DOMINION TEXTILE INC.

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Annual Report

CORPORATE PROFILE

Dominion Textile Inc., which began operations in 1905, is the largest Canadian supplier of textiles and textile-related products. Its international network of offices, plants, subsidiaries and associated companies now extends to almost 125 locations in 50 countries.

The mission of Dominion Textile Inc. is to serve worldwide markets profitably with quality products while seeking opportunities to apply corporate resources to areas other than textiles. The fundamental goal of the Corporation is to attain and maintain leadership positions in selected market segments.

The operations of Dominion Textile Inc. are divided into three major geographical regions: Canada, with sales of $572 million or 62% of total sales; the United States, with sales of $252 million or 27%, and overseas operations with a total of $102 million of sales or 11%. Sales of associated companies, in which the Corporation holds an interest of less than 50%, reached $91 million, but are not consolidated with those of the Corporation. If the $32 million of exports from Canada are included, sales outside this country represent 42% of the total.

In Canada, Dominion Textile Inc. is engaged in the design, production, finishing and marketing of a wide range of:

- woven fabrics for the apparel industry, including sleepwear, blouses, shirting, leisurewear, career apparel, rainwear, outerwear; indigo-dyed denim, drills and twills for the jeans producers;
- consumer products such as sheets, bedspreads, comforters, blankets, draperies, towels;
- knitted sportswear and leisurewear;
- spun yarns for knitters and weavers;
- woven and nonwoven industrial products engineered to meet the requirements of many manufacturing and process industries.

Operations in the United States include the manufacture and sale of denim, polyester/cotton and cotton yarns, geotextile products and plastic accessories for the apparel industry.

On the international scene, outside North America, the Corporation manufactures or distributes interlinings, cut linings, fusible fabrics, indigo-dyed denim for the apparel trade and a diversified line of nonwoven fabrics sold to a wide variety of industries.

Dominion Textile Inc. is comprised of 75 subsidiary and associated companies. The Corporation operates 31 manufacturing facilities: 18 in Canada (10 in Québec, 7 in Ontario, 1 in Nova Scotia), 7 in the United States, 5 in Europe and 1 in Hong Kong.

Total employment at 30 June 1986 was 10 500. There were 7 750 employees in Canada, 2 250 in the United States and 500 in operations elsewhere in the world, mainly in Europe. In Canada, the distribution of employment was: Québec, 5 325; Ontario, 2 000; and Nova Scotia, 425.

At 30 June 1986, the Corporation had 17 000 shareholders and 99.0% of the outstanding Common shares were held by Canadian residents. The major shareholder is the Caisse de dépôt et placement du Québec which owns 13.2% of the Common shares. The balance of the capital stock is widely held by institutional and individual investors.

PRINCIPAL OPERATING COMPANIES

DOMINION TEXTILE INC.

- Dominion Textile – Canada
  - Apparel Fabrics Company
  - Consumer Products Company
  - Dominion Yarn Company
  - Industrial Fabrics Company
  - Dominion Fashion Group
  - Wabasso Canada Inc.
  - Textile Management Services Inc.
- Dominion Textile (USA) Inc.
  - Swift Textiles, Inc.
  - Linn-Corriher Corporation
  - Mirafi Inc.
  - Howard Cotton Company
- Dominion Textile (International) BV
  - DHJ Industries SpA (Italy)
  - DHJ Industries Europe SA (France)
  - DHJ Industries AG (Switzerland)
  - DHJ Industries (Far East) Ltd. (Hong Kong)
  - DHJ Industries Deutschland GmbH (FRG)
  - DHJ Industries (UK) Ltd. (England)
  - SENFA SA (France)
  - DHJ Canada Inc. (Canada)

Associated companies: Argentina, Belgium, Brazil, Canada, Chile, Colombia, Ecuador, France, Hong Kong, Italy, Mexico, Portugal, South Africa, Spain, Switzerland, Tunisia and Venezuela.

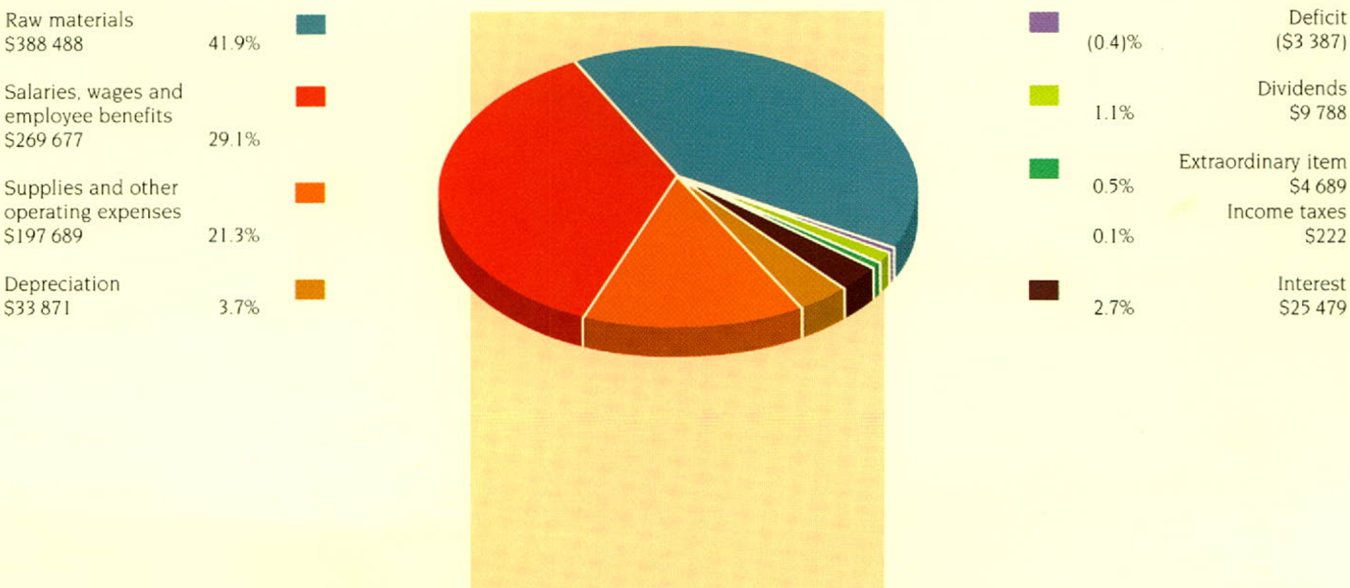
HIGHLIGHTS

for the year ended June 30
(in thousands of dollars)

	1986	1985
Sales	$926 516	$765 870
Net income (loss) before extraordinary item	11 090	(14 375)
Net income (loss) after extraordinary item	6 401	(14 375)
Financial resources generated from operations	$ 45 704	$ 1 582
Additions to fixed assets	39 304	33 374
Working capital	$270 569	$206 643
Total assets	737 720	672 564
Long term debt	145 039	146 969
Shareholders' equity	380 013	305 867
Number of Common shares (in thousands)		
Average outstanding during the year	15 763	14 109
Outstanding at year end	16 593	14 743
In dollars per Common share		
Net income (loss)		
— Before extraordinary item	$ 0.56	$ (1.18)
— After extraordinary item	0.27	(1.18)
Dividends	0.48	0.66
Book value	18.08	18.71

DISTRIBUTION OF 1986 SALES DOLLAR

(in thousands of dollars)



Thomas R. Bell

The mission of Dominion Textile Inc. is to serve worldwide markets profitably with quality textile and textile-related products, while seeking opportunities to apply corporate resources to areas other than textiles.

The Corporation will accomplish its mission through disciplined attention to four main strategies:

- **focus on business segments which enable the Corporation to maintain and enhance its leadership position;**
- **pursue the principle of decentralization by placing decision-making authority at the lowest appropriate levels;**
- **identify acquisition and other opportunities in promising businesses...;**
- **expand programs to link business opportunities around the globe.**

Current year financial results

The past fiscal year was one of recovery from perhaps the most difficult period experienced in the Corporation's history. In total, sales reached a record level of $927 million for the fiscal period ended 30 June 1986. This represents an increase of 21% versus a year ago, of which approximately 7% is accounted for by the addition of Wabasso products which were acquired late in the previous fiscal year. Despite continued highly competitive business conditions, all geographic areas recorded significant sales volume increases. Year-over-year sales increases for Canada were 18%, while in the United States and International operations increases were respectively 31% and 17%.

Profits for the year were $11.1 million before taking into account an extraordinary charge of $4.7 million relating to plant closures and a discontinued business. Earnings per Common share before and after the extraordinary charge were $0.56 and $0.27 respectively as compared to a prior year loss of $1.18 per Common share.

The Corporation entered the past fiscal year with a strike in progress at four of its Canadian manufacturing facilities, Richelieu Fabrics, Salaberry Yarn, Beauharnois Finishing and the Fiberworld plant at Hawkesbury. Settlements at these locations were reached on 30 August 1985. As a result, the first quarter of the fiscal year was unprofitable with the lingering effects depressing subsequent quarters and reducing the profit for the full fiscal year. Despite the strike, it was gratifying to note the steady improvement in profitability with the passing of each quarter.

During the year it was decided to close certain manufacturing facilities in Canada and to cease operating a joint venture in the United States. Consistent with our stated intention to downsize and consolidate some operations, we have closed the consumer products plant at Montmorency, Québec, on 30 April 1986 and the apparel fabrics plant at St-Jean sur Richelieu, Québec, and the sales yarn plant at Valleyfield, Québec, effective 30 June 1986. The modern manufacturing machinery from these facilities is being redeployed to other Canadian plants where it will be used more efficiently, in many cases on a seven-day basis. Additionally, in light of the slow progress being made in penetrating the asphalt binder market, we suspended activity at Pavement Technologies, Inc., Seattle, Washington. The total extraordinary charge net of taxes resulting from these decisions, recorded in the income statement, was $4.7 million or $0.29 per Common share.

