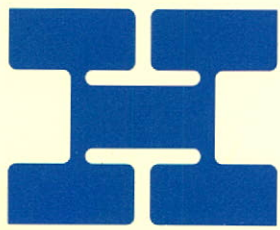


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**D.H. HOWDEN  
& CO. LIMITED**

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ANNUAL REPORT  
1985

## Highlights (in thousands)

	1985	1984
Gross sales	\$106,608	\$111,638
Net income	961	853
Basic earnings per common share	\$1.92	\$1.71
Working capital	17,176	17,440
Decrease (increase) in operating net assets	(209)	101
Ratio of current assets to current liabilities	2.71:1	2.83:1
Shareholders' equity per common share	\$23.94	\$22.52
Return on net worth	8.53%	8.00%
Dividends paid on common shares	\$ .50	\$ .50

## Directors

JOHN W. ADAMS, F.C.A.  
Chairman, Emco Limited

T. BRAYL COPP  
President, Copp Builders' Supply  
Company Limited

TONY J. CRNCICH  
Chairman and Chief Executive Officer  
Big V Pharmacies Company Ltd.

JOHN B. CRONYN  
Company Director, John Labatt Limited

PETER R. LOCKYER  
Partner, Harrison, Elwood, Barristers  
and Solicitors

KEITH A. MITCHELL  
Retired: Formerly Senior Vice President,  
Beaver Lumber Company Limited

W. MOWBRAY SIFTON  
Chairman, Sifton Properties Limited

DAVID H.M. STEWART  
Chairman of the Board,  
D.H. Howden & Co. Limited

MICHAEL C. TUCKER  
President, D.H. Howden & Co. Limited  
and Pro Hardware (Canada) Limited

### Head Office

635 Southdale Road,  
P.O. Box 2485  
London, Ontario N6A 4G8

### Quebec Office

Distribution Howden  
750 St-Jean-Baptiste, Bureau: 150,  
Quebec City G2E 5J5

### Auditors

Touche Ross & Co.

## Officers

D.H.M. STEWART  
Chairman of the Board

M.C. TUCKER  
President

S.R. MILLAR  
Vice President Administration  
and Secretary

K.G. ALLASTER, C.A.  
Vice President Finance and Treasurer

F.P. FORAN  
Vice President - Sales

M.C. HUMPHREY  
Vice President - Distribution

R.C. McKERLIE  
Vice President - Merchandising

### Listing of Common Stock

Toronto Stock Exchange

### General Counsel

Harrison, Elwood, Barristers and  
Solicitors

### Transfer Agent & Registrar

The Canada Trust Company, Toronto

### Annual Meeting

The Annual Meeting of the  
Shareholders of the Corporation  
will be held in the Lounge Gallery,  
London Regional Art Gallery,  
421 Ridout Street, North, London,  
Ontario, on Thursday, the 22nd of May,  
1986, at the hour of 11:30 a.m.

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## Report to Shareholders

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**C**onsolidated sales for 1985 were \$106.6 million and when compared with 1984 sales of \$111.6 million, show a decrease of 4.5%.

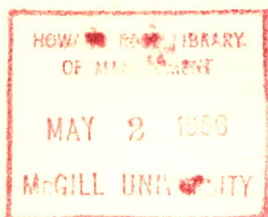
Consolidated net profit was \$960,538 (\$1.92 per common share) compared to \$852,952 in 1984 (\$1.71 per common share).

The results for 1985, although improved somewhat over 1984, continued to reflect expenses from problem stores carried over from the early 1980's. This, by and large, has been cleaned up and we can expect to return to more normal standards for bad debt reserves in the future. Sales to franchised dealers grew, and we continued to build and enhance programs that in the long run will help ensure our marketing position in the future.

Howden has, over the years, developed into a marketing organization whose sole source of revenue and profit is based on our ability to influence consumer spending in our retail customers' stores. Because of this, we have put our primary emphasis on the development of marketing programs and systems which have completely restructured our franchising organizations over the last five years and positioned us for future growth and stability.

### **Do-it Center Development**

Late in 1984, we became the licensee for the highly successful Do-it center marketing program, which we immediately positioned to sell to the building supply/home center retailer. During 1985, we opened four Do-it centers and signed an additional 21. At present, 18 of the 21 are underway with their store renovations and remerchandising and are scheduled for openings early in 1986. It is significant that four of these stores, including some of the largest, are in the Province of Quebec and specifically in Montreal. This will give us a tremendous boost in Quebec and a nucleus of stores from which to grow. We were greatly encouraged by the results of the new Do-it stores that opened during 1985, since some experienced sales increases of as much as 50%. The Do-it center concept, positioned primarily for home centers and building supply dealers, is right for the 80's and will provide a strong base for us to continue our growth in conjunction with building supply groups across Canada.



