

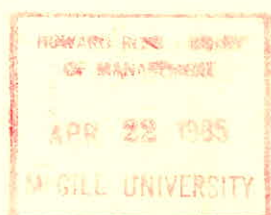
Primarily as a result of acquisitions over the past two years, **revenues** were at record levels and **earnings per share** nearly doubled.

Return on equity also increased substantially, moving toward Federal's minimum **profitability** objective.

In the larger context, a number of steps were taken which laid an even stronger **foundation** for planned **growth** between now and 1995.

That some of these strategies are generating immediate results is almost beside the point.

**Our corporate focus is on the longer term.**



Federal Industries is a diversified management company, headquartered in Winnipeg, Canada. Through its operating Groups, Federal is involved in transportation, aerospace and industrial distribution in North America and internationally.

The Company has assets of nearly \$450 million, and annual sales of \$573 million. A program of ambitious, but prudent, future growth is set out in the Company's Corporate Long Range Plan which is available on request.

More than 97% of the Common and Preferred Shares outstanding are owned by residents of Canada. Shares are traded on the Toronto and Winnipeg Stock Exchanges.

### **Annual Meeting**

The Annual Meeting of the Shareholders will be held at the Westin Hotel, Two Lombard Place, Winnipeg, Manitoba, on May 10, 1985, at 11:00 a.m.

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# 1984 was a successful year for Federal Industries, with growth in the three areas of greatest concern to the investor: sales, profits and return on equity.

Largely as a result of strategic acquisitions over the past two years, revenues were at record levels – totalling \$573 million, versus \$204 million in 1983.

Net earnings for the year before extraordinary items were \$15.2 million, compared to \$5.9 million in 1983, exceeding the Company's previous record earnings by almost 40%. Earnings per share, at \$1.97 nearly doubled the \$1.02 earned in 1983. Fully diluted earnings per share for 1984 were \$1.84, compared to \$1.02 for 1983.

At year-end, an extraordinary non-cash writedown of \$15.2 million or \$2.57 per share, was taken in the Company's White Pass Railway investment. This action allows management to plan the disposition of assets valued in excess of \$14 million and to focus on future opportunities. Earnings per share after this extraordinary writedown were a loss of 60¢.

Return on common equity grew by nearly 75% to 12.4% – another step towards the minimum threshold of 15%. Hand in hand with this growth is a continuing commitment to maintain adequate equity levels to protect your investment in the Company from recessionary impacts of the business cycle.

Although over half of 1984 sales were generated by the Industrial Distribution Group, Transport and Aerospace made important contributions to revenue growth and profitability. Among 1984's key developments:

- Russelsteel and Canadian Motorways, companies acquired over the past two years, made substantial profit contributions. Return on our investment in both companies exceeded 20%.
- The new dry bulk handling system at Thunder Bay Terminals attracted much higher potash throughput and contributed to substantial gains in tonnages, revenues and profits.
- While the Cyprus Anvil Mine remained closed, White Pass and Yukon's petroleum distribution and drill-rig moving operations produced a small profit – a substantial achievement under the circumstances. Indicative of the greater balance achieved by Federal's program of internal growth and acquisition, White Pass' northern revenue accounted for less than 6% of the Company's 1984 total.
- Reorganization and restructuring at Standard Aero cut costs and generated greater operating efficiency. Important new strategies devised in 1984 resulted in the establishment of a major U.S. based aircraft

maintenance facility in early 1985.

The balance of this Report provides a detailed assessment of performance for the year – and the Company's bright future prospects.

We regret that Campbell L. Searle has advised the Board of Directors that he will not be standing for re-election at our upcoming Annual Meeting. In his nearly fifteen years of service as a Director, Mr. Searle was a constant source of wise counsel. His contribution to the growth of Federal Industries was a significant one.

On behalf of the Board of Directors,



John F. Fraser  
*President and Chief Executive Officer*



Stewart A. Searle  
*Chairman of the Board*

For the year ended December 31

(\$ million)	1984	1983	1982
Sales	572.6	203.8	179.2
Earnings before interest, taxes, and extraordinary items	43.4	20.2	19.3
Interest charges	17.5	8.8	7.9
Net income (before extraordinary items)	15.2	5.9	6.0
Cash flow	24.0	12.5	13.9
Working capital	137.4	126.5	50.5
Total assets	449.7	377.0	199.6
Earnings per Common Share (before extraordinary items)	\$ 1.97	\$ 1.02	\$ 1.25
Equity per Common Share	\$ 15.11	\$ 16.02	\$ 16.46
Return on common equity	12.4%	7.1%	7.8%
Common Shares outstanding	5,915,579	5,887,211	4,694,613

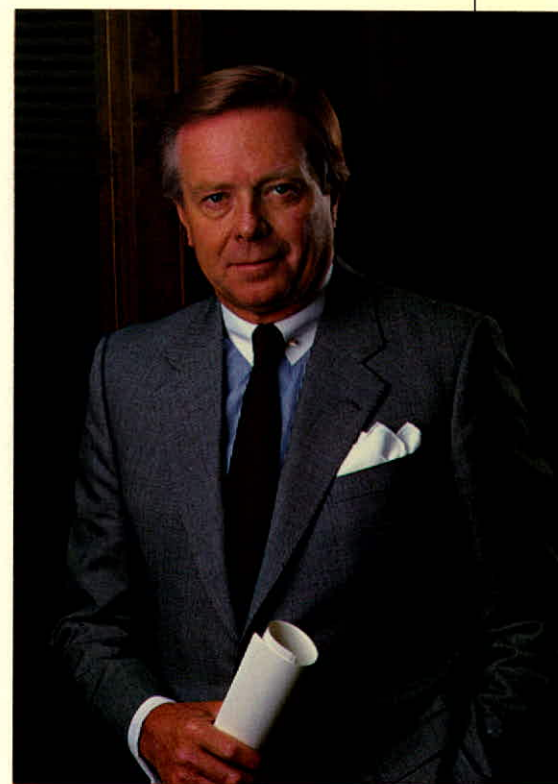
**I**ncreases in your Company's sales and earnings during 1984 were both gratifying and substantial. However, a number of developments during the year promise to be even more important to our future growth and development.

1. Our 1982 Corporate Long Range Plan identified the twin objectives of reducing Federal's dependency on the natural resource sector of western Canada and of improving the geographical balance of the Company's revenues. In 1984, a further goal of reducing the cyclical volatility of existing operations was adopted, and will be implemented through future acquisitions.
2. The importance of our resource and regional independence strategy was demonstrated by the profit contributions

of Canadian Motorways and Russelsteel, acquired in late 1983. Not only was the strategy sound, it was successfully and effectively accomplished.

3. Although results of the aviation parts distribution segment are still unacceptable, resolutions to difficult operational problems were achieved with the aid of direct participation by corporate management. The ability and willingness to provide this kind of support is a key strength of your Company.

4. At year-end, the Company recorded a \$15,219,000 write-down in its White Pass Railway investment, recognizing the probability that this operation, shut down since 1982, will not reopen. The extraordinary charge to income does not represent a cash outlay, but rather

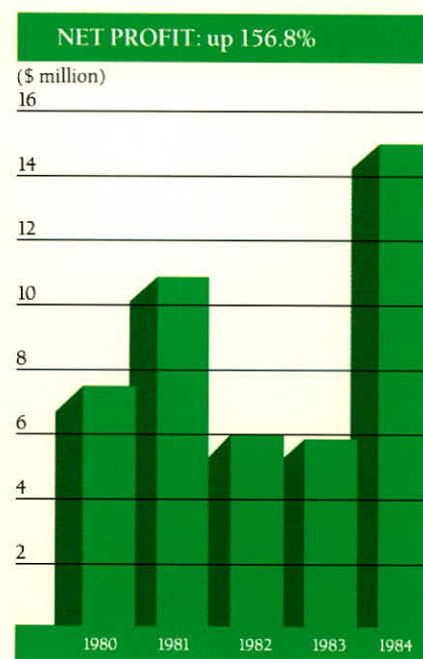
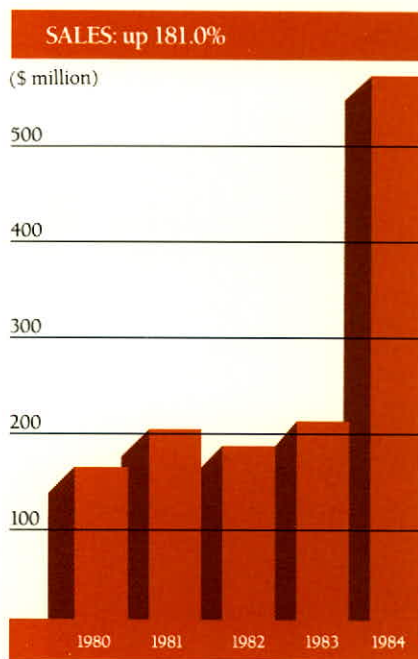


**John F. Fraser**  
President and Chief Executive Officer

freed management to plan the disposition of assets worth millions of dollars, and to direct efforts toward the many opportunities ahead.

5. During 1984 your Company was substantially strengthened by the addition of new and experienced managers at both Corporate and Group levels. Management depth is the prime assurance that future growth will be prudently and competently achieved.

Without question, the main responsibility of the Corporate office is to provide for the development of a strong, loyal and performance-oriented management team. Working with such a team, we can build and implement successful long-range strategies, while retaining the



Before extraordinary items, where applicable.

ability to quickly correct problems that inevitably occur. During 1984 solid progress was made in each of these areas.

While substantial improvements have been made, I want to assure our shareholders that we are not satisfied. Your management is actively pursuing a number of initiatives to continue and extend the current favourable trends.

First, we are concentrating on improving our return on shareholders' equity. Each one of our three Groups — Aerospace, Transport and Industrial Distribution — will be focussing on unique niches having the potential to provide above average returns. This concentration on the high profit sectors of their industries, together with a continued emphasis on the increased productivity of capital and labour, should lead to a

steady rise in equity returns in the years ahead.

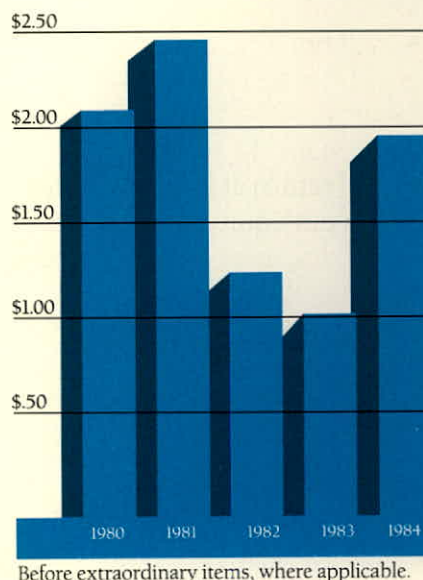
Second, for the past several months our planning department has been carrying out extensive investigations to determine the industry segment we will focus on in making our next major acquisition — targeted for approximately 1986. Since our existing groups tend to track the business cycle fairly closely, our next move is planned to have operating characteristics that dampen this cyclical effect, thereby aiding the stable earnings growth goal to which we are committed.

Third, we will continue to hone our skills at managing diversity. We believe that this is a business in itself, and that within this business, managing managers is our key function. Refinement of these disciplines is our chosen path to prudent growth.

Fourth, our balanced approach and transaction competence has been proven. While conventional wisdom says that new acquisitions tend to pull down earnings during the early years, the Canadian Motorways and Russelsteel acquisitions were planned to achieve excellence in both short and long-term earnings. One of these has been accomplished, and the outlook for the other is good.

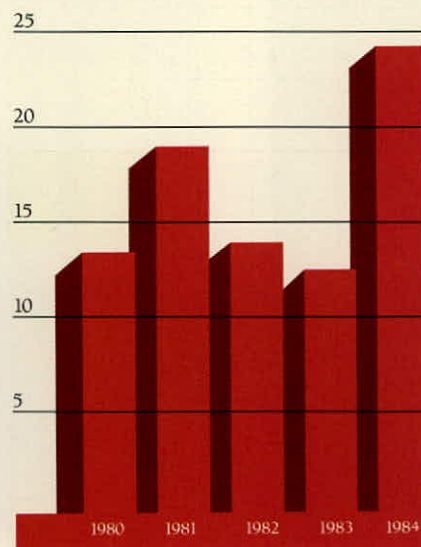
In closing, I would like to assure our shareholders that the actions taken over the past six years have substantially strengthened your Company, given it much better balance, and provided a solid foundation for future growth. These achievements are largely a result of the efforts of loyal and dedicated managers and staff, who willingly contributed the extra effort needed.

#### EARNINGS PER SHARE: up 93.1%



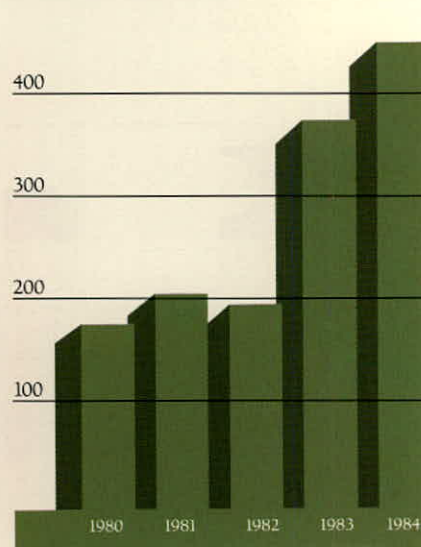
#### CASH FLOW: up 92.4%

(\$ million)



#### TOTAL ASSETS: up 19.3%

(\$ million)  
500



Perhaps the most striking aspect of our 1984 results was the strong performance of Canadian Motorways Ltd. and Russelsteel Inc.

Acquired in June of 1983, Canadian Motorways generated a rate of return on investment of 20% after tax. Russelsteel, which was purchased on the last day of 1983, produced a return of more than 25%.

Even better results are forecast for both organizations in 1985 – in line with our determination to move all of the Company's operations toward returns on equity in excess of 20%.

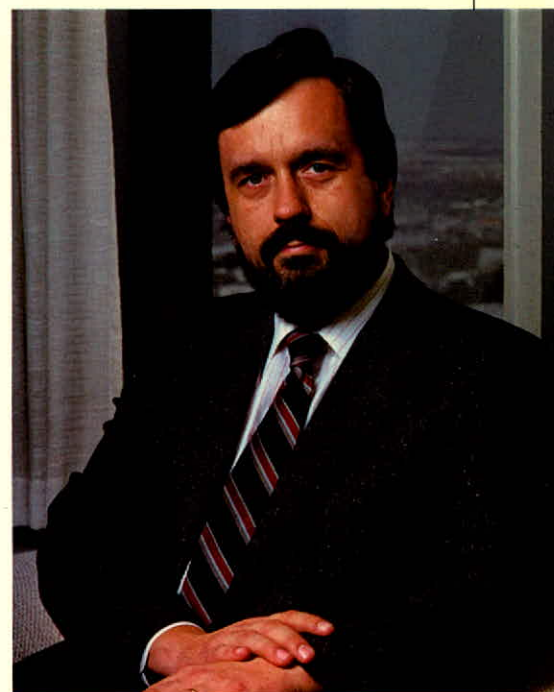
Acquisitions will be largely responsible for meeting Federal's growth objectives in the years to come, and like the Company's other primary building blocks, fiscal prudence and management excellence, our acquisitions are governed by closely-defined criteria. The purpose is

not solely to impose useful discipline, but rather to channel, direct and focus human and financial resources into industry segments that will help us to achieve excellence in rates of return, stability and growth.

Recent economic cycles have demonstrated unprecedented volatility. So we've added another major acquisition strategy – to adjust the mix of businesses owned by Federal to dampen or counteract the effect of cycles on earnings growth.

Because of the uncertainty of future events, and because the degree of economic volatility has been so significant, we're also adjusting the mix of operations within our Groups to provide both greater elasticity to changes in demand for our services and higher liquidity.