The restructuring of the manufacturing facilities of the Corporation improves its productivity through the reduced number of locations and the ability to utilize more effectively its capital assets. The introduction of extra shifts at the remaining plants has offset the jobs lost at those which were closed and the number of people employed in Canada remains at approximately 7 800. In total, worldwide employment levels are unchanged at 10 500 people.

Details of specific activities in each of our Corporation's businesses are recorded in the section entitled "Report on Operations".

Corporate mission

In order to put the above decisions in perspective and before turning to a discussion of future development, we would like to outline briefly the corporate mission statement which has been further refined from last year's initial position.

The mission of Dominion Textile Inc. is to serve worldwide markets profitably with quality textile and textile-related products, while seeking opportunities to apply corporate resources to areas other than textiles. The fundamental goal of the Corporation is to attain and sustain leadership positions in selected market segments.

The short term objectives are to increase the sales volume of the Corporation significantly, targeted to double in size over the next five years, while providing a superior return to our shareholders through appreciation in share values and payment of an appropriate level of dividends.

The Corporation will accomplish its mission through disciplined attention to four main strategies:

— Focus on business segments which enable the Corporation to maintain and enhance its leadership position;

— Pursue the principle of decentralization by placing decision-making authority at the lowest appropriate levels;

— Identify acquisition and other opportunities in promising businesses in order to grow not only in textiles but also to effect diversification into new products and markets;

— Expand programs to link business opportunities around the globe.

We recognize that the achievement of the corporate mission and execution of its strategies are dependent upon the quality and dedication of our employees. This requires an environment in which individuals can develop and use their own talents to fulfill both personal and corporate goals. We will continue to foster employees' involvement and recognize their many significant contributions to the success of the Corporation.

Corporate development

The Corporation's acquisition programs are one of its main expansion thrusts and are focused on textiles and in other businesses in Canada, the United States and international markets. The unsuccessful attempt to acquire Avondale Mills, a US sales yarn and apparel fabrics company, was a move to grow in and secure leadership positions in markets which fulfill our objectives. A number of options remain open to us which present opportunities for growth and we are optimistic about developments on this front.

Our commitment to an acquisition-based strategy is demonstrated by the recently negotiated line of credit of $120 million US and by the $65 million issue, in June, of Convertible Preferred stock which strengthens our balance sheet. The size and ready acceptance of the preferred stock issue indicate that there is support in the investment community for this program.

We continue our evaluation of joint ventures and other forms of business cooperation where both the Corporation and others can contribute to successful business enterprises. A tangible example is our recent equity participation with the International Finance Corporation, a World Bank subsidiary, the Tunisian government and other development banks in Sitex, a company which manufactures denim in Tunisia for the European market. Other examples include a real estate company and a major European marketing arrangement with DuPont for nonwoven products, such as "Tyvek", as well as other opportunities still in the formative stage.

Consistent with the goal of achieving leadership positions within targeted business areas, the Corporation has entered into a number of licensing agreements. Among these are the arrangements for bedroom and bathroom fashion products between our Consumer Products Company and Cannon Mills, a unit of Fieldcrest Cannon, Inc. of Eden, N.C., and Alfred Sung of Toronto, Ontario. In addition, a variety of licenses for active sports and leisurewear have been acquired by the Dominion Fashion Group.

The corporate mission and strategies also establish the basic direction for capital spending programs for our existing businesses. During the past fiscal year, expenditures totalled $39.3 million and were focused on projects such as the addition of a finishing plant to the Boland denim manufacturing complex in Columbus, Georgia, the completion of the modernization of the sales yarn facility at Long Sault, Ontario, and on numerous projects to achieve cost reduction, quality improvement and improved customer service in Canada, the United States and overseas facilities.

Directors and officers
It is with regret that this year the Corporation will lose the services of Mr. Roderick O.A. Hunter, as a director, since he has now reached the mandatory retirement age. Mr. Hunter has earned the respect and admiration of all those who have worked with him over the past 12 years. We extend to him our best wishes and gratitude for the wise counsel and support he has provided to the Corporation.

It is with great pleasure that we advise that Mr. Ron Eden of Toronto, President and Chief Executive Officer of Guthrie Canadian Investments Limited, has agreed to stand for election as a member of the Board.

During the year, Mr. John A. Boland, Senior Vice-President, US Operations, reached retirement age. Mr. Boland served with the Corporation since the acquisition of DHJ Industries, Inc. in 1975 not only as a senior officer but also with direct responsibility for the United States denim fabric and sales yarn operations. We extend to him our best wishes and sincere thanks for his significant contribution to the success of the Corporation.

Outlook
We have entered a new business environment as compared to the past decade which was characterized by high inflation and commodity prices, extremely volatile foreign exchange rates and economic growth patterns. The outlook is for a period of low inflation or perhaps even one of disinflation, slow but steady GNP growth, weak commodity prices and intensified international competition. These factors will no doubt be associated with a new set of economic circumstances. However, it is expected that the overall climate in combination with the steps we are taking will be one in which improved corporate performance can be achieved.

Of particular interest to the Corporation is the recent rapid decline in the price of raw cotton. Over the past several years, worldwide cotton supplies have exceeded consumption largely as a result of the People's Republic of China becoming a net exporter of cotton in contrast to their previous position as a net importer. As a consequence, effective 1st August 1986, the US cotton price support system has been modified to permit US cotton growers to compete in world markets. These lower raw cotton prices should permit us to improve our global competitive position.

The present economic order has also had a significant impact on our other major cost factor, labour. Wage and salary adjustments of the past fiscal year have reduced the impact of previous agreements in Canada which significantly eroded our ability to compete. In addition, we have negotiated improved operating flexibility to permit better utilization of capital resources. Our Canadian companies will be subject to a wage re-opener clause in the fall of 1986 and spring of 1987 for the final year of a three-year contract expiring in fiscal 1988. The overall outlook is for improved employer/employee relations and cooperation to meet the intense global competition.

On 1st August 1986, the Multi-Fibre Arrangement (MFA) of the GATT, involving more than 50 countries and first negotiated in 1974, was formally renewed with a protocol extending it for five years. This arrangement provides the mechanism for developing countries and particularly the least developed nations to improve their economies through expanded exports of apparel and textile products while allowing the developed countries some control over the rate and distribution of import penetration into their domestic markets. It is important that a balance be struck between these two objectives so that a climate exists in which domestic industries can maintain employment and plan and invest for the future with greater confidence.

On 30 July 1986, the Canadian government announced its new Textile and Clothing Import Policy. The policy reflects the government's concern for the effect on Canadian employment of low cost clothing imports which have grown at a rate of 11% per year since 1981 in a market that has had an annual growth rate of only 2.3%. The MFA provides Canada with the ability to negotiate bilateral agreements with developing countries that should realize its goal of bringing the rise of textile imports more in line with the growth of the economy as a whole. This can be accomplished with a definitive commitment and consistent administration by our government officials. The adoption of such a stance is essential if we are to avoid further damage to the Canadian employment picture.

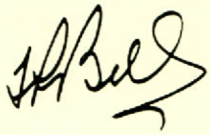
We do not expect the current free trade negotiations between Canada and the US to have a significant impact on our business in the near term.

The Corporation believes that Canada's future economic growth cannot be achieved by a continuation of the status quo. We believe that the process of negotiations aimed at a freer trade agreement between the two countries could have long term beneficial effects for both parties. Dominion Textile also recognizes that any such agreement will not be without its cost and dislocations to many constituents, including this Corporation. As participant in the Sectoral Advisory Group on International Trade (SAGIT) related to textiles, footwear and leather, we will be able to make recommendations to our government on transition requirements to minimize these costs, both human and economic.

In the meantime, we intend to adapt our operations to improve our competitiveness and to be in a position to exploit whatever form of free trade results from this initiative.

Just as the past fiscal year represents a marked improvement from the previous year, we look to the coming year as one of opportunity and one in which further progress in sales growth and satisfactory shareholder returns can be realized. We will continue to focus on strengthening our leadership positions and resolving remaining problem areas. In summary, results should be significantly improved from the past fiscal year.

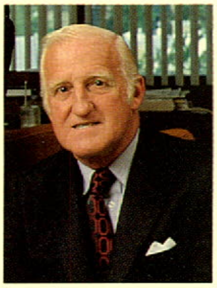
On behalf of the Board of Directors,



Chairman, President and
Chief Executive Officer

Montréal, 12 August 1986

A TRIBUTE TO RONALD H. PEROWNE



In his 17 years at the helm of Dominion Textile, Ronald H. Perowne not only participated in the exceptional challenges of the textile industry in Canada, but shaped and embodied them as well.

From 1969 when he became president to his retirement as chairman of the board last fall, sales of the Corporation quadrupled, growing from nearly $200 million to some $800 million. In the midst of that period the Corporation acquired DHJ Industries, Inc. of New York, dramatically extending its market reach to become a truly international company and one of the major textile firms in North America.

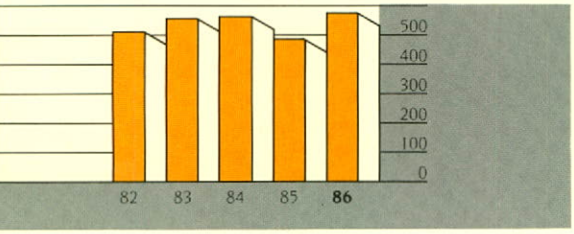
While these facts provide a picture of the external strength of the Corporation, Mr. Perowne's most lasting contribution lies in the inner strength and confidence he has helped instill in the organization. A hard driving, highly competitive leader with a strong sense of fair play, he makes things happen. He creates an atmosphere which encourages others to live up to their potential, making both the Corporation and the individual stronger for it.

Mr. Perowne has done much to heighten the profile of the industry in Canada, dispelling some of the myths and candidly voicing his opinions on major issues.

The overall result of this leadership is an organization with a devoted and responsive management team, challenged by the ever-increasing competition of this volatile industry.

