Oshawa Annual Report 1985

For the fiscal year ended January 25, 1986

Pictured on the cover and elsewhere in this Annual Report are examples of the 31 supermarkets acquired in 1985 by Oshawa divisions and converted to the IGA or Food City banners. These stores have substantially broadened the Company's penetration in the important Oshawa to Niagara Falls, and Halifax-Dartmouth markets. Cover photos (from left) are Clayton Park IGA, Halifax, 25,000 square feet; Thorold Stone Road Food City, Niagara Falls, 27,000 square feet; Gerrard Street Food City, Toronto, 35,000 square feet; and Wentworth IGA, Oshawa, 26,000 square feet.

The Oshawa Group Limited is a Canadian company principally engaged in the marketing of food, general merchandise and pharmaceuticals.

From its beginning in 1914 as a wholesaler in the old produce market in downtown Toronto (pictured at left) the Company's operations now span eight provinces through a network of distribution centres and retail outlets.

Oshawa supplies 455 IGA franchise markets as well as many other food outlets and convenience stores. It owns and operates 112 supermarkets of which 54 are Food City, 44 IGA, six Dutch Boy and eight others.

It also operates 38 Towers and 10 Bonimart department stores, 50 Drug City and Metro Drug Stores, 23 pharmacies, 53 restaurants, cafeterias and snack bars, and 12 gas bars.

The Company provides food service to restaurants, hospitals, hotels and institutions. Other activities include produce wholesaling, vegetable packing, a dairy, public cold storages, a commercial laundry and revenue producing realty.

This annual report highlights another year of record sales and earnings.

The Oshawa Group Limited Class A shares are listed on the Toronto Stock Exchange and the Montreal Exchange.

La version française
de ce rapport sera
envoyée sur demande

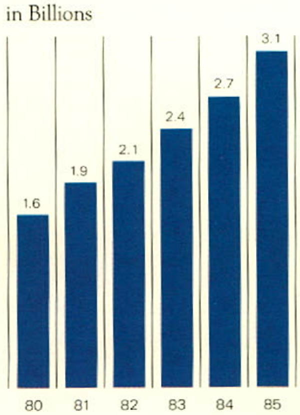
Financial Highlights

For the Year Ended January 25, 1986

(in thousands of dollars except per share)	1986 January 25	1985 January 26	% Change
Operations			
Sales and other revenue	$3,102,447	$2,665,774	+ 16.4
Earnings before extraordinary items	40,860	36,179	+ 12.9
Net earnings	40,986	36,179	+ 13.3
Capital Expenditures	64,887	30,043	+ 116.0
Financial Position			
Working capital	101,981	111,007	− 8.1
Long term debt	56,918	56,255	+ 1.2
Shareholders' equity	260,381	226,084	+ 15.2
Total assets	567,684	483,922	+ 17.3
Per Share			
Earnings before extraordinary items	2.57	2.28	+ 12.7
Net earnings	2.58	2.28	+ 13.2
Dividends	.48	.40½	+ 18.5
Book value	16.35	14.22	+ 15.0
Key Ratios			
Return on sales	1.32%	1.36%	
Return on opening equity	18.1%	18.5%	
Current ratio	1.44:1	1.59:1	
Debt to total equity	.22:1	.25:1	
Average number of shares outstanding	15,915,525	15,865,953	+ 0.31

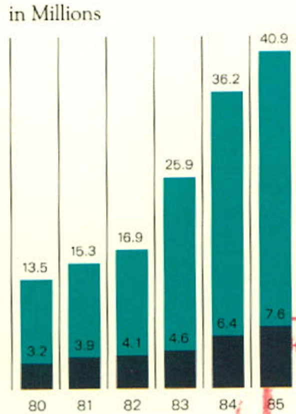
Sales

in Billions



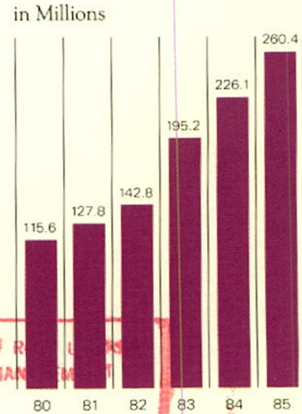
Earnings from Operations
Dividends

in Millions



Shareholders' Equity

in Millions



Report to Shareholders

For the ninth consecutive year, The Oshawa Group Limited achieved record sales and earnings. Sales increased 16.4% to $3.1 billion and earnings from operations were up 12.9% to $40.9 million ($2.57 per share compared with $2.28). Return on sales was 1.3% and on opening shareholders' equity was 18.1% after interest and income taxes. Of the sales increase, 4.7% was attributable to acquisitions at midyear and 11.7% to existing operations. Earnings growth, however, was moderated by costs related to the acquisitions.

