever-present operator.

The old manual switchboard with which the operator of yesteryear could handle only a limited number of calls per hour is now replaced by automated positions (TOPS), a major contribution to the mechanization of communications. As a result of these changes, traffic administration has become more efficient although the operator still remains a valuable link between the subscriber and the telephone network as well as a comforting presence in emergency situations.

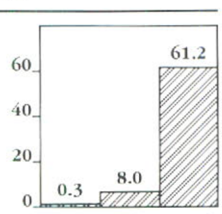
Also worthy of praise are the sustained efforts over a period of sixty years by our installers, repairmen and construction crews. These men, whose knowledge and experience have long been passed down by word of mouth, overcame obstacles to access remote territories and make telephone service available often before even roads were built.

These network construction pioneers endured the hardships of our rugged climate. Many stories can be told of how freezing rain and winter storms knocked out manual exchanges and so often crippled the pole line network, a network sometimes serving over twenty rural subscribers on a single wire. Their dreams of improved facilities are largely fulfilled now as individual line service, digital transmission and fiber optic routes are rapidly being implemented throughout our territory.

Telephone operators have always attended diligently to public safety.

Our courageous network construction crews helped overcome distances.

Evolution of Salaries and Wages (millions of dollars)



In the management of its human resources, Québec-Téléphone recognizes the contribution of its employees to the success of the Company's mission. The recent implementation of a philosophy committed to excellence has created a vigorous pooling of internal talents and energies. Increased customer satisfaction is the absolute indicator of success in this undertaking.

The management employees' compensation policy was modified effective April 1, 1986 to better reward the individual merit of employees in the pursuit of their respective objectives. The same objectives are being used in the negotiation of a new labor contract for the 280 professionals, who are members of the *Syndicat des agents de maîtrise de Québec-Téléphone* and whose agreement expired on June 28, 1986.

Competitive salaries, a better retirement plan and improved job protection in a context of technological change were key elements in the three labor agreements covering some 1,300 craft workers, telephone operators, clerical employees and technicians. These contracts which expired on November 12, 1985 were signed on August 12, 1986 and extend through November 12, 1988.

THE HUMAN ELEMENT

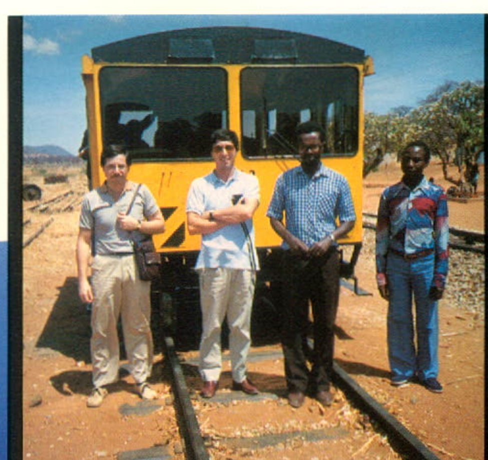
New administrative training courses were introduced on personnel selection and supervision, fundamentals of management and quality circles. In office automation, training in word processing was intensified for secretarial staff. Training in the use of personal computers and electronic mail is presently being emphasized.

During 1986, our training personnel travelled to each district to instruct employees on improved marketing techniques for our new products and services. This approach proved more profitable and economical, and was greatly appreciated by the participants.

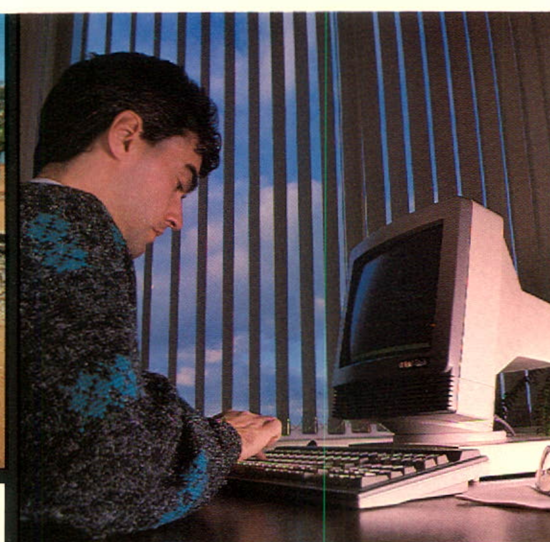
Technical training given to trainees from Rwanda in the first quarter of 1986 laid the groundwork for promising co-operative agreements with African countries. Training and control programs in the maintenance and operation of long-distance networks were developed and implemented to help these countries benefit from Québec-Téléphone's expertise in serving vast territories with low population density and extreme weather conditions.

Finally, significant efforts were made in the occupational health and safety sector. A joint central committee was formed to coordinate sector-based committees within each Company district. Québec-Téléphone also contributed to two public campaigns on safety. One dealt with the use of vehicle headlights for daytime driving and the other promoted a toll-free telephone number for emergency calls to the new Québec Poison Control Centre.

A corporate philosophy based on excellence will foster better cohesion of talent and energy.



Québec-Téléphone representatives evaluate the condition of the Tanzanian Railway Corporation's telephone plant.



To meet the challenge of office automation, training in personal computers is intensified.

The combination of telephone and telegraph long contributed to business productivity.

THE TELEGRAPH

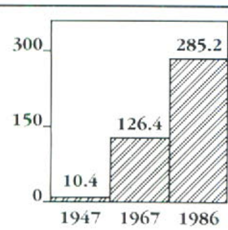
It was back in 1948 that Jules-A. Brillant established in Rimouski a telegraph service which, until its closure in 1982, was extensively used. This method of transmitting written messages required attentive listening by the operator, complete discretion and deep sympathy in the announcement of family bereavements.

Attentiveness and discretion were the leading qualities of our telegraph operators.

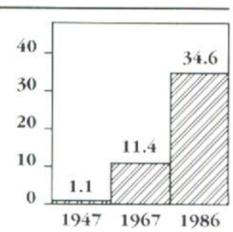
A marked advantage of the telegraph was the written confirmation of the message. When the service was introduced, the cost for sending a 10-word daytime message was 30 cents while an overnight message five times longer cost only 50 cents.

Abolished in the seventies with the widespread introduction of teletypewriters in businesses, the telegraph nevertheless contributed to bring out of isolation the sparse populations of the North Shore and Gaspé regions.

Terminals in Service (thousands)



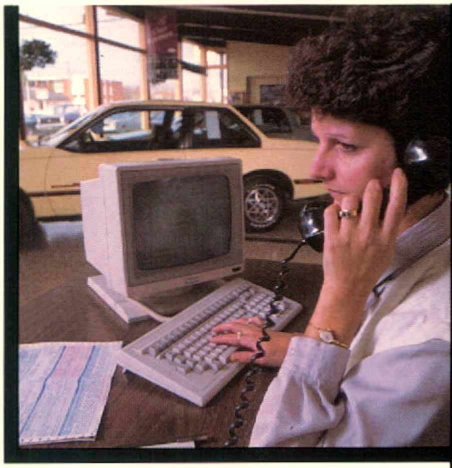
Toll Messages Handled (millions)



A task force was mandated last October to make an in-depth study of the work methods of the employees whose daily tasks influence customer satisfaction. The group will make recommendations for restructuring the Marketing and Customer Service department effective the summer of 1987. The development of a master plan involves extensive consultation with employees concerning the nature and distribution of the work as well as training and development requirements. The ultimate objective is the efficient marketing of new products and services from a perspective of continued good subscriber relations.

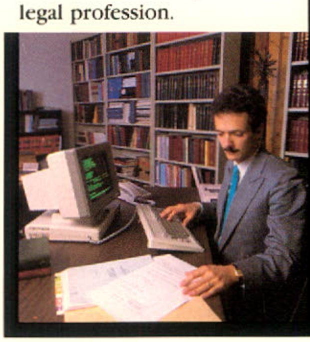
The mechanization of customer files advanced a step further in 1986 with the transfer to magnetic disk of the contents of some 180,000 cards previously stored on manual rotary files. This permits direct CRT screen display of the appropriate information at each service call. The resulting faster, more precise retrieval of data helps improve the quality of each customer contact. To further improve efficiency, the Company adopted in November a five-year plan for global automation of customer service activities.