**ACQUISITION YARDSTICKS**  
Our acquisition criteria, spelled out in detail in the Corporate Long Range Plan, are used to

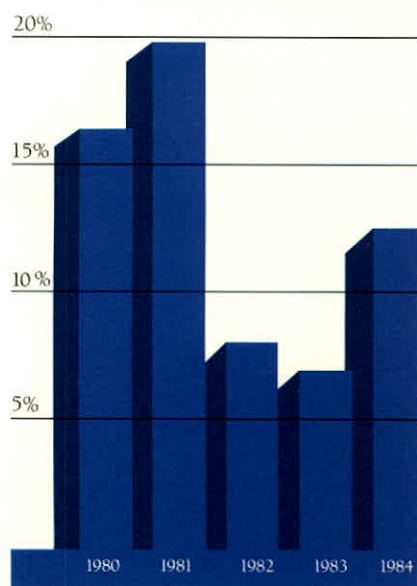


**John S. Pelton**  
Vice-President, Finance

evaluate new purchases and to re-assess, on a regular basis, our existing investments. For example, in pursuing "stand-alone" acquisitions (organizations which are fully staffed and can report directly to Federal) we look for companies that:

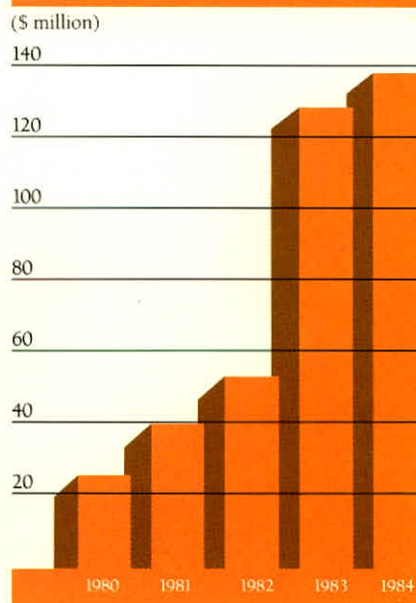
- Are management intensive
- Sell primarily to other businesses
- Serve well established markets
- Will not jeopardize Federal's long-term goals
- Will not drop our rate of return on net assets below our minimum 25% objective for more than one fiscal year
- Will return at least 15% after tax on our equity investments
- Are similar in size to Federal's existing Groups
- Are working-capital versus fixed-capital intensive
- Have proven management with well demonstrated capability to run the business
- Have a corporate culture compatible with ours

#### RETURN ON EQUITY: up 74.6%



Based on opening common equity.

#### WORKING CAPITAL: up 8.6%



- Dominate a clearly-defined market or are positioned to do so
- Are geographically diverse
- And meet a variety of other criteria aimed at balancing our portfolio of companies.

During the year, no "stand-alone" acquisitions were made. However, four "tuckunder" purchases were completed. Because of their size and the nature of their business, these companies have been "tucked under" existing management in two of our operating Groups.

The Industrial Distribution Group was most active, acquiring Can Copco Steel, Chatham Steel and Wirth Inc. Located in Windsor, Ontario, Can Copco is a small steel distributor specializing in the automotive trade. Chatham Steel, a medium-sized regional distributor based in Vancouver, is being merged into Russelsteel's operations there. Both companies were purchased essentially for inventory value, and strengthen existing market positions. Wirth Inc. and its Canadian affiliate are metals trading companies, importing and exporting steel and related products, aluminum, and refractory materials. An 89.9% interest was purchased, with key management retaining the balance. The acquisition was financed primarily through a 10-year note taken back by the vendor.

Ron Jackson Transport Ltd., a specialist in moving drilling rigs, materials and equipment throughout northern Alberta, was acquired by White Pass Systems Ltd., a unit of the Transport Group. The company's assets were purchased at a cost

of \$2.6 million and operations have been integrated into the Group's existing drill rig hauling business, forming one of Canada's largest companies in the field.

Each of these acquisitions was made at favourable prices and represents a significant opportunity, with forecast returns on net assets well in excess of our benchmark of 25%.

#### THE BALANCE SHEET

Maintaining balance sheet strength is a key element in Federal Industries' growth plans because, success aside, we believe it is management's responsibility to ensure the survival of the Company even under the worst circumstances. In turn, this basic guideline determines the amount and type of debt the business can carry.

The appropriate debt level varies from division to division and from year to year depending on the types of businesses we're operating, their relative volatility to changes in demand, and developments in the marketplace and economy. Our assumption is that we should be able to "ride out" a significant downturn in all of these areas at the same time.

One specific example of our approach to fiscal prudence was the financing of the Russelsteel acquisition. Although debt was available to us, we concluded that Federal needed an additional \$25 million in equity to complete the transaction on our terms.

As a result, we went to the market with a Preferred Share offering which stated clearly that, unless our investors voiced their approval by purchasing

the issue, we would forego the acquisition. The market voted an overwhelming "yes". Our initial offering of \$25 million became \$40 million, and 2,500 new shareholders joined Federal Industries.

The \$15 million raised in excess of our Russelsteel purchase requirements was augmented during the year by \$8.5 million, leaving current cash balances not needed in operations of \$23.5 million. These funds are earmarked for early investment in our Groups, and at present rates of return, could add a minimum incremental \$3 million in after tax earnings.

In addition, we have unused lines of credit of nearly \$70 million which are dedicated to supporting growth in working capital for our existing operations, with resulting increases in profitability.

Clearly, "operational leverage" can have a dramatic effect on our return on equity, and this leverage can be increased by keeping our base of expenses and assets to a minimum. In fact, we've been successful in reducing assets and unnecessary overhead expenditures in good times as well as bad, during growth periods as well as recessions. In 1984, even as they grew, each of our Groups was able to trim unnecessary fat.

The bottom line effect of fiscal prudence, acquisition criteria and operational leverage is to increase the cash available from internal sources — further enhancing our ability to pursue growth objectives, without diluting shareholders' interests.

#### BANKING

At the beginning of 1985, Federal completed an agreement with

The Bank of Montreal, Toronto Dominion Bank, The Canadian Imperial Bank of Commerce and Citicorp Canada, consolidating all domestic Canadian banking relationships and establishing uniform terms for borrowing. In recognition of Federal's balance sheet strength, new flexibility was achieved — paving the way for the Company to participate in a wider range of financial activities, such as issuing its own paper.

Federal Industries acts as a "central banker" to its group of companies, with the aim of providing improved cash management capabilities, reduced transaction charges, and the lowest cost of funds.

Complementing this head office cash management is a program of cash flow optimization at the operational level. That is, each Group is responsible for establishing and maintaining methods, techniques and controls that maximize cash flow which the centralized treasury then handles in the most efficient fashion.

At the end of the year, investments in marketable securities and cash balances exceeded \$35 million, of which \$23.5 million was in Preferred Shares. This liquidity, together with the positive anticipated cash flow from operations, should provide all necessary cash for Canadian expansion in the medium-term.

#### DEBT AND INTEREST

At Federal, it's our policy that long term debt should be matched by assets whose economic value, even in the most difficult of market and economic circumstances, will produce sufficient cash flow for debt retire-

ment. While the debt/equity ratio is important, we believe the ability to service annual debt requirements without adversely affecting operations is paramount. Great care is exercised when we enter into long term debt agreements.

At Thunder Bay Terminals Ltd., for example, the \$70 million facility was built entirely with the proceeds of a 15-year fixed rate bond issue. As the sponsor of a new system to move western coal to its generating stations on the Great Lakes, Ontario Hydro underpinned the bonds with an unconditional covenant to provide debt servicing. Since recourse is limited to the assets themselves, this qualifies as "project financing".

This is not an isolated example. Wherever possible, it is our policy to fix long term rates because of the necessity for planning of our debt service. Short term debt, normally with a floating rate, is used to finance the working capital assets of the Company. The level of total debt should be modest at the bottom of an economic market cycle, and increase primarily to finance asset growth as economic activity increases.

In summary, Federal Industries tends to avoid debt in periods of recession, but will accept rapidly-increasing levels of short term debt to support growth in working capital during economic expansion. Our intention is to protect shareholders' rates of return when the economy is slow, while creating greater potential in growth phases, all within our overall policy of fiscal prudence.

#### SHARE CAPITAL

Our program of private placements and public issues, which began in 1980, has been successful for the Company and its investors. Significantly, all shareholders who participated in our four issues and who have held the securities have made substantial gains. This is a key factor for the future, because our rapid expansion will continue to require access to equity markets. The type of equity to be issued will be that which is most beneficial to all shareholders at the time.

Dividend levels, now at about 25% of average sustainable earnings, are expected to increase as earnings grow, but in roughly the same percentage relationship. We believe our investors are motivated primarily by the opportunity for capital appreciation afforded through rapid growth and improving returns on equity retained.

So that investors understand our policies and prospects, shareholder relations, both directly and through the investment community, are an important consideration.

Your Company's goals for return on equity are aggressive — aiming for a minimum 15% return after tax and towards achievable levels greater than 20%. Our success in attaining these goals is a reflection of the returns on net assets achieved by the operating Groups. Here, the minimum criteria for existing operations is 25%. Where the industry segment is cyclical, this 25% is measured as an average over the length of the cycle. Our goals in this area will be modified periodically to reflect longer term inflation trends.

We are often asked when and if Federal Industries will move into industries having a little higher profile — a more “hi tech” orientation than such things as trucking, industrial distribution and overhauling aircraft engines. After all, the free world has entered the “age of information”, and vast fortunes have been made from investments in computers, robots and such technology. When will Federal join the hi tech action?

Well of course, we have joined the “age of information”. Some of our systems of information management are “state of the art”, and virtually every Federal company is actively upgrading their computerized management information systems on a continuing basis. But none of our companies operate in fields the ordinary businessperson would define as “hi tech” — nor do we expect them to be in the near future. Let me tell you why.

Simply stated, Federal Industries is “management intensive” as opposed to “product intensive”. At corporate office, our role is *managing managers*, and management science is our prime field of research and development. We believe this is an area offering great rewards to our shareholders, and one where great advances are being made. Let's look at where the money is being made in North America today and in recent years.

George Linton, a columnist for *The Globe and Mail*, recently published a list of ten companies on the Toronto Stock Exchange's

300 most active list having the greatest increase in share value since 1979. Seven of the ten were in very basic “lo tech” industries.

*Forbes* magazine regularly publishes a list of “Up and Comers”, the 300 companies they have chosen as rising stars based on growth and profitability. Inclusion on this select list requires a five year average return on equity of 15%, a tough hurdle for most young companies. Eight of the top ten on *Forbes'* most recent list are decidedly lo tech, as are the vast majority of all the “Up and Comers”. An analysis of the entire list shows that only about 10% of the qualifiers are what could be called “hi tech”, and that return on equity is comparable between companies most of us would perceive as “hi tech” and those we'd deem “lo tech”. In five year average growth rate, the successful hi tech companies included on this list attained a higher rate of growth than the lo tech companies, but this factor is offset by the much greater difficulty in spotting which hi tech company will succeed at any given time. Betting on hi tech companies is a high risk game.

*INC.* is a magazine dedicated to entrepreneurial endeavors, and they recently published a list of 500 relatively small companies they deem to be outstanding examples of the rebirth of entrepreneurial effort in North America. Once again, the vast majority of the companies listed are lo tech, and the hi tech companies show an even smaller growth advantage over the lo



R.J. Vahsholtz  
Vice-President, Planning

tech companies than is the case on the *Forbes* list.

Perhaps you found the data summarized above surprising? Well, we do live in the age of information, and most of what we read in the business press is what's new and the big success stories. Technology is high profile right now and for good reasons, but as the authors of the best seller *In Search of Excellence* so clearly demonstrated, there's far more to excellence than having a great idea (the great majority of the companies on their list are also lo tech).

Once again, the facts show that there are no real shortcuts to outstanding performance. Good profits and solid growth come from *good management* more than any other factor — and *management excellence* is and will remain central to Federal's objectives.

**"In the years ahead, concern in management will shift once more to the structure, composition, and qualification of top management and of the people in it".**

Peter Drucker  
*Managing In Turbulent Times*

We share Dr. Drucker's opinion of the need for increasingly effective management in the coming decades. Developing and implementing an organizational framework that would carry us to 1995 and beyond was one of our prime objectives for 1984.

We began by studying the ways our operating companies related to each other, how they worked or could work together, and how they were managed.

Our conclusion was to structure the subsidiary operating companies into Groups based on industries with each Group headed by a Chief Executive Officer with considerable experience in each industry. While it was not an immediate priority, sooner or later, a system based on Group Chief Executive Officers would be the right management structure for Federal Industries' operations. By acting now, we could get a valuable head start on the day when the structure would be a necessity. This organization provides for the necessary management depth to allow effective, prudent delegation of operating authority, with each Group pursuing its own particular expansion path within the guidelines of

Federal's long-range plan.

During the year, three Group Chief Executive Officers were named for each of our three industry groups: Transport, Aerospace and Industrial Distribution — with the logistics and relationships of the Group CEOs built into the Corporate Long Range Plan.

The approach is consistent with our commitment to day-to-day operating autonomy and to developing and rewarding entrepreneurial management.

Here's how it works:

- The Group CEO reports to Jack Fraser, Federal Industries' President and Chief Executive Officer.
- The senior executive of each operating company within the Group reports directly to the Group CEO. All senior managers of each operating company have direct access to Federal's corporate office staff to transfer information — but all directives flow through the Group CEO line.
- In principle, the Group CEO is located in the office of the largest operating company in the Group. In practice, our intent is that each Group CEO be "where the action is".
- We don't believe in "mini-head offices". The Group CEO has access to staff and services at corporate head office as required, and is supported largely by the operating staff of the company where he is located.
- The Group CEO will have extensive industry and operating experience but his prime responsibility will be the traditional responsibilities of a Chief Executive Officer. He may fill a "Chief Operating Officer's" role on occasion, but only temporarily. The prime responsibility is to see that excellent management and sound strategies are employed in each company in his Group.
- Group CEOs are also *ex officio* members of Federal's Executive Committee, providing their specific perspective and knowledge where required.

Our purpose in establishing the Group structure was to foster better decision making. The results for 1984 indicate that we are succeeding, and we look forward to similar positive results in the years to come.



**William E. Watchorn**  
*Vice-President and Assistant Secretary*

*The Federal Industries Aerospace Group repairs and overhauls aviation and industrial engines and accessories at Winnipeg, Manitoba, provides commercial airframe maintenance at Phoenix, Arizona, and distributes aviation parts and accessories in North America, western Europe and the Far East.*

Over the past few years, aerospace markets have undergone rapid and pervasive change, caused by many factors including de-regulation and the rapid changes in energy costs.

Understandably, this change has created problems; but has also meant significant opportunities, many of which have been identified and are being pursued by the Federal Industries Aerospace Group as part of an ambitious five-year development plan for Standard Aero.

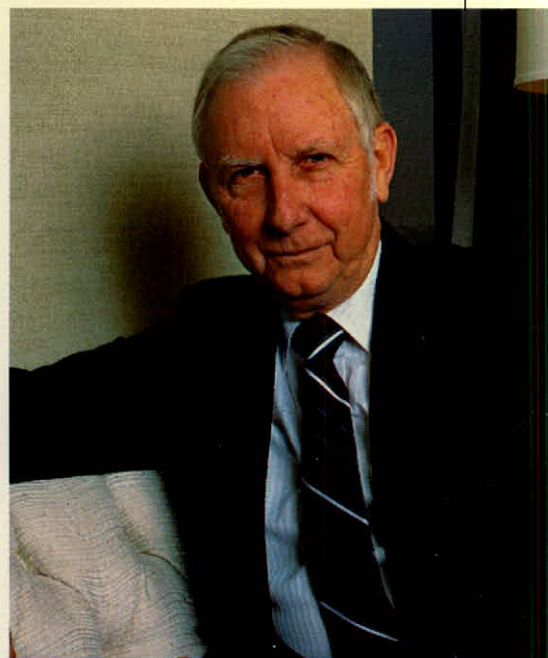
Aerospace markets are highly competitive, and strategic information is jealously guarded. However, two important aspects of Standard Aero's strategy have already unfolded.

The first was the integration of marketing and administrative activities between Standard Aero Limited (overhaul and remanufacturing of aircraft accessories and small and medium-size turbine and piston engines) and Standard Aero Inc. (worldwide distribution of parts and accessories). The result of this program has been lower manufacturing and sales costs in serving a cus-

tomers base that is largely common to both companies – while still catering to the unique requirements of each business and maintaining product line profitability for accountability.

As a result of the integration, Standard Aero Inc. will now function as a parts distribution division in support of – and supported by – the Group's overhaul division. Greater sales will be created for both by providing technical and parts support through one marketing organization under the Standard Aero trade name.

The second was the establishment in early 1985 of Standard Aero's first air frame maintenance presence in the United States through Standard Aero (Western) Inc. From its base in Phoenix, Arizona, this new company will service a large



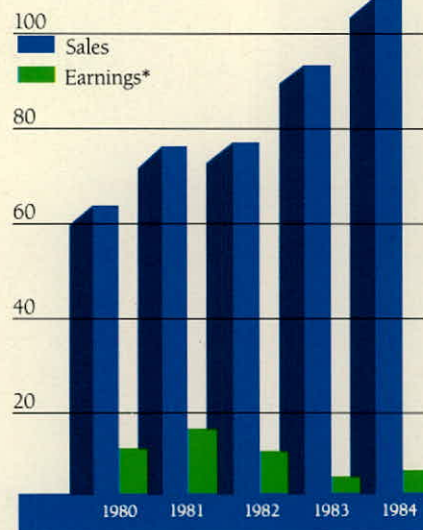
**Edward G. Kelley**  
President and Chief Executive Officer  
Aerospace Group

and growing market among regional, commuter and cargo airlines which don't have their own maintenance facilities. Standard Aero has assumed a long term lease on an existing 285,000 square-foot building (North America's largest independent facility) at Phoenix Sky Harbour International Airport, one of the continent's busiest air terminals.