Food segment sales of $2.6 billion increased 18.2% (12.6% exclusive of acquisitions). The principal thrust behind this improvement was the strong performance of the growing number of IGA Associates. Segment profit of $57.3 million was up 9.8%. The improvement in food results was significant in the light of the growth in the number of competitive super stores. Despite these pressures and the lowest level of food price inflation in many years, Oshawa continued to increase its sales and market share.

General merchandise segment sales of $504 million increased 6.9%. Profit of $12.4 million set a new record and was 26.0% ahead of the previous year. The cyclical expansion of the Canadian economy in 1985 brought rising employment, growing personal disposable incomes and a higher level of consumer confidence, all of which created a favorable economic climate for general merchandise retailers. Towers/Bonimart sales growth reflected both the stronger economy and aggressive merchandising in its silver anniversary year.

In August, 1985 the Company made two important acquisitions. The larger was the purchase of 22 Canada Safeway supermarkets in the Toronto-Hamilton area, and a small dairy. Seven of the stores were converted to Food City and 15 to IGA. These units complement existing corporate and franchised locations. Refurbishment, equipment replacement, product mix adjustment and the addition of in-store bakeries, delicatessens and expanded produce departments were largely completed prior to year-end. In Nova Scotia, nine supermarkets, the wholesale, produce and food service businesses and a 200,000 square foot distribution centre were acquired from Dominion Stores Limited. The retail outlets, principally located in the Halifax-Dartmouth area were converted to IGA. Integration of computer and distribution systems, and upgrading of the stores are expected to be completed by the end of the first quarter of 1986. Both acquisitions were financed from internal resources. Because of the magnitude of the expenses associated with assimilating the acquisitions, a portion of the start-up costs will be amortized over three years.

The approaching termination of the lease for the Dominion Mushroom farm, the need for large capital expenditures and an erratic profit performance over several years prompted the closure of this operation in January, 1986. Losses before interest and income taxes up to the closing announcement were $1 million. Cost of closing, amounting to $400,000 after income taxes recovered, has been included in extraordinary items.

The financial position of the Company continued to be strong despite record capital expenditures of $65 million. Year-end working capital was $102 million and debt to equity ratio .22 to 1.

The Company made further progress in the development and implementation of sophisticated electronic systems for retailing, warehousing and administration. These advances have produced better and more timely information, leading to improved management controls, productivity and profitability.

The Canadian food retailing industry continued in a state of flux with changing store formats, shifts in market share and the emergence of a number of small regional operators. Concurrently, Oshawa continued to emphasize its franchise programs, upgrade its corporate supermarkets to meet current consumer requirements and maintain a good balance between wholesale and retail growth.

In the department store industry, the scramble for market repositioning created turmoil with substantial changes occurring in merchandising strategies and promotional activities.

At Towers/Bonimart Department Stores, studies which commenced in 1984 have led to the development of the promotional department store of the future. A prototype unit is scheduled for opening in Nova Scotia later this year. Concurrently, a second prototype was designed to serve smaller markets and provide new opportunities for expansion. The first of these also will open this year.

Looking Ahead

Consistent with the Company's strategic plan, the concentration of reinvestment will be directed towards Oshawa's core business. Capital expenditures in 1986 will total $45 million, an amount similar to 1985 excluding $26 million for the fixed assets of the acquisitions. These funds will be applied largely to store equipment and renovation, warehouse requirements, rolling stock and data processing hardware and software.

Complementing the Company's investment in its wholesale activities, IGA Associates continue to expand and upgrade existing stores and open new outlets. In 1986, 16 IGA markets will be constructed, seven of which will replace smaller existing units. Twenty will be enlarged and 29 upgraded. IGA expansion will be further enhanced by the expected growth in membership of an anticipated 20 new Associates. Corporate food store expansion will include three new supermarkets and one enlargement. There also will be four major modernizations. In addition, two Towers department stores will open and three are scheduled for major renovations. Four drug stores will be added.

The Company's 737,932 square foot Sudbury City Centre was sold subsequent to the year-end. This will further strengthen Oshawa's financial position and result in an extraordinary gain in 1986.

In the year ahead management's mettle will be tested by intensifying competition, lower inflation and increased corporate income tax rates. However, the momentum of Oshawa's growth, together with the full-year's effect of last year's acquisitions, indicates further increases in sales and market share. Earnings improvement also should be enhanced by profits from the 1985 acquisitions and the absence of losses from the closed mushroom farm.

Allister P. Graham, President and Ray D. Wolfe, C.M., Chairman

Acknowledgments

We express our gratitude to Albert Shifrin, Q.C., and Murray C. Goldman who have retired from the Board of Directors after long and meritorious service. Mr. Shifrin was a director since Oshawa became a public company in 1959 and Mr. Goldman, a long time company executive, since 1963.