OUR SERVICES



Québec-Téléphone stresses greater use of management software by automobile dealers.

Since its introduction, the Signature telephone has been a constant favorite with consumers.



Access to data banks increased efficiency in the legal profession.

Digital conversion of the *Messager* paging service enhanced its versatility.

Intensive promotion of touch calling stimulated the demand for custom calling features in the localities served by electronic switches. New options for residence and business clients are automatic call forwarding, call waiting, speed calling of frequently dialed numbers and three-way calling. Within two years, the number of lines available with these features will have more than tripled, contributing to the growth of telephone service revenues.

In July 1986, Québec-Téléphone became distributor and service representative for new electronic key systems manufactured by Trillium. These dependable, high-performance midscale terminals are offered to small and medium-sized businesses at very competitive prices.

In early 1986, the urban centers of Sept-Îles, Baie-Comeau, Gaspé, New Carlisle, Rimouski and Saint-Georges-de-Beauce were all linked to Datapac – Telecom Canada's data transmission network. This nationwide system offers packet switching and the efficient interaction of terminals and computers at affordable prices. It is also the network base for new intelligent systems: Envoy 100 for electronic messaging and iNet 2000 for access to data banks.

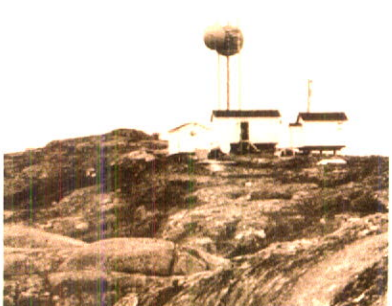
With custom-tailored solutions to the computerization needs of businesses, Québec-Téléphone has intensified its distribution of management software to specific target clients: car dealers, building contractors, transport and distribution firms. Many factors have contributed to the success of this effort: equipment reliability, user-personalized training, after-sale service availability and constant software update.

The evolution of the mobile communications market justified the introduction at Rimouski in October 1986 of a digital version of the *Messager* service. Also worthy of mention is the recent awarding to Québec-Téléphone of a contract for about 700 paging receivers to be used by various provincial departments in the Greater Québec City region.

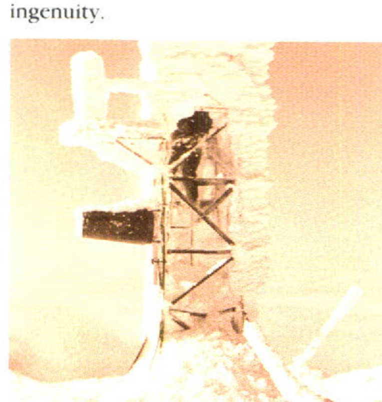
TECHNOLOGICAL MILESTONES

1930 – First voice signal amplifier repeaters on toll circuits.
1936 – Short-wave radio telephone relay between Rimouski and Baie-Comeau.
1937– Common battery manual switchboards replace magneto types.
1946 – Simultaneous transmission of more than one conversation over the same pair of wires.
1947 – First private teletypewriter service.
1948 – Step-by-step switching.
1956 – Connection of Québec-Téléphone to the American automatic toll network.
1958 – Microwave transmission.
1962 – Crossbar switching.
1965 – First mobile radio telephone network.
1967 – Automatic dialing of long-distance calls.
1971 – Automatic Number Identification.
1973 – Electronic switching.
1976 – Completed automation of telephone service. Introduction of Messager *service (paging).*
1979 – Implementation of Telephone Operator Position System (TOPS) in Rimouski.
1981 – Digital switching.
1984 – Installation of fiber optic cables.

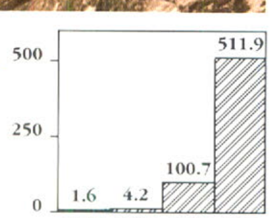
On the North Shore, we provide communication services to many isolated communities.



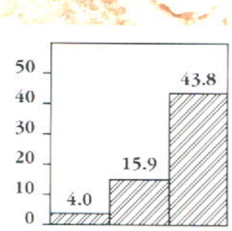
Our severe winters demand hard work and ingenuity.



Telecommunications Property, at Cost (millions of dollars)



Gross Capital Expenditures (millions of dollars)



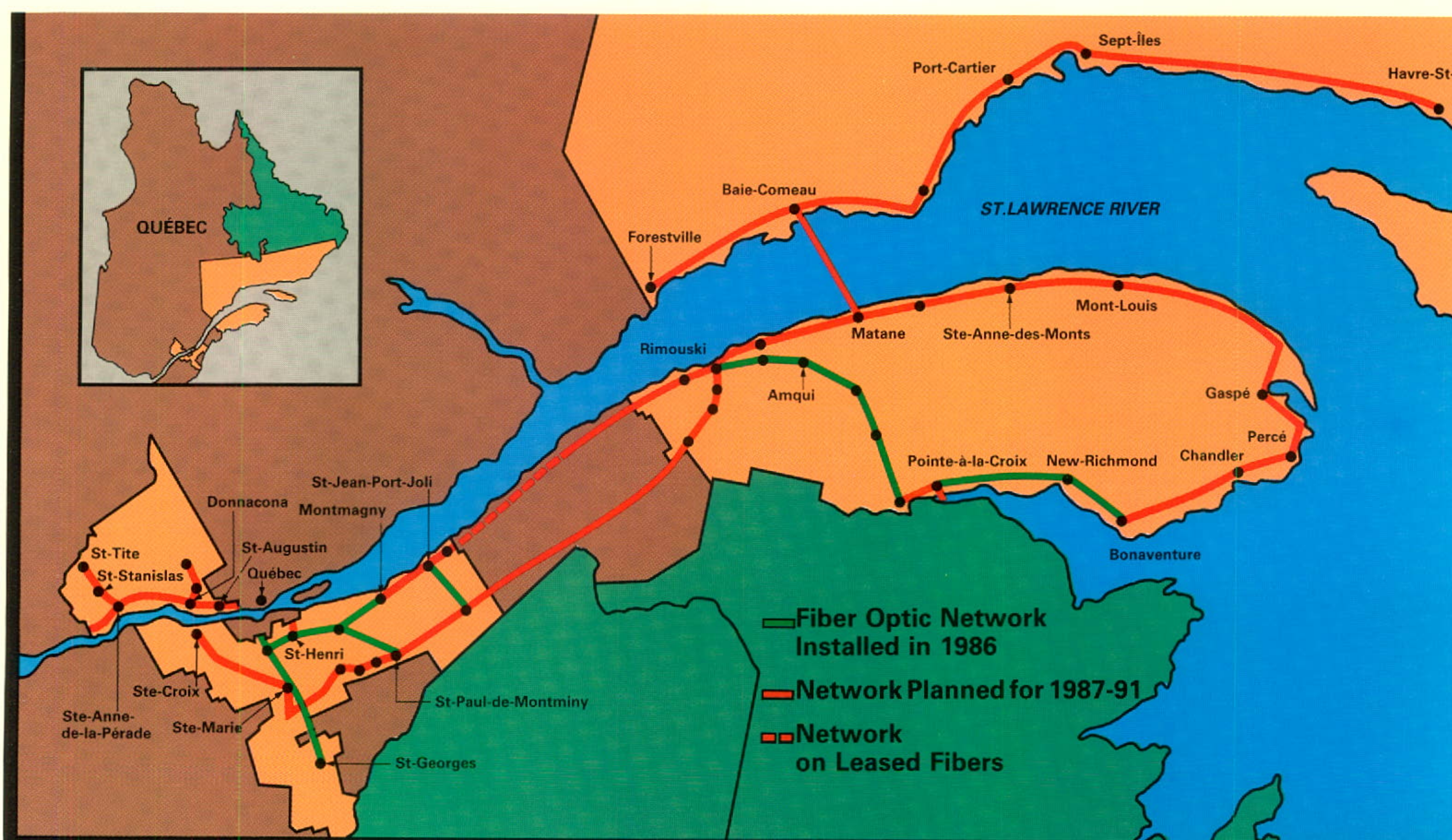
In an order issued on June 20, 1986, the *Régie des services publics* of Québec approved the total upgrading program of subscriber lines in rural areas submitted by Québec-Téléphone. Under this program, the service shared by more than two subscribers ceases to be available whenever the number of individual or two-party lines in a given exchange reaches 80 % of all lines in service. As of December 31, 1986, rural upgrading was completed in 74 % of the Company's exchanges. Initiated in 1980, this service improvement program will be completed in 1990.