Mr. Perowne continues to take an active interest in the corporation as a director and chairman of the executive committee as well as director of several subsidiaries.

For spring 1987, both plain shade and print fabrics sold to garment manufacturers will feature earth tones recently popularized by the Oscar winning film "Out of Africa".



Sales – Canadian operations
(in millions of dollars)

Career apparel, work clothing and uniforms, is a significant product group of the Apparel Fabrics Company.

CANADIAN OPERATIONS

Sales by the Canadian operations of $572.3 million were 18% higher than in the previous year and take into account the contribution of Wabasso Canada Inc. acquired toward the end of fiscal 1985. Income from operations improved to $6.2 million compared with a loss of $13.5 million last year with increased earnings in all segments.

Capital expenditures of $22 million to rationalize and modernize manufacturing facilities will place Canadian operations in a more competitive position, better able to satisfy customer needs.

At year end, the open order position was 38% ahead of last year, reflecting a more favourable business environment.

Apparel Fabrics Company

In fiscal 1986, sales were 13.5% higher than in the previous year. Denim, career apparel fabrics and home furnishing fabrics, all showed improvement while other apparel fabrics were affected by the unabated rise of garment and fabric imports.

Results suffered from a strike in two plants which began during the previous fiscal year and which was settled at the end of August 1985. The strike prevented the company from fully developing its spring collection for 1986, thereby provoking some negative effects for the following six months. In order to keep customers supplied with fabrics during the strike, sourcing of denim from the Corporation's overseas and US operations was arranged and commission finishing was contracted from other Canadian and US companies, with the resulting extra costs being borne by the company.

Because of the continuing erosion of the market by high levels of clothing imports which, in unit terms, have grown at a compounded annual rate of 11% since 1981, a decision was taken to close an apparel fabrics plant in Canada. The plant at St-Jean, Québec, was selected and accordingly it did not return to full production following the strike. Costs associated with the closure and the transfer of some equipment from St-Jean to other plants affected profits during the year.

A large proportion of the remaining equipment at St-Jean will now be transferred to other apparel fabrics plants. The net result of this redeployment of assets will be fewer but better equipped plants, most functioning with weekend shifts. Moreover, greater use will be made of the most modern equipment permitting a better return on investment and improved product quality.

During the last fiscal year, the Consumer Products Company introduced a new collection of percale sheets designed by Alfred Sung. This new product contributed to the success of the fall line.

Dominion Textile distributes a complete collection of fashion coordinates for the bathroom, including towels, bath mats and other accessories.

The year finished with improving momentum and stronger business conditions. All weaving plants except St-Jean were running at full capacity, inventories were under good control and the open order position was 36% better than at the close of the previous year. Consequently, a better performance is expected from the Apparel Fabrics Company in 1987. A major influence on the longer term will be the determination with which the government applies its recently announced textile policy through renegotiated international bilateral trade agreements.

Consumer Products Company

Sales were 9.4% lower than in the previous year and although results were better they remained unprofitable.

Markets were mixed during the year and were soft during the last half. The situation was aggravated by a flood of imports which reached disruptive levels. The government intervened to impose quotas on previously unrestrained imports of towels from Brazil. Additional government action is being sought to establish restraints on imports of sheets from certain low wage countries which presently have free access to the Canadian market, although their exports to the US and the European Community are under restraints.

The closure of the weaving plant at Montmorency, Québec, which began in fiscal 1985 was completed in 1986. The consolidation of sheeting production at Sherbrooke, Québec, together with the added requirements for "Wabasso" brand sheets resulted in increased output from Sherbrooke, greater use of equipment and the start up of a weekend shift.

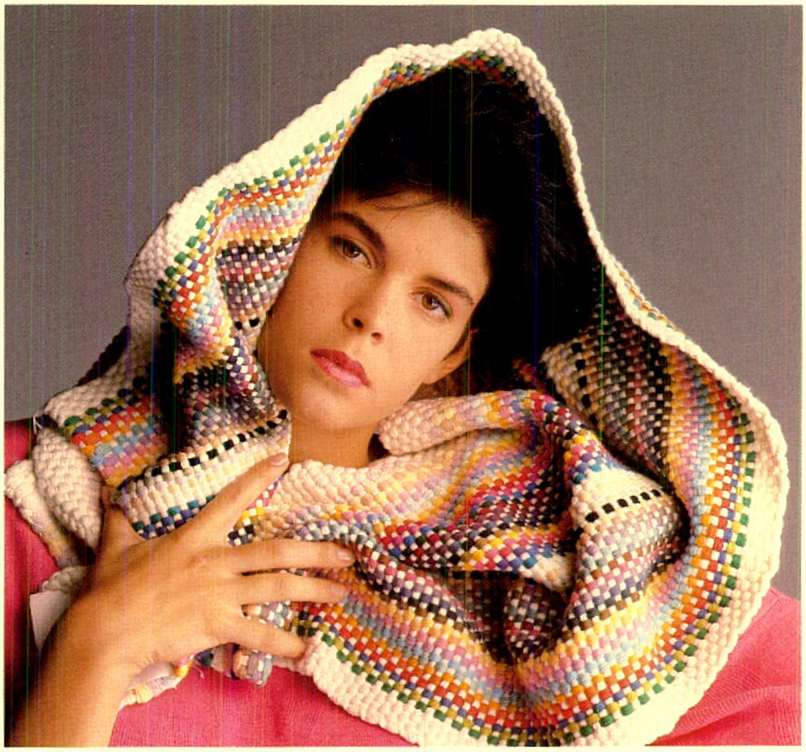
Additional shuttleless looms for sheeting installed at Magog, Québec, and terry looms for towels installed at Iroquois, Ontario, at the beginning of the year were also operating with weekend production in the second half of the year, thereby optimizing the use of this new equipment.

Transitional and training costs associated with these innovations affected earnings adversely in 1986 but the changes effected have strengthened the competitiveness of the operations for the future.

Concentrating its efforts on the higher value added and more fashionable market segments, the Consumer Products Company has developed and introduced a number of new products. Percale sheets have been introduced under the "Texmade" label and a license agreement has been signed with the Canadian designer Alfred Sung for high styled bedroom and bathroom products. A license agreement was also entered into for the well known American brand name "Cannon" covering both bathroom and bedroom products

Wabasso Canada Inc. manufactures and markets fully coordinated soft home fashions under the "Wabasso", "Dorma", "Mary Quant" and "Harmonie" brand names.

Industrial fabrics are engineered to meet the requirements of many manufacturing and process industries. This buffing wheel is used mainly for polishing metals.



The Dominion Yarn Company offers a new colour coordination service, "Colorplay", providing fashion and colour direction to customers.

for the Canadian market. The "Caldwell" product line is expanding into coordinated bathroom fashions and accessories to increase its share of this profitable business segment.

The company has excellent brand name franchises and market position and continues to improve manufacturing performance and marketing effectiveness. Therefore, while business conditions will continue to be difficult, the Company fully expects to be profitable in fiscal 1987.

Wabasso Canada Inc.

Wabasso Canada Inc. was moderately profitable during its first full year of operations.

The company continued its drive towards upgraded home fashions, with growth in percale and coordinated bedding products and a significantly improved towel line.

Capital spending during the year included the installation of on-line computer systems designed to improve customer service and increase inventory turnover.

During the period, the home fashions market in Canada has continued the price promotional trends established in previous years. That factor, together with imports from newly developing countries which have reached record levels, has made markets extremely competitive. However, the offsetting effects of new product and market diversification should allow the company to maintain profitably its overall position in the coming year.

Dominion Yarn Company

Both sales volume and profit margins of the Dominion Yarn Company increased considerably compared with last year, reflecting the strong market demand for knitting yarns. This improvement was also due to substantial investment in new open-end spinning technology and better customer service supported by the consolidation of warehousing, distribution and administrative offices in one location closer to major customers.

The results were achieved despite the serious growth of imports of yarns from low wage countries which precipitated the closure of the Salaberry, Québec, yarn plant at the end of the fiscal year. Earnings were affected by losses attributable to the strike at that plant which continued through the first two months of the fiscal year and the costs of phasing out its operations.

The expansion of the Long Sault, Ontario, yarn plant was completed ahead of schedule. Its high quality, competitive cost products contributed importantly to the improved profits. The installation of a new mop yarn facility

"Penmans" sportswear is a basic business segment of the Dominion Fashion Group.

Industrial fabrics are used in the manufacture of conveyor belts such as those found in the mining industry and in quarries.

at the Domil yarn plant using open-end technology was also completed during the year.

The full benefit of these installations will be realized in the coming fiscal year and that, together with the favourable business conditions which are expected to persist through the year, should make possible continued improvement in performance.

Industrial Fabrics Company
The Industrial Fabrics Company recorded another excellent year of operations in fiscal 1986. Sales were 7.7% better than last year, reflecting strong activity in the automotive industry coupled with increased export business.

Quality and customer service were the major focus of attention during the year and results have been very encouraging. Control of fixed expenses and general cost reduction measures have also shown positive results.

The fourth quarter was particularly strong and all manufacturing facilities were running at full capacity at the beginning of the new year. Open orders are 26% ahead of last year. Overall customer demand is strong in spite of a slight softening in the automotive industry and a high level of activity in industrial businesses is expected through the coming year.

The Fiberworld Division also recorded higher sales despite a strike at the Hawkesbury, Ontario, plant which continued two months into the fiscal year. The improvement in sales was spurred mainly by a strong demand for carpet backing. The outlook for this business for 1987 is positive.

Dominion Fashion Group
The Dominion Fashion Group, formerly Penmans Company, achieved much better performance in fiscal 1986. Sales increased by 13% in a stronger market for knitwear. Although a small net loss was incurred, better control and performance in every aspect of the operations produced a steady improvement throughout the year and profitable results in the last quarter.