Our progress was made possible through the outstanding efforts of our many dedicated and resourceful employees. To them, our customers, suppliers and the public we serve, we extend our sincere thanks.

R. Wolfe   A.P. Graham

Ray D. Wolfe, C.M. Chairman and Chief Executive Officer	Allister P. Graham President and Chief Operating Officer

March 20, 1986

Oshawa Profile

Wholesale and Retail Food

The wholesale and retail food divisions, representing 78.2% of 1985 consolidated sales, operate in four geographic regions – in Ontario, Oshawa Foods, Toronto, Dutch Boy Food Markets, Kitchener and Elliott Marr and Company Limited, London; in Quebec, Hudon et Deaudelin limitée, Montreal; in Western Canada, Codville Distributors, Winnipeg, Saskatoon and Regina, and in Atlantic Canada, Bolands Limited, Dartmouth, Nova Scotia and Moncton, New Brunswick.

Sales and Other Revenue by Division

(in millions)	1985	1984	% Increase
Oshawa Foods, Dutch Boy and Elliott Marr	**$1,152.1**	$1,003.9	14.8
Hudon et Deaudelin	**818.3**	664.7	23.1
Codville Distributors	**311.1**	291.4	6.8
Bolands	**212.7**	138.5	53.6
	2,494.2	2,098.5	18.9
Less intra-segment sales and other revenue	**28.2**	21.0	34.3
	$2,466.0	$2,077.5	18.7

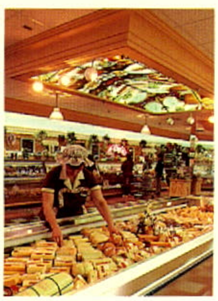
Operations

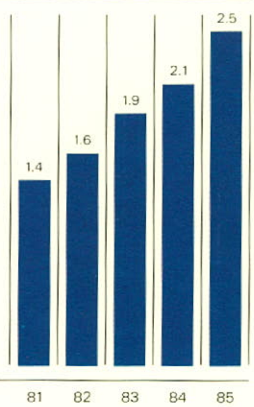
The wholesale and retail food divisions supply a full line of grocery, produce, dairy, frozen food, meat and non-food products to franchised food markets, convenience stores, cash & carry units, non-affiliated independents and Company-owned supermarkets. The table illustrates the number of stores served.

	Ontario	Quebec	Western Canada	Atlantic Canada	1985	1984
IGA Food Markets						
Franchised	143	159	106	47	**455**	424
Company-owned	18	2	7	17	**44**	21
Other Food Markets						
Franchised	141	137	308	–	**586**	588
Company-owned	65	2	1	–	**68**	61
Convenience stores	76	264	99	–	**439**	321
Cash and Carry	–	13	5	2	**20**	19

Sales in Billions

Five year compound growth 15%





Food Service and Produce

Food service and produce companies operating in Ontario contributed 5.4% of 1985 consolidated sales. Food service companies are Hickeson-Langs Supply Company, Toronto, Hamilton, London and Ottawa; Langs Cold Storage, Hamilton and London, and Model Laundry, Toronto. Produce companies are The Ontario Produce Company, Toronto and Bradford; The White and Company, Toronto, and Dominion Mushroom Company, Pickering.

Sales and Other Revenue by Division

(in millions)	1985	1984	% Increase
Food Service			
Hickeson-Langs	**$101.2**	$ 87.8	15.3
Langs Cold Storage	**3.3**	2.9	13.8
Model Laundry	**2.8**	2.6	7.7
	107.3	93.3	15.0
Produce			
Ontario Produce and White and Co.	**60.8**	57.6	5.6
Dominion Mushroom Company	**2.3**	2.9	(20.7)
	63.1	60.5	4.3
	$170.4	$153.8	10.8

Operations

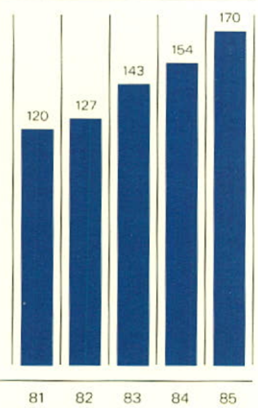
Hickeson-Langs distributes grocery, frozen food and meat products to the food service industry, and provides a juice and coffee dispenser service to restaurants, hotels and other customers. Langs Cold Storage offers blast freezing and commercial frozen storage facilities to processors of fruit, vegetables, meat and juice.

Model Laundry provides a rental service for uniforms and linens to retail stores and industrial plants.

Ontario Produce and White and Company are full-service wholesalers of imported and domestic fruit and vegetables to retailers and jobbers, and are principal purchasing agents of produce for Oshawa Foods. Ontario Produce also operates a vegetable packing plant at Bradford, Ontario.