### **Pro Hardware Development**

We also completed the planning and development of the new Pro logo and store image program that was launched late in 1985. We opened a pilot store in the White Oaks shopping mall in October 1985, complete with all the new components of the marketing program. The introduction of this new concept was a complete success, and the store has continued to attract favourable comments from both consumers and existing Pro hardware dealers. As a result, in conjunction with customer stores, we have ten conversions to the new format underway for Spring openings. Specifically the new concept will provide for brighter and better designed stores, improved merchandising displays, and greater overall consumer appeal. We feel this program will be the foundation for a new era in Pro hardware marketing.

Advertising support for our Pro customers continued with ten catalogue events that were more competitively priced at retail than ever before. These events were supported by a very aggressive TV program in each of the Provinces of Ontario and Newfoundland. The theme line was, "If it's not a Pro, just what kind of hardware store is it?" The program was an outstanding success and will be repeated again in 1986. Overall, it has provided for much greater consumer awareness and acceptance of our Pro hardware stores.

### **Systems Development**

We continue to lead the industry in the development of electronic dealer communication systems. The Displayphone was introduced in 1984 and has now grown in use to over 400 on-site units. Displayphone is the method by which either a dealer or our sales personnel can communicate directly with our computer in London to obtain vital product information. It is supported by Bell Canada's iNet Information Network, which provides low cost access from any point in Canada. A new application for Displayphone, developed this year, was in the area of electronic mail. This new program allows us to both send and receive messages electronically from our customers and sales staff. In 1986, we are also testing with selected vendors the same accessing process as a means of communicating directly both with our dealers and amongst ourselves.

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We also successfully launched a point-of-sale cash register system called CashHandler. This low cost but effective cash register with computer support is providing accounts receivable, item history, and a variety of other information to our retail customers on a very low cost basis. This system is supported by our communication network which communicates directly with our customer's computer, thereby eliminating duplication of file maintenance work. Twenty dealers began using this system in 1985.

### **Distribution Development**

As a national distributor serving consumers and selective retailers from coast-to-coast, Howden operates from two large, central distribution centres which are located in London and total some 400,000 square feet.

Utilizing state-of-the-art computer and data communications technology, Howden receives customer orders, sales, inventory and financial data from all regions of Canada on an immediate and economical basis.

During 1985, the Howden fleet (consisting of 36 tractor units, 70 trailer units and 7 straight trucks) travelled a total of 5,802,000 kilometers servicing all of our customers on a weekly basis – with the exception of Newfoundland and Northern B.C., which are scheduled on a bi-weekly basis.

The Howden fleet maximizes truck utilization by delivering merchandise to the retailer and then picking up new merchandise from suppliers on the return trip in order to replenish inventory at the central distribution centres.

### **Future Development**

The success of any organization is ultimately determined by its ability to adapt to the changing market place. The last five years have seen a tremendous rebuilding within our organization to meet both a rapidly changing market place and dealer network. We feel we are successfully responding to the marketing requirements of the 80's and 90's with the programs now being launched which include: store retrofit/image, merchandising, communication, training and market analysis. Our overriding mission statement of "We Think Retail" is reflected in every program and in every job within our organization. Our entire staff has been devoted to serving our customers better with existing services while at the same time introducing new programs into our stores. Their support, spirit and co-operation cannot be overstated nor can their ongoing enthusiasm shown toward the success of our business in general. We expect that the next five years will be challenging and will provide new growth opportunities not only for our existing customers but for new customers as well.



D.H.M. Stewart, Chairman of the Board



M.C. Tucker, President

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## **Auditors' Report**

The Shareholders,  
D.H. Howden & Co. Limited.

We have examined the consolidated balance sheet of D.H. Howden & Co. Limited as at December 31, 1985 and the consolidated statements of income, retained earnings and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the Corporation as at December 31, 1985 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.

London, Ontario  
February 21, 1986.

TOUCHE ROSS & CO.  
Chartered Accountants.

## **Management's Report to the Shareholders**

The financial statements of the Corporation have been prepared by management in accordance with generally accepted accounting principles consistently applied. Management is responsible for all information in the Annual Report and financial and operating data in the Report are consistent, where appropriate, with the financial statements.