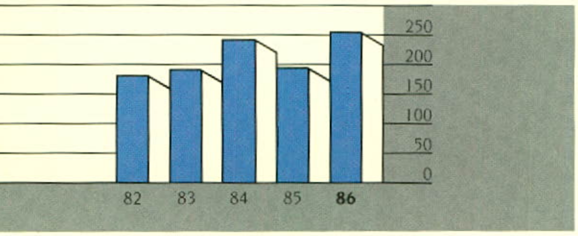
The change of name to Dominion Fashion Group reflects a new market-driven organization focused on business unit profitability and with a broader range of products.

Exclusive licenses for the manufacture and sale of world class products have been entered into for "Yves Saint Laurent" and the "Beach Boys" active and leisurewear and for "Everlast", "Louisville Slugger" and "Weider" sports clothing.

Open orders to year end were 72% ahead of last year. Inventories are low and the market outlook is strong. With new product introductions ready, fiscal 1987 promises to be a good year for the Dominion Fashion Group.

One of the geotextile fabric applications is for erosion control of river banks.

Through its Canadian operations, Swift Textiles, Inc. and its European affiliates, Dominion Textile Inc. is among the top denim producers in the world.



Sales – United States operations
(in millions of dollars)

UNITED STATES OPERATIONS

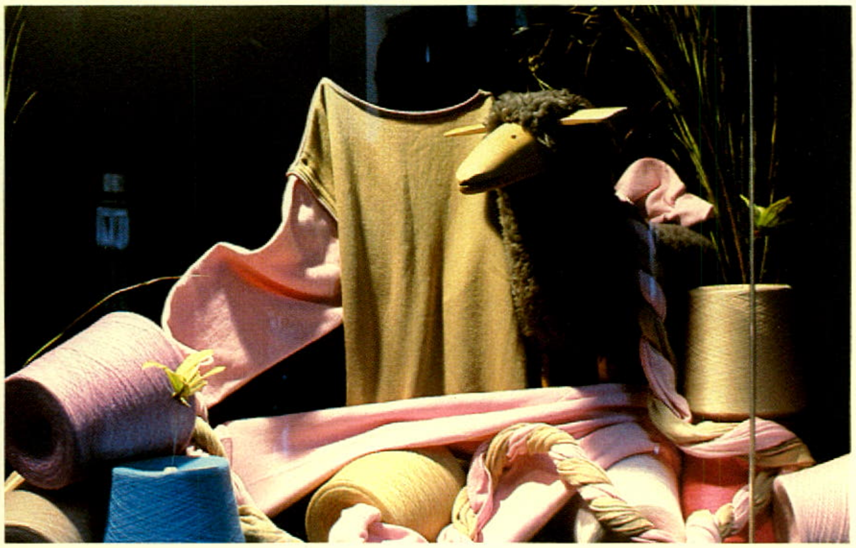
In the United States, sales of $251.9 million were 31% higher than in the prior year, resulting in an operating income of $20.1 million compared to an operating loss of $4.3 million in the previous year. All business units had much higher sales and each contributed to the overall positive results. In general, the performance reflected a better business climate, despite soaring imports of textile products and a continued widening of the textile trade deficit in the United States.

Swift Textiles, Inc.
Swift Textiles, Inc. experienced an outstanding turnaround. Manufacturing facilities ran at 100% of capacity during fiscal 1986. Prices recovered as the jeans industry turned from fashion to basic jeans. The implementation of "Swift Response", a just-in-time inventory and customer service concept, strengthened Swift's position with the major branded jeans producers. Industry inventories remained well in balance with demand, while Swift's inventories reached all-time lows.

During the year, new weaving machines were added and the denim finishing plant was completed for a total capital spending of $11.3 million for the year.

Jeans sales are still strong and full operating schedules are expected for fiscal year 1987 which should be another excellent year for Swift.

Linn-Corriher Corporation
In the United States, markets for sales yarn were depressed when the year began and Linn-Corriher's performance



These elegant knitted garments are made of 100% cotton and polyester/cotton yarns distributed by Linn-Corriher Corporation.

during the first half was marred by curtailed production schedules. Through the balance of the fiscal year there was a steady strengthening of demand and in the final quarter market conditions were strong.

In these circumstances Linn-Corriher Corporation recorded a 39% sales volume increase over the previous year and improved its operating cost performance. Although a net loss was sustained in the year, the third and fourth quarters were profitable.

The installation of knotless high speed winding equipment to improve quality and efficiency at the Corriher plant was the only major capital expenditure during the year. Additional major investments are scheduled for the modernization of the production processes in the coming year to enhance Linn-Corriher's market position through improved product quality, lower costs and broader product lines.

While apparel and yarn imports continue to be a major concern, the company approaches the new year with cautious optimism. Market conditions are vastly improved compared with the same period last year and the entire organization has been strengthened. Open orders are approximately 80% greater than the prior year and market predictions for knit fabrics are favourable.

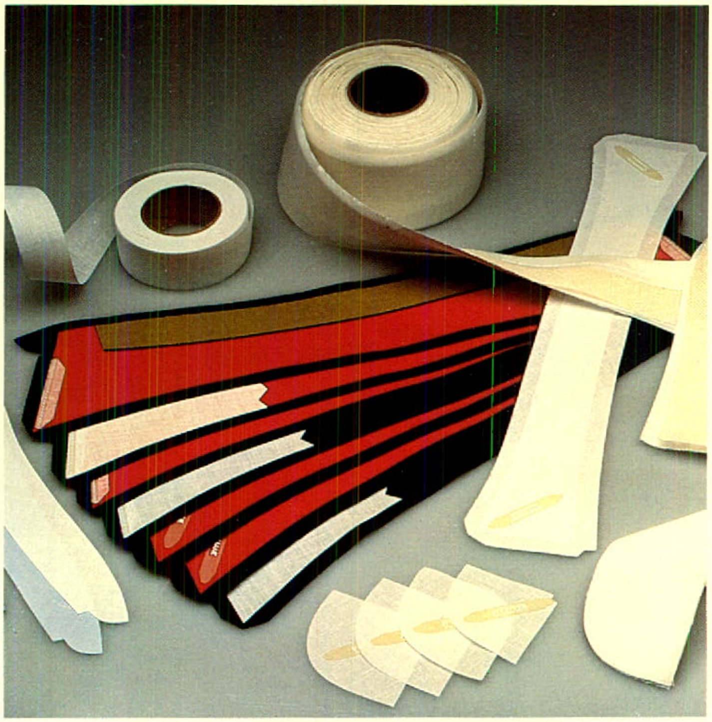
Mirafi Inc.

Sales of Mirafi Inc. increased by 12% over the previous year as a result of the continued strength of the US economy and increased activity in most sectors of the construction industry. Increased sales of specialty products along with stringent inventory control and overhead cost reduction programs resulted in much improved profits over fiscal 1985.

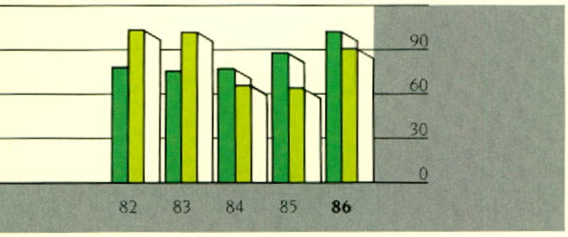
Mirafi's strategic thrust for the coming year is to continue to expand its specialty product business and, at the same time, restructure the marketing and distribution organization to compete more effectively in the standard nonwoven and woven tape fabric markets.

The outlook for the US economy and construction industry for the coming year appears favourable and management is looking forward to increased sales and profits in the new year.

This greenhouse uses thermal screens made of aluminized "Tyvek". "Tyvek" is a nonwoven fabric produced by DuPont and distributed by DHJ Industries in Europe.



DHJ Industries Europe is active in the manufacture of garment interlinings, waist bands, shoulder pads, bias bindings and shoe linings.



Sales – International operations
(in millions of dollars)

Subsidiary companies
Associated companies

INTERNATIONAL OPERATIONS

International operations had a record year in fiscal 1986. Sales amounted to $102.3 million, significantly up from prior year levels and earnings advanced 59%. Additionally, sales of associated companies which are not consolidated totalled $91.0 million as compared to $64.4 million in the previous year.

International operations comprise a wide geographical and product base which inevitably results in some variations in financial performance. However, this is also the strength of these operations; adverse changes in individual market conditions create opportunities in other areas. This is exemplified by the shift of labour intensive industry to low cost countries creating opportunities for International operations to provide technology and to benefit from changes in worldwide sourcing patterns.

Demand for premium quality interlinings remained strong throughout the period. DHJ continued to maintain its pre-eminent position as "the" supplier to the traditional shirt interlining sector.

Another application of "Tyvek" nonwovens is industrial protective garments.

Through its International operations, Dominion Textile is one of two exclusive distributors of DuPont's "Tyvek" fiber to the European markets. The "Tyvek" nonwoven is slit into ribbons and, as in this example, is hand-knitted.

In addition, a complete customer service is provided to the industry, including computerized pattern grading, cutlinings and technical support. As part of this program, International operations are increasingly moving into related sectors and to date are active in the manufacture of garment interlinings, waist bands, shoulder pads, shoe interlinings, thermal drapes and packaging. Considerable emphasis is placed on diversification into related areas which provide high added value to products and increased revenue.

Engineered nonwoven structure (ENS) products continued to advance, particularly the "Tyvek" fabric made by DuPont and for which the international group is one of two exclusive distributors in Europe. During the year, a major sales and marketing reorganization was undertaken to exploit market growth.

Demand for denim sourced from the Tunisian plant remained buoyant reflecting, among other factors, the significant improvements in quality and service achieved over the last few years. At year end, Swift Textiles International Limited committed further capital as an equity investment in these operations which will be utilized in a major modernization program to provide additional capacity.

Business conditions in fiscal 1987 continue to be favourable and results similar to those achieved in 1986 are expected. Emphasis will continue to be on exploiting geographical and technological strengths together with widening the product base into related sectors.