Sales in Millions

Five year compound growth 10%



General Merchandise

The General Merchandise Group which accounted for 16.0% of 1985 consolidated sales, includes Towers Department Stores Inc. (Bonimart in the Province of Quebec), Kent Drugs Limited and the Restaurant Division, all with head offices in Toronto, Ontario.

Sales and Other Revenue by Division

(in millions)	1985	1984	% Increase
Towers Department Stores	**$415.1**	$389.1	6.7
Kent Drugs	**80.1**	73.8	8.5
Restaurants	**8.5**	8.2	3.7
	$503.7	$471.1	6.9

Operations

Towers Department Stores has 48 locations in Ontario, Quebec,* Nova Scotia, New Brunswick and Prince Edward Island. The two stores in Prince Edward Island are combination food and general merchandise units.

Kent Drugs Limited operates 50 drug stores under the Drug City and Metro Drugs names in Ontario, Manitoba and New Brunswick, as well as pharmacies in 18 Towers units, four supermarkets and one free standing location. The Restaurant Division consists of 53 restaurants, cafeterias and snack bars within or adjacent to Towers Department Stores.

*Ten Quebec department stores operate under the name of Bonimart.

Real Estate

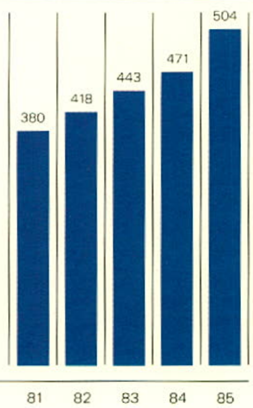
Oshawa's Real Estate division negotiates construction and/or leasing of locations for new franchised and corporate retail stores and distribution centres. Extensive site research, engineering, planning and construction supervision as well as legal and financial services are provided. These services are valuable to IGA Associates and other independents in expanding and improving their operations.

The division also manages the Company's real estate holdings and administers a large number of third-party leases.

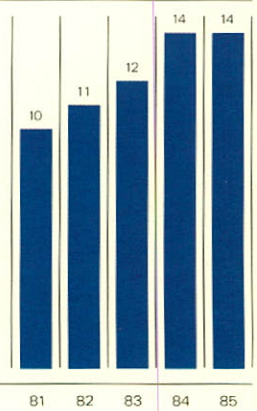
Real estate holdings include a shopping and commercial centre in downtown Sudbury, Ontario, with gross building area of 737,932 square feet, and shopping centres in Montreal and St. Jean, Quebec, with gross building areas of 648,673 square feet and 142,746 square feet respectively. Also included are a number of owned and leased plazas which are sublet to the food and general merchandise divisions and third parties, as well as land for future development or sale.

(in millions)	1985	1984	% Increase
Revenue	**$14.3**	$13.8	3.6

Sales in Millions — Five year compound growth 8%



Revenue in Millions — Five year compound growth 9%



Wholesale and Retail Food

Oshawa's wholesale and retail food divisions achieved another record year in 1985. Sales growth of 18.9% to $2.5 billion was the highest in a decade. Part of the increase was attributable to acquisitions at midyear, referred to in the Report to Shareholders. Exclusive of the new operations, sales improved by 12.5%. Despite deferment of a portion of the start-up and integration costs to be amortized over the next three years, the acquisitions adversely affected earnings in the second half. Earnings before corporate expenses, interest and income taxes were up 8.8%.

Inflation was at its lowest level in many years and real growth in the food industry relatively static. Supermarket sales were also affected by the increasing use of food as promotional features in drug and general merchandise stores. In pursuit of increased sales, many retailers implemented longer hours and Sunday openings, added fresh specialty departments and services, and offered major price discounts on staple items.

Nevertheless, Oshawa increased market share in all areas of Canada in which the Company operates. This was largely the result of entrepreneurial management at both franchised and corporate levels. Regional decision making allowed flexibility to respond quickly to changing conditions. Effective advertising and merchandising programs tailored to local needs, superior customer service and new and upgraded stores also contributed.

The opening of super warehouse combination stores by some competitors presented a new challenge. However, Oshawa continued to grow through expansion and upgrading of franchised units, recruitment of new IGA Associates, enlargement and major remodeling of corporate supermarkets with more and extensive specialty departments, and the acquisitions.

Exclusive of outlays by IGA Associates, food group capital expenditures during 1985 were a record $55 million, which included $26 million relating to the acquisitions.

Food store expansion in 1985 resulted in a net increase of 31 franchised IGA units and 118 convenience stores. During the year 16 IGA Associate units were enlarged and 40 renovated. Net increase in corporate supermarkets was 29 including 17 which were renovated; two existing stores were expanded and two upgraded.