Because a precise determination of many assets and liabilities is dependent upon future events, the preparation of periodic financial statements necessarily involves the use of estimates and approximations. These have been made using careful judgment and with all information available up to February 21, 1986. The financial statements have, in management's opinion, been properly prepared within reasonable limits of materiality and within the framework of the accounting policies summarized in note 1 of the notes to the consolidated financial statements.

The Board of Directors annually appoints an Audit Committee, a majority of whom are not employees of the Corporation. The committee meets with management, the Corporation's internal auditors, and the independent auditors to review any significant accounting and auditing matters and discuss the results of audit examinations. The Audit Committee also reviews the financial statements and the auditors' report and submits its finding to the Board of Directors for their consideration in approving the financial statements.

London, Ontario  
February 21, 1986

Michael C. Tucker  
President

Kingsley G. Allaster  
VP Finance & Treasurer

**Consolidated Balance Sheet** as at December 31, 1985

<b>Assets</b>	<b>1985</b>	1984
<b>Current</b>		
Cash	\$ 156,779	\$ 129,503
Accounts receivable	12,086,636	13,266,864
Inventories	14,058,733	12,798,196
Prepaid expenses	678,441	671,715
Income taxes recoverable	219,585	103,596
	<b>27,200,174</b>	26,969,874
<b>Property, plant and equipment</b> (Notes 2 and 3)	<b>5,465,072</b>	5,561,950
	<b>\$32,665,246</b>	\$32,531,824
<b>Liabilities</b>	<b>1985</b>	1984
<b>Current</b>		
Bank indebtedness (Note 4)	\$ 500,000	\$ —
Accounts payable and accrued liabilities	8,344,856	8,413,244
Current portion of long-term debt (Note 5)	895,907	893,331
Current portion of obligation under capital leases (Note 3)	283,464	223,592
	<b>10,024,227</b>	9,530,167
<b>Long-term debt (Note 5)</b>	<b>9,418,229</b>	10,344,137
<b>Obligation under capital leases (Note 3)</b>	<b>497,262</b>	669,730
<b>Security deposits (Note 6)</b>	<b>754,700</b>	727,500
<b>Contingent liabilities (Note 7)</b>		
<b>Shareholders' Equity</b>		
<b>Capital stock</b>		
Common shares		
Authorized 950,000 shares		
Issued 500,000 shares	564,546	564,546
<b>Retained earnings</b>	<b>11,406,282</b>	10,695,744
	<b>11,970,828</b>	11,260,290
	<b>\$32,665,246</b>	\$32,531,824

On behalf of the Board

Director D.H.M. STEWART

Director M.C. TUCKER

See accompanying notes to consolidated financial statements.



**Consolidated Statement of Changes in Financial Position**

For The Year Ended December 31, 1985

	1985	1984
<b>Cash provided by (used in) operations</b>		
Net income for the year	\$ 960,538	\$ 852,952
Items not requiring cash		
Depreciation and amortization	685,834	624,443
Working capital provided by operations	1,646,372	1,477,395
(Increase) decrease in operating net assets	(208,964)	101,359
Dividends paid	(250,000)	(250,000)
	<b>1,187,408</b>	1,328,754
<b>Financing</b>		
Increase (decrease) in bank indebtedness	500,000	(2,400,000)
Proceeds from long-term debt	—	2,500,000
Decrease in long-term debt	(925,908)	(1,153,578)
(Decrease) increase in obligations arising from capitalization of leases	(172,468)	30,433
Proceeds from security deposits	113,200	210,000
Repayment of security deposits	(86,000)	(71,000)
	<b>(571,176)</b>	(884,145)
<b>Cash invested</b>		
Expenditures for property, plant and equipment	654,837	680,600
Disposals of property, plant and equipment	(65,881)	(294,983)
	<b>588,956</b>	385,617
<b>Increase in cash</b>	<b>27,276</b>	58,992
<b>Cash at beginning of year</b>	<b>129,503</b>	70,511
<b>Cash at end of year</b>	<b>\$ 156,779</b>	<b>\$ 129,503</b>
<b>Decrease (increase) in operating net assets provided by</b>		
Decrease (increase) in		
Accounts receivable	\$1,180,228	\$ 880,365
Inventories	(1,260,537)	2,477,659
Other current assets	(122,715)	(418,571)
(Decrease) increase in		
Accounts payable and accrued liabilities	(68,388)	(1,553,051)
Other current liabilities	62,448	(1,285,043)
	<b>\$ (208,964)</b>	<b>\$ 101,359</b>

See accompanying notes to consolidated financial statements.