Sales

Consolidated sales during the year increased by 21% from $765.9 million to $926.5 million. This was attributable to the US operations increase in sales by 31%, the Canadian operations by 18% and the International operations by 17%. The composition of the sales by geographic region did change with a shift towards sales in the United States.

Sales of associated companies, in which the Corporation holds an interest of less than 50%, have increased to $91 million from $64 million in the previous year. Also, after including $32 million of exports from Canada, sales outside this country represent 42% of the total.

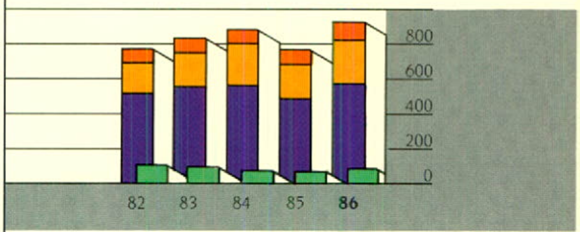
Net income

(before extraordinary item)

Net income improved steadily from the second quarter results up to and including the fourth quarter. For the twelve-month period, net income before extraordinary item was $11.1 million as compared to a net loss of $14.4 million in the previous year. Earnings per Common share before extraordinary item for the year were $0.56, a substantial improvement over a loss of $1.18 per Common share experienced last year. Results include the cost of the takeover attempt for Avondale Mills and the foreign exchange gain realized as a result of a reorganization in the International and US financial structure.

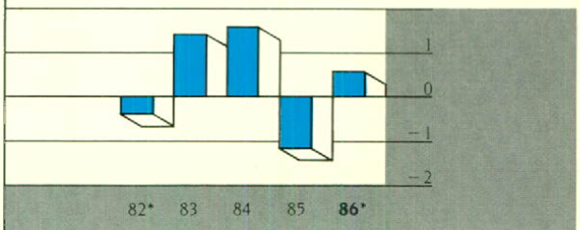
Extraordinary item

During the process of rationalizing certain operations, the apparel fabrics plant at St-Jean, Québec, the consumer products plant at Montmorency, Québec, and the sales yarn plant at Valleyfield, Québec, were closed. Also, the operation of Pavement Technologies Inc. in the United States was discontinued in light of the slow progress being made in penetrating the asphalt binder market. These decisions resulted in an extraordinary charge net of taxes of $4.7 million or $0.29 per Common share.



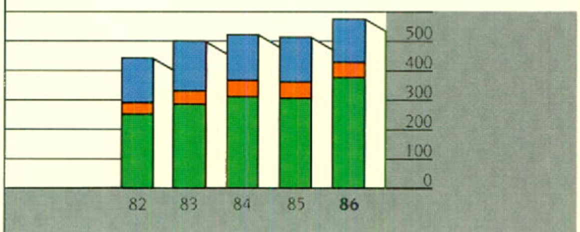
Sales by major operating groups
(in millions of dollars)

- International operations
- United States operations
- Canadian operations
- Associated companies



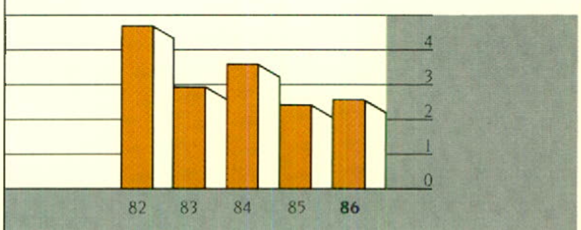
Net income per Common share
(in dollars)

*Before extraordinary item



Capital structure
(in millions of dollars)

- Long term debt
- Minority shareholders' interest and deferred taxes
- Shareholders' equity



Capital spending per share
(in dollars)

Capital structure
Shareholders' equity is $380.0 million compared with $305.9 a year earlier. Long term debt decreased by $1.9 million, resulting in a total year end debt of $145 million. The total debt to equity ratio was improved to 34:66 versus 39:61 last year.

Capital expenditures
Capital spending in the year totalled $46.4 million. After deducting grants principally from the Canadian Industrial Renewal Board and investment tax credits, the net outlay incurred by the Corporation was $39.3 million.

In total, $21.8 million were invested in Canada, $15.1 million in the United States and the balance in International operations.

Working capital
Working capital increased to $270.6 million at year end compared with $206.6 million a year earlier. The ratio of current assets to current liabilities improved to 2.7 from 2.3 at the end of 1985.

The principal components of working capital were affected by the higher level of sales bringing about accounts receivable increase of $31.3 million. Inventories increased by $22.4 million which was primarily due to the addition of Wabasso Canada Inc. and the fact that the Apparel Fabrics Company and Dominion Yarn Company were on strike at the beginning of the year and had reduced their inventories at that time.

Cash and term deposits increased by $8.7 million to $21.9 million. Also, the level of short term borrowings was reduced by approximately $3.6 million.

Financing activity
In December 1985, Dominion Textile (International) BV concluded the negotiations of a five-year term note for $15 million US. To date, only $10 million US ($14 million CAN) of this facility has been issued and was used to restructure its debt. The balance of the drawdown is planned for future international acquisition.

Quarterly results

Fiscal year ended June 30, 1986	First quarter	Second quarter	Third quarter	Fourth quarter	Year
Sales (in millions)	$180.5	$248.0	$237.1	$260.9	$926.5
Net income (loss) (in millions)*	(6.9)	4.1	5.0	8.9	11.1
Earnings per Common share*	(0.50)	0.24	0.29	0.53	0.56
Dividends per Common share	0.12	0.12	0.12	0.12	0.48
Fiscal year ended June 30, 1985					
Sales (in millions)	$169.7	$196.3	$187.7	$212.2	$765.9
Net income (loss) (in millions)	(2.2)	0.1	(4.7)	(7.6)	(14.4)
Earnings per Common share	(0.21)	(0.03)	(0.37)	(0.57)	(1.18)
Dividends per Common share	0.18	0.18	0.18	0.12	0.66

*Before extraordinary item

Share prices and trading volumes

Fiscal year ended June 30, 1986	First quarter	Second quarter	Third quarter	Fourth quarter	Total
High	$12.50	$15.63	$19.50	$23.63	
Low	$10.63	$10.50	$14.25	$18.25	
Volume	562 300	1 921 100	3 024 100	3 031 400	8 538 900
Fiscal year ended June 30, 1985					
High	$16.13	$15.88	$13.25	$12.25	
Low	$14.75	$12.25	$10.75	$10.00	
Volume	372 300	984 100	1 359 700	1 020 300	3 736 400

In June 1986, Dominion Textile (USA) Inc. confirmed the short term $120 million US facility to be used for acquisition purposes in the United States.

Late in the fiscal year, the Corporation undertook a major equity financing. By way of a private placement, 2 million Second Preferred shares, Series D, and 600 000 Second Preferred shares, Series E, were issued at a price of $25 per share. The $65 million gross proceeds were used to purchase for cancellation the Second Preferred shares, Series A, and the remainder was included in corporate funds.

The Dividend Reinvestment and Share Purchase Plan remains a popular financing vehicle with the Common shareholders, raising over $25 million of new equity during the year.

The Employee Share Purchase Plan raised $374 000 during the year.

DIRECTORS

**Jean Béliveau, Montréal
Senior Vice-President, Corporate Affairs
Club de Hockey Canadien, Inc.

*Thomas R. Bell, Montréal
Chairman, President and Chief Executive Officer
Dominion Textile Inc.

Purdy Crawford, Q.C., Montréal
President and Chief Executive Officer
Imasco Limited

J.V. Raymond Cyr, Montréal
Chairman, President and Chief Executive Officer
Bell Canada

*Alex D. Hamilton, Montréal
Company Director

**Roderick O.A. Hunter, Winnipeg
Company Director

**Gordon H. Lennard, Calgary
President
G.H. Lennard Corporation Ltd.

Alex R. McAslan, Montréal
Executive Vice-President, Operations
Dominion Textile Inc.

Charles A. McCrae, Montréal
Executive Vice-President, Administration and Resources
Dominion Textile Inc.

*Cal. N. Moisan, Montréal
President and Chief Executive Officer
SPB Canada Inc.

*Ronald H. Perowne, Montréal
Company Director

*David F. Sobey, Stellarton, Nova Scotia
Chairman and Chief Executive Officer
Sobeys Stores Limited

*Member of the Executive Committee
**Member of the Audit Committee

OFFICERS

CORPORATE

Thomas R. Bell
Chairman, President and Chief Executive Officer

Charles A. McCrae
Executive Vice-President, Administration and Resources

Alex R. McAslan
Executive Vice-President, Operations

William N. Gagnon
President, International operations

Milo A. Smith
Vice-President, Finance

Sandy Mackay-Smith
Vice-President, Secretary and General Counsel

André Côté
Vice-President, Corporate and External Affairs

Guy R. Lacroix
Vice-President, Human Resources, and Assistant to the Executive Vice-President, Operations

Claude Perron
Vice-President, Corporate Planning and Development

Pierre L. Roy
Treasurer

Robert B. Anderson
Assistant Comptroller

Marie Baillargeon
Assistant General Counsel and Assistant Secretary

OPERATIONS

Canada

Paul-É. Boudreault
President, Apparel and Industrial Fabrics Company

Dennis Godfrey
President, Dominion Yarn Company

Peter McConnell
President, Wabasso Canada Inc.