For a total expenditure of just over \$2.6 million (U.S.), Standard purchased valuable inventory and equipment from Republic Airlines, the former lessee, and established an important foothold in U.S. airline maintenance markets. Services initially offered at the new facility will include airframe maintenance and related services such as painting and cleaning. In the short to medium term, services will be expanded to include avionics and compo-

#### FIVE YEAR REVIEW

(\$ million)



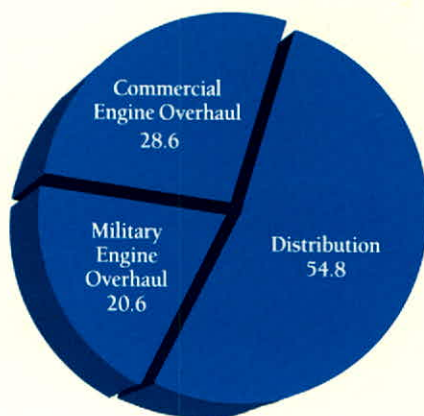
\*From operations, before taxes, extraordinary items and interest.

nent overhaul, large engine repair and a variety of other airline support functions.

While other important opportunities are being pursued, Standard Aero's aircraft engine overhaul facility in Winnipeg remains the cornerstone of Group operations. The 11.3% increase in sales in 1984 reflected greater penetration of the U.S. turbine engine overhaul market, a pick-up in Canadian turbine-powered helicopter activity and an increase in military overhaul. The overall increase in commercial sales was better than 12%. Revenues from military overhaul contracts with the Canadian Armed Forces grew by nearly 9%.

Reflecting Standard Aero's aggressive pursuit of additional foreign and military business,

**SALES DISTRIBUTION**  
(For the year ended Dec. 31, 1984)  
In millions of dollars



several initiatives were undertaken to obtain overhaul contracts from the Middle East, South East Asia and the United States military. Overall, non-Canadian overhaul accounted for more than 25% of sales. Of

total overhaul revenue, approximately 42% was generated from military sources, with the balance from commercial customers.

Standard Aero's new sales initiatives will enhance the existing activities of branch operations in Montreal, P.Q., Vancouver, B.C., Van Nuys, California, and Dallas, Texas, as well as those of the Standard Aero service centre network: Trans Quebec and LaVerendrye (Quebec), Field Aircraft Services (Croydon, UK), Alfa Romeo Aviation Spa (Italy), SECA (France), OGMA (Portugal) and SAEOL (Singapore).

To counterbalance the additional cost involved in generating U.S. business, and to improve productivity over the longer term, operations at the Winnipeg complex have been



*Standard Aero (Western) Limited has established an important foothold in U.S. commercial airline maintenance by opening North America's largest independent facility at Sky Harbour International Airport, Phoenix, Arizona. The 285,000 square-foot building is capable of handling two DC10's – or six 727's – at a time.*

re-structured and re-oriented around six product lines, rather than by job function. The result will be greater output without sacrificing quality, and an estimated \$1 million annual saving in labour costs.

While growth in markets for aviation parts and accessories remained sluggish, sales for Standard Aero Inc. did continue on a general upward trend particularly in the latter part of the year. While the Company continued to incur losses, results were considerably improved over the previous year. In 1985, a continuing emphasis will be placed on programs to improve margins and reduce costs.

Among the more important factors which shaped 1984 for the Group:

- A number of key management changes were made which strengthened the Group's ability to respond to the needs of the market.
- The SATCOM advanced computer system became fully operational in the U.S. — guaranteeing overnight deliveries to customers throughout the country.
- The central warehouse, containing over 37,000 new and overhauled items, was relocated to Minneapolis in March, and after an initial shakedown in the second quarter, provided



*Standard Aero Limited's Winnipeg plant will begin servicing the popular Pratt and Whitney PT6 turbine engine by mid-1985. Training programs for Standard Aero personnel were part of preparations for the PT6 underway in 1984.*

quick and efficient support for all distribution branches.

- Several new parts and accessories product lines were secured for distribution.
- Work was begun on the implementation of a full repair and overhaul capability for the Pratt & Whitney PT6 turbine engine, used extensively on commuter aircraft which will be fully operational at the Winnipeg facility by mid-1985.
- Sales of airline ground support equipment of PF Industries Incorporated increased by 17% to \$3.4 million.
- Relocation began for turbine engine overhaul at Winnipeg. By June, 1985, these operations will occupy a new 70,000

square-foot building, specifically designed to meet the needs of this product line.

Working together, the overhaul and parts businesses of Standard Aero are expected to see continued real growth in revenue and a substantially higher increase in profitability.

More new product franchises and international marketing arrangements will be negotiated and a solid base will be set for possible expansion in U.S.-based overhaul of jet engines and for a significant increase in the existing commercial aviation parts distribution business.

The Federal Industries Industrial Distribution Group distributes general line, flat-rolled and specialty steel products in Canada and the United States, markets industrial valves, piping components and related products, and imports carbon steel, aluminum, refractory materials, rails, wire and pipe products.

As forecast in last year's Report, Industrial Distribution was a major force in building Federal's 1984 earnings. The Group contributed more than 50% of overall revenue, effectively counterbalancing the effects of the continuing downturn in the North American natural resource sector.

In its first year as part of Federal Industries, the Group generated revenue of \$308 million. Earnings from operations were \$18.1 million — a substantial achievement given below average activity in the Company's western Canadian markets.

#### SALES DISTRIBUTION

(For the year ended Dec. 31, 1984)  
In millions of dollars



During the year, the Ontario market showed considerable improvement, driven by demand for consumer durables such as automobiles and related products. While capital spending continued to lag behind the demand for consumer products, there was a modest but steady increase in demand for a wide range of steel products.

Of particular importance to the future was the re-organization carried out during 1984 by the Group. Three divisions were created and senior executives promoted from within the Group to run them.

**Canadian Steel Service Centres** is now the largest steel service centre operation in Canada. With gross assets of approximately \$100 million and more than 680 employees, this division processes and distributes flat rolled and general line carbon steel and related products from 15 locations across Canada. President is A.M. Shkut.

**The International Division** consists of two units. Russel International, operating from Toronto, distributes Canadian and foreign steel and steel products in the United States and other countries. President is N.B. Katzman. The Wirth companies, with offices in the United States and Canada, specialize in importing carbon steel, aluminum, refractory materials, rails, wire and pipe products into North America. President is M.F. Wirth.



**Wayne P.E. Mang**  
President and Chief Executive Officer  
Industrial Distribution Group

**The Specialty Distribution Division** trades as Lytle Specialties and is Canada's largest distributor of industrial valves, piping components and related products — with eight branches across the country. President is D.K. Hurst.

**U.S. Steel Service Centers**, a fourth division, to be established in 1985, will be comprised of U.S.-based service centres which will be acquired over time.

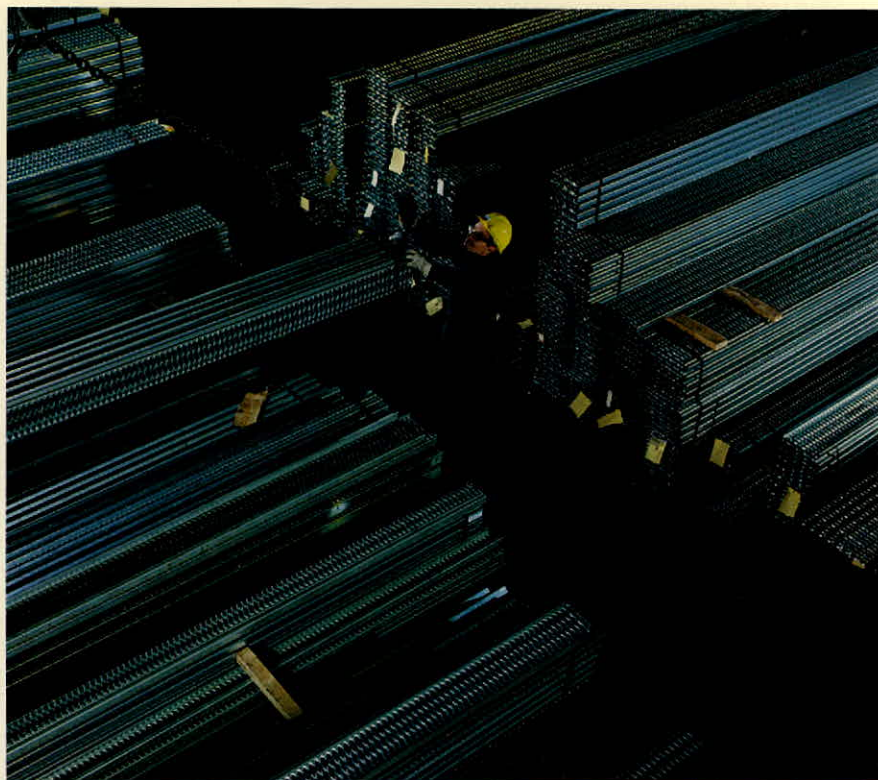
While 1984 was largely a year of consolidation and restructuring, a number of notable developments took place:

- The Canadian Steel Service Centre Division made two "tuckunder" acquisitions in the fourth quarter. A substantial increase in British Columbia sales and better prospects for growth resulted from the \$1.2 million purchase of the assets and operations of Vancouver-based

Chatham Steel. Russelsteel's existing plant and management were combined into the Chatham Steel location. In addition, Can Copco Steel Limited of Windsor, Ontario — a small service centre, selling specialty steel products primarily to the automotive industry — was acquired for \$250,000.

- Effective June 1, a majority interest was acquired in Wirth Inc. and its Canadian subsidiary. These companies import and distribute steel and aluminum products principally in the United States. Over the final five months of 1984, these established, well-run companies generated profits as forecast.

- Late in the year, there was some indication of stabilization of markets for the Specialty Distribution Division — along with a revival of major capital



*Russelsteel acquired two regional steel service centre operations in 1984. Expansion by acquisition into United States markets is planned.*

projects that had been shelved for several years. This trend is

expected to continue into 1985 and have a positive impact on sales.

Overall, 1985 should see sales gains over 1984, with relatively constant profit margins. While operating expenses will increase in absolute terms, they should be lowered as a percentage of sales.

The greatest impact will be made through a full year's contribution from Wirth Inc., Chatham Steel and Can Copco which, together, will add in excess of \$30 million in revenue.



*Companies in the Industrial Distribution Group import and export a variety of steel products. Here, 30 tonnes of steel plate from B & T Steel, Hamilton, Ontario, move across the border at Fort Erie.*

The Federal Industries Transport Group provides truck transportation services in Canada and the northern United States, operates a bulk product transshipment terminal, transports drilling rigs and related equipment in western Canada and distributes petroleum products in Yukon.

While 1984 was a year of substantial change for the Transport Group, it was nevertheless a very successful one. Revenues increased by 42% and earnings from operations increased by 30.5% to \$23.1 million.

## Canadian Motorways Ltd.

In its first full year as a Federal Industries company, Canadian Motorways performed well. Sales of \$105.4 million and operating earnings of \$7.5 million were achieved despite a slow start in the first quarter. From the second quarter on, volumes and profits continued to grow — enhanced by innovative marketing and efforts to reduce operating costs and increase productivity. As a measure of this performance, on the year, Motorways achieved a return of 20% on Federal's initial investment.

In addition:

- The contract-hauling Cougar Division was expanded by the establishment of Cougar Pacific, based in Vancouver. The new division, which began operation in the fourth quarter, will concentrate on traffic flowing

north and south from the Port of Vancouver.

- To capitalize on rapidly-escalating demand for courier services in Canada, "Motopak" was formed late in the year to offer overnight courier services, using existing equipment, in an area stretching from Thunder Bay, Ontario to the Alberta/Saskatchewan border.
- More than 100 tractors were sold and replaced by rental equipment.
- To reduce costs, terminals at North Portal and Estevan, Saskatchewan were combined, and the terminal at Kenora, Ontario sold at a gain and replaced with a leased facility.
- Operating authorities were extended to all highway points between Prince George and

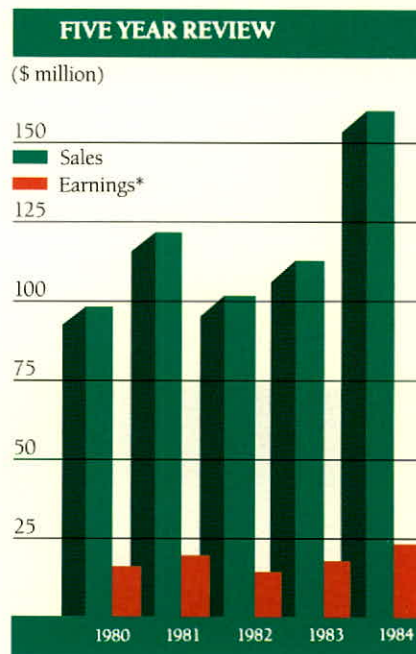


**Thomas H. King**  
President and Chief Executive Officer  
Transport Group

Prince Rupert, B.C. The Company's fourth international border crossing authority was secured at Pigeon River, Ontario.

- In January of 1985, management of Canadian Motorways was restructured. Thomas H. King, President and Chief Executive Officer of the Federal Industries Transport Group assumed the position of Chief Executive. J. Marshall Cumberland, a seasoned transportation executive with many years of experience in the trucking field, was appointed Executive Vice President and Chief Operating Officer.

In 1985, management of Canadian Motorways will continue to keep costs under tight control while aggressively pursuing new markets. Due to a slowly strengthening western Canadian economy, and Motorways' pre-eminent position in



\*From operations, before taxes, extraordinary items and interest.



*Canadian Motorways' High-Tech Express division provides a specialized cross-Canada transportation services, carrying computers and other delicate office equipment.*

western markets, forecasts are for good growth in both sales and share of market for general freight, contract and specialized trucking operations. This, combined with anticipated freight rate increases, should improve both revenue and earnings in 1985.

#### **Thunder Bay Terminals Ltd.**

With volumes of all commodities at record levels, Thunder Bay Terminals enjoyed its best year ever. At \$23.1 million, sales increased more than 10%, generating operating earnings of \$13.0 million, up 8.3% from 1983.

Coal remained the Terminal's mainstay, with 3,923,300 tonnes being transshipped, an increase of 30% over the previous single season record, set in 1982. Gains were the result of partial shutdown of Ontario Hydro's Pickering Nuclear Station and higher than expect-

ed power consumption over the winter of 1983/84.

Non-coal commodities also flowed in greater quantities. Potash volumes totalled 1,262,075 tonnes, an increase of 24% over the previous high. The primary factor in this increase was the removal by the U.S. Department of Agriculture of the "Payment in Kind" program for corn, as well as increased awareness

on the part of shippers of the advantages of the rail/water transportation system through Thunder Bay.

Completion of the \$5.8 million dry bulk handling system at the Terminal – allowing simultaneous and separate handling of coal and other dry commodities – paid important benefits. Beyond more efficient potash handling, the system enabled the Terminal to demonstrate lower costs and reduced product degradation to the agricultural industry.

Shipments of agricultural products through the Terminal continued to grow and future marketing efforts will concentrate on urea, sunflower seeds, canola, barley and other commodities.

The impact of an anticipated decline in coal tonnage for 1985 should be largely offset by increased throughput of potash and agricultural commodities and by slightly higher terminal handling rates. The net result should be operating profits close to those of 1984.

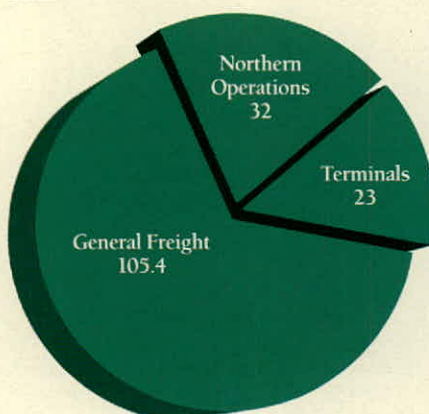
#### **The White Pass and Yukon Corporation Limited**

The continued closure of the Cyprus Anvil mine, and a decision by the Canadian Government to support road transportation to tidewater for mineral concentrates, resulted in major changes at White Pass in 1984.

At the end of the year, a decision was taken to writedown more than \$15 million of rail and marine transportation assets which had been idle for

#### **SALES DISTRIBUTION**

(For the year ended Dec. 31, 1984)  
In millions of dollars





*As part of a cost reduction program, Motorways now rents (rather than owns) more than 100 tractors.*

White Pass", the core companies which will be built upon in the years to come.