Favorable customer response to major renovations which continue to be implemented in Food City stores are reflected in higher customer counts and sales. Above (from left) are St. Catharines Food City, the new Scott-Vine Food City, St. Catharines, and North Bay Food City. At right, a shopper enjoys the pleasant ambience of an enlarged and upgraded Food City produce department.

Renovation of Company-owned stores has significantly enhanced shopping environment.

IGA signs went up on 31 franchised food markets in 1985, some with unique design.

Ontario Operations

Ontario is served by Oshawa Foods, Dutch Boy Food Markets and Elliott Marr and Company Limited, operating a total of four distribution centres in Toronto, Kitchener and London, Ontario.

Sales of $1.2 billion were up 14.8%. Exclusive of sales of the 22 supermarkets and the dairy acquired from Canada Safeway on August 26, 1985, the improvement amounted to 8.0%. While earnings were satisfactory, they were somewhat lower as a result of costs associated with the integration and start-up of the acquisition, a more competitive market environment for Dutch Boy and the cost of introducing a new franchise program at Elliott Marr.

Significant shifts in the Ontario market occurred in 1985, with Dominion Stores selling, closing or converting its stores to franchised units and Safeway withdrawing from Southern Ontario. The principal results of these changes were that Oshawa and one other operator have grown significantly and that some of the closed stores have reopened under the banners of independent chains. The Ontario market also saw the emergence of a number of retail units emphasizing produce and meat and the super warehouse combination store.

The purchase of the Safeway stores provided Oshawa Foods with a unique opportunity to broaden its market share in Southern Ontario. The additional units complement existing locations and present warehouse, buying, merchandising and other support services are sufficient to accommodate the substantially increased volume. However, many of the newly acquired stores required renovation. Accordingly a program of refurbishment and equipment replacement was immediately undertaken as was the addition of in-store bakeries and delicatessens. The stores have been remerchandised, staffs retrained and special advertising and promotions instituted.

The Safeway purchase included a fluid milk plant in Oakville, providing Oshawa Foods with its first entry into food processing.

Nine IGA franchised stores opened during the year, of which three were conversions from other programs and four replacements for outdated units. Two stores were closed and one transferred to a competing program for a net increase of two. Of an additional 14 that were renovated, eight were enlarged. Corporate store expansion included the 22 acquired stores, three new Food City outlets, one of which replaced an older and smaller unit, and four renovations of existing stores, two of which were expanded.

New store construction by IGA Associates materially contributed to Oshawa's sales growth. Among the new IGA franchised food markets opened in 1985 was a 25,760 square-foot unit in Sutton, Ontario (at left), which has the facade of an old-time railway station. Above (from left) are the in-store bakery of the newly opened Schomberg, Ontario IGA; the Verdoold family and one of their vintage auto collection in their Sutton store, and the produce department of the new Pringle Creek IGA, Whitby, Ontario.

In the latter half of the year, Elliott Marr introduced the E.M.A. (Elliott Marr Associates) franchise program which closely parallels Oshawa Foods' IGA program. Initial results have been encouraging.

Quebec Operations

Hudon et Deaudelin limitée continued its strong sales performance which has produced an average increase of 20% per annum for the past five years. The 1985 improvement was 23.1% with approximately half coming from existing units. The remainder came from the part-year effect of new stores and the results of a full year's wholesale produce business. Earnings improved at a greater rate than sales.

The advances achieved by this division in a slow-growth market were all the more significant in the face of a substantial increase in the number of super warehouse combination stores and more aggressive competition.

Seventeen franchised IGA Boniprix stores were added and 33 outlets renovated including six which were enlarged.

Western Canada Operations

Codville Distributors operating in Saskatchewan, Manitoba and Northwestern Ontario achieved a modest sales increase of 6.8% and a similar improvement in earnings.

Wholesale sales to unaffiliated independents and smaller chains were affected by continuing intensive price wars in major population centres and the negative impact of poor weather conditions on crops and tourism. Nevertheless, sales to the steadily growing IGA component were up by 12.5%, partly due to the introduction of a new merchandising program.

Eleven new IGA markets were opened in 1985 and another replaced a smaller store. Five were renovated and two were enlarged and refurbished.

Atlantic Canada Operations

Bolands Limited operating in the four Atlantic Provinces recorded a 53.6% sales increase, reflecting the acquisition in August, 1985 of most of the Nova Scotia wholesale and retail business of Dominion Stores Limited. Exclusive of the additional business, sales improvement in this no-growth, high unemployment market was 4.5%. Even after absorbing most of the expenses associated with integration of the acquisition, earnings were up more than 10%.

These IGA Boniprix units in Quebec are examples of the improved shopping facilities provided customers as a result of store replacements, enlargements and refurbishments. Above (clockwise) are a renovated outlet in Ste. Foy, a new IGA Boniprix in Chambly, and expanded stores in Thetford Mines and Ste. Therese.