Erwin M. Mertens
President, Consumer Products Company

Gary Wilson
President, Dominion Fashion Group

Arthur P. Earle
Senior Vice-President, Development and Research

United States

H. Alton Conner
President, Linn-Corriher Corporation

C. Robert Koon
President, Swift Textiles, Inc.

E. John Macfarlane
President, Mirafi Inc.

Herman F. Riddle
President, Howard Cotton Company

International

William N. Gagnon
President, International operations

CONSOLIDATED STATEMENT OF INCOME

for the year ended June 30

	1986	1985
	(in thousands of dollars)	
Sales	**$926 516**	$765 870
Operating costs	**893 059**	776 767
Income (loss) from operations	**33 457**	(10 897)
Interest expense	**25 479**	22 898
Income (loss) from operations after interest — Note 1	**7 978**	(33 795)
Share in net income of associated companies	**2 549**	1 538
Other income — Note 2	**3 652**	1 729
Income (loss) before income taxes	**14 179**	(30 528)
Income taxes (credits) — Note 3	**222**	(15 947)
	13 957	(14 581)
Minority interest	**(2 867)**	206
Net income (loss) before extraordinary item	**11 090**	(14 375)
Extraordinary item — Note 4	**(4 689)**	—
Net income (loss) for the year	**$ 6 401**	$ (14 375)
Per Common share, after preferred dividends		
Before extraordinary item	**$ 0.56**	$ (1.18)
After extraordinary item	**$ 0.27**	$ (1.18)

CONSOLIDATED STATEMENT OF RETAINED EARNINGS

for the year ended June 30

	1986	1985
	(in thousands of dollars)	
Balance at beginning of year	**$123 090**	$149 123
Net income (loss) for the year	**6 401**	(14 375)
	129 491	134 748
Dividends —		
Cumulative First Preferred	**5**	5
Second Preferred — Series A	**1 190**	1 200
Second Preferred — Series C	**1 007**	1 091
Common		
$0.48 per share in 1986 and $0.66 in 1985	**7 586**	9 362
	9 788	11 658
Expenses on Preferred shares issued (net of income taxes)	**715**	—
Balance at end of year	**$118 988**	$123 090

CONSOLIDATED BALANCE SHEET

as at June 30

ASSETS	1986	1985
	(in thousands of dollars)	
Current assets		
Cash and term deposits	**$ 21 903**	$ 13 176
Accounts receivable	**159 031**	127 762
Inventories — Note 5	**242 844**	220 465
Prepaid expenses	**6 933**	5 305
	430 711	366 708
Investments and advances — Note 6	**12 434**	7 743
Land, buildings and equipment — Note 7	**292 575**	295 395
Other assets	**2 000**	2 718
	$737 720	$672 564

LIABILITIES AND SHAREHOLDERS' EQUITY	1986	1985
Current liabilities		
Short term borrowings — Note 8	**$ 33 298**	$ 36 938
Accounts payable and accrued liabilities	**102 591**	101 983
Dividends payable	**2 253**	2 321
Income taxes payable	**5 134**	3 869
Long term debt due within one year — Note 9	**16 866**	14 954
	160 142	160 065
Long term debt — Note 9	**145 039**	146 969
Deferred income taxes	**25 502**	34 920
Minority interest in subsidiaries	**27 024**	24 743
Shareholders' equity		
Capital stock — Note 11		
Preferred	**80 072**	30 079
Common	**175 609**	149 772
	255 681	179 851
Retained earnings	**118 988**	123 090
Cumulative translation adjustment — Note 12	**5 344**	2 926
	380 013	305 867
	$737 720	$672 564

On behalf of the Board:

Director

Director

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION

for the year ended June 30

	1986	1985
	(in thousands of dollars)	
Financial resources generated		
Net income (loss) before extraordinary item	**$ 11 090**	$ (14 375)
Depreciation	**33 871**	31 019
Deferred income taxes	**(3 855)**	(14 642)
Share in net income of associated companies	**(2 549)**	(1 538)
Dividends received from associated companies	**1 446**	1 736
Minority interest	**2 867**	(206)
Other non-cash items	**2 834**	(412)
Total generated from operations	**45 704**	1 582
Proceeds from disposal of fixed assets	**5 090**	2 687
New financing		
Common shares	**25 837**	18 405
Second Convertible Preferred shares, Series D and E (net of $1 175 related issuance expenses)	**63 825**	—
Preferred shares issued by a subsidiary to minority shareholders	**—**	12 000
Foreign currency translation adjustment — Note 12	**1 621**	1 106
Total financial resources generated	**$142 077**	$ 35 780
Financial resources applied		
Increase (decrease) in elements of working capital, other than cash items	**$ 54 719**	$ (9 092)
Increase (decrease) in investments and advances — Note 6	**2 331**	(112)
Additions to fixed assets	**39 304**	33 374
Fixed assets acquired by a subsidiary	**—**	17 500
Extraordinary item — Note 4	**5 561**	—
Reduction of long term debt, net	**2 403**	6 775
Purchase of Second Preferred shares, Series A	**15 000**	—
Dividends declared	**9 788**	11 658
Other items — net	**604**	1 470
Total financial resources applied	**$129 710**	$ 61 573
Increase (decrease) in net cash position	**$ 12 367**	$ (25 793)
Cash and term deposits	**$ 8 727**	$ (31 873)
Short term borrowings	**3 640**	6 080
Increase (decrease) in net cash position	**$ 12 367**	$ (25 793)
Increase (decrease) in elements of working capital, other than cash items		
Increase (decrease) in current assets		
Accounts receivable	**$ 31 269**	$ (15 029)
Inventories	**22 379**	11 781
Prepaid expenses	**1 628**	819
(Increase) decrease in current liabilities		
Accounts payable and accrued liabilities	**(608)**	(5 927)
Dividends payable	**68**	77
Income taxes payable	**(1 265)**	861
Long term debt due within one year	**(1 912)**	(714)
	51 559	(8 132)
Incomes taxes payable transferred to deferred income taxes	**3 160**	(960)
	$ 54 719	$ (9 092)

MANAGEMENT REPORT

The accompanying consolidated financial statements of Dominion Textile Inc. and its subsidiary companies and all information in the annual report are the responsibility of management and have been approved by the Board of Directors.

The consolidated financial statements contained herein have been prepared by management in accordance with generally accepted accounting principles in Canada appropriate in the circumstances and conform in all material respects with international accounting standards. These statements necessarily include some amounts that are based on the best estimates and judgement of management and in their opinion present fairly the Corporation's financial position and results of its operations. The consolidated financial statements have been examined by Touche Ross & Co., Chartered Accountants, and their report is included herein. Financial information used elsewhere in the annual report is consistent with that in the financial statements.

The reliability of the financial information is determined from the Corporation's accounting records and related systems of internal controls. The systems of internal controls include formal policies and procedures which are designed to provide reasonable assurance that assets are safeguarded and that reliable financial records are maintained. The Corporation has an Internal Audit department whose function includes the review of the accounting records and related systems of internal controls to ensure that they are adequate and functioning as intended.

The Board of Directors annually appoints an Audit Committee, comprised of three directors. None of the three directors on the Audit Committee is a member of management. The Committee meets with management, the internal auditors and the independent auditors to review any significant accounting and auditing matters and to discuss the results of audit examinations. The Audit Committee also reviews the financial statements, the auditors' report and all other information in the annual report and recommends their approval to the Board of Directors.

Chairman, President and
Chief Executive Officer

C.A. McCrae

Executive Vice-President,
Administration and Resources

AUDITORS' REPORT

The Shareholders,
Dominion Textile Inc.

We have examined the consolidated balance sheet of Dominion Textile Inc. as at June 30, 1986 and the consolidated statements of income, retained earnings and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the Corporation as at June 30, 1986 and the results of its operations and the changes in 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

Chartered Accountants

Montréal (Québec)
August 11, 1986

June 30, 1986

The Corporation's financial statements are prepared in accordance with accounting principles generally accepted in Canada and conform in all material respects with international accounting standards. The most significant policies are as follows:

Principles of consolidation
The consolidated financial statements include the accounts of Dominion Textile Inc. and all its subsidiary companies, with provision for the interest of minority shareholders. All material intercompany items are eliminated.

The acquisitions of all subsidiary companies are accounted for on a purchase basis. The assets and liabilities (adjusted to appropriate carrying values) of the companies acquired have been consolidated with those of the Corporation. The adjustment to carrying values is amortized over the economic life of the applicable assets.

Translation of foreign currencies
Assets and liabilities of Dominion Textile Inc. denominated in foreign currencies are translated at the exchange rates in effect at the balance sheet date. Gains and losses on translation are reflected in net income of the period, except for unrealized foreign currency gains and losses on long term monetary assets and liabilities which are reported as a deferred charge and amortized over the remaining lives of related items on a straight-line basis.

The assets and liabilities denominated in a foreign currency for self-sustaining foreign operations are translated at exchange rates in effect at the balance sheet date. The resulting gains and losses are accumulated in a separate component of shareholders' equity. Revenue and expense items are translated at average exchange rates prevailing during the period.

For self-sustaining operations in hyperinflationary countries, monetary assets and liabilities are translated at the rates in effect at the balance sheet date, whereas non-monetary assets and liabilities are translated at rates prevailing at the respective transaction dates. Revenues and expenses are translated at average rates prevailing during the period except for cost of inventory used, depreciation and amortization which are translated at historical exchange rates. Translation gains and losses are reflected in net income of the period.

Inventory valuation
Materials and supplies in inventories are valued at the lower of average cost and net realizable value. The cost of work in process and finished goods inventories includes raw materials, direct labour and certain manufacturing overhead expenses. Adequate provision is made for slow moving and obsolete inventories.

Investment in associated companies
The investment in companies which are not majority owned is carried at the Corporation's equity therein. For those companies operating in countries where exchange control regulations or other circumstances create uncertainty as to the repatriation of earnings, the investment is carried at cost less write-downs for permanent impairment.

Fixed assets and depreciation
Fixed assets are stated at historical cost. Depreciation is provided on a straight-line basis at varying rates which amortize the cost of the assets over their economic life. For the most part buildings are amortized over 25 years and machinery and equipment over 10 to 15 years.

Pension plans
The Corporation and its subsidiaries have a number of pension plans, both of a contributory and non-contributory nature. All pension plans are trusteed and are being funded. The unfunded past service pension liability is estimated to be $3 490 000 as at June 30, 1986 ($5 031 000 at June 30, 1985) and is being amortized over a period not longer than determined by actuarial estimates and government regulations.