The best evidence of the Company's renewed activity during 1984 was at White Pass Systems Ltd., the newly-formed division specializing in large scale movements of oil drilling rigs and camps. As exploration activity continued to rebound in western Canada, Systems drew upon the considerable experience of its management and employees to become a significant force in the industry in its first year of operation. Late in the year, the Company made a strategic acquisition of the assets of Ron Jackson Transport Ltd. for \$2.6 million. The purchase adds a northern Alberta market pres-

ence as well as equipment and know-how that will be essential to future expansion.

During 1984, White Pass Systems carried out work in Alberta, northern British Columbia, Yukon and Northwest Territories via the Dempster Highway. Over the next year, calling on its own people as well as independent contract drivers who provide their own tractors, White Pass Systems intends to expand its base of operations into Saskatchewan, to other points in British Columbia and Northwest Territories.

In White Pass' Alaska and Yukon operations, profit growth was achieved against prevailing economic currents. The major

two years or more.

With both marine shipping and the railway suspended, and the former general freight trucking operations amalgamated into Canadian Motorways, White Pass is a considerably smaller organization, one that has been restructured to be able to move quickly to capitalize on opportunities.

As a measure of this, White Pass managed to make an operating profit in 1984, despite continuing stagnation in Yukon's economy. This achievement is particularly noteworthy because it was made on the strength of the petroleum distribution, oil rig moving, and docking and terminalling businesses that represent "the new



*Record tonnages of coal and potash moved through Thunder Bay Terminals in 1984. A dedicated dry bulk handling system, installed during the year, moved potash efficiently and effectively. The system is expected to attract greater tonnages of agricultural commodities to the Terminal.*



*In its first year of operation, White Pass Systems Ltd. became a major force in Canadian oilfield transportation. A strategic acquisition, made toward the end of the year, strengthened Systems' hand even further. Significant growth is expected in the years to come.*

factor in this growth was petroleum distribution. While sales volumes were impacted negatively by slow economic conditions, White Pass petroleum operations provided higher levels of both cash flow and profits. During the year, White Pass signed a three-year extension of its agency agreement with Chevron U.S., covering distribution of petroleum products in Skagway, Alaska.

In other significant developments:

- \$1.3 million (U.S.) in dock modifications, funded by the State of Alaska and the City of

Skagway, were completed at the Skagway Terminal Company. Originally designed to handle lead zinc concentrates, the Terminal will now generate sales and profits by offering docking and terminalling services to cruise ships which make Skagway a port-of-call during the tourist season.

- The lawsuit lodged by White Pass against Cyprus Anvil Mining Co. was settled in September, and had a positive after-tax effect.

Late in the year, Mr. Marvin Taylor, formerly manager of

the White Pass Rail Division, was promoted to Executive Vice President and Chief Operating Officer, White Pass and Yukon Corporation, responsible for operations in Yukon and Alaska. Mr. Taylor has relocated from Skagway to Whitehorse, and will spearhead future growth in White Pass' northern operations.

For 1985, increased profits for White Pass are expected as a consequence of increased penetration of oil field transportation, greater use of the Skagway Terminal, and strengthening margins for petroleum products.

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# CONSOLIDATED BALANCE SHEET

Assets	At December 31, 1984.		\$000
	1984	1983	1982
<b>Current</b>			
Cash and short term deposits	\$ 11,728	\$ 18,551	\$ 4,342
Short term investments	23,470	—	—
Accounts receivable	110,185	73,990	25,340
Income taxes recoverable	3,010	2,770	1,149
Inventories (Note 3)	135,806	105,259	49,586
Prepaid expenses	2,308	2,052	667
Claims recoverable	318	380	304
Current portion of long term receivable (Note 4)	3,850	3,850	3,850
<b>Total current assets</b>	<b>290,675</b>	<b>206,852</b>	<b>85,238</b>
<b>Fixed (Note 5)</b>			
Property, plant and equipment	224,421	254,547	161,164
Accumulated depreciation	83,468	100,277	54,780
	<b>140,953</b>	<b>154,270</b>	<b>106,384</b>
<b>Other</b>			
Long term receivable (Note 4)	3,408	2,702	1,925
Other investments, at cost	4,346	3,027	2,366
Deferred charges	5,328	5,162	145
Goodwill	2,113	2,043	2,072
Other intangible assets	2,909	2,913	1,439
	<b>18,104</b>	<b>15,847</b>	<b>7,947</b>
	<b>\$449,732</b>	<b>\$376,969</b>	<b>\$199,569</b>

Liabilities	At December 31, 1984	\$000		
		1984	1983	1982
<b>Current</b>				
Bank overdraft and secured indebtedness (Note 7)		\$ 53,246	\$ 10,344	\$ 9,683
Accounts payable and accrued liabilities		92,154	62,372	18,562
Dividends payable		1,629	801	652
Current portion of long term debt		6,271	6,861	5,799
<b>Total current liabilities</b>		<b>153,300</b>	<b>80,378</b>	<b>34,696</b>
<b>Long term debt (Note 6)</b>		<b>146,492</b>	<b>146,311</b>	<b>71,895</b>
<b>Deferred income taxes</b>		<b>11,215</b>	<b>7,567</b>	<b>7,342</b>
<b>Minority interest (Note 8)</b>		<b>6,496</b>	<b>5,500</b>	<b>5,500</b>
<b>Total liabilities</b>		<b>317,503</b>	<b>239,756</b>	<b>119,433</b>
<b>Contingencies and commitments (Note 15)</b>				
<b>Shareholders' Equity</b>				
Share capital (Note 9)		88,166	87,662	32,433
Retained earnings		42,888	49,551	47,703
Cumulative translation gain (Note 1B)		1,175	—	—
		<b>132,229</b>	<b>137,213</b>	<b>80,136</b>
		<b>\$449,732</b>	<b>\$376,969</b>	<b>\$199,569</b>

On behalf of the Board

*Stewart A. Seale*

Director

*J. H. H. H.*

Director

See accompanying notes to financial statements.

# CONSOLIDATED STATEMENT OF EARNINGS

For the year ended December 31, 1984	\$000		
	1984	1983	1982
<b>Sales and services</b> (Note 12)	<b>\$572,591</b>	<b>\$203,798</b>	<b>\$179,193</b>
Cost of sales and operating expenses	521,874	177,824	153,323
Depreciation	9,584	7,092	7,159
Amortization	614	155	74
Interest on long term debt	17,077	8,427	6,760
Other interest expense	2,957	1,317	1,649
Investment income	(2,503)	(984)	(492)
Gain on sale of fixed assets	(2,907)	(1,504)	(685)
	<b>546,696</b>	<b>192,327</b>	<b>167,788</b>
<b>Earnings before income taxes and extraordinary item</b>	<b>25,895</b>	<b>11,471</b>	<b>11,405</b>
<b>Provision for income taxes</b> (Note 11)			
Current	1,177	2,335	1,782
Deferred	9,014	2,841	3,222
	<b>10,191</b>	<b>5,176</b>	<b>5,004</b>
<b>Earnings before extraordinary item</b>	<b>15,704</b>	<b>6,295</b>	<b>6,401</b>
<b>Extraordinary item</b> (Note 14)	<b>15,219</b>	<b>—</b>	<b>—</b>
<b>Net earnings</b>	<b>485</b>	<b>6,295</b>	<b>6,401</b>
<b>Earnings allocated to minority shareholders</b>	<b>491</b>	<b>371</b>	<b>372</b>
<b>Net earnings (loss) for the year</b>	<b>\$ (6)</b>	<b>\$ 5,924</b>	<b>\$ 6,029</b>
<b>Earnings (loss) per Common Share</b> (Note 10)			
Before extraordinary item	\$ 1.97	\$ 1.02	\$ 1.25
Extraordinary item	(2.57)	—	—
Including extraordinary item	<b>\$ (.60)</b>	<b>\$ 1.02</b>	<b>\$ 1.25</b>

See accompanying notes to financial statements.

For the year ended December 31, 1984	\$000		
	1984	1983	1982
<b>Balance, beginning of year</b>	<b>\$49,551</b>	<b>\$47,703</b>	<b>\$44,849</b>
Net earnings (loss) for the year	(6)	5,924	6,029
Share issue expenses, net of tax	—	(1,025)	—
Loss on redemption of shares	—	—	(671)
	<b>49,545</b>	<b>52,602</b>	<b>50,207</b>
<b>Dividends</b>			
Class II Preferred Shares, Series A	259	259	159
Class II Preferred Shares, Series B	3,444	—	—
Class A Common Shares	2,908	2,744	2,238
Class B Common Shares	46	48	107
	<b>6,657</b>	<b>3,051</b>	<b>2,504</b>
<b>Balance, end of year</b>	<b>\$42,888</b>	<b>\$49,551</b>	<b>\$47,703</b>

See accompanying notes to financial statements.

## Auditors' Report

Touche Ross & Co.  
Suite 2000, 360 Main Street  
Winnipeg, Manitoba R3C 3Z3  
(204) 942-0051

To the Shareholders,  
Federal Industries Ltd.

We have examined the consolidated balance sheet of Federal Industries Ltd. at December 31, 1984 and the consolidated statements of retained earnings, earnings and changes in finan-

cial 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 Company at December 31, 1984 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.

*Touche Ross & Co.*

Chartered Accountants

Winnipeg, Manitoba,  
March 15, 1985.

# CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION

For the year ended December 31, 1984		\$000	
	1984	1983	1982
<b>Operating activities</b>			
Net earnings for the year	\$ (6)	\$ 5,924	\$ 6,029
Depreciation	9,584	7,092	7,159
Amortization	614	155	161
Deferred income taxes	9,014	2,841	3,222
Accrued revenue in respect of deferred income taxes (Note 4)	(2,725)	(2,379)	(2,380)
Gain on sale of fixed assets	(2,907)	(1,504)	(685)
Earnings allocated to minority shareholders	491	371	372
Extraordinary item, net of impact on working capital of \$5,239	9,980	—	—
<b>Working capital from operations</b>	<b>24,045</b>	<b>12,500</b>	<b>13,878</b>
Accounts receivable	(22,114)	(143)	5,827
Inventories	(19,079)	458	985
Accounts payable and accruals	11,099	945	(5,762)
Other	(564)	(1,937)	(5,769)
<b>Net cash from (used in) operations</b>	<b>(6,613)</b>	<b>11,823</b>	<b>9,159</b>
<b>Financing Activities</b>			
Additional long term debt financing	9,854	24,859	9,130
Decrease in long term debt	(11,455)	(10,415)	(4,537)
Issue of shares (Note 9)	458	55,170	2,876
Redemption of shares	—	—	(1,330)
Long term debt assumed on acquisition of subsidiary companies	—	61,034	186
Minority interest in net assets of subsidiaries acquired	876	—	—
Increase in long term receivable net of deferred income tax component of \$2,725 (Note 4)	(706)	(777)	(98)
Dividends	(5,783)	(2,854)	(2,104)
Dividends paid by subsidiary company to minority shareholders	(371)	(371)	(372)
<b>Total financing activities</b>	<b>(7,127)</b>	<b>126,646</b>	<b>3,751</b>
<b>Investing activities</b>			
Acquisition of subsidiary companies			
Working capital acquired, excluding cash funds	(5,904)	(62,918)	(3,490)
Fixed assets acquired	(63)	(48,275)	(602)
Other non-current assets acquired	—	(6,787)	(109)
Excess of cost of subsidiary companies over book amount of net assets acquired	—	—	(3,293)
Purchase of fixed assets	(11,234)	(8,538)	(3,183)
Proceeds on sale of fixed assets	4,164	3,337	901
Other	522	(1,740)	641
<b>Total investing activities</b>	<b>(12,515)</b>	<b>(124,921)</b>	<b>(9,135)</b>
Increase (decrease) in cash, including \$1,228 (1983 — \$15,672; 1982 — Nil), due to acquisition of subsidiary companies	(26,255)	13,548	3,775
Cash, beginning of year	8,207	(5,341)	(9,116)
<b>Cash, end of year</b>	<b>\$ (18,048)</b>	<b>\$ 8,207</b>	<b>\$ (5,341)</b>

Note: Cash represents cash and short term investments, net of bank indebtedness.

See accompanying notes to financial statements.

For the year ended December 31, 1984

# **1. Summary of significant accounting policies**

## **a. Principles of consolidation**

The consolidated financial statements include the accounts of the Company and all subsidiaries. The names of the principal subsidiaries, which are essentially all wholly owned, are as follows:

Canadian Motorways Ltd.  
 Russelsteel Holdings Inc.  
 Russelsteel (U.S.A.) Inc.  
 Standard Aero Limited  
 Standard Aero Holdings Inc.  
 The White Pass and Yukon Corporation Limited  
 Thunder Bay Terminals Ltd.  
 Wirth Limited (89.9% owned)  
 Wirth Incorporated (89.9% owned)

All material inter-company balances, transactions and profits have been eliminated.

## **b. Foreign currency translation**

The accounts of certain subsidiaries of The White Pass and Yukon Corporation Limited are maintained in United States dollars. These accounts represent integrated foreign operations and have been translated into Canadian dollars as follows: current assets, current liabilities and long term debt at exchange rates prevailing at the end of the year; fixed assets and depreciation substantially on the basis of rates prevailing at date of acquisition; income and expenses (other than depreciation) on the basis of average exchange rates during the year. Exchange gains or losses from such translation practices have been included in consolidated earnings.

The accounts of Russelsteel (U.S.A.) Inc., Wirth Incorporated and certain subsidiaries of Standard Aero Limited are maintained in United States dollars. These accounts represent self-sustaining foreign operations and have been

translated into Canadian dollars as follows: assets and liabilities at exchange rates prevailing at the end of the year; income and expenses on the basis of average exchange rates during the year. The adjustment arising from the translation of these accounts has been deferred and included in shareholders' equity as a cumulative translation gain. The adjustment at December 31, 1983 was not material and was included in accounts payable and accrued liabilities.

## **c. Valuation of inventories**

Inventories have been valued at the lower of cost and net realizable value.

## **d. Capitalization of leases**

All material leases of a capital nature have been recorded as fixed assets and long term debt obligations.

## **e. Revenue recognition — bulk handling terminal contract**

A portion of the revenues accruing under the bulk handling terminal contract between Thunder Bay Terminals Ltd. and Ontario Hydro is being recognized on a basis that reflects an approximate constant return over each of the fifteen years of the initial term of the contract. (See Note 4).

## **f. Depreciation**

Depreciation on property, plant and equipment is provided at rates which are estimated to amortize the original cost of such assets over their useful lives.

## **g. Amortization**

Deferred charges include prepaid rent, patents and sales contracts which are being amortized over their life expectancy. Amortization of these items in 1984 was \$474,000 (1983 — \$13,000).

Goodwill on the balance sheet represents the excess cost of sub-

sidary companies over the book amount of net assets acquired, less amounts amortized. Amortization for 1984 was \$51,000 (1983 — \$51,000).

Intangible assets include:

(i) \$1,542,000 of licences, operating rights and franchises which are not being amortized and, (ii) organizational costs of subsidiary companies, amounts paid for distribution agreements and research materials, which are being amortized over a ten year period. Amortization for these assets in 1984 was \$89,000 (1983 — \$91,000).

## **h. Income taxes**

The Company follows the tax allocation method of accounting for income taxes whereby earnings are charged with income taxes relating to reported earnings.

Differences between such taxes and taxes currently payable are reflected in deferred income taxes and arise because of differences between the time certain items of revenue and expense are reported in the accounts and the time they are reported for income tax purposes.

Potential tax reductions that may result from the application of losses against future taxable income are not recognized until recovery out of future taxable income is virtually certain.

## **i. Basic earnings per share**

Earnings per common share are calculated using the weighted daily average number of common shares outstanding. The calculation of fully diluted earnings per share is described in Note 10.

## **j. International accounting standards**

The accompanying financial statements are prepared in accordance with accounting principles generally accepted in Canada and conform in all material respects with international accounting standards.

## 2. Acquisition of subsidiary companies

Effective May 31, 1984, the Company, through its subsidiaries, acquired an 89.9% interest in steel and metal trading businesses which are being carried on in the United States and Canada by Wirth Incorporated and Wirth Limited.

Operations of these companies are included in the accounts from the date of acquisition.