Pursuing its efforts to convert the traditional analog network to an integrated digital network, Québec-Téléphone focused on shortening distances between its subscribers and their central office. Also, in numerous exchanges, the Company optimized the quality of transmission and arranged for the possibility of more elaborate communications in the future. The replacement of several electromechanical switching systems by powerful digital machines linked to many remote units provides the network with a more functional and economical configuration. The digital equipment introduced in 1986 on the South Shore of Québec City,

THE NETWORK

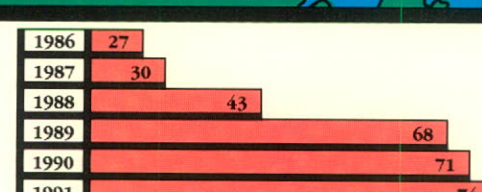
in the Matapédia and Baie-des-Chaleurs areas is better able to meet the growing demand of our subscribers. The digitization also brought about other advantages such as centralized administration, constant quality transmission unaffected by distance, a reduction in the number of signal amplifiers and lower operating costs.

Our five-year construction plan which, between 1987 and 1991, calls for investments of about $ 275 million focuses mainly on a higher pace of network digitization by greater integration of the access, switching and transmission functions. This emphasis requires new forms of cooperation within the Company as well as greater training and development efforts for motivating employees to fully participate in this technological renewal.



Fiber optic additions to Québec-Téléphone's long-distance network: a five-year plan.

% of Digital ► Lines on Total Installed Lines



THE NETWORK (continued)

To perfect the digital conversion of its infrastructures, Québec-Téléphone revised in November 1986 the design philosophy of its subscriber line network. By separating feeder and distribution cables, the Company will optimize their utilization, lower its operating costs and reduce the impact of network troubles on customers. The implementation of this significant program will start immediately and extend over several years.

The use of fiber optics for toll transmission is developing rapidly in the telecommunications industry. In 1984, the Company had only 50 km of optical cable installed near Québec City. By the end of 1986, there were 455 km between the eastern and western limits of our territory. During the next five years, over $ 25 million will be invested in the optical conversion of our network. Besides the integration of voice, images and data, the fiber optic medium offers an expanded service capability never imagined, which will characterize tomorrow's information-based society.

TERRITORIAL ECONOMY

The confidence demonstrated by consumers and the business community within the territory served by Québec-Téléphone has stimulated economic activity in 1986, generating growth in line with the provincial trend.

After years of stagnation, the primary sector showed new vigour in the forestry sector and relative stability in commercial fisheries. The North Shore Region, largely dependent on mining and forest-related activities maintained its position, with confidence in a brighter future.

The manufacturing industry played a prominent role in the economy of the Québec Region. Numerous small and medium-sized enterprises of all types experienced sustained growth in terms of investment, exports and job creation.

Taking advantage of a favorable economic climate, the housing industry was prosperous in the outskirts of Québec City and in the Lower St.Lawrence and Gaspé regions. In addition, tourism proved to be the major growth factor of the tertiary sector.

MAIN EVENTS

First Quarter

— Commercial introduction of Signature, a most popular push-button telephone.

— Access to Telecom Canada's Datapac network for six exchanges of the Company's territory.

— Completion of Phase III of Québec Region's South Shore digitization program.

Second Quarter

— Three-for-one split of Québec-Téléphone's Common shares.

— Abolition of the rate supplement charged for urban-type telephone service in rural areas.

Third Quarter

— Installation of fiber optic cables over 227 km between Rimouski and New Richmond.

— Replacement of the central data processing computer by a higher-capacity system.

— Distribution by Québec-Téléphone of Trillium telephone systems.

60th 1927-87

The Gaspé Peninsula largely benefited from stimulating tourism activity through improved infrastructures and an influx of foreign visitors lured by the value of the Canadian dollar.

For 1987, Québec-Téléphone foresees a moderate economic growth in line with the provincial trend. It expects a higher volume of toll traffic stimulated by lower rates and a slight increase of revenues derived from data transmission.

— Signature of the collective agreement covering hourly-paid employees.

Fourth Quarter

— Introduction of an improved paging service, the digital *Messager*.
— Order issued by the *Régie des services publics* covering, among other matters, the Company's rate of return on Common equity for 1986 and 1987.
— Launching of a campaign to make employees more aware of a service strategy focusing on quality.

After 50 years of service, Mr. Ernie Whittom received well-deserved recognition from Québec-Téléphone.

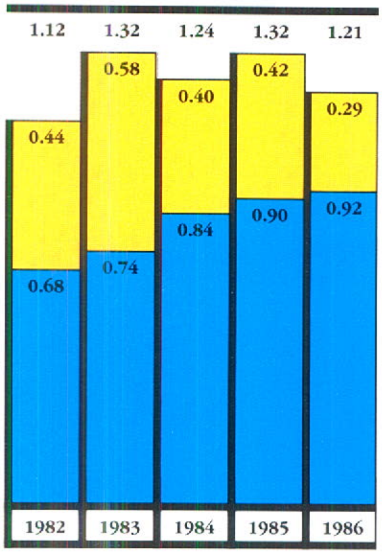
Telephones from different eras will be displayed in our future telephone museum.

A RICH PAST

In 1986, Ernie Whittom celebrated an exceptional achievement: fifty years of dedicated service with Québec-Téléphone. Born in Paspébiac, Ernie was only fourteen years old when he joined the Company on July 8, 1936. His starting salary was $ 30 per month for a 60-hour workweek. As an installer-repairman, he travelled extensively in Southern Gaspé during several decades. In 1975, he began coordinating technical studies in the New Carlisle district. A few months before his retirement in October, Mr. Whittom received from his Québec-Téléphone colleagues a well-deserved expression of gratitude.

We must equally be grateful to those who have the foresight to recognize and protect valuable work-related items of everyday life for the benefit of future generations. Mr. Ernest Gagnon, a retiree from Matane, is one such person who, since 1948, painstakingly restored an impressive collection of antique telephones which Québec-Téléphone recently acquired. This collection becomes even more interesting as we approach our 60th anniversary. The importance of this historical collection will soon be highlighted through the creation of a telephone museum, an additional tourist attraction for Rimouski.