New, enlarged and renovated stores substantially upgraded the image of IGA Boniprix in Quebec.

Acquisition of 22 Ontario supermarkets brought increased market share.

Financial Review

Sales

Consolidated sales and other revenue of $3.1 billion in the year ended January 25, 1986 increased $437 million or 16.4%. Food contribution to the improvement was $405 million (93%) and general merchandise $32 million (7%). Compound average annual sales and other revenue growth over the last five years was 13.5%.

Earnings

Earnings before extraordinary items were up 12.9% to $40.9 million ($2.57 per share) and represented 1.32% of sales. Increased earnings by all operating groups and slightly lower interest expense were partially offset by a reduction in interest income. The effective income tax rate of 42.6% was a half percent less than in the previous year. After extraordinary items of $126 thousand, net earnings amounted to $41.0 million ($2.58 per share).

Food segment earnings of $57.3 million before interest and income taxes rose 9.8%, general merchandise of $12.4 million, 26.0% and real estate of $5.3 million, 3.2%.

Interest expense of $6.9 million compared with $7.3 million in 1984. Interest earned of $4.1 million was down from $5.5 million principally due to the use of funds for acquisitions.

Dividends

Dividends of 48 cents per share were paid in 1985, up from 40½ cents per share in 1984. Of the $7.6 million declared in 1985, $949 thousand was paid by the issuance of 34,625 Class A shares under the provisions of the optional stock dividend policy.

The quarterly dividend rate has been increased from 12½ cents to 14 cents effective with the payment of June 10, 1986 to shareholders of record May 19, 1986.

Financial Position

The Company continues to have a strong balance sheet as summarized as follows.

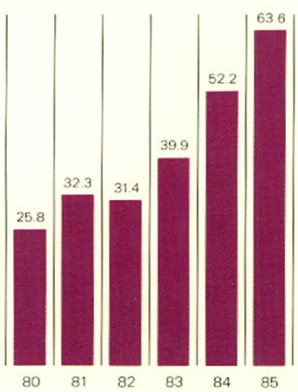
(in millions)	1985	1984	Increase (Decrease)
Current assets	**$335**	$301	$34
Current liabilities	**233**	190	43
Working capital	**102**	111	(9)
Fixed and other assets	**232**	183	49
Assets employed	**$334**	$294	$40
Financed by:			
Long term debt	**$ 57**	$ 56	$ 1
Deferred income taxes	**17**	12	5
Shareholders' equity	**260**	226	34
	$334	$294	$40

Working capital of $102 million was down only $9 million despite record capital expenditures of $65 million.

Within working capital, bank indebtedness net of cash and short-term investments of $19.5 million reflected a reduction of $36.3 million in liquid resources. This was more than accounted for by the investment in accounts receivable, inventories and fixed assets of the businesses purchased in August, 1985.

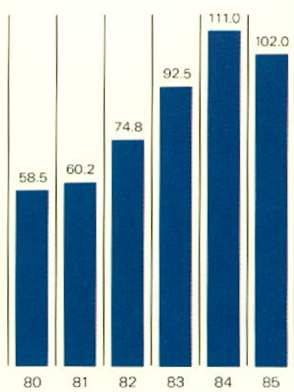
Cash Flow from Operations

in Millions

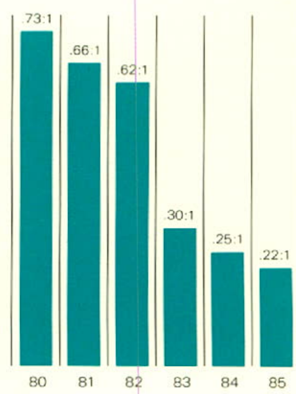


Working Capital

in Millions



Debt to Equity Ratio



Long term debt of $56.9 million was about the same as at the previous year-end and consisted of obligations at equal or lower than current market interest rates. Debt-to-equity ratio of .22 to 1 allows for substantial capacity for debt financing.

Capital expenditures included $26 million relating to the acquisition of Safeway stores and dairy in Southern Ontario and most of Dominion Stores' retail and wholesale operations in Nova Scotia. The balance of $39 million was used for the upgrading of retail food and department stores, replacement of transportation fleets, warehouse modernization and the installation of electronic equipment and software. The 1986 plan calls for a capital program of $45 million.

The Company's shopping and commercial centre in Sudbury, Ontario has been sold with the closing of the transaction in the new fiscal year. This will result in an extraordinary gain and will further strengthen Oshawa's financial position by a reduction in mortgage debt of $14 million and an increase in cash resources of $19 million.