These acquisitions, which were accounted for by the purchase method, are included in the Industrial Distribution Group and are summarized as follows:

	\$000
Net assets acquired at fair market values at acquisition dates:	
Current assets	\$28,458
Current liabilities	21,326
	7,132
Fixed assets	63
	7,195
Minority interest in net assets	876
	\$ 6,319
Consideration:	
Cash	\$ 169
Note payable, 19%, due 1994	6,150
	\$ 6,319

## 3. Inventories

	\$000		
	1984	1983	1982
<b>Aerospace Group</b>			
Aviation parts	\$ 45,577	\$ 28,104	\$ 27,699
Aircraft engines	5,052	6,405	5,470
Work in process	4,301	3,207	3,149
	54,930	37,716	36,318
<b>Transport Group</b>			
Petroleum products held for sale	6,151	7,650	8,825
Spare parts and supplies	1,785	3,437	3,054
Terminal division spare parts and supplies	1,482	1,429	1,389
	9,418	12,516	13,268
<b>Industrial Distribution Group</b>			
Metals division	64,976	49,498	—
Valve division	6,482	5,529	—
	71,458	55,027	—
	\$135,806	\$105,259	\$ 49,586

## 4. Terminal handling facility – Thunder Bay, Ontario

### a. Coal handling facility

Thunder Bay Terminals Ltd. has entered into a long term contract with Ontario Hydro for the construction and operation of a bulk terminal handling facility at Thunder Bay, Ontario. The total cost of the terminal is \$69,851,000 of which \$53,953,000 relates to facilities which became operational on March 1, 1979 and \$15,898,000 relates to terminal facilities which became operational in 1981.

The cost of the terminal has been financed by the issue of \$71,496,000 aggregate principal amount, 9<sup>5</sup>/<sub>8</sub>% First Mortgage Sinking Fund Bonds, Series A. As at December 31, 1984, the Series A bonds issued and outstanding aggregated \$52,754,000. The terms and conditions of the Series A bond issue are provided for in a Deed of Trust and Mortgage dated as of October 12, 1977 between Thunder Bay Terminals Ltd. and the trustee for the bondholders.

Under the terms of the agreements with Ontario Hydro, Thunder Bay Terminals Ltd. will receive, over the initial fifteen year term of the contract, contractual amounts of revenue including specific revenue components to cover all payments required for the redemption of all of the Series A bonds and for income taxes. These revenue components become recoverable as and when the bond and income tax payments become due and payable. The use of the cash received in respect of these specific revenue components is restricted to the redemption of the Series A bonds and the payment of income taxes.

The amounts receivable over the fifteen years of the initial term of the contract to cover the redemp-

tion of the Series A bonds represent the revenues required to pay for the capital cost of the terminal facility. The net contribution to earnings from these revenues (total amounts receivable less depreciation on the terminal) is recorded in the accounts so as to reflect an approximate constant annual return over each of the fifteen years.

At December 31, 1984, the accrued revenues receivable from Ontario Hydro for the redemption of Series A bonds amount to

\$7,258,000 of which \$3,408,000 is long term and \$3,850,000 is current. The long term accrued revenues receivable for the payment of income taxes amount to \$13,561,000 (1983 – \$10,837,000; 1982 – \$8,458,000), all of which relate to deferred income taxes. Because the \$13,561,000 to be received is restricted to the payment of income taxes, the liability for the deferred income taxes has been netted against the long term receivable.

**b. Potash handling facility**  
On September 16, 1983, Thunder Bay Terminals Ltd. entered into agreements with Canadian Pacific Limited for (i) the management and supervision of the construction of a dry bulk handling facility; and (ii) an exclusive license to operate the facility. The initial term of the potash handling agreement commenced upon completion of construction of the dry bulk handling facility on April 1, 1984 and is scheduled to terminate on February 28, 1994.

5. Fixed assets		1984		\$000	1983	1982
	Cost	Accumulated Depreciation	Net	Net	Net	
<b>Aerospace Group</b>						
Land and buildings	\$ 4,695	\$ 2,372	\$ 2,323	\$ 3,699	\$ 2,358	
Machinery and equipment	9,434	4,944	4,490	2,210	2,313	
	14,129	7,316	6,813	5,909	4,671	
<b>Transport Group</b>						
Northern operations						
Storage facilities	4,133	798	3,335	3,626	3,637	
Pipeline	1,174	829	345	405	438	
Skagway terminal	6,690	4,481	2,209	2,239	2,239	
Rail	—	—	—	25,893	25,917	
Ship and containers	—	—	—	500	639	
Automotive equipment	10,992	6,702	4,290	59	91	
Land and buildings	4,889	2,065	2,824	1,776	1,681	
Machinery and equipment	2,657	1,376	1,281	634	728	
Freight hauling						
Automotive equipment	42,600	34,166	8,434	11,304	3,561	
Land and buildings	20,558	3,026	17,532	19,227	1,359	
Machinery and equipment	8,198	3,464	4,734	3,570	151	
Terminal						
Handling facilities	70,217	17,560	52,657	55,718	58,843	
Assets held for sale	14,762	—	14,762	2,365	2,207	
	186,870	74,467	112,403	127,316	101,491	
<b>Industrial Distribution Group</b>						
Land and buildings	13,684	601	13,083	13,529	—	
Machinery and equipment	8,234	759	7,475	7,296	—	
	21,918	1,360	20,558	20,825	—	
<b>Other corporate assets</b>						
	1,504	325	1,179	220	222	
	\$224,421	\$ 83,468	\$140,953	\$154,270	\$106,384	

Included in the amounts reported above are assets under capital leases of \$3,623,000 (1983 – \$4,833,000; 1982 – \$3,194,000) and related accumulated depreciation thereon of \$1,784,000 (1983 – \$2,089,000; 1982 – \$1,912,000).

6. Long term debt		\$000		
	1984	1983	1982	
<b>Aerospace Group</b>				
Bank loan, secured, 1/2% above United States prime rate	\$ —	\$ —	\$ 1,842	
Bank loan, secured, 2 1/4% above United States prime rate, due 1987	—	—	160	
Bank loan, secured, 13.05%–13.43%, due 1990	6,618	6,222	—	
Note payable, 15%, due 1984	—	—	1,071	
Other	—	49	9	
	6,618	6,271	3,082	
<b>Transport Group</b>				
Thunder Bay Terminal				
First mortgage bond, 9 3/8% (Note 4)	48,904	52,754	56,604	
Promissory note, secured, 15% 1986 to 1987	1,280	—	325	
Capitalized lease obligations, 8.2%–14.4%	1,288	1,785	1,039	
Government of Canada non-interest bearing loan, secured by certain rail assets	4,500	4,750	5,000	
Government of Yukon Territory non-interest bearing loan, secured by certain rail assets	—	—	1,000	
Alaska Industrial Development Authority Port Facility 13 3/4% bond, 1985 to 1998	4,697	4,368	4,672	
Mortgages, 10 5/8%–12 1/2%, 1985 to 1988	3,243	3,409	—	
Bank loan, secured, 1/2% above U.S. prime rate	178	403	—	
Bank loan, secured, 1/4% above prime rate	6,400	9,000	—	
Other	30	6	18	
	70,520	76,475	68,658	
<b>Industrial Distribution Group</b>				
Industrial Development Bond, 7 1/2%	1,189	1,245	—	
Note payable, 12.36%, due 1988	55,000	55,000	—	
Note payable, 19%, due 1994	6,150	—	—	
Mortgages, 7 3/4%–8%	60	623	—	
Capitalized lease obligations	79	124	—	
	62,478	56,992	—	
<b>Corporate debt</b>				
Bank loan, secured, 13.05%–13.43%, due 1990	6,618	6,222	—	
Note payable	165	220	—	
Capitalized lease obligations, 14 1/4%–16 1/2%	93	131	155	
	6,876	6,573	155	
	\$146,492	\$146,311	\$ 71,895	

The aggregate amount of maturities over the next five years is approximately as follows: 1985 – \$6,271,000; 1986 – \$6,231,000; 1987 – \$6,192,000; 1988 – \$60,337,000; 1989 – \$4,804,000.

## 7. Bank overdraft and secured indebtedness

Bank indebtedness is secured by a pledge of shares in subsidiaries, assignment of book debts and inventories, specific pledges of certain inventories and fixed and floating charges on certain fixed assets.

## 8. Minority interest

Minority interest is \$5,500,000 of 6 3/4% preferred shares of The White Pass and Yukon Corporation Limited (1983 – \$5,500,000; 1982 – \$5,500,000), and \$996,000 of common equity of Wirth Limited and Wirth Incorporated.

## 9. Share capital

a. At December 31, 1984 the authorized share capital of the Company consists of:

- i. an unlimited number of Class A convertible Common Shares without nominal or par value;
- ii. an unlimited number of Class B convertible Common Shares without nominal or par value;
- iii. an unlimited number of Class I Preferred Shares without nominal or par value, issuable in series; and
- iv. an unlimited number of Class II Preferred Shares without nominal or par value, issuable in series; to date the directors have authorized:

28,760 Convertible Class II Preferred Shares, Series A, with annual cumulative cash dividends of \$9.00 per share payable in quarterly instalments. These shares are convertible on or before May 20, 1992 on the basis of approximately 6.41 Class A Common Shares for each Class II Preferred Share, Series A.  
1,600,000 \$2.0625 Cumulative Redeemable Convertible Class II Preferred Shares, Series B, with annual cash dividends of \$2.0625 per share payable in quarterly instalments. This series of Class II Preferred Shares is redeemable

subject to certain conditions being met at prices ranging from \$26.25 per share in 1986 to \$25.00 per share in 1993 and thereafter. These shares are convertible on or before the earlier of December 15, 1990 and the date fixed for redemption on the basis of approximately 1.37 Class A Common Shares for each Class II Preferred Share, Series B.

Both the Class A Common Shares and the Class B Common Shares are inter-convertible at any time at the option of the holder on a share for share basis. The basic difference between the two classes of shares is that dividends on Class A Common Shares are payable in the form of cash dividends, while dividends on Class B Common Shares are presently payable in the form of stock dividends, payable in Class B Common Shares.

The directors have the authority to issue the Class I and Class II Preferred Shares in series and fix the designation, rights, privileges and conditions to be attached to each series, except the Class I shares shall be entitled to preference over the Class II shares with respect to the payment of dividends and the distribution of assets in the event of liquidation, dissolution or winding-up of the Company.

b. During 1984 the following shares were issued:

- i. 685 Class A Common Shares on conversion of 500 Class II Preferred Shares, Series B, originally issued for \$12,500;
- ii. 25,000 Class A Common Shares for an aggregate consideration of \$458,000 under the terms of the stock purchase plan; and
- iii. 2,683 Class B Common Shares as stock dividends of \$47,000, of which \$12,000 was accrued at December 31, 1983. An additional 576 Class B shares were issued as stock dividends of \$11,000 on January 1, 1985.

c. The number of shares issued and outstanding at December 31 was as follows:

	1984	1983	1982
Class II Preferred, Series A	28,760	28,760	28,760
Class II Preferred, Series B	1,599,500	1,600,000	—
	<u>1,628,260</u>	<u>1,628,760</u>	<u>28,760</u>
Class A Common	5,829,228	5,788,727	4,530,419
Class B Common	86,351	98,484	164,194
	<u>5,915,579</u>	<u>5,887,211</u>	<u>4,694,613</u>

d. The recorded values of the shares issued and outstanding at December 31 were as follows:

	1984	1983	1982
Class II Preferred, Series A	\$ 2,876	\$ 2,876	\$ 2,876
Class II Preferred, Series B	39,987	40,000	—
Common Shares	45,303	44,786	29,557
	<u>\$88,166</u>	<u>\$87,662</u>	<u>\$32,433</u>

e. In 1978, the shareholders confirmed a by-law authorizing a stock purchase plan, the purpose of which is to provide loans to employees of the Company and subsidiary companies for the purchase of Class A

Common Shares of the Company. During the year, 25,000 shares were issued to an officer of the Company and an officer of a subsidiary company at their market value for an aggregate consideration of \$458,000.

f. In December 1981 the directors approved a share option plan, the purpose of which is to provide employees of the Company and its subsidiaries with the opportunity to participate in the growth and development of the Company. At December 31, 1984, 282,000 authorized and unissued Class A Common Shares of the Company

have been reserved and set aside for purposes of the plan. The options are exercisable on a cumulative basis to the extent of 20% per year of total options granted, except that under certain specified conditions they become exercisable immediately. Details of options granted to officers of the Company and its subsidiaries are as follows:

Year of Issue	Number of Shares	Exercise Price	Exercisable Per Year	Exercisable To Date	Year of Expiry
1981	180,000	\$12.6875	36,000	144,000	1991
1983	20,000	11.5118	4,000	8,000	1993
1983	10,000	12.5000	2,000	4,000	1993
1984	15,000	16.9100	3,000	3,000	1994
	<u>225,000</u>		<u>45,000</u>	<u>159,000</u>	

# 10. Earnings per Common Share

a. Basic earnings per Common Share are calculated using the weighted daily average number of

Common Shares outstanding.

b. Fully diluted earnings per Common Share are as follows:

	1984	1983	1982
Fully diluted earnings per share before extraordinary item	\$1.84	\$1.02	\$1.25
Extraordinary loss on write-down of rail assets	N/A	—	—
Fully diluted earnings (loss) per share after extraordinary item	<u>\$(.60)</u>	<u>\$1.02</u>	<u>\$1.25</u>

Fully diluted earnings per share are calculated under the assumption that all convertible Preferred Shares were converted at the beginning of the year and that stock options outstanding during the year had been exercised at the beginning of the year, or when granted. Imputed earnings on the proceeds from the exercise of the options and the net dividend saving on the conversion of Preferred Shares of \$459,755 were calculated using a 12.37% after tax rate of return.

# 11. Income taxes

a. The Company's effective income tax rates are derived as follows:

	1984	1983	1982
Average combined tax rate	49.8%	51.1%	48.1%
Dividend Income	(2.9)	—	—
Inventory tax allowances	(5.7)	(5.6)	(5.5)
Reduced rate on capital gains	(0.6)	(5.3)	—
Unrecorded tax benefits related to losses of subsidiary companies	1.6	3.3	4.6
Manufacturing and processing tax credits	—	(1.3)	(2.3)
Investment tax credits	(2.7)	(0.3)	(1.6)
Other	(0.1)	3.2	0.6
Average effective tax rate	39.4%	45.1%	43.9%

b. Certain subsidiaries of the Company have tax loss carry forwards of approximately \$4,540,000 and investment tax credit carry forwards of approximately \$1,494,000 available to reduce future taxable income and taxes payable. The potential benefits of these carry forwards will be recorded as the benefits are received.

12. Segmented information	\$000		
	1984	1983	1982
<b>Sales &amp; Services</b>			
Aerospace Group	\$109,412	\$ 97,935	\$ 75,995
Transport Group			
Northern operations	32,494	32,604	66,438
Freight hauling	105,418	61,464	19,407
Terminal	23,053	20,937	22,180
Industrial Distribution Group	310,868	—	—
	581,245	212,940	184,020
Inter-segment eliminations	(8,654)	(9,142)	(4,827)
	<u>\$572,591</u>	<u>\$203,798</u>	<u>\$179,193</u>
<b>Segment Margin</b>			
Aerospace Group	\$ 5,003	\$ 4,006	\$ 8,125
Transport Group			
Northern operations	2,566	2,367	2,923
Freight hauling	7,549	3,407	(1,567)
Terminal	13,018	12,022	12,901
Industrial Distribution Group	18,121	—	—
	46,257	21,802	22,382
Inter-segment eliminations	(30)	(97)	(339)
	46,227	21,705	22,043
Interest expense	(20,034)	(9,744)	(8,409)
Investment income	2,503	984	492
Other corporate expenses	(2,801)	(1,474)	(2,721)
Earnings from operations	25,895	11,471	11,405
Provision for income taxes	(10,191)	(5,176)	(5,004)
Allocated to minority shareholders	(491)	(371)	(372)
Extraordinary item	(15,219)	—	—
Net earnings (loss)	<u>\$ (6)</u>	<u>\$ 5,924</u>	<u>\$ 6,029</u>
<b>Capital Expenditures</b>			
Aerospace Group	\$ 1,781	\$ 2,175	\$ 1,613
Transport Group			
Northern operations	3,303	355	429
Freight hauling	4,047	33,243	1,126
Terminal	237	168	542
Industrial Distribution Group	844	20,825	—
Other corporate assets	1,022	47	75
	<u>\$ 11,234</u>	<u>\$ 56,813</u>	<u>\$ 3,785</u>
<b>Depreciation and Amortization</b>			
Aerospace Group	\$ 1,061	\$ 1,006	\$ 598
Transport Group			
Northern operations	951	500	1,483
Freight hauling	3,097	2,400	1,835
Terminal	3,290	3,292	3,272
Industrial Distribution Group	1,734	—	—
Other corporate assets	65	49	45
	<u>\$ 10,198</u>	<u>\$ 7,247</u>	<u>\$ 7,233</u>

12. Segmented information (continued)	\$000		
	1984	1983	1982
<b>Identifiable Assets</b>			
Aerospace Group	\$ 90,532	\$ 66,950	\$ 64,108
Transport Group			
Northern operations	45,667	54,011	54,351
Freight hauling	50,871	56,466	7,804
Terminal	64,195	66,949	68,601
Industrial Distribution Group	169,477	112,793	—
Other corporate assets	28,990	19,800	4,705
	<b>\$449,732</b>	<b>\$376,969</b>	<b>\$199,569</b>

12a. The Company has segmented its operations on the basis of the major industries in which it operates as described below:

- i. The Aerospace Group's operations consist of the remanufacturing and rebuilding of aircraft engines and distribution of aviation parts and accessories.
- ii. The Transport Group's operations consist of the distribution of petroleum and related consumer products; the provision of truck transportation services; and the operation of major bulk handling terminal facilities.

iii. The Industrial Distribution Group's operations consist of the distribution of general line, flat-rolled and specialty steel products, metals trading and the distribution of industrial valves, piping components and related products.