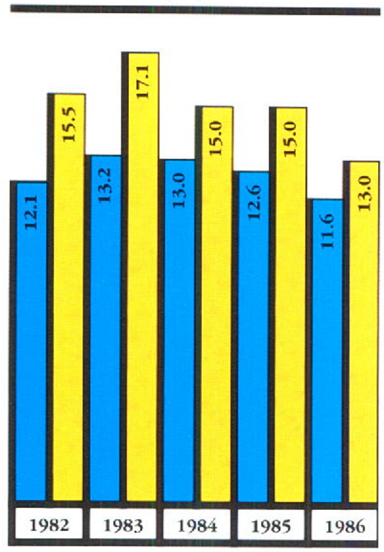
Earnings and dividends per Common share (dollars)



Dividends declared

Reinvested earnings

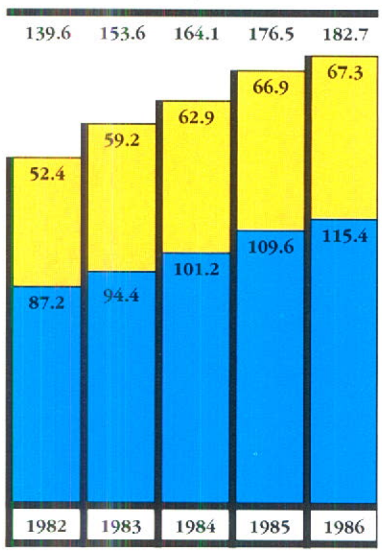
Rates of return (%)



On average invested capital

On average common share equity

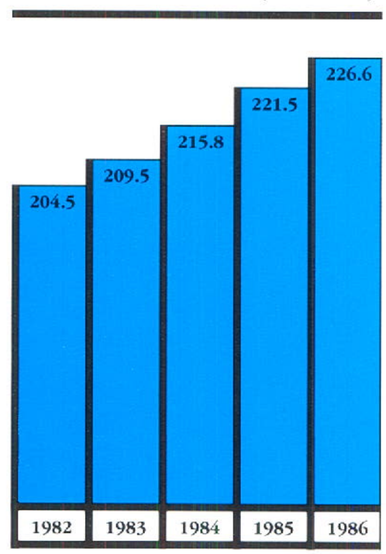
Operating revenues (millions of dollars)



Long-distance service

Local service and other revenues

Subscriber lines in service (thousands)



In its order 85-057-C issued on November 10, 1986, the *Régie des services publics* of Québec set a 13 % maximum rate of return on average Common share equity for 1986. To comply with this decision, the *Régie* ordered the Company to credit the local basic rate for the month of December 1986 to each of its residence and business subscribers. The *Régie* also directed the Company to create a $ 10.0 million research and development fund to be charged to expenses for the year 1986.

Moreover, in its order 85-015-A also issued on November 10, 1986, the *Régie* set the maximum depreciation rate at 6 % in 1986 for most of the assets in the regulated sector and restricted the depreciation expenses for capital recovery of certain assets.

All data appearing in the present report reflect the three-for-one stock split effective April 16, 1986.

Earnings

Net income for the year ended December 31, 1986 was $ 19.9 million as compared to $ 21.7 million for 1985. Earnings

FINANCIAL REVIEW

per Common share were $ 1.21 compared to $ 1.32 last year while the average number of Common shares outstanding totalled 15,702,830 for 1986 compared to 15,509,131 in 1985. The rate of return on average invested capital was 11.6 % versus 12.6 % in 1985. Dividends declared on Common shares during 1986 totalled $ 14.4 million or $ 0.91 ⅔ per share compared with $ 13.9 million or $ 0.89 ⅔ per share in 1985. The dividend payout ratio for the last twelve months was 76.0 % versus 67.8 % for the preceding year.

Revenues
Revenues for the year ended December 31, 1986 reached $ 182.7 million, 3.5 % over the $ 176.5 million obtained in 1985. Local service revenues went down $ 3.8 million or 6.6 % against the preceding fiscal year, to total $ 54.4 million as compared with $ 58.2 million in 1985. This decrease is due mainly to the credit of $ 3.1 million given in December 1986 to all subscribers in accordance with the order 85-057-C of the *Régie des services publics* of Québec and also to the transfer to Other Revenues in the Statement of Income, of revenues derived from the lease of terminal equipment and other deregulated services. These other revenues were $ 13.5 million compared to $ 9.2 million in 1985.

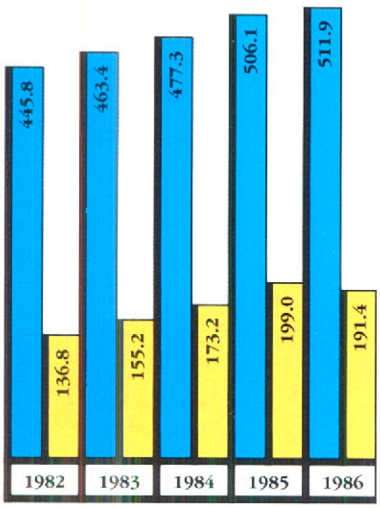
Revenues from toll services, which represent 63.2 % of operating revenues (62.1 % in 1985) went up 5.3 % to $ 115.4 million compared with $ 109.6 million in 1985. The volume of billed long-distance messages continued to rise in 1986, reaching 31.2 million, 6.5 % over last year. Furthermore, revenues from Wide Area Telephone Service (WATS) again experienced a very strong growth, totalling $ 18.9 million compared to $ 17.2 million in 1985 for a 9.8 % gain. Finally, revenues from private line services showed a moderate growth of 1.1 % over 1985.

Expenses
As a whole, expenses for the year ended December 31, 1986 increased by $ 10.3 million or 7.9 % over the preceding year to a level of $ 141.1 million against $ 130.8 million in 1985. This increase is mainly attributable to the expensing in 1986 of an amount of $ 10.0 million for the creation of a research and development fund by the Company in accordance with the order 85-057-C issued by the *Régie* and to the rise of salaries and fringe benefits. It was however partly offset by a decrease of 14.5 % in depreciation expenses which were $ 30.3 million for the fiscal year of 1986 compared with $ 35.5 million for 1985. This is due to the provisions of the order 85-015-A mentioned previously.

Labor Relations
On August 12, 1986, Company negotiators and the *Syndicat des employés d'exécution de Québec-Téléphone,* local 5044 of the C.U.P.E., signed three collective labor agreements covering some 1,300 trade workers, operators, clerical employees and technicians whose contracts had expired on November 12, 1985. These agreements are for a three-year term.

Negotiations were also undertaken in May 1986 with the *Syndicat des agents de maîtrise de Québec-Téléphone* for the renewal of the labor contract of about 280 professionnal employees whose agreement expired June 28, 1986.

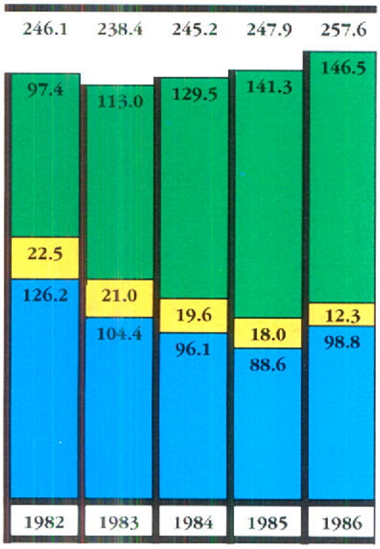
Telecommunications property
(millions of dollars)



Telecommunications property, at cost

Accumulated depreciation

Capital structure
(millions of dollars)



Debt (including short-term)

Preferred shares

Common share equity

Telecommunications Property

In 1986, investments in telecommunications property amounted to $ 43.8 million, $ 4.5 million more than in 1985 and $ 4.3 million over the $ 39.5 million budgeted at the beginning of the year. This upward variation is mainly due to an advance in the schedule for a fiber optic cable installation program to meet the increase in the number of toll circuits and the demand for modernized equipment. This fiber optic cable addition will also provide certain new facilities planned for the use by Telecom Canada.

More than the half of the funds used in 1986, $ 26.0 million, was allocated to the expansion of basic telephone service. The modernization and improvement in services required $ 15.6 million, of which $ 5.3 million were invested in the rural upgrading program to provide single or two-party line service in rural areas to some 4,400 additional subscribers.

During the next five years, the Company plans to invest nearly $ 275.0 million for expanding and modernizing its facilities and meeting the demand for telecommunications services for which it will need to raise about $ 55.0 million in new funds on the financial markets.

Capital Structure

During the Special General Meeting of Shareholders held immediately after the Annual General Meeting on April 1, 1986, Special By-law No. 93 was approved and ratified, amending the articles of the Company and authorizing a three-for-one split of the Company's Common shares issued and outstanding at the close of business on April 16, 1986.

Under the Employees' Stock Purchase Plan, 72,891 Common shares were issued during the fiscal year ended December 31, 1986. In addition, 6,704 $ 1.68 Cumulative Redeemable Convertible Subordinate Preferred shares Series B were converted into 20,112 Common shares before termination of the conversion right on June 30, 1986.