Pension payments made to retired employees not covered by these plans are charged to operations when paid.

Net income (loss) per Common share
Net income (loss) per Common share is calculated using the weighted average number of Common shares outstanding during the fiscal year, after deducting dividends on Preferred shares. The average number of Common shares outstanding for 1986 and 1985 was 15 762 630 and 14 108 986 respectively.

June 30, 1986

Note 1 — Income (loss) from operations after interest	**1986**	1985
	(in thousands of dollars)	
Income (loss) from operations after interest includes provision for the following:		
Depreciation	**$ 33 871**	$ 31 019
Remuneration of directors and officers	**3 514**	2 566
Interest on long term debt	**18 289**	19 099
Interest on other borrowings	**7 190**	3 799

Note 2 — Other income		
Royalties and commissions	**$ 461**	$ 967
Income from investments	**761**	398
Gain on disposal of fixed assets	**340**	131
Realized foreign exchange gains — Note 2 (a)	**3 482**	—
Costs of attempted acquisition	**(1 978)**	—
Other items, net	**586**	233
	$ 3 652	$ 1 729

(a) Foreign exchange gains realized as a result of a reorganization of the Corporation's International and US financial structure.

Note 3 — Income taxes (credits)		
The Corporation's income tax provision in the consolidated statement of income differs from the Canadian corporate tax rate for the following reasons:		
Incomes taxes (credits) based on combined basic Canadian federal and provincial rate of 46%	**$ 6 522**	$ (14 043)
Increase (decrease) in taxes resulting from		
Manufacturing and processing profit deductions	**459**	1 603
Inventory allowance	**(1 363)**	(1 824)
Investment tax credits	**(1 533)**	(1 253)
Share in net income of associated companies	**(1 173)**	(707)
Foreign tax differential	**(2 741)**	319
Other	**51**	(42)
Actual income taxes (credits)	**$ 222**	$ (15 947)
Income taxes (credits)		
Current	**$ 4 077**	$ (1 305)
Deferred	**(3 855)**	(14 642)
Total income taxes (credits)	**$ 222**	$ (15 947)

Note 4 — Extraordinary item

	1986	1985
	(in thousands of dollars)	

In conjunction with the Corporation's intention to discontinue a number of lines of business and to redeploy the Corporation's resources to a narrower range of products, the decision has been taken to close certain manufacturing facilities in Canada and to cease operating a joint venture in the United States.

Accordingly, an extraordinary charge of $4 689 000 has been made against earnings for the year, which consists of

	1986	1985
Write-down of fixed assets	$ 1 928	—
Provision for anticipated cash costs	5 561	—
	7 489	—
Less: Reduction in income taxes — deferred	2 800	—
	$ 4 689	—

Note 5 — Inventories

The major inventory classifications are as follows:

	1986	1985
Raw materials	$ 48 030	$ 48 153
Work in process, including grey fabric for further processing	78 373	81 752
Finished goods	102 081	77 201
Supplies	14 360	13 359
	$242 844	$220 465

Note 6 — Investments and advances

	1986	1985
Investment in associated companies	$ 8 141	$ 5 781
Other investments and advances — at cost	4 293	1 962
	$ 12 434	$ 7 743

Note 7 — Land, buildings and equipment

	1986	1985
Land and buildings	$149 799	$152 565
Machinery and equipment	394 565	433 392
Total at cost	544 364	585 957
Less: Accumulated depreciation	266 750	290 912
	277 614	295 045
Assets held for disposal at estimated realizable values	14 961	350
	$292 575	$295 395

Note 8 — Short term borrowings

Short term borrowings of $22 288 000 by subsidiary companies are secured by assignment of accounts receivable and inventories. In addition $9 000 000 of long term borrowings by a subsidiary company are also secured by assignment of accounts receivable and inventories.

Note 9 — Long term debt	1986	1985
	(in thousands of dollars)	
Parent Corporation		
Secured		
Sinking fund debentures — Notes 9(a) and 11(e)		
Series A maturing March 31, 1988 at 5⅝% interest	**$ 13 196**	$ 13 196
Series B maturing April 15, 1990 at 6¾% interest	**5 483**	5 483
Series D maturing July 15, 1989 at 10½% interest	**2 978**	2 978
Series E maturing December 15, 1995 at 14% interest	**25 200**	27 600
Series F maturing January 15, 1993 at 14% interest	**32 800**	36 400
Capitalized lease obligations		
Due 1987 to 1989 at an average of 11% interest	**972**	1 289
Unsecured		
Term note		
Due 1987 — Note 9(b), (payable in US dollars)	**3 329**	7 062
Subsidiaries (payable in Canadian dollars)		
Secured		
Term note		
Due 1987 — Note 9(c)	**9 000**	9 283
Subsidiaries (payable in US dollars)		
Secured		
Industrial Development Revenue Bonds		
Due 1996 at 13.7% interest — Note 9(d)	**23 503**	23 446
Due 1987 to 1996 at 8% to 8.9% interest	**1 382**	1 379
Due 1990 at 7.45% interest	**2 074**	2 069
Other loans and mortgages	**2 289**	2 541
Unsecured		
Term notes		
Due 1987 to 1991 at the London inter-bank offered rate plus ⅝ of 1% interest	**13 825**	—
Due 1987 to 1990 at the London inter-bank offered rate plus ¾% to 1% interest	**15 484**	18 205
Due 1987 to 1993 at 10% interest	**2 277**	2 594
Due 1987 to 1993 at 10¼% interest	**1 044**	1 193
Capitalized lease obligations		
Due 1987 to 2003 at an average of 12% interest	**4 166**	4 461
Other liabilities	**2 903**	2 744
Total long term debt — Note 9(e)	**161 905**	161 923
Deduct: Amounts due within one year	**16 866**	14 954
Total (CAN $82 273 000; US $45 400 000)	**$145 039**	$146 969

(a) Sinking fund debentures are secured by a floating charge on all the assets (except real and immovable properties) of the Corporation. The Corporation has purchased $2 484 000 Series A, $1 392 000 Series B and $2 722 000 Series D in anticipation of sinking fund requirements.

Note 9 — Long term debt (continued)

(b) The interest rate fluctuates at the Corporation's option with changes in the lender's New York prime rate plus ½% to ¾% or the London inter-bank offered rate plus ¾% to 1%.

(c) The interest rate fluctuates at the Corporation's option with changes in the banker's acceptance rate plus ½ of 1%, the London inter-bank rate plus ½ of 1% or the lender's fixed interest rate.

(d) The provisions of the agreements for these obligations require, among other things, that certain subsidiaries (i) maintain working capital and net worth above specified minimum levels, (ii) maintain the ratio of debt to net worth within prescribed limits and (iii) limit the payment of dividends. The bonds are secured by a charge on the fixed assets of a subsidiary and are callable at the option of the Corporation beginning in 1987.

(e) After allowing for pre-payments, the aggregate annual payments required on long term debt for years ending June 30 are:

	(in thousands of dollars)
1987	$ 16 866
1988	36 693
1989	18 153
1990	26 565
1991	13 716
1992 — 2003	49 912
	$161 905

Note 10 — Leases

As at June 30, 1986 the future annual minimum payments for building and equipment leases that have initial non-cancellable terms in excess of one year are as follows:

	(in thousands of dollars)
1987	$ 5 479
1988	4 357
1989	3 564
1990	3 196
1991	2 864
1992 — 1999	8 338
	$ 27 798

Note 11 — Capital stock	1986	1985
	(in thousands of dollars)	
Cumulative First Preferred — Note 11(a)		
Authorized — 4 306 shares		
Outstanding — 712 shares (1985 — 791 shares)	**$ 72**	$ 79
Second Preferred — Notes 11(b) and 11(c)		
Authorized — unlimited shares		
Outstanding — 3 200 000 shares		
Series A — 600 000 shares	—	15 000
Series C — 600 000 shares	**15 000**	15 000
Series D — 2 000 000 shares	**50 000**	—
Series E — 600 000 shares	**15 000**	—
Common — Note 11(d)		
Authorized — unlimited shares		
Issued — 16 593 395 shares (1985 — 14 742 527 shares)	**175 609**	149 772
	$255 681	$179 851

(a) Cumulative First Preferred shares are entitled to a fixed yearly dividend of $7 per share.

(b) During June 1986 the Corporation purchased for cancellation the entire 600 000 Second Preferred shares — Series A for a consideration of $14 730 000.

(c) Second Preferred shares — Series C are entitled to a cumulative floating rate dividend equal to one-half of a Canadian Bank's prime rate plus 1.30% calculated and adjusted quarterly.

Second Preferred shares — Series D and Series E are entitled annually to a cumulative dividend of $1.8125 per share, payable quarterly.

The Second Preferred shares — Series D and Series E are convertible into Common shares of the Corporation at any time until June 30, 1996 at a price of $23.57 on the basis of 1.06 Common shares for each Second Preferred share. The Corporation has reserved 2 756 000 shares for this purpose.

The Second Preferred shares are redeemable, in whole or in part, at the option of the Corporation after June 30, 1985 for Series C, and after June 30, 1989 for Series D and Series E at prices declining from $26 each to $25 each on and after June 30, 1990 for Series C and June 30, 1991 for Series D and Series E. The Corporation may only redeem Series D and Series E shares between July 1, 1989 and June 30, 1991 provided that the current market price of the Common shares is equal to or greater than 125% of the current conversion price.

The Corporation has agreed to offer to purchase 120 000 Second Preferred shares, Series C per annum commencing July 1, 1998, and four percent (4%) of the issued and outstanding Second Preferred shares, Series D per annum commencing July 1, 1996.