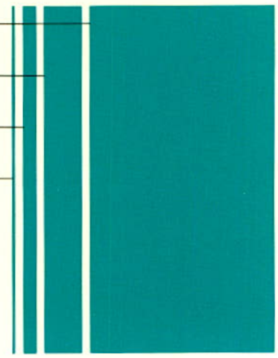
Shareholders' Equity

Shareholders' equity of $260.4 million ($16.35 per share) was up $34.3 million. Return after income taxes on opening shareholders' equity was 18.1%.

Philip F. Connell, F.C.A.
Senior Vice President Finance
and Chief Financial Officer

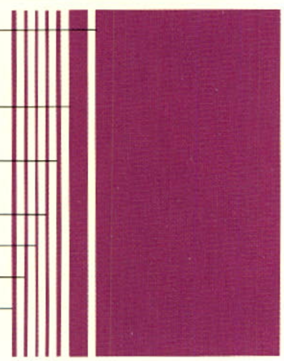
Sales and Other Revenue

1985	
78.4%	Wholesale and Retail Food
15.8%	General Merchandise
5.4%	Food Service and Produce
.4%	Real Estate



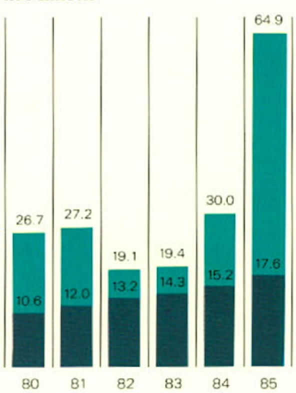
Distribution of Sales Dollar

1984	1985	
87.71	87.98	Merchandise, services and related expenses
9.06	8.93	Payroll and employee benefits
1.03	.98	Corporation income taxes
.57	.57	Depreciation
.27	.22	Interest
.24	.25	Dividends paid
1.12	1.07	Retained for growth
100.00	100.00	



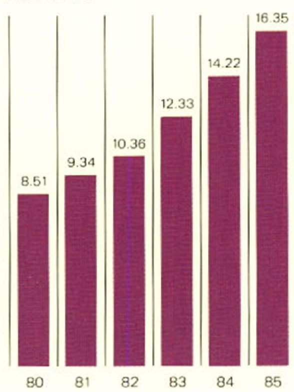
Capital Expenditures
Depreciation

in Millions



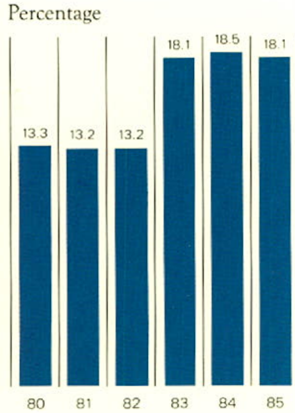
Shareholders' Equity per Share

in Dollars



Return on Equity

Percentage



Responsibility for Financial Reporting

The management of The Oshawa Group Limited is responsible to the Board of Directors for the preparation and integrity of the financial statements and related information of the Company. These have been prepared in accordance with generally accepted accounting principles consistently applied and are based on management's best information and judgments.

To provide assurance in fulfilling its responsibilities, management maintains appropriate accounting records which incorporate sound systems of internal control designed to safeguard the Company's assets and ensure proper accounting of all of its business transactions.

In support of carrying out these responsibilities management and the Directors have the assistance of the internal audit department, the external auditors and the Audit Committee of the Board all of whom review and report on such matters.

The Company's external auditors, Wm. Eisenberg & Co. conduct an independent examination of accounting records, policies, procedures and internal controls in accordance with generally accepted auditing standards and express their opinion on the financial statements.

The Audit Committee of the Board consisting of a majority of outside Directors meets with both Wm. Eisenberg & Co. and the Director of Internal Audit to review their audit findings. It then reports to the Board of Directors prior to the approval of the audited financial statements for publication.

Ray D. Wolfe, C.M.
Chairman and Chief
Executive Officer

Philip F. Connell, F.C.A.
Senior Vice President and
Chief Financial Officer

Auditors' Report to the Shareholders

We have examined the consolidated balance sheet of The Oshawa Group Limited as at January 25, 1986 and the consolidated statements of earnings, retained earnings and changes in cash 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 as at January 25, 1986 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Wm. Eisenberg & Co.
Chartered Accountants

Toronto, Canada
March 11, 1986

Consolidated Statement of Earnings

For the year ended January 25, 1986

(in thousands of dollars)	1986	1985
Sales and other revenue	$3,102,447	$2,665,774
Cost of sales and expenses		
Cost of sales and expenses before the undernoted items:	3,010,879	2,585,192
Interest (note 6)	6,908	7,258
Depreciation	17,572	15,189
	3,035,359	2,607,639
	67,088	58,135
Interest earned	4,077	5,464
Earnings before income taxes and extraordinary items	71,165	63,599
Income taxes	30,305	27,420
Earnings before extraordinary items	40,860	36,179
Extraordinary items (note 7)	126	–
Net earnings	$ 40,986	$ 36,179
Earnings per share before extraordinary items	$2.57	$2.28
Net earnings per share	$2.58	$2.28
Average number of shares outstanding	15,915,525	15,865,953