**Consolidated Statement of Income**

For The Year Ended December 31, 1985

	1985	1984
<b>Gross Sales</b>	<b>\$106,608,193</b>	\$111,638,222
Less sales tax	<b>5,046,930</b>	4,932,134
	<b>101,561,263</b>	106,706,088
<b>Cost of sales and operating expenses other than items noted below</b>	<b>97,785,062</b>	102,828,157
Interest – bank indebtedness	<b>157,410</b>	478,953
– long-term debt	<b>1,396,019</b>	1,414,483
Depreciation and amortization	<b>685,834</b>	624,443
	<b>100,024,325</b>	105,346,036
<b>Income before income taxes</b>	<b>1,536,938</b>	1,360,052
<b>Income taxes</b>	<b>576,400</b>	507,100
<b>Net income for the year</b>	<b>\$ 960,538</b>	\$ 852,952
<b>Basic earnings per common share</b>	<b>\$1.92</b>	\$1.71

**Consolidated Statement of Retained Earnings**

For The Year Ended December 31, 1985

	1985	1984
<b>Retained earnings, beginning of year</b>	<b>\$10,695,744</b>	\$10,092,792
<b>Net income for the year</b>	<b>960,538</b>	852,952
	<b>11,656,282</b>	10,945,744
<b>Dividends</b>		
Common shares	<b>250,000</b>	250,000
<b>Retained earnings, end of year</b>	<b>\$11,406,282</b>	\$10,695,744

See accompanying notes to consolidated financial statements.

**Notes to Consolidated Financial Statements**

December 31, 1985

**1. Summary of significant accounting policies**

The consolidated financial statements have been prepared in accordance with generally accepted accounting principles consistently applied and those of particular significance are set out below.

## a) Principles of consolidation

The consolidated financial statements include the accounts of the Corporation and its wholly-owned subsidiaries, D.H. Howden Stores (Central) Limited, Cowan Hardware (1968) Limited, Howden-Howland Limited and Pro Hardware (Canada) Limited.

## b) Inventories

Inventories consist of finished goods and are valued at the lower of cost on a first-in, first-out basis and net realizable value.

## c) Property, plant and equipment

Property, plant and equipment are recorded at cost. When an asset is sold, or otherwise disposed of, the related cost and accumulated depreciation are removed from the respective accounts and any gain or loss on disposition is recognized in earnings. Commencing in 1979, equipment leased under contracts is capitalized and the related lease obligations are reflected as liabilities. Depreciation and amortization are provided on the various classes of assets using the following methods at the following rates:

Buildings	5% straight-line
Roadways	4% - 8% declining balance
Equipment	20% - 30% declining balance
Leasehold improvements	Straight-line over term of lease
Equipment under capital leases	Straight-line over the economic life of the asset

**2. Property, plant and equipment**

	1985	1984
Building and roadways	\$3,767,341	\$3,767,341
Equipment and leasehold improvements	3,305,029	2,872,670
Equipment under capital leases	1,600,588	1,474,401
	<b>8,672,958</b>	8,114,412
Less accumulated depreciation and amortization	4,004,581	3,349,157
	<b>4,668,377</b>	4,765,255
Land	796,695	796,695
	<b>\$5,465,072</b>	\$5,561,950

**3. Leases**

For all leases entered into after January 1, 1979, the Corporation has adopted the recommendations for accounting for leases issued by the Canadian Institute of Chartered Accountants. The recommendations have not been adopted on a retroactive basis.

## a) Capital leases – commencing after January 1, 1979

The capitalized value and amortization of such leases is contained in Note 2 to these consolidated financial statements.

## b) Capital leases – commencing prior to January 1, 1979

The following is an analysis of equipment and building leases currently defined as capital leases for which the current recommendations have not been adopted. These are included in the consolidated financial statements as operating leases during the transitional period. Had such leases been accounted for as capital leases, the effect on the balance sheet for 1985 and 1984 comparative figures would have been as follows:

**Assets**

	1985	1984
Buildings, at capitalized value	\$1,930,074	\$1,930,074
Equipment, at capitalized value	177,253	177,253
	<b>2,107,327</b>	2,107,327
Less accumulated amortization	943,901	887,547
	<b>\$1,163,426</b>	\$1,219,780

**Liabilities and Shareholders' Equity**

Current portion of obligation under capital leases	\$ 44,651	\$ 109,253
Obligation under capital leases	1,409,613	1,454,264
Deferred income taxes	(148,327)	(175,306)
	<b>1,305,937</b>	1,388,211
Retained earnings	(142,511)	(168,431)
	<b>\$1,163,426</b>	\$1,219,780

A prior period adjustment of \$167,544 to reduce the opening balance of 1984 retained earnings would have been required to reflect the capitalization of leases on a retroactive basis.