Inter-segment sales are accounted for at prices comparable to open market prices for similar products and services.

b. The Aerospace Group had domestic sales to foreign customers, principally in Europe, of \$9,118,000 (1983 — \$7,354,000; 1982 — \$8,606,000).

### 13. Directors' remuneration

The aggregate remuneration of directors and senior officers of the Company is as follows:

	Federal Industries Ltd.		The White Pass and Yukon Corporation Limited	
	No.	Amount	No.	Amount
As Directors				
1984	9	\$ 72,100	6	\$6,000
1983	9	\$ 63,250	6	\$6,000
1982	9	\$ 31,500	6	\$6,400
As Officers				
1984	6	\$639,055	—	—
1983	8	\$704,184	—	—
1982	6	\$575,513	—	—

3 officers are also directors of the Company (1983 — 3 officers; 1982 — 4 officers).

### 14. Extraordinary item

\$000

Write down of railway and related assets and provision for costs of continued suspension of railway operations, net of deferred income taxes of \$4,191,000

\$15,219

### 15. Contingencies and commitments

a. The Company has an investment of \$2,150,000 (1983 — \$1,650,000; 1982 — \$1,650,000) in Preferred Shares of and loans to a company that is highly leveraged, with substantially all of its debt repayable on demand. Although its lenders have not indicated their intent to demand repayment, should such an event occur it is unlikely that it would be able to meet such repayment demand. In these circumstances, liquidation could result and the Company could suffer a loss on its investment.

b. The Company and its subsidiary companies have operating lease commitments with varying terms requiring annual rental payments of approximately \$2,715,000 (1983 — \$686,000; 1982 — \$480,000).

### 16. Other

a. At December 31, 1984, loans to officers of the Company represented housing loans of \$244,000 (1983 — \$256,000; 1982 — \$168,000) and a loan under the stock purchase plan of \$274,000 (1983 and 1982 — Nil).

b. Certain of the prior years' figures have been restated to reflect the current year's presentation.

The audited financial statements in this Annual Report are based on historical cost accounting, which matches actual costs incurred with actual revenues received. To highlight the effect of inflation on financial assets of the business, the Canadian Institute of Chartered Accountants (CICA) has recommended that corporations provide supplemental information to show the effect of inflation on the balance sheet and results of operations for the year. The primary focus is upon specific changes in prices of assets and in expenses associated with the use of fixed assets or the sale of inventories. It is a method of measuring their current values in terms of what the assets would cost to purchase or produce at the balance sheet date or at the date of use of fixed assets or sale of goods produced.

Current cost accounting amounts for the Company's assets were determined for the most part by using appropriate specific indices or reliable market prices. For property, plant and equipment this method assumes the assets would be replaced with like technology, although this would not always be the case. The current cost of sales was determined by adjusting the historical costs by the estimated specific price changes which occurred between the time of production and the time of sale.

This method of reporting requires the use of numerous assumptions and estimates, and accordingly, the resulting information, presented below, is not a precise indication of the effects of inflation on the results of your Company. In addition, the provision for income taxes, according

to the CICA recommendations, remains unchanged, since adjustments to income under the current cost computations are not deductible for tax purposes. This results in a tax rate which is considerably higher than normal. Accordingly, management feels that the pretax comparison of operating results on an historic and current cost basis is more meaningful than the net of tax amounts.

The current cost loss of \$6.9 million for 1984, as shown in the schedule below, is based on an operating capability concept of capital. This concept measures income and loss generated by an enterprise from all sources of capital, whether provided by lenders or shareholders. To measure income attributable to shareholders on a current cost basis, the CICA recommends the calculation of a "financing adjustment". It is based on the supposition that the funds required to maintain a company's operating capability (replace the assets it consumes) will be provided by a combination of shareholder and borrowed funds. The financing adjustment aims to provide a measure of the increases in current costs that would be financed by debt. Recognizing this adjustment mitigated the inflation-adjusted loss by \$2.6 million.

Two items of general inflation information are presented. The first "Excess of increase in current cost over the effect of general inflation" provides a comparison of the specific price change adjustments and changes that would have resulted from general inflation level appli-

cation. This differential was \$2.1 million for 1984. The second is "General purchasing power gain on net monetary liabilities". Holders of cash and other monetary assets lose purchasing power during periods of inflation — "debtor's gain". Your Company has greater monetary liabilities than monetary assets and the general purchasing power gain thereon helps preserve the general purchasing power of the shareholders' equity. On the CICA basis of calculation, which excludes deferred income taxes as a monetary item, your Company would have reported a net gain in purchasing power of approximately \$4.4 million.

As a final item of disclosure, we present a comparative schedule of consolidated assets on the basis of current and historical costs. This table shows there is an apparent increase in Common Shareholders' equity from historical to current cost accounting of \$3.5 million.

In arriving at the foregoing estimates, judgment has been exercised with respect to the treatment of certain asset groups. For example, in the case of Thunder Bay Terminals, no adjustment has been made for the incremental cost of replacing assets, since funding is covered on a "current cost" basis with Ontario Hydro, the company's principal customer.

Despite the obvious weaknesses inherent in estimating and the apparent anomalies, as with tax rates, your Company supports the disclosure of inflation accounting information to enable readers of the financial statements to obtain a more informed assessment of the Company's results.

## Consolidated Statement of Earnings on a Current Cost Basis

Under an Operating Capability Concept of Capital for the year ended December 31, 1984

	\$000		
	Historical 1984	Current Cost 1984	1983*
Sales and services	\$572,591	\$572,591	\$211,466
Cost of sales and operating expenses	521,874	523,984	191,313
Depreciation	9,584	10,304	9,469
Amortization	614	614	147
Interest on long term debt	17,077	17,077	8,744
Other interest expense	2,957	2,957	1,369
Investment income	(2,503)	(2,503)	(1,021)
Gain on sale of fixed assets	(2,907)	—	—
	546,696	552,433	210,021
Earnings on a current cost basis before income taxes	25,895	20,158	1,445
Provision for income taxes			
Current	1,177	1,177	2,423
Deferred	9,014	9,014	2,948
	10,191	10,191	5,371
Net earnings (loss) on a current cost basis before extraordinary item	15,704	9,967	(3,926)
Extraordinary item	15,219	15,219	—
Net earnings (loss)	485	(5,252)	(3,926)
Earnings allocated to minority shareholders	491	491	385
Net earnings (loss) on a current cost basis for the year	(6)	(5,743)	(4,311)
Financing adjustment	—	2,553	1,280
Dividends on Preferred Shares	(3,703)	(3,703)	(269)
Net earnings (loss) attributable to Common Shareholders on a current cost basis under an operating capability concept of capital	\$ (3,709)	\$ (6,893)	\$ (3,300)

Based on the current cost adjustments made to income during the year the financing adjustment amounts to \$3,119,000 (1983\* – \$2,092,000). \* Comparative data for 1983 has been restated into 1984 dollars.

## Reporting the Effects of Changing Prices

Supplementary Information

for the year ended December 31, 1984

	\$000	
	1984	1983*
Increase in current cost amounts of inventory and property, plant and equipment	\$ 4,881	\$ 6,401
Effect of general inflation	2,799	4,946
Excess of increase in current cost over the effect of general inflation	\$ 2,082	\$ 1,455
General purchasing power gain on net monetary liabilities	\$ 4,430	\$ 1,086

## Schedule of Consolidated Assets on a Current Cost Basis

	\$000		
	Historical 1984	Current Cost 1984	1983*
Inventory	\$135,806	\$138,170	\$109,219
Property, plant and equipment – net	\$140,953	\$142,066	\$160,074
Net assets (Common Shareholders' equity)	\$ 89,353	\$ 92,829	\$ 98,123

\* Comparative data for 1983 has been restated into 1984 dollars.

**SEGMENTED INFORMATION**

	Aerospace Group		Industrial Distribution		Transport Group		
					Freight Hauling Services		
(\$000)	1984	1983	1982	1984*	1984	1983	1982
Sales	\$109,412	\$97,935	\$75,995	\$310,868	\$105,418	\$61,464	\$19,407
Inter segment sales	5,369	7,055		2,831		1,260	1,767
	104,043	90,880	75,995	308,037	105,418	60,204	17,640
Segment operating profit before interest and taxes	5,003	4,006	8,125	18,121	7,549	3,407	(1,567)
Investment income							
Interest expense							
Inter segment interest							
General corporate expenses							
Earnings from operations before income taxes							
Income taxes							
Net earnings before minority interest and extraordinary items							
Identifiable assets	90,532	66,950	64,108	169,477	50,871	56,466	7,804
Corporate assets							
Industrial Distribution *							
Total assets							
Capital expenditures	1,781	2,175	1,613	844	4,047	33,243	1,126
Depreciation and amortization	1,061	1,006	598	1,734	3,097	2,400	1,835

\*Industrial Distribution Group was acquired December 31, 1983.

## Transport Group

## Consolidated

Northern Operations			Terminal					
1984	1983	1982	1984	1983	1982	1984	1983	1982
\$32,494	\$32,604	\$66,438	\$23,053	\$20,937	\$22,180	\$581,245	\$212,940	\$184,020
454	827	3,060				8,654	9,142	4,827
32,040	31,777	63,378	23,053	20,937	22,180	572,591	203,798	179,193
2,536	2,270	2,584	13,018	12,022	12,901	46,227	21,705	22,043
						2,503	984	492
						(25,058)	(12,583)	(10,031)
						5,024	2,839	1,622
						(2,801)	(1,474)	(2,721)
						25,895	11,471	11,405
						10,191	5,176	5,004
						\$ 15,704	\$ 6,295	\$ 6,401
45,667	54,011	54,351	64,195	66,949	68,601	420,742	244,376	194,864
						28,990	19,800	4,705
							112,793	
						\$449,732	\$376,969	\$199,569
3,303	355	429	237	168	542			
951	500	1,483	3,290	3,292	3,272			

# CONSOLIDATED HISTORICAL SUMMARY

For the twelve months ended	31 Dec. 84	31 Dec. 83	31 Dec. 82	31 Dec. 81
<b>Income Information (\$000)</b>				
Sales and services	572,591	203,798	179,193	192,690
Gross earnings from operations	50,717	25,974	25,870	35,736
Net earnings before extraordinary items	15,213	5,924	6,029	10,914
Extraordinary items	(15,219)	—	—	24
Net earnings after extraordinary items	(6)	5,924	6,029	10,938
Depreciation	9,584	7,092	7,159	6,649
Interest on long term debt	17,077	8,427	6,760	6,503
Income taxes	10,191	5,176	5,004	10,462
Earnings (loss) per Common Share (\$)	(0.60)	1.02	1.25	2.44
Earnings (loss) per Common Share excluding extraordinary items (\$)	1.97	1.02	1.25	2.43
<b>Balance Sheet Information (\$000)</b>				
Current assets	290,675	206,852	85,238	91,084
Current liabilities	153,300	80,378	34,696	51,036
Working capital	137,375	126,474	50,542	40,048
Fixed assets — Net	140,953	154,270	106,384	109,974
Other assets	18,104	15,847	7,947	5,246
Total assets	449,732	376,969	199,569	206,304
Long term debt	146,492	146,311	71,895	68,313
Deferred income taxes	11,215	7,567	7,342	6,500
Minority interest	6,496	5,500	5,500	5,500
Shareholders' equity	132,229	137,213	80,136	74,955
<b>Other Information</b>				
Gross margin ratio %	8.9	12.7	14.4	18.5
Return on equity %	12.4	7.1	7.8	19.8
Debt/equity ratio	.98	.97	.77	.79
Current ratio	1.90	2.57	2.46	1.78
Net earnings before extraordinary items as % of sales	2.7	2.9	3.4	5.7
No. Common Shares outstanding (A & B)	5,915,579	5,887,211	4,694,613	4,789,774
Dividend per Share				
Class A (\$) Note 1	.50	.50	.45	.275
Class B (\$) Note 2	.50	.50	.45	.275
Price range of stock (\$)				
High	20.75	16.50	14.00	15.87
Low	16.00	10.37	8.25	10.00
Shareholders' equity per Common Share (\$)	15.11	16.02	16.46	15.65

NOTES: (1) Payable in cash dividends.

(2) Payable by way of stock dividend in Class B Shares.  
These Class B Shares were created in May, 1980.

31 Dec. 80	31 Dec. 79	31 Dec. 78*	31 Mar. 78	31 Mar. 77	31 Mar. 76
159,226	126,716	112,987	99,830	78,848	106,729
29,264	18,173	11,293	7,779	7,095	13,390
7,407	1,789	714	(17)	591	2,161
(290)	—	(1,527)	(2,498)	891	514
7,117	1,789	(813)	(2,515)	1,482	2,675
5,615	5,227	3,974	3,431	3,743	4,361
8,319	7,969	3,120	1,074	1,267	1,575
7,158	1,756	1,475	1,611	573	2,999
1.98	.51	(.23)	(.73)	.43	.78
2.06	.51	.21	(.01)	.17	.63
69,032	56,490	50,044	49,039	52,508	41,306
44,805	41,880	39,386	44,618	42,457	29,381
24,227	14,610	10,658	4,421	10,051	11,925
102,250	119,092	112,574	98,398	60,369	61,506
7,965	16,135	13,347	7,635	5,840	6,028
179,247	191,717	175,965	155,072	118,717	108,840
68,853	95,043	82,542	59,396	22,034	24,174
5,079	5,525	6,091	5,744	5,193	5,255
5,500	5,500	5,500	5,500	5,500	6,794
55,010	43,769	42,446	39,814	43,533	43,236
18.4	14.3	10.0	7.8	9.0	12.5
16.9	4.2	1.6	—	1.4	5.1
1.05	1.73	1.53	1.16	.41	.44
1.54	1.35	1.27	1.10	1.24	1.41
4.7	1.4	.6	—	.7	2.0
3,944,006	3,528,900	3,488,900	3,438,900	3,438,900	3,438,900
.20	.20	.20	.35	.40	.40
.20	—	—	—	—	—
15.25	8.00	7.12	8.00	6.00	6.25
6.37	5.50	4.90	4.90	4.80	3.70
13.95	12.40	12.17	11.58	13.24	12.57

\*Unaudited

**SUMMARIZED QUARTERLY FINANCIAL INFORMATION (UNAUDITED)**

	Three months ended				Year ended
1984	March 31	June 30	Sept. 30	Dec. 31	Dec. 31
Sales (\$000)	114,556	128,133	164,913	164,989	572,591
Gross earnings from operations (\$000)	8,376	12,911	15,197	14,233	50,717
Gross margin percentage	7.3%	10.1%	9.2%	8.6%	8.9%
Net earnings* (\$000)	1,386	3,717	5,298	4,812	15,213
Earnings per Common Share*	\$ .08	\$ .48	\$ .75	\$ .66	\$ 1.97
Market price of Common Shares					
High	18.00	18.875	20.75	20.25	20.75
Low	16.00	16.625	18.00	18.00	16.00
Number of Common Shares traded	329,545	218,800	180,822	313,629	1,042,796

	Three months ended				Year ended
1983	March 31	June 30	Sept. 30	Dec. 31	Dec. 31
Sales (\$000)	34,307	41,357	42,356	85,778	203,798
Gross earnings from operations (\$000)	2,530	6,406	6,248	10,790	25,974
Gross margin percentage	7.4%	15.5%	14.8%	12.6%	12.7%
Net earnings* (\$000)	(1,817)	1,770	2,308	3,663	5,924
Earnings per Common Share*	\$ (.40)	\$ .35	\$ .44	\$ .63	\$ 1.02
Market price of Common Shares					
High	13.50	15.00	16.50	16.50	16.50
Low	10.37	13.12	14.50	14.50	10.37
Number of Common Shares traded	361,100	672,400	232,100	74,500	1,340,100

	Three months ended				Year ended
1982	March 31	June 30	Sept. 30	Dec. 31	Dec. 31
Sales (\$000)	47,822	47,462	45,293	38,616	179,193
Gross earnings from operations (\$000)	6,659	8,390	5,808	5,013	25,870
Gross margin percentage	13.9%	17.7%	12.8%	13.0%	14.4%
Net earnings* (\$000)	1,434	2,658	817	1,120	6,029
Earnings per Common Share*	\$ .30	\$ .57	\$ .15	\$ .23	\$ 1.25
Market price of Common Shares					
High	13.75	14.00	11.50	11.75	14.00
Low	11.00	10.25	8.50	8.25	8.25
Number of Common Shares traded	106,800	207,000	361,000	326,700	1,001,500

\* Before extraordinary items

# KEEP IT SIMPLE MAKE IT HAPPEN

*The Management Principles  
that guide Federal Industries*

In late 1981, before "corporate culture" became a buzzword, Federal embarked upon an ambitious program to deal with this management challenge that has proven to be a stumbling block for many companies, and diversified companies in particular.