As of December 31, 1986, some 5,900 shareholders held 15,730,404 outstanding Common shares. The major shareholder, *La Compagnie de Téléphone Anglo-Canadienne*, owned 50.3 % of the Company's total shares.

FINANCIAL STATEMENTS

QUÉBEC-TÉLÉPHONE

MANAGEMENT'S REPORT

To Our Shareholders:

The consolidated financial statements of Québec-Téléphone as well as the financial information included in this annual report are the responsibility of Management and have been approved by the Board of Directors. These consolidated financial statements have been prepared in conformity with Canadian generally accepted accounting principles and, where appropriate, include amounts that are based on best estimates and judgments. Financial information presented elsewhere in this annual report is consistent with that in the consolidated financial statements.

The Company has a high-quality system of internal accounting controls and of audit within the limits of acceptable costs. These controls are designed to provide reasonable assurance that financial transactions are properly recorded and executed in accordance with required approvals, that consolidated financial statements are properly prepared and assets safeguarded.

The Board of Directors fulfils its responsibility with regard to the consolidated financial statements contained in this annual report principally through its Audit Committee, consisting solely of outside directors, which meets periodically with Management as well as with the internal and external auditors. The latter have full and free access to the Audit Committee and meet with it, with and without Management being present, to discuss auditing and financial reporting matters.

These financial statements have been examined by the shareholders' auditors, *Arthur Andersen & Cie* and *Samson Bélair*, chartered accountants.

On behalf of Management,

Simon Soucy
Vice President - Finance
and Treasurer

Raymond Sirois
President and Chief
Executive Officer

AUDITORS' REPORT

To the Shareholders of Québec-Téléphone:

We have examined the consolidated balance sheets of Québec-Téléphone (a Québec company) and subsidiary as of December 31, 1986 and 1985, and the related consolidated statements of income, reinvested earnings and changes in financial position for the years then ended. Our examinations were 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 accompanying consolidated financial statements appearing on pages 17 to 25, inclusive, present fairly the financial position of Québec-Téléphone and subsidiary as of December 31, 1986 and 1985, and the results of their operations and the changes in their financial position for the years then ended in accordance with generally accepted accounting principles applied on a consistent basis.

Samson Bélair
Chartered Accountants

Arthur Andersen & Cie
Chartered Accountants

January 23, 1987

STATEMENT OF INCOME

For the years ended December 31	1986	1985
	Thousands of dollars	
Revenues		
Local service	$ **54,359**	$ 58,172
Long-distance service	**115,413**	109,594
Other	**13,485**	9,224
Less: uncollectible accounts	**590**	465
	182,667	176,525
Expenses		
Maintenance	**36,839**	36,936
Depreciation (Note 2)	**30,315**	35,451
Other operating expenses	**50,891**	45,295
Taxes other than income taxes	**13,043**	13,112
Research and development (Note 2)	**10,000**	—
	141,088	130,794
Operating income	**41,579**	45,731
Other income (Note 3)	**2,303**	1,729
Income before financial expenses and income taxes	**43,882**	47,460
Financial expenses (Note 4)	**8,765**	10,286
Income before income taxes	**35,117**	37,174
Income taxes (Note 5)	**15,190**	15,511
Net income	**19,927**	21,663
Dividends on Preferred and Subordinate Preferred shares	**979**	1,147
Net income applicable to Common shares	$ **18,948**	$ 20,516
Earnings per Common share (Note 8)	$ **1.21**	$ 1.32
Dividends declared per Common share (Note 8)	$ **0.91 ⅔**	$ 0.89 ⅔
Average number of Common shares outstanding (thousands) (Note 8)	**15,703**	15,509

REINVESTED EARNINGS

For the years ended December 31	1986	1985
	Thousands of dollars	
Balance at beginning of year	$ **60,654**	$ 54,046
Net income	**19,927**	21,663
	80,581	75,709
Less: dividends on Common shares	**14,396**	13,908
dividends on Preferred and Subordinate Preferred shares	**979**	1,147
	15,375	15,055
Balance at end of year	$ **65,206**	$ 60,654

BALANCE SHEET

QUÉBEC-TELEPHONE

As at December 31	1986	1985
ASSETS	Thousands of dollars	
Telecommunications property, at cost		
Buildings, plant and equipment	$ 491,485	$490,366
Less: accumulated depreciation (Note 6)	191,448	199,023
	300,037	291,343
Land	1,952	1,924
Property under construction	11,185	7,983
Construction materials, at average cost	7,313	5,799
	320,487	307,049
Investment and other assets		
Investment in Common shares of Telesat Canada, at cost (Note 7)	600	600
Net investment in leases	1,057	696
	1,657	1,296
Current assets		
Accounts receivable	20,290	19,152
Prepaid expenses and other	3,932	2,541
	24,222	21,693
Deferred charges		
Unamortized discount and expenses on long-term debt	733	826
Unrealized foreign exchange loss	4,506	5,414
Other	239	355
	5,478	6,595
Total assets	$ 351,844	$336,633

On behalf of the Board of Directors, February 4, 1987

Raymond Sirois

Raymond Sirois, Director

Hervé Belzile, Director

As at December 31	1986	1985
SHAREHOLDERS' EQUITY AND LIABILITIES	Thousands of dollars	
Shareholders' equity (Note 8)		
Common share equity		
Common shares	$ **81,335**	$ 80,610
Reinvested earnings	**65,206**	60,654
	146,541	141,264
Subordinate Preferred shares	**3**	111
Preferred shares	**12,250**	17,921
	158,794	159,296
Long-term debt (Note 9)	**83,230**	87,441
Current liabilities		
Cheques issued in excess of bank balances	**5,979**	3,032
Short-term liabilities (Note 10)	**15,530**	1,131
Accounts payable		
Affiliates	**886**	1,744
Other	**10,904**	8,384
Advance billing	**3,422**	3,274
Dividends payable	**3,796**	3,819
Income taxes payable	**379**	3,605
Accrued interest	**3,673**	4,458
Other accrued liabilities	**9,012**	9,402
	53,581	38,849
Provision for research and development (Note 2)	**10,000**	—
Deferred income taxes	**46,239**	51,047
Total shareholders' equity and liabilities	$ **351,844**	$336,633

Simon Soucy

Simon Soucy
Vice President - Finance and Treasurer

CHANGES IN FINANCIAL POSITION

For the years ended December 31	1986	1985
	Thousands of dollars	
Cash provided from (used for) operating activities		
Net income applicable to Common shares	$ **18,948**	$ 20,516
Expenses not requiring cash		
Depreciation	**30,315**	35,451
Provision for research and development	**10,000**	—
Deferred income taxes	**(4,808)**	(5,822)
Allowance for funds used during construction	**(818)**	(869)
Other	**900**	1,442
	54,537	50,718
Net change in other current assets and liabilities excluding short-term liabilities (Note 11)	**(5,143)**	6,070
	49,394	56,788
Cash provided from (used for) financing activities		
Common shares issued	**617**	5,127
Redemptions of Preferred shares	**(5,630)**	(1,486)
Repayments of long-term debt	**(229)**	(185)
Change in short-term notes	**10,715**	(8,605)
	5,473	(5,149)
Cash provided from (used for) investing activities		
Additions to telecommunications property, net	**(43,057)**	(37,740)
Change in net investment in leases	**(361)**	46
	(43,418)	(37,694)
Increase in cash and cash equivalents before dividends on Common shares	**11,449**	13,945
Dividends on Common shares	**(14,396)**	(13,908)
Increase (decrease) in cash and cash equivalents	**(2,947)**	37
Cash and cash equivalents at beginning of year	**(3,032)**	(3,069)
Cash and cash equivalents at end of year	$ **(5,979)**	$ (3,032)

For the years ended December 31, 1986 and 1985

1. Significant Accounting Policies

The financial statements have been prepared in conformity with Canadian generally accepted accounting principles, and in accordance with prevailing practices in the Canadian telecommunications industry. Certain reclassifications were made in the financial statements of the preceding year to conform to the presentation adopted in 1986.