## c) Lease payments

The following is a schedule of future minimum lease payments for leases capitalized by the Corporation and for those capital leases treated as operating leases during the transitional period.

	Capital Leases	Operating Leases
Year ending December 31, 1986	\$368,009	\$ 675,000
1987	282,707	642,000
1988	188,995	594,000
1989	88,596	374,000
1990	15,410	263,000
	943,717	2,548,000
Less amounts representing interest at various rates ranging from 9.26% to 19%	162,991	—
	780,726	2,548,000
Less portion due within one year	283,464	—
	<b>\$497,262</b>	<b>\$2,548,000</b>

**4. Bank indebtedness**

Accounts receivable have been assigned as security for bank indebtedness.

**Notes to Consolidated Financial Statements** (continued)

December 31, 1985

<b>5. Long-term debt</b>	<b>1985</b>	1984
10¾% mortgage, payable \$24,091 monthly including interest and maturing July 1, 1989 with land and building pledged as security.	<b>\$2,514,136</b>	\$2,537,468
Term bank loan, payable \$870,000 principal annually plus interest with a final principal payment of \$2,580,000, maturing May 1, 1992 with interest varying from time to time related to the lender's cost of borrowing. The rates at December 31, 1985 were: 13¼% on \$2,700,000, 10½% on \$2,600,000 and 13½% on \$2,500,000. A fixed and floating charge debenture on all Corporate assets has been pledged as security. Such security is subordinate to that provided for the mortgage and the bank indebtedness described in Note 4.	<b>7,800,000</b>	8,700,000
	<b>10,314,136</b>	11,237,468
Less portion due within one year	<b>895,907</b>	893,331
	<b>\$9,418,229</b>	\$10,344,137

**6. Security deposits**

Security deposits represent funds deposited by certain dealers in accordance with their franchise agreements. These deposits are refundable upon termination of the franchise agreement.

The security deposits are included in equity for purposes of calculating financial compliance ratios.

During the year the Corporation issued \$113,200 (1984 - \$210,000) and redeemed \$86,000 (1984 - \$71,000) of security deposits.

**7. Contingent liabilities**

The Corporation was contingently liable at December 31 for guarantees of franchise store leases in the amount of \$990,000 (1984 - \$1,369,000).

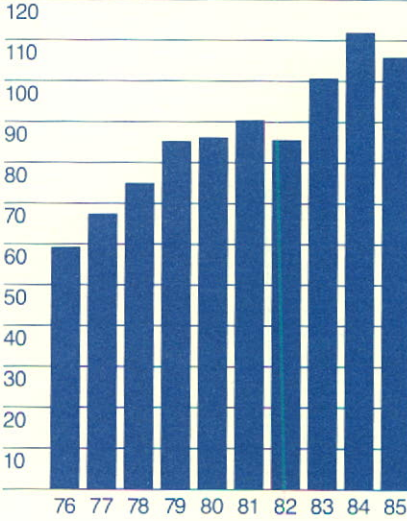
**8. Income taxes**

A reconciliation of the statutory income tax rate to the effective income tax rate is as follows:

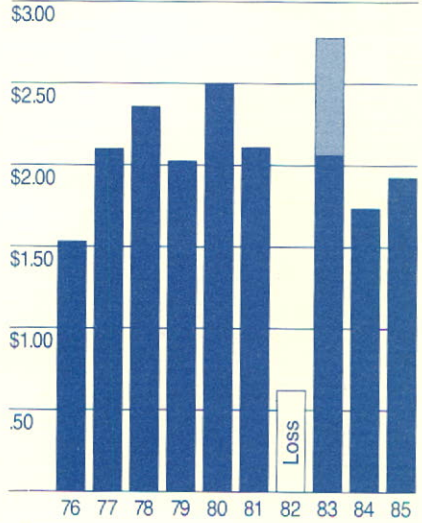
	<b>1985</b>	1984
Statutory income tax rate in Canada	<b>51.9%</b>	51.0%
Inventory credit	<b>(13.0)</b>	(17.5)
Other	<b>(1.4)</b>	3.8
Effective income tax rate	<b>37.5%</b>	37.3%