(d) The following is a summary of the Common shares issued during the two years ended June 30, 1986:

	NUMBER OF SHARES		VALUE	
	1986	1985	**1986**	1985
			(in thousands of dollars)	
Balance at beginning of year	**14 742 527**	13 325 909	**$149 772**	$131 367
Dividend reinvestment and share purchase plan	**1 821 182**	1 384 535	**25 463**	18 026
Employee share purchase plan	**29 686**	32 083	**374**	379
Balance at end of year	**16 593 395**	14 742 527	**$175 609**	$149 772

(e) The deeds of trust and mortgage relating to the Sinking fund and Collateral debentures contain certain restrictions, customarily found in deeds of this type, pertaining to the amount of long term debt which may be issued, the declaration or payment of dividends and the reduction of capital. At June 30, 1986 the amount of shareholders' equity not restricted under the terms of the deeds was $101 228 000.

Note 12 — Cumulative translation adjustment

	1986	1985
	(in thousands of dollars)	
The components of the accumulated foreign currency translation adjustment, as reported on the consolidated balance sheet, are as follows:		
Balance at beginning of year	**$ 2 926**	$ 474
Unrealized gains (losses) on non-current items		
Land, buildings and equipment	**1 544**	5 481
Long term debt	**(568)**	(3 295)
Minority interest in subsidiaries	**(194)**	(703)
Other items, net	**15**	(137)
	797	1 346
Unrealized gains on current items	**1 621**	1 106
	2 418	2 452
Balance at end of year	**$ 5 344**	$ 2 926

Note 13 — Commitments and contingencies

At June 30, 1986, the Corporation has outstanding fixed asset appropriations of $22 082 000.

Notes receivable discounted by foreign subsidiaries amount to approximately $7 508 000.

Note 14 — Segmented information

The Directors have determined that the Corporation operates within the textile industry in various geographic areas which, for the 12 months ended June 30, can be segmented as follows:

(in millions of dollars)

	Canada		United States		Europe and other		Eliminations		Consolidated totals	
	1986	1985	**1986**	1985	**1986**	1985	**1986**	1985	**1986**	1985
Sales to outsiders	**$572.3**	$486.2	**$251.9**	$191.9	**$102.3**	$ 87.8	**$ —**	$ —	**$926.5**	$765.9
Transfer among geographic locations	**—**	—	**81.1**	81.3	**—**	—	**(81.1)**	(81.3)	**—**	—
	$572.3	$486.2	**$333.0**	$273.2	**$102.3**	$ 87.8	**$ (81.1)**	$ (81.3)	**$926.5**	$765.9
Income (loss) from operations	**$ 6.2**	$ (13.5)	**$ 20.1**	$ (4.3)	**$ 7.2**	$ 6.9			**$ 33.5**	$ (10.9)
Identifiable assets	**$476.9**	$442.4	**$187.9**	$176.0	**$ 64.8**	$ 48.4			**$729.6**	$666.8
Investment in associated companies									**8.1**	5.8
Total assets									**$737.7**	$672.6

Note 15 — Comparative figures

Certain of the 1985 figures have been reclassified to conform with the presentation adopted in 1986.

TEN-YEAR REVIEW

	1986	1985	1984	1983*	1982	1981	1980	1979	1978	1977	1976
Summary of operations											
(in millions of dollars)											
Sales	**$926.5**	$765.9	$877.8	$822.4	$767.3	$864.8	$756.9	$667.4	$560.0	$498.9	$475.4
Income (loss) from operations	**33.5**	(10.9)	65.5	56.9	31.8	100.5	86.2	60.5	44.0	37.2	34.1
Income (loss) before income taxes	**14.2**	(30.5)	43.8	31.9	(3.9)	74.8	66.2	44.1	31.9	25.5	22.3
Income taxes	**0.2**	(15.9)	18.5	11.8	(2.8)	28.6	26.9	18.4	12.5	10.4	8.8
Other items, net	**(2.9)**	0.2	(2.1)	(1.0)	(1.8)	(3.3)	(4.4)	(.3)	(1.2)	(.6)	(3.9)
Net income (loss)**	**6.4**	(14.4)	23.1	19.1	(14.4)	42.9	34.9	25.4	18.2	13.3	9.6
Interest — Long term debt	**18.3**	19.1	20.4	20.5	22.6	18.4	10.1	9.3	7.8	6.2	6.0
— Other	**7.2**	3.8	3.1	5.9	14.8	8.6	11.6	9.2	6.0	7.8	7.8
Financial resources generated from operations	**45.7**	1.6	64.0	48.4	20.7	68.2	59.8	42.9	39.2	30.1	26.3
Additions to fixed assets	**39.3**	33.4	46.9	34.8	51.5	63.9	33.4	22.2	19.2	22.1	18.7
Depreciation	**33.9**	31.0	24.8	22.1	18.9	15.6	14.3	12.6	13.9	13.9	14.2
Balance sheet highlights											
(in millions of dollars)											
Working capital	**270.6**	206.6	240.6	245.0	199.8	251.8	190.6	170.8	134.5	116.8	106.1
Land, buildings and equipment — at cost	**544.4**	586.0	534.1	484.2	454.1	449.2	390.2	344.6	326.9	313.4	304.7
Total assets	**737.7**	672.6	685.6	661.4	613.5	655.6	541.7	442.9	386.6	362.3	349.5
Long term debt	**145.0**	147.0	151.2	166.0	147.7	159.8	119.0	92.9	108.1	110.1	104.4
Shareholders' equity	**380.0**	305.9	311.0	290.7	257.6	278.8	223.4	195.0	139.5	124.2	115.5
Data per Common share* **											
(in dollars)											
Net income (loss)**	**0.27**	(1.18)	1.59	1.41	(1.43)	3.93	3.66	3.02	2.31	1.71	1.23
Financial resources generated	**2.76**	(.05)	4.69	3.90	1.77	6.40	6.46	5.11	4.98	3.85	3.37
Dividends	**.48**	.66	.72	.72	1.02	1.06	.94	.73	.64	.60	.60
Book value	**18.08**	18.71	21.08	20.04	20.39	23.14	21.50	19.19	17.37	15.85	14.75
Market value — High	**23.63**	16.13	20.50	19.63	19.00	22.25	16.50	15.13	12.25	9.50	10.00
— Low	**10.50**	10.00	14.25	8.75	8.75	13.50	12.00	10.25	7.88	6.88	7.50
Statistical data											
Working capital ratio	**2.7**	2.3	2.5	2.5	2.2	2.4	2.1	2.3	2.1	2.0	1.9
Net income (loss) as a percentage of sales	**0.7**	(1.9)	2.6	2.3	(1.9)	5.0	4.6	3.8	3.3	2.7	2.0
Net income (loss) as a percentage of average Common shareholders' equity	**1.5**	(6.0)	7.7	6.8	(6.6)	18.2	18.1	16.7	13.8	11.2	8.5
Number of shareholders	**17 000**	10 900	6 700	6 300	6 800	6 700	5 300	5 300	5 700	5 700	6 000
Average number of Common shares outstanding (in thousands)	**15 763**	14 109	13 161	11 788	10 965	10 251	8 864	8 383	7 855	7 811	7 809
Number of employees at year end	**10 500**	10 500	11 500	12 300	12 100	13 700	13 900	13 200	12 600	12 000	13 100

* In 1983 the Corporation changed its method of accounting for foreign currency translation; prior years' results were not restated.

** After extraordinary charges of $4.7 million in 1986, $11.5 million in 1982, and $1.2 million in 1977 or $0.29, $1.05 and $0.16 per Common share respectively.

*** Data per Common share for net income (loss) and financial resources generated are after Preferred dividends.

SHAREHOLDER INVESTMENT PLAN

Shareholders wishing to acquire additional Common shares of Dominion Textile Inc. can take advantage of the Shareholder Dividend Reinvestment and Share Purchase Plan. This plan provides a convenient method for shareholders, other than US residents, to reinvest their Common share cash dividends in new Common shares of Dominion Textile Inc. at 95% of the average market price. Participants in this plan may also invest monthly optional cash payments, to a maximum of $4 000 per quarter, in new Common shares of Dominion Textile Inc. at 100% of the average market price.

Shareholders participating in the Dividend Reinvestment and Share Purchase Plan pay no brokerage commissions or service charges on the acquisition of these shares and all administrative costs of this plan are borne by Dominion Textile Inc.

Additional information can be obtained from

Dominion Textile Inc.
Dividend Reinvestment and Share Purchase Plan
c/o The Royal Trust Company
Corporate Trust Division
630 Dorchester Blvd. West
Montréal (Québec)
H3B 1S6

The average market prices (AMP) of the Dominion Textile Common shares issued as a result of the participation under the Dividend Reinvestment and Share Purchase Plan are as follows:

July 22, 1985	$11.738
August 21, 1985	$11.619
September 23, 1985	$11.144
October 21, 1985	$10.925
November 21, 1985	$13.556
December 23, 1985	$14.188
January 21, 1986	$14.900
February 21, 1986	$15.506
March 21, 1986	$18.694
April 21, 1986	$19.775
May 21, 1986	$21.850
June 23, 1986	$21.881

Stock Transfer Agent, Registrar and Dividend Disbursing Agent
The Royal Trust Company: principal offices in Montréal, Toronto, Winnipeg, Regina, Calgary and Vancouver.

Stock Exchange Listings
Montréal and Toronto.

Head Office
1950 Sherbrooke Street West
Montréal (Québec) H3H 1E7

Annual Meeting
The annual meeting of shareholders will be held at 3:30 p.m., Eastern Daylight Time, on Wednesday, 22 October 1986, at Le Château Champlain Hôtel, Place du Canada, Montréal.

Si vous préférez recevoir ce rapport en français, veuillez vous adresser au Secrétaire, case postale 6250, Montréal (Québec) H3C 3L1

Our cover

Dominion Textile Inc. produces and sells denim fabrics to the North American and European markets in a variety of styles and finishes: basic indigo-dyed, grey, black and printed denims for various end-uses: jeans, pants, jackets, skirts or shirts.

Litho Canada H&V

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