The regulated activities of the Company are subject to regulations of the *Régie des services publics* of Québec. Deregulated activities are not shown separately as they only represent a small portion of the Company's business. The capital investment for regulated and deregulated activities is considered by the *Régie* as capital invested by the Company to be used when calculating the Company's rate of return.

Earnings per Common Share
Earnings per Common share are calculated using the quarterly weighted average number of outstanding Common shares eligible for quarterly dividend.

Consolidation
The financial statements include the accounts of *La Compagnie de Téléphone Bonaventure et Gaspé, Limitée*, an inactive wholly-owned subsidiary.

Telecommunications Property
Telecommunications property is recorded at original cost and includes certain costs related to pension, payroll taxes and funds used during construction, applicable to the construction activity. The original cost of retired telecommunications property is charged to accumulated depreciation or to construction materials, when such property can be re-used; therefore, no gain or loss on retirement is recognized in the statement of income.

Depreciation
Depreciation of telecommunications property is mainly calculated according to the straight-line method using rates based on the estimated service life of the assets. Depreciation of these properties which regroup telephone sets and related wiring, "frozen-said assets", deregulated since July 1983, had been established under an accelerated recovery plan ending in the beginning of the 1990's.

Amortization of Discount and Expenses on Long-Term Debt
Discount and expenses on long-term debt are amortized using the straight-line method over the life of the related debt.

Income Taxes
The Company uses the tax allocation method to account for income taxes.

Long-Distance Service Revenues
The Company receives part of its long-distance service revenues pursuant to agreements with other telecommunications companies for services provided jointly. The Company's actual share of the joint business cannot be specifically determined before the completion of settlement studies. Related provisions are recorded in the books.

Translation of Foreign Currencies
Purchases of materials, operating costs and interest paid in foreign currencies are stated in these financial statements in Canadian dollars at the rate of exchange prevailing at the transaction date.

The long-term debt payable in U.S. funds is reflected in the financial statements at the Canadian dollar equivalent at the rate of exchange prevailing at the date of the balance sheet. Resulting gains or losses are amortized over the remaining life of this long-term debt.

Leases
Revenues from operating leases are accounted for at the time the services are provided to customers. In the case of sales-type leases, the gain or loss realized on the sale of the product is recorded at the effective date of the lease. Finance income related to sales-type leases is recognized in such a way as to produce a constant rate of return on the residual investment in leases.

2. *Régie des services publics* of Québec

Two orders were issued by the *Régie des services publics* of Québec on November 10, 1986. The order 85-057-C set the maximum rate of return on average common shareholders' equity to 13 % for 1986 and 12.5 % for 1987; it also directed the creation of a research and development fund in 1986. The order 85-015-A set the total depreciation expense to $ 30.3 million in 1986 and $ 33.1 million in 1987 as well as directed the write-off of certain fixed assets called frozen.

To comply with these orders, the Company charged to the fiscal period expenses an amount of $ 10 million to create a research and development fund in the telecommunications field; it also credited $ 3.1 million corresponding to one month of local basic service to its subscribers.

Moreover, the Company reduced by $ 7.8 million the depreciation expense forecast for 1986 by applying new depreciation rates on certain assets covered by the accelerated recovery program for which costs of new acquisitions are expensed since July 1983. This revision impacts on the recovery period of those assets by extending it up to the beginning of the 1990's while it was previously planned to end in 1989. Also, in accordance with the order 85-015-A, the Company wrote off some $ 28 million of fixed assets, mainly composed of inside wiring and applications software; these fixed assets were totally depreciated.

3. Other Income

Among others, this caption includes the allowance for funds used during construction. This allowance which amounted to $ 818,000 in 1986 ($ 869,000 in 1985) was applied to the telecommunications property at the rate of 12.64 % (13.00 % in 1985) and credited to other income. This rate reflects the Company's rate of return on total invested capital for the previous year.

4. Financial Expenses

	1986	1985
	Thousands of dollars	
Interest on long-term debt	$ 8,366	$ 8,374
Other interest — net amount	(293)	1,243
Amortization of unrealized loss on foreign currency	599	576
Amortization of discount and expenses on long-term debt	93	93
	$ 8,765	$ 10,286

5. Income Taxes

The Company has been assessed by the Department of National Revenue and by the *ministère du Revenu* of Québec up to and including December 31, 1985.

The reconciliation of the statutory and effective income tax rates is as follows:

	1986	1985
Statutory income tax rate (federal and provincial)	41.5 %	41.5 %
Provision for foreign exchange loss	0.7	0.6
Reversal of deferred income taxes, at historical rates	(0.4)	(1.9)
Federal surtax	2.0	1.2
Other items	(0.5)	0.3
Effective income tax rate	43.3 %	41.7%

Income taxes are as follows:

	1986	1985
	Thousands of dollars	
Current	$ 20,274	$ 20,970
Deferred	(5,084)	(5,459)
	$ 15,190	$ 15,511

6. Accumulated Depreciation

	1986	1985
	Thousands of dollars	
Balance at beginning of year	$ 199,023	$ 173,228
Depreciation of the year	30,315	35,451
Less: buildings, plant and equipment retired (net value)	10,081	9,656
write-off of frozen-said assets	27,809	—
Balance at end of year	$ 191,448	$ 199,023

For 1985, the total depreciation expense includes the accelerated depreciation of $ 2.8 million. The composite depreciation rate was 6.08 % in 1986 (7.51 % in 1985).

7. Investment

The investment in 60,000 Common shares of Telesat Canada, representing 1.0 % of the total outstanding shares, is recorded at original cost. There is no quoted market value for this investment; however, its estimated book value was $ 1,603,000 as at December 31, 1986.

8. Shareholders' Equity

Number of Shares at December 31

	Authorized	Outstanding	
		1986	1985
Common shares without nominal or par value	Unlimited	**15,730,404**	15,637,401
$ 1.68 Cumulative Redeemable Convertible Subordinate Preferred shares Series B of the par value of $ 15 each	541,322	**215**	6,919
Cumulative Redeemable Preferred shares of the par value of $ 20 each	1,297,279	**612,491**	896,064

During 1986, transactions related to the capital stock were as follows:

	Common	Subordinate Preferred	Preferred
Shares outstanding at December 31, 1985	15,637,401	6,919	896,064
Issued	72,891	—	—
Redeemed	—	—	(283,573)
Converted	20,112	(6,704)	—
Shares outstanding at December 31, 1986	**15,730,404**	**215**	**612,491**

Common Shares

During the Special General Meeting of Shareholders, held on April 1, 1986, Special By-Law No. 93, which modifies the Company's articles by subdividing each Common share of the Company issued and outstanding at the close of business on April 16, 1986 into three Common shares, was approved and ratified by the shareholders. Common share 1985 data have been restated to reflect the split.

During 1986, 72,891 Common shares were issued for $ 617,000 under the Employees' Stock Purchase Plan.

In addition, 6,704 $ 1.68 Cumulative Redeemable Convertible Subordinate Preferred shares Series B were converted into 20,112 Common shares.

Subordinate Preferred Shares

As of December 31, 1986, more than 85 % of the original issue of the $ 1.68 Cumulative Redeemable Convertible Subordinate Preferred shares Series B had been converted into Common shares.

The right to redeem these shares into Common shares, at the option of the holders, ended on June 30, 1986, and the Company has the option at any time to redeem all or part of the outstanding Series B shares at the agreed upon redemption price.