Following is a quote from Federal's Corporate Long Range Plan dated March 26, 1982:

*We think our ability to manage diversity can be enhanced by developing a "Federal Culture", a way of going based on broad management principles that apply equally to all businesses we're in.*

*We've taken the business principles Jack Fraser has developed over the years and boiled them down to a set of general statements that we believe to be valid for any business we're in or contemplate being in ... By formally adopting these principles, we hope to enable the presidents to understand them better and spread them through their organizations more effectively.*

By the time those words were written,

the Principles had been reviewed, and there was general agreement on their meaning. Since 1982, the Principles have been presented in various forums of Federal's management and they have been widely circulated and used throughout Federal's diversified operations. While a new acquisition is under investigation and when one is completed, a review and discussion of the Principles is a high priority item. Most importantly, the understanding and acceptance of these simple Principles has become deeper and more widespread.

Each year, the Principles are included in the Corporate Long Range Plan, and they form a cornerstone of Federal's planning and operations. These Principles have become such a fundamental part of Federal's management that it is appropriate to feature them in this annual report to the shareholders.

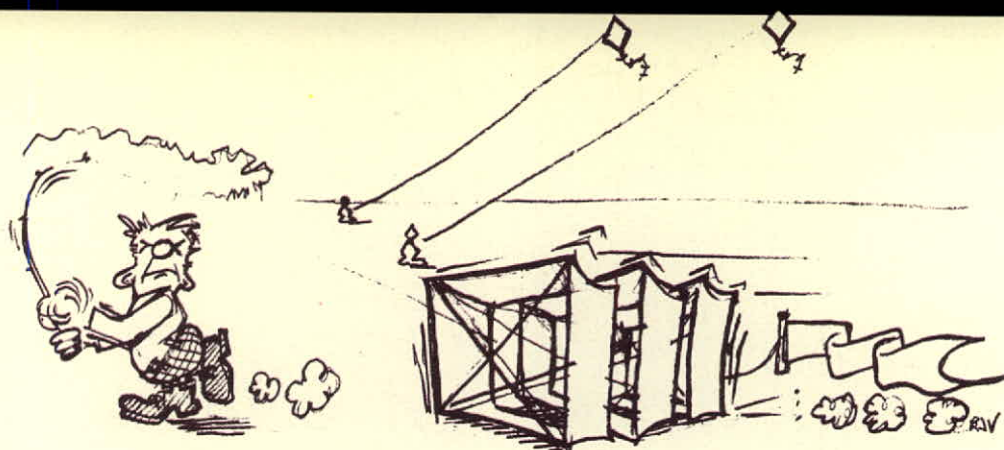
They are reproduced here as they originally appeared, along with some commentary intended to give some idea of how they are used.

The underlined caption below is a quote from Peter Drucker, and while it is not one of the Principles, it is the prime reason that having management principles is essential to management excellence. It's easy to say "Do the Right Things", but how do we know what the right things are? It's all too easy to fall into the trap of accepting the routines of business as the "right things", because such routines have a way of routinely delivering the expected results. Thinking about what we do in the context of accepted principles of management, is a way of making us think objectively about what we do. Federal is a company that espouses a team approach to management, so it is important that all members of the

team focus their attention on what's right, as opposed to who's right.

OVER THE YEARS, WE'VE DESERVED A LOT OF BUSINESSMEN CLEVERLY AND EARNESTLY WORKING HARD AT THEIR BUSINESS, AND IN MANY CASES, FAILING. WE'VE BEEN IN THAT POSITION OURSELVES. WE'VE LEARNED THAT THERE'S A BIG DIFFERENCE BETWEEN DOING THINGS RIGHT AND DOING THE RIGHT THINGS.





## KEEP IT SIMPLE

BUSINESS HAS BECOME COMPLEX AND IT'S EASY TO GET BOGGED DOWN IN DETAILS. THERE ARE MANY FACETS TO MOST BUSINESS PROBLEMS, ALL OF WHICH MUST BE CONSIDERED. SOME ASPECTS ARE VITAL AND LEAD TO THE ESSENCE OF THE PROBLEM. ONCE THE HEART OF THE MATTER IS FOUND, THE ANSWER TO THE PROBLEM IS OBVIOUS.

This is the foundation of the Principles. Who has not used this phrase in one way or another? Yet there is no question that this is the most misunderstood and most widely abused of all the Principles. Keep it Simple was the theme

of the 1983 Federal Management Seminar, and it was viewed as a means of getting to and understanding the Fundamentals of each Federal company's business.

The great nuclear physicist Dr. Edward Teller, as a frustrated Hungarian high school student, wrote in his diary:

*"What is called understanding is often no more than a state where one has become familiar with what one does not understand."*

Trying to simplify from such a faulty "understanding" is perilous indeed. Later in his life, Dr. Teller wrote a book entitled *The Pursuit of Simplicity* in which he

defined "understanding" as getting used to a set of facts and becoming familiar enough with them to be able to use them to successfully predict outcomes.

This is the kind of understanding that is sought as a basis for planning, and at the 1983 Federal Management Seminar, a system of Fundamentals Analysis was used to help each operating company come to an understanding of the Fundamentals of its business. The result was a quantum leap in the quality of strategic planning among most of the managers who participated in the Seminar.

## KEEP IT SIMPLE REQUIRES UNQUESTIONABLE ETHICS

THE LAW SAYS WHAT'S LEGAL, BUT "LAW" HAS BECOME COMPLEX AND UNCLEAR. GREAT BUSINESSES ARE BUILT ON A FOUNDATION OF STRICTEST INTEGRITY. LISTEN TO YOUR HEART TO KNOW WHAT'S RIGHT, AND ALWAYS DO THE RIGHT THING.

Everybody has some code of ethics to which they subscribe and what one person of integrity might judge to be "unquestionably ethical", another might find



quite unacceptable. Each annual edition of the Corporate Long Range Plan in recent years has defined "Unquestionable Ethics" by asking managers to pose this question to themselves when in doubt:

*"If my decision on this matter was published in The Globe and Mail, would it embarrass Federal's Directors?"*

This has proven to be a valuable guide to making the right decision in matters of ethics and integrity.

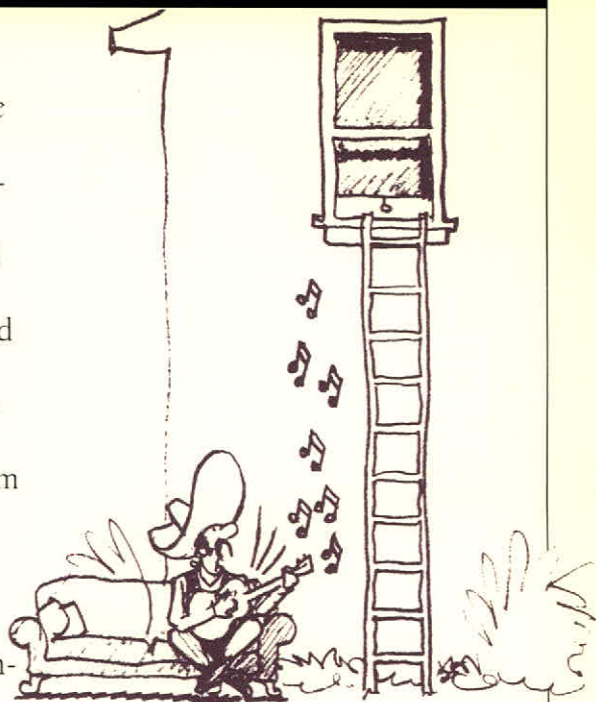
## KEEP IT SIMPLE. SET CLEAR GOALS

A GOAL TELLS YOU WHERE YOU'RE GOING AND IF IT'S CLEAR, IT GIVES YOU A PRETTY GOOD IDEA OF HOW TO GET THERE. DREAMS ARE NICE, BUT GOOD OBJECTIVES ARE ATTAINABLE AND LEND THEMSELVES TO DEFINITE, SOUND, STRATEGIES.

In a strategically oriented company like Federal, the setting of Clear Goals is at the core of good strategy. Some people mistake "clear" goals for "precisely quantified" goals, an error that unduly limits strategic management.

When the mines closed in the Yukon Territory in 1982, a crisis was created for White Pass. After very careful deliber-

ation a Clear Goal was set: Use this crisis to find a long-term solution to the Company's excessive dependence on volatile and limited markets. That's a broad goal, yet it directed management to address every idea and every resource toward resolving the Fundamental problem that had plagued White Pass since its inception. In the storm of controversy that has surrounded the transportation issue in Yukon since 1982, White Pass has been able to be very flexible, yet highly consistent, in exploring possible solutions to this very difficult problem, because Tom King, the CEO of White Pass, knew its goal. The company is now



restructured and can be consistently profitable without volumes traditionally provided by the mining sector.

I'M HOME HONEY.. I  
BROUGHT THE BOSS  
FOR POTLUCK.. HOPE  
YOU DON'T MIND..?



KEEP IT SIMPLE..

## ... NO SURPRISES

A MARK OF GOOD MANAGEMENT IS THE ABILITY AND COURAGE TO SAY WHAT YOU'RE GOING TO DO AND DO IT.. AND IF YOUR PLANS DON'T WORK OUT AS ANTICIPATED, GIVE WARNING AS SOON AS POSSIBLE TO THOSE WHO ARE COUNTING ON YOU.

"Surprises," Jack Fraser says, "are for birthday parties." A good manager knows what he

or she is going to do, and does it. Yet in these turbulent times, it is impossible to anticipate or control all the increasing number of variables. In Federal's planning process, management makes its best guess as to what is coming up, and plans accordingly, leaving room to maneuver in proportion to the degree of volatility faced. Managers are

judged on their performance in delivering as forecast and on their ability to communicate the changes that arise, doing so in a timely manner, so that appropriate adjustments can be made by all parties affected, and surprises can be avoided.

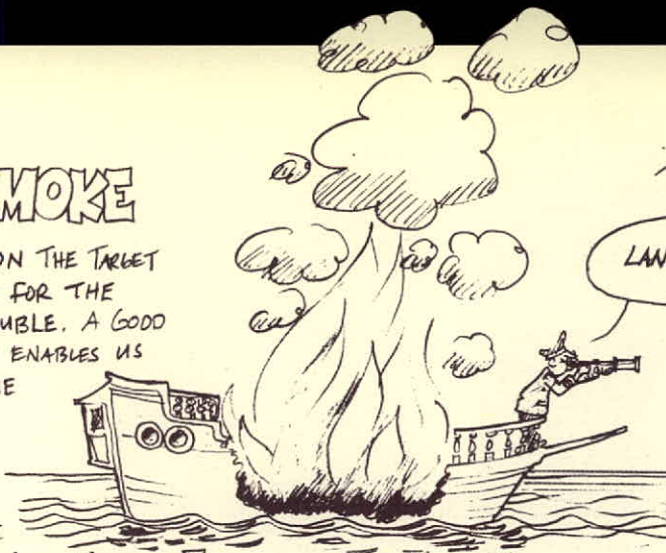
At one time, Federal owned a bulk terminal on the west coast that, for reasons common to the business, delivered one Surprise after another. From the experience gained, Thunder Bay Terminals Limited was designed from scratch to do its job in a steady, predictable and profitable manner, and has done so since the day it opened.

KEEP IT SIMPLE...

## ... SMELL SMOKE

WE KEEP OUR EYES ON THE TARGET AND OUR NOSE ALERT FOR THE FIRST SIGNS OF TROUBLE. A GOOD NOSE FOR PROBLEMS ENABLES US TO FOCUS OUR PRIME ATTENTION ON THE BIG PICTURE.

For a long time it has been clear that we don't Smell Smoke with our noses, but just how one manager reads the early warning signals while another doesn't know what's happening until the operating results come out, is something of a mystery.



Psychologists suggest that we Smell Smoke, in fact, with our right brains. Whether that's right or not, it is clear that some people are more able to develop the knack than others.

Back in 1979, Federal was still struggling with the turnaround, and Standard Aero was our only sure winner. That year, it

delivered record profits, as it did in 1980 and in 1981. But in 1979, Jack Fraser Smelled Smoke, and in 1980, he initiated actions to correct the problems that arose in 1982. Now in 1985, we understand what was going wrong six years ago, but due to Smelling Smoke, the corrective actions are essentially completed, and Ed Kelley, the Aero-space Group CEO, is sniffing the wind for new opportunities.

KEEP IT SIMPLE. SET

## HIGH STANDARDS

WE ARE HIGH BECAUSE WE'VE FOUND THAT PERFORMANCE WELL BEYOND THE ORDINARY IS REALISTICALLY ACHIEVABLE, GIVEN CLEAR STRATEGIC THINKING. REACHING FOR THE TOP DISCIPLINES OUR THINKING AND HELPS US FIND A WAY TO MAKE IT HAPPEN.

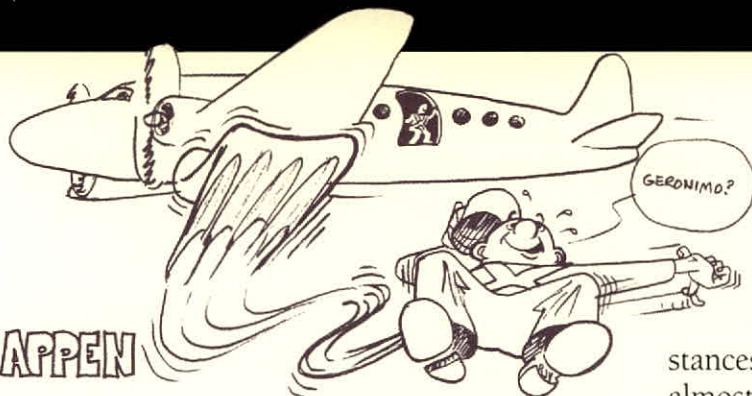
It's easy to dream big dreams and post them as standards of achievement to be aimed for ... but that's not what we mean by High Standards. High Standards are a "way of going", an approach to business that is exemplified by the old phrase "If a thing is worth doing, it's worth doing well".

A young man in our summer program for business students was handed an assignment to find information on a major industry, where to the best of

our knowledge, no such information existed, except in the files of private companies. He tried all the available public sources with negligible success and faced a decision: Should he turn in the usual kind of wordy but meaningless analysis of available data, or go get the information needed? Having High Standards, he went out and knocked on doors and asked for the information he sought. When thrown out, he

went back. With persistence and honesty, he got the information, because his High Standards allowed him to accept no less.





## ...MAKE IT HAPPEN

A MANAGER'S PRIME RESPONSIBILITY IS TO BE EFFECTIVE... DO WHAT NEEDS DOING AND GET ON TO THE NEXT STEP. SOMETIMES MAKING DECISIONS IS A BIT SCARY AND IT'S EASY TO FALL BACK ON FURTHER ANALYSIS. EFFECTIVENESS DEPENDS ON GOOD PLANNING, CLOSE COORDINATION AND TIMELY DECISIONS. WHEN ITS TIME TO JUMP, JUMP.

At the 1984 Federal Management Seminar, we talked about three factors that help give meaning to the Make it Happen Principle:

Make What Happen?

Build on Strengths.

Take Results Oriented Action.

In other words, determine just What it is you're setting out to accomplish; muster whatever Strengths you have that are

applicable; and go to work — to start some productive Action.

In talking about these notions, we agreed that the focus of this Principle should be on the it of "Make it Happen", whereas most people emphasize the Make. Peter Drucker says "Focus on Contribution", and we believe that the most meaningful way to Make it Happen is to carefully determine and agree upon what it is we're going to Make Happen. In each task, what is the one thing that will contribute most to achieving the overall objective? Once that is accomplished, it is often possible to arrange circum-

stances so that "it" happens almost by itself. You can simply LET it happen.