# Financial Review

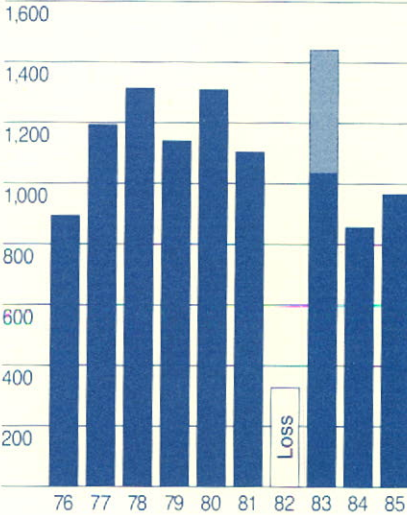
**Gross Sales** (in millions of dollars)



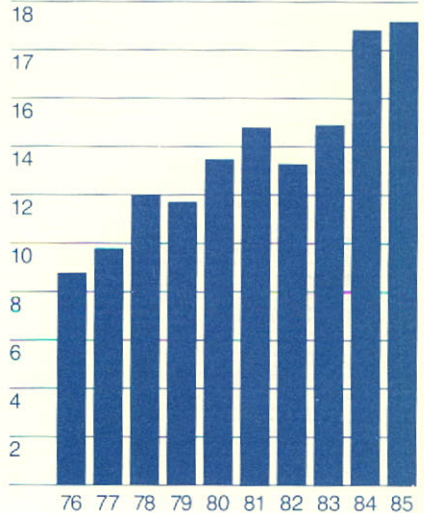
**Earnings Per Common Share** (dollars)



**Net Income** (in thousands of dollars)



**Working Capital** (in millions of dollars)

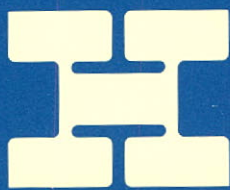


**10 Year Highlights**

(in thousands)

	1985	1984	1983	1982 (Restated)
<b>Operating Results</b>				
Gross sales	\$106,608	\$111,638	\$100,405	\$85,308
Income before income taxes and extraordinary items	1,537	1,360	1,744	(529)
Income taxes	576	507	707	(209)
Income before extraordinary item	961	853	1,037	(320)
Extraordinary item	—	—	393	—
Net income	961	853	1,430	(320)
Retained earnings	11,406	10,696	10,093	8,913
<b>Financial Position</b>				
Accounts receivable	12,087	13,267	14,147	13,609
Inventories	14,059	12,798	15,276	10,344
Total current liabilities	10,024	9,530	14,768	11,447
Working capital	17,176	17,440	15,082	13,475
Property, plant and equipment	5,465	5,562	5,801	5,439
Total long-term liabilities	10,670	11,742	10,226	9,009
Shareholders' equity	11,971	11,260	10,657	10,070
Return on net worth (January 1)	8.53%	8.00%	14.20%	(3.00%)
<b>Per Common Share</b>				
Earnings before extraordinary item	\$1.92	\$1.71	\$2.07	\$ (.68)
Net earnings	1.92	1.71	2.86	(.68)
Shareholders' equity	23.94	22.52	21.31	18.96
Dividend paid	.50	.50	.50	.50

1981 (Restated)	1980	1979	1978	1977	1976 (Restated)
\$90,092	\$86,787	\$85,108	\$75,011	\$67,874	\$59,806
1,828	2,416	1,943	2,390	2,057	1,583
737	1,082	792	1,053	851	680
1,091	1,334	1,151	1,337	1,206	903
—	—	—	—	—	—
1,091	1,334	1,151	1,337	1,206	903
9,502	8,678	8,141	7,241	6,126	5,126
17,025	12,399	12,933	10,823	9,120	7,242
13,801	10,588	11,250	11,219	8,326	7,919
16,550	9,505	12,979	10,228	7,794	6,583
15,014	13,745	11,975	12,120	9,980	8,957
5,485	5,385	5,017	873	766	614
10,215	9,413	7,748	4,650	3,692	3,407
10,675	9,854	9,344	8,395	7,220	6,339
11.07%	14.28%	13.71%	18.51%	19.02%	16.13%
\$ 2.15	\$ 2.50	\$ 2.06	\$ 2.40	\$ 2.14	\$ 1.59
2.15	2.50	2.06	2.40	2.14	1.59
20.13	17.54	15.93	14.29	12.27	10.45
.50	.475	.425	.375	.325	.30



HOWDEN