Preferred Shares

			Shares outstanding at December 31			
			1986	1985	**1986**	1985
Series					Thousands of dollars	
1955	5 %	(sinking fund)	**19,382**	34,794	$ **388**	$ 696
1956	5 %	(sinking fund)	**9,509**	14,054	**190**	281
1965	4 ¾ %		**400,000**	400,000	**8,000**	8,000
1973	7 ¾ %	(purchase fund)	**183,600**	197,200	**3,672**	3,944
1977	7 %	(sinking fund)	—	250,016	—	5,000
					$ **12,250**	$ 17,921

In order to meet the sinking fund requirements for the 1955 and 1956 Series, payments to be made before the end of fiscal 1991 will be as follows: $ 12,560 in 1989 and $ 25,000 for each of the years 1990 and 1991. In addition, the Company must make all reasonable efforts to redeem each year 9,000 Preferred shares Series 1973, at a price not exceeding $ 20.

The Company has met all requirements with respect to sinking and purchase funds.

9. Long-Term Debt

First Mortgage Bonds

Series	Rate	Maturing		Issued Thousands of dollars	1986	1985 Thousands of dollars
H	5 ½ %	June 1,	1987	$ 6,000	$ 3,775	$ 3,915
I	6 %	October 15,	1990	5,000	4,122	4,222
J	7 %	January 2,	1989	5,000	5,000	5,000
L	9 ⅛ %	April 15,	1991	7,500	358	358
M	8 ¾ %	May 15,	1992	7,500	7,500	7,500
N	8 ½ %	March 15,	1993	8,500	8,500	8,500
O	9 ¾ %	July 1,	1994	16,500 (U.S.)	22,790	23,077
P	11 ⅞ %	October 15,	1995	15,000	15,000	15,000
Q	10 ⅝ %	December 15,	1996	20,000	20,000	20,000
Less: current portion					3,815	131
					$ 83,230	$ 87,441

The Trust Deeds of the Company require the use of a sinking fund or the pledge of additional unmortgaged property for each of the series as follows:

a) Series H and I
Annual payment of 1 ½ % of the principal amount of the bonds issued.

b) Series J, M, N, O, P and Q
Annual payment of 1 % or additional mortgage of 1 ½ % of the principal amount of bonds issued; the Company has constantly used the latter alternative.

c) Series L
Annual payment of $ 8,960 representing 2 % of the aggregate principal amount of bonds issued and not prepaid on April 15, 1975.

To meet the sinking fund requirements and the debt retirements, the following payments will have to be made during the next five years: $ 3,815,000 in 1987, $ 84,000 in 1988, $ 5,084,000 in 1989, $ 3,959,000 in 1990 and $ 314,000 in 1991.

First Mortgage Bonds of all series are secured equally and rateably under a fixed and specific hypothec, mortgage, pledge, charge, cession and transfer of/and on all immovable property, such as buildings, equipment, telephone lines and apparatus, rights-of-way and similar rights and a floating charge on all other assets.

10. Short-Term Liabilities

	1986	1985 Thousands of dollars
Short-term notes		
Bank	$ 215	$ 1,000
Promissory notes	11,500	—
Current portion of long-term debt	3,815	131
	$ 15,530	$ 1,131

The average interest rate on short-term notes was 10.09 % in 1986 and 10.16 % in 1985.

The Company's policy is to utilize short-term notes as interim financing.

The short-term notes are considered in computing the average debt service cost and the rate of return on average invested capital.

11. Net Change in Other Current Assets and Liabilities Excluding Short-Term Notes

	1986	1985 Thousands of dollars
(Increase) decrease in current assets		
Accounts receivable and other	$ (1,138)	$ 522
Prepaid expenses and other	(1,391)	(1,345)
Increase (decrease) in current liabilities		
Accounts payable and other	612	4,011
Income taxes payable	(3,226)	2,882
	$ (5,143)	$ 6,070

12. Pension Plan

The Company maintains a pension plan for the benefit of its employees and complies with the requirements of the Québec Supplemental Pension Plans Act. The unfunded liability, determined by actuarial valuation, is funded by annual payments charged to operating expenses in accordance with legal requirements.

Based on the last actuarial valuation, the unfunded liability was $ 2,269,000 as of December 31, 1986 and will be amortized by annual instalments of $ 292,000 including interest, up to December 31, 2000.

The Company improved the pension plan of its employees at additional costs of $ 2.6 million in 1986 and $ 0.9 million in 1985 which were recorded in the results of the related fiscal years.

Pension costs were $ 5,371,000 for the year ended December 31, 1986 and $ 3,097,000 for 1985.

13. Capital Expenditures Program

The capital expenditures program in 1987 is estimated at $ 54.0 million, including the cost of re-usable material and equipment; purchase commitments amounting to approximately $ 6.1 million have been made in connection therewith as of December 31, 1986.

14. Remuneration of Directors and Officers

The total direct remuneration, including benefits, paid to directors and officers was $ 899,000 in 1986 and $ 777,000 in 1985.

15. Related Party Transactions

GTE International Incorporated, GTE Service Corporation, *La Compagnie de Téléphone Anglo-Canadienne, Microtel Limitée, GTE Sylvania Canada Limitée* and Dominion Directory Company Limited and their respective subsidiaries are direct or indirect affiliates of the Company.

The Company's policy is to purchase high-quality goods and services at the best possible price. Consequently, no advantage is given to affiliates and transactions with these are made on a competitive basis, that is at the same or better conditions which would have prevailed if the parties had not been affiliated.

Out of a total disbursement of $ 92.5 million in dividends, goods and services, in 1986 the Company has paid $ 12.5 million to affiliates.

QUARTERLY FINANCIAL DATA 1986 (unaudited)

QUÉBEC-TÉLÉPHONE

Three months ended	March 31	June 30	Sept. 30	Dec. 31 *
				Thousands of dollars
Revenues	$ 44,183	$ 45,955	$ 47,525	$ 45,004
Maintenance	8,400	8,289	9,611	10,539
Depreciation	9,034	9,239	9,599	2,443
Other operating expenses	11,234	11,217	13,376	15,064
Taxes other than income taxes	3,552	3,711	3,674	2,106
Research and development	—	—	—	10,000
	32,220	32,456	36,260	40,152
Operating income	11,963	13,499	11,265	4,852
Other income	524	600	479	700
Income before financial expenses and income taxes	12,487	14,099	11,744	5,552
Financial expenses	2,581	2,655	2,466	1,063
Income before income taxes	9,906	11,444	9,278	4,489
Income taxes	4,223	4,826	3,986	2,155
Net income	5,683	6,618	5,292	2,334
Dividends on Preferred and Subordinate Preferred shares	273	264	265	177
Net income applicable to Common shares	$ 5,410	$ 6,354	$ 5,027	$ 2,157
Earnings per Common share	$ 0.35	$ 0.40	$ 0.32	$ 0.14
Dividends declared per Common share	$ 0.22 ⅔	$ 0.23	$ 0.23	$ 0.23

Note: All data related to Common shares were restated to reflect the three-for-one stock split effective April 16, 1986.

* Financial data for the 4th quarter of 1986 reflect the effects of orders 85-057-C and 85-015-A issued by the *Régie des services publics* of Québec on November 10, 1986. (See note 2 accompanying financial statements.)