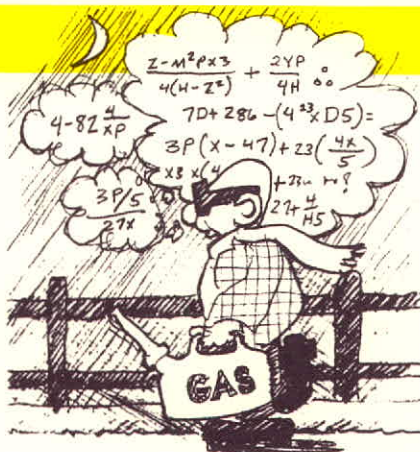
Russelsteel is well known for the effectiveness of its teamwork. They're a large organization, yet everybody seems to know what's going on, and they get things done — a real Make it Happen organization. Wayne Mang, the CEO of the Industrial Distribution Group, credits this ability of his organization to the quality of management they've assembled over many years, the spirit of trust and teamwork they all share, and a well-honed system of incentives. This team enables Wayne and other senior managers to spend their time determining precisely what "it" is, and "letting" it happen.

MAKE IT HAPPEN. GET THE

## RIGHT INFORMATION

WE'RE SURROUNDED BY INFORMATION IN THE FORM OF FACTS, OPINION, GOSSIP, "CONVENTIONAL WISDOM" AND BELIEFS. FROM ALL THIS DATA, ALMOST ANY CONCLUSION CAN BE SUPPORTED. AN OPEN INQUISITIVE MIND HELPS SORT OUT THE RIGHT AND RELEVANT FACTS TO REACH SOUND OPINIONS AND CONCLUSIONS.

At Federal's Corporate Office, our quest for the Right Information is never ending, and we have kept after some of our operating people for information to the point where they submit reams of data, and still



we have great difficulty determining just what is happening that is important. Other managers send in a couple of pages and an occasional phone call that keeps us fully informed. What's the difference?

The difference is in relevance and objectivity. No "standard" set of financial data can anticipate what is vital to an operating business, and the ability to assemble "facts" to support any rational conclusion is well developed in our society. The Right Information may be facts, opinions, or even hunches, and what is "Right" changes from time to time.

John Pelton, our V.P. Finance, has a marvelous skill at putting together "win-win" deals, largely because he digs deep enough to get the Right Information.

MAKE IT HAPPEN...

## RESPECT YOUR HUNCHES

IN THE NORMAL COURSE OF TENDING TO BUSINESS, WE ARE EXPOSED TO VAST QUANTITIES OF DATA. FACED WITH A PROBLEM, WE CONSCIOUSLY ANALYSE THE FACTORS WE PERCEIVE TO BE RELEVANT. SUCH ANALYSIS MAY MISS IMPORTANT ELEMENTS, BUT THE SUBCONSCIOUS MIND CAN SORT THROUGH ITS ENORMOUS STOREHOUSE AND PROVIDE THE INSIGHT WE CALL A "HUNCH". WHEN THAT STILL SMALL VOICE INSIDE YOU WHISPERS, DON'T IGNORE IT.

Shareholders reading this section should be advised that we do *not* make multimillion dollar decisions based on a hunch.

Hunches are not so mysterious these days. It seems that our minds include a vast assembly of odd bits of data that for one reason or another have stayed with us in a big mental drawer called the "subconscious". For reasons not well understood, we

are able to tap this lode of information, but only in a non-directed way that is quite different from the "logical" processes we have come to prize so highly. Because this "intuitive" information is so elusive, many ignore it and others discount its validity. In fact, the "hunches" that spring from this source are

the foundation of most of the world's great ideas, brought to reality by someone who had the willingness to listen and the discipline to pursue the idea to its logical base.

When we buy a company, our decision to *investigate* is often based on a hunch. But detailed analysis of the facts always precedes our decision to buy.



MAKE IT HAPPEN. KEEP

## TRENDING RIGHT

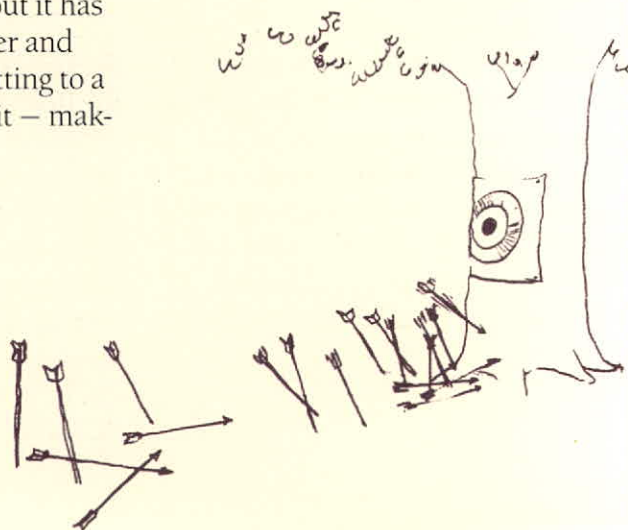
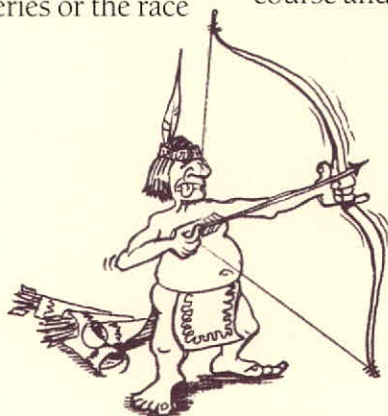
GETTING TO THE GOAL IS TOUGH, AND SETBACKS ARE NOT UNCOMMON, AS LONG AS OUR TREND IS RIGHT, INCREMENTAL IMPROVEMENTS AND CONTINUING COMMITMENT WILL GET US THERE.

A graph of the growth of compound interest shows that the growth starts slowly and picks up momentum dramatically along the way. People who hope to win big at lotteries or the race

track — who lack the patience to plan ahead for the things they deem important — waste this most valuable wealth building tool, expending their efforts looking for a bonanza. They generally fail to reach their destination because they skip some very important first steps.

Most business processes follow a similar pattern, but it has been demonstrated over and over again that committing to a course and sticking to it — mak-

ing incremental progress all along the way — pays bigger returns than seem likely at the time the process is initiated. Our acquisition skills grow each time we make a transaction, providing a basis for projecting incrementally bigger deals as we progress toward our objective.

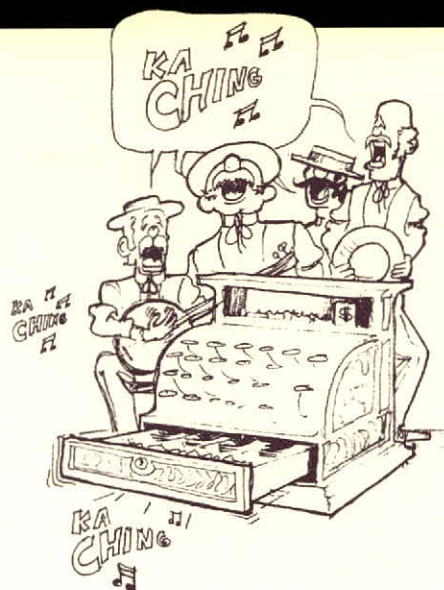


MAKE IT HAPPEN...

## ... MAINTAIN HARMONY

UNANIMITY OF PURPOSE AND PRINCIPLES MAKES FOR SOUND AND EFFECTIVE DECISIONS FLOWING FROM CONSENSUS. THE FEDERAL FORMULA CALLS FOR STRONG PEOPLE WORKING TOGETHER IN AN ATMOSPHERE OF MUTUAL RESPECT AND TRUST. THIS KIND OF CONSENSUS MANAGEMENT MULTIPLIES STRENGTHS AND ADDS TO THE FUN OF BUSINESS.

In the "good old days", the boss said what was to be done, and the employees were happy — happy to have a job. Today, strong and competent people have more choice, and the fact that they show up regularly for



work and have the necessary skills does not mean they will be productive. Harmony can be

created by a good working environment, but it is *Maintained* by conditions in which reality is in accord with expectations.

These Principles may have little meaning to new employees of Federal, or to employees hearing them for the first time. They take on meaning, and help Maintain Harmony, when our people see them in use. Federal's Executive Committee thrashes through tough issues, pulling no punches and driving toward a consensus ... and Maintains Harmony all the way.

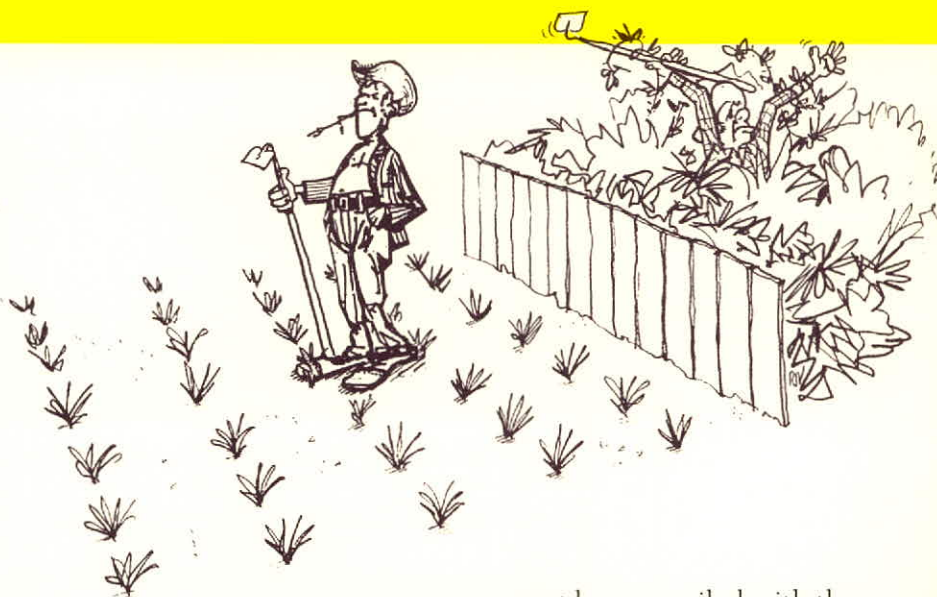
MAKE IT HAPPEN...

## ... NO POLITICS

COMPANY POLITICS, LIKE WEEDS, ARE ALWAYS WITH US. ALLOWED TO FLOURISH, THEY CHOKER GROWTH, DESTROY TRUST, AND VIOLATE ALL THESE PRINCIPLES. WE ERADICATE POLITICS WHENEVER WE FIND THEM, AND ALLOW THE CROPS TO PROSPER, NURTURED BY THESE PRINCIPLES.

Company politics can be defined as an individual putting personal objectives ahead of corporate objectives and doing so in a manner that is harmful to the company's interests. The best treatment for Politics, as in gardening, is to create and maintain an atmosphere where individual and corporate goals are in Harmony — where the "weeds" of Politics cannot prosper.

When a competent manager in a Federal company fails to perform to expectations within



the limits of his or her ability, the first step we take is to review the extent to which personal and corporate objectives are in concert. Many times we have found that objectives have diverged, and a change of responsibility can restore performance. In other cases, changed personal goals

cannot be reconciled with the interests of the company, and the interests of both parties are best served by going separate ways. The ability to make such assessments fairly, honorably, and with good will, is perhaps the greatest test of management judgement.

THESE PRINCIPLES PROVIDE A CORNERSTONE FOR BUILDING OUR COMPANY. UNDERSTANDING, ACCEPTANCE, AND RIGOROUS APPLICATION OF THEM WILL CONTINUE TO SET FEDERAL APART FROM, AND AHEAD OF THE CROWD, PROVIDING A LINKAGE BETWEEN OUR DIVERSIFIED COMPANIES.

BUILDING TRUST IS A BUZZWORD THESE DAYS, AND WE KNOW THAT THESE PRINCIPLES BUILD TRUST IN ADDITION TO THEIR PRIME FUNCTION OF GUIDING US TOWARD GOOD MANAGEMENT DECISIONS.

THESE PRINCIPLES ARE NOT UNIQUE TO FEDERAL. WE DON'T INVENT THEM; WE'RE NOT THE ONLY ONES WHO USE THEM; AND THEY'RE NOT THE ONLY PRINCIPLES WE USE. BUT THEY EXPRESS OUR WAY OF GOING. THEY ARE PRIME TOOLS WE'RE USING TO BUILD A GREAT CANADIAN COMPANY.

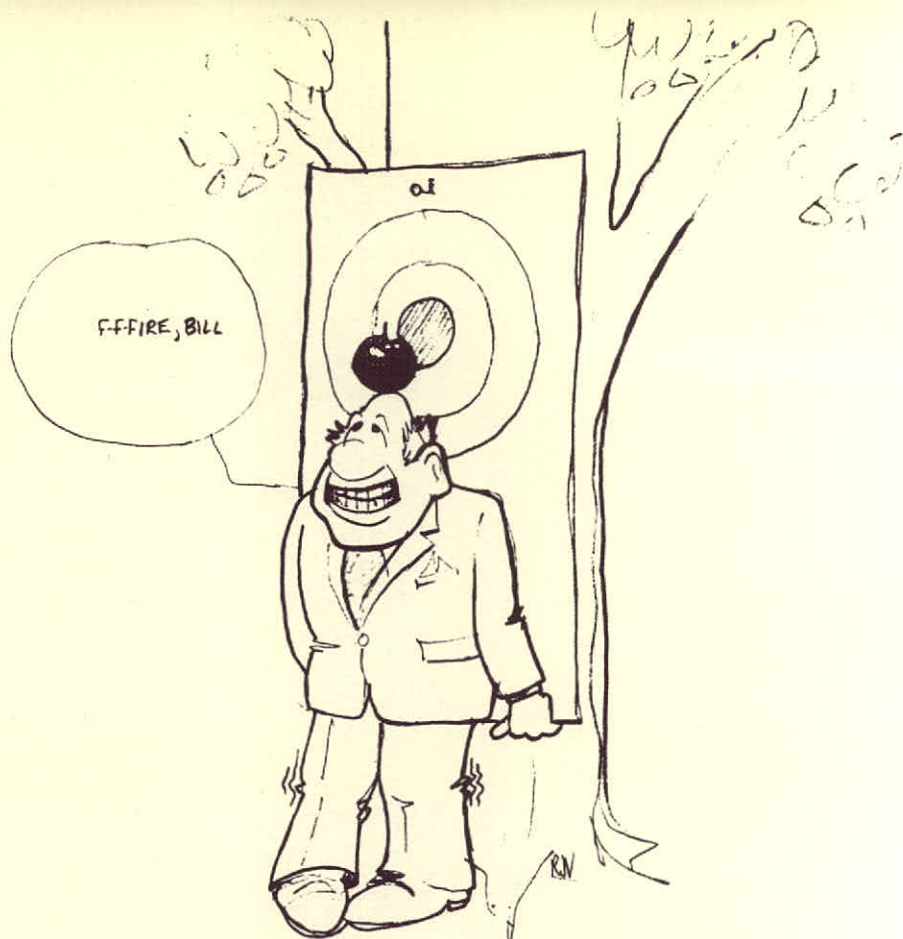
These Principles, as you see them reproduced here, were originally sketched in pencil by R. J. Vahsholtz as rough drafts that would be redrawn, polished and refined before achieving wide distribution. We decided the roughs were OK for inclusion in the 1982 Corporate Long Range Plan. In 1983, we reviewed them and found no changes needed, and in 1984 we reached the same conclusion. Now we've become sort of attached to them, so we present them here as they were orig-

inally written and drawn. The Principle illustrated by this is Keep it Simple.

Since the "official" introduction of the Principles in 1982, there have been three Federal Management Seminars built around the theme of understanding these Principles, and more are planned. Endless hours of discussion and research have gone into understanding and communicating the meaning of the Principles

among Federal's Management teams. They have become prime tools Bill Watchorn uses for "keeping in touch" with our subsidiaries. At all levels, understanding has increased and communications have improved as a result, and no one is showing signs of being bored when the Principles come up for further discussion.

They serve their purpose well.



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2400 - One Lombard Place  
Winnipeg, Manitoba, Canada  
R3B 0X3  
(204) 942-8161

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**Standard Aero Limited**

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Winnipeg, Manitoba  
R2R 0S8  
(204) 775-9711

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**Standard Aero Inc.**

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(612) 835-9250

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(807) 623-6921

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(403) 668-7621

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**White Pass Systems Ltd.**  
16045 114th Avenue  
Edmonton, Alberta T5M 2Z3  
(403) 451-4355

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Toronto, Ontario M6M 2M2  
(416) 245-3333

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P.O. Box 5009, 535 Bowes Road  
Downsview, Ontario M3M 3B5  
(416) 669-6454

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Montreal, Quebec H3C 2V4  
(514) 483-5520

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