FIVE-YEAR REVIEW

	1986	1985	1984	1983	1982
Selected results and reinvested earnings items					
(thousands of dollars)					
Revenues	**$ 182,667**	$ 176,525	$ 164,066	$ 153,596	$ 139,587
Maintenance and other operating expenses	**87,730**	82,231	74,417	67,116	62,534
Depreciation	**30,315**	35,451	32,635	28,453	24,627
Taxes other than income taxes	**13,043**	13,112	13,086	12,114	11,190
Research and development	**10,000**	—	—	—	—
Total operating expenses	**141,088**	130,794	120,138	107,683	98,351
Financial expenses	**8,765**	10,286	12,369	13,029	13,927
Income taxes	**15,190**	15,511	13,812	14,707	13,182
Net income	**19,927**	21,663	19,345	19,430	15,634
Dividends on Preferred and Subordinate Preferred shares	**979**	1,147	1,270	1,385	1,507
Net income applicable to Common shares	**18,948**	20,516	18,075	18,045	14,127
Dividends on Common shares	**14,396**	13,908	12,334	10,104	8,576
Selected balance sheet items					
(thousands of dollars)					
Telecommunications property, at cost	**$ 511,935**	$ 506,072	$ 477,267	$ 463,385	$ 445,771
Accumulated depreciation	**191,448**	199,023	173,228	155,232	136,819
Common share equity	**146,541**	141,264	129,511	112,966	97,431
Preferred and Subordinate Preferred shares	**12,253**	18,032	19,572	20,986	22,480
Long-term debt	**83,230**	87,441	86,306	85,235	116,465
Short-term liabilities	**15,530**	1,131	9,766	19,212	9,770
Financial statistics					
Earnings per Common share (4)	**$ 1.21**	$ 1.32	$ 1.24	$ 1.32	$ 1.12
Dividends declared per Common share (4)	**$ 0.91 ⅔**	$ 0.89 ⅔	$ 0.84 ⅓	$ 0.74	$ 0.67 ⅔
Dividend payout ratio	**76.0 %**	67.8 %	68.2 %	56.0 %	60.7 %
Common equity per share (1)(4)	**$ 9.32**	$ 9.03	$ 8.55	$ 8.04	$ 7.45
Common share market price (2)(4)					
High	**$ 16.00**	$ 15.00	$ 11.33	$ 10.50	$ 6.96
Low	**$ 13.63**	$ 11.17	$ 9.63	$ 6.58	$ 5.25
Close	**$ 14.13**	$ 14.50	$ 11.33	$ 10.00	$ 6.96
Return on average Common share equity	**13.0 %**	15.0 %	15.0 %	17.1 %	15.5 %
Return on average invested capital (3)	**11.6 %**	12.6 %	13.0 %	13.2 %	12.1 %
Average debt service cost (3)	**10.5 %**	10.5 %	10.8 %	10.2 %	10.6 %
Debt ratio (3)	**40.3 %**	35.7 %	39.2 %	43.8 %	51.3 %
Interest coverage on long-term debt (times)	**5.17**	5.44	4.94	4.17	3.54
Other statistics					
Average number of Common shares (thousands) (4)	**15,703**	15,509	14,611	13,642	12,666
Number of Common shareholders (1)	**5,935**	5,806	6,312	3,955	3,617
Number of employees (1)	**1,978**	1,972	1,993	2,023	2,036
Salaries and wages (thousands of dollars)	**$ 61,216**	$ 59,577	$ 56,879	$ 52,605	$ 50,213
Gross capital expenditures (thousands of dollars)	**$ 43,787**	$ 39,255	$ 31,734	$ 29,190	$ 34,869
Telecommunications property per subscriber line in service (1)	**$ 2,259**	$ 2,285	$ 2,212	$ 2,212	$ 2,180
Subscriber lines in service (1)	**226,580**	221,471	215,751	209,492	204,455
Terminals in service (1)	**285,231**	290,597	290,892	290,713	287,318
Toll messages handled (thousands)	**34,553**	32,903	31,099	29,501	28,175

(1) At December 31
(2) Valuation day value (December 22, 1971): $ 4.58 ⅓ per share
(3) See note 10 to financial statements
(4) All data related to Common shares were restated to reflect the three-for-one stock split effective April 16, 1986

BOARD OF DIRECTORS

Hervé Belzile †
Chairman of the Board
Alliance compagnie mutuelle d'assurance-vie
(Director since 1971)

Jean Gaulin *
President
Ultramar Canada, Inc.
(Director since 1985)

John E. Hougton ‡
President and Chief Executive Officer
The Ontario Paper Company Limited
and *La Compagnie de Papier Q.N.S., Limitée*
(Director since 1985)

James L. Johnson
President and Chief
Operating Officer
GTE Service Corporation
(Director since 1980)

Charles Mercier *
Vice President -
Marketing and Customer Service
Québec-Téléphone
(retired since September 1, 1986;
was Director since 1975)

Roger Néron †
Administrator
(Director since 1983)

Bernard Panet-Raymond * †
President
O.R.C. Canada Inc.
(Director since 1968)

Claude Pratte, Q.C. * ‡
Advocate
(Director since 1964)

Raymond Sirois * *
Chairman of the Board,
President and Chief Executive Officer
Québec-Téléphone
(Director since 1969)

Kent B. Foster
Group Vice President -
Telephone Operating Group
GTE Service Corporation
(Director since 1985)

Antoine Turmel, O.C. ‡
Administrator
(Director since 1973)

* * president of executive committee
* member of executive committee
† member of audit committee
‡ member of compensation committee

OFFICERS

Raymond Sirois
President and Chief Executive Officer

Robert Duchesne
Vice President -
Marketing and Customer Service

Ghislain Bouchard
Vice President -
Human Resources and Legal Affairs,
Secretary

Gilles Laroche
Vice President -
Network Engineering and Construction

Simon Soucy
Vice President -
Finance and Treasurer

Yvon Gendron
Vice President -
Business Development

Andrée Bélanger
Assistant Secretary

INFORMATION TO SHAREHOLDERS

Head Office
6, rue Jules-A.-Brillant
Rimouski, Québec G5L 7E4

Incorporation and Regulation
Québec-Téléphone is incorporated under the laws of Québec by Letters Patent dated June 7, 1927 and its regulated activities are subject to the regulatory authority of the *Régie des services publics* of Québec.

Major Shareholder
As at December 31, 1986, *La Compagnie de Téléphone Anglo-Canadienne,* 8750, chemin de la Côte-de-Liesse, Saint-Laurent, Québec owned 7,919,847 Common shares of Québec-Téléphone, or 50.3 % of outstanding Common shares.

Dividends
Dividends on Common, Preferred and Subordinate Preferred shares are usually payable on the first day of January, April, July and October of each year.

Listing of Shares
Common shares, 4 ¾ % Preferred shares Series 1965, 7 ¾ % Preferred shares Series 1973 and $ 1.68 Cumulative Redeemable Convertible Subordinate Preferred shares Series B are listed on the Montréal and Toronto stock exchanges.

The 5 % Preferred shares Series 1955 and 1956 are listed on the Montréal stock exchange.

Stock Transfer Offices
Trust Général du Canada, 1100, rue University, Montréal, Québec H3B 2G7, is the Registrar and Transfer Agent for all classes of shares of the Company. *Compagnie Trust Royal* is the Co-Transfer Agent and Registrar for the 4 ¾ % Preferred shares Series 1965, at its offices in Toronto and Winnipeg, and is the Co-Transfer Agent and Registrar for the 7 ¾ % Preferred shares Series 1973, for the $ 1.68 Cumulative Redeemable Convertible Subordinate Preferred shares Series B and for the Company's Common shares at its offices in Saint John, N.-B., Toronto, Winnipeg, Regina, Calgary and Vancouver.

Valuation Day
The value of a Common share of the Company on valuation day, December 22, 1971, recognized by the Department of National Revenue for capital gains tax purposes, was $ 4.58 ⅓, after reflecting the three-for-one stock split effective April 16, 1986.

Trustee for Bonds
Trust Général du Canada
1100, rue University
Montréal, Québec H3B 2G7

Bankers
Banque Nationale du Canada
Banque de Montréal

Publications Available to Shareholders
Interim Reports are published quarterly and sent to shareholders in February, May, August and November. The Annual Report is mailed to registered shareholders in March along with the notice of annual general meeting for Common shareholders.

Duplicate Shareholder Information
Every effort is made to eliminate duplication in our shareholders mailing list. However, if a shareholder has more than one holding, duplication cannot be avoided unless he requires the Company or its Transfer Agent to merge his accounts under exactly the same name and address.

Annual Meeting
Usually, the annual meeting is held in April; this year, the meeting will take place at 11:00 a.m., E.S.T., Wednesday, April 1, 1987 at *Hôtel St-Louis,* 214, rue St-Edmond, Rimouski, Québec.

1987

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QUEBEC-TELEPHONE

Head Office: 6, rue Jules-A. Brillant, Rimouski, Québec G5L 7E[illegible]