Consolidated Statement of Retained Earnings

For the year ended January 25, 1986

(in thousands of dollars)	1986	1985
Balance, beginning of year	$131,741	$101,985
Add: Net earnings	40,986	36,179
	172,727	138,164
Less: Dividends		
–Class A shares	7,473	6,284
–Common shares	165	139
	7,638	6,423
Balance, end of year	$165,089	$131,741

The Oshawa Group Limited

Consolidated Balance Sheet

January 25, 1986

(in thousands of dollars)	1986	1985
Assets		
Current assets		
Cash and short term investments	$ 11,945	$ 40,500
Accounts receivable	96,304	76,041
Inventories	214,910	176,744
Real estate held for sale	6,244	2,256
Prepaid expenses	5,726	4,971
	335,129	300,512
Fixed assets (note 2)	217,534	174,976
Other assets (note 3)	15,021	8,434
	$567,684	$483,922
Liabilities		
Current liabilities		
Bank indebtedness	$ 31,412	$ 23,628
Accounts payable and accrued liabilities	195,410	153,145
Income taxes payable	4,932	11,200
Current portion of long term debt	1,394	1,532
	233,148	189,505
Long term debt (note 4)	56,918	56,255
Deferred income taxes	17,237	12,078
Shareholders' equity		
Capital stock (note 5)		
Authorized		
Unlimited number of Class A and Common shares		
Issued		
15,585,619 Class A shares (1985–15,550,994)	95,248	94,299
342,752 Common shares	44	44
	95,292	94,343
Retained earnings	165,089	131,741
	260,381	226,084
	$567,684	$483,922

Approved on behalf of the Board

R. Wolfe

Ray D. Wolfe, Director

P. Connell

Philip F. Connell, F.C.A., Director

The Oshawa Group Limited

Consolidated Statement of Changes in Cash Position

For the year ended January 25, 1986

(in thousands of dollars)	1986	1985
Cash provided from:		
Operating activities:		
Earnings before extraordinary items	$ 40,860	$ 36,179
Charges to earnings not affecting cash:		
Depreciation	17,572	15,189
Deferred income taxes	5,159	818
	63,591	52,186
Changes in working capital components other than cash	(27,313)	(6,723)
	36,278	45,463
Financing activities:		
Issue of long term debt	2,979	1,527
Issue of Class A shares as dividends	949	1,105
Repayment of long term debt	(2,316)	(2,655)
	1,612	(23)
Investing activities:		
Purchase of fixed assets	(64,887)	(30,043)
Disposal of fixed assets	4,757	1,637
Other	(6,461)	1,990
	(66,591)	(26,416)
Dividends	(7,638)	(6,423)
Change in cash position	(36,339)	12,601
Cash, beginning of year	16,872	4,271
Cash, end of year	$(19,467)	$ 16,872
Represented by:		
Cash and short term investments	$ 11,945	$ 40,500
Bank indebtedness	(31,412)	(23,628)
	$(19,467)	$ 16,872

Notes to Consolidated Financial Statements

(in thousands of dollars)

1. Summary of Significant Accounting Policies

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its subsidiaries.

Inventories

Warehouse inventories are valued at the lower of cost and net realizable value with cost being determined on a first-in, first-out basis. Retail inventories are valued at the lower of cost and net realizable value less normal profit margins as determined by the retail method of inventory valuation.

Real Estate Held for Sale

Real estate held for sale is valued at the lower of cost and net realizable value. Cost includes development expenses and carrying charges including applicable interest on general borrowings.

Fixed Assets and Depreciation

Major enlargements, remodelings and improvements are charged to the appropriate fixed asset accounts. The cost of maintenance and repairs which does not extend the life of an asset is charged against earnings.

Fixed assets are recorded at cost, which in the case of land and buildings includes carrying costs incurred during development, construction and the initial leasing period, and are depreciated on a straight line basis at rates sufficient to amortize the cost of the assets over their estimated useful lives as follows:

Classification	Estimated Useful Life
Buildings	20 to 40 years
Equipment	4 to 10 years
Leasehold improvements	term of lease plus first option to a maximum of 20 years
Property under capital leases	term of lease

Development and Opening Expenses

Development and opening expenses of new stores are written off in the year of opening.

Sale of Stores and Properties

Gains and losses on the sale of stores and properties, other than major operating facilities, are considered an integral part of the Company's operations and are included in ordinary income.

Fiscal Year

The fiscal year of the Company ends on the fourth Saturday in January.

2. Fixed Assets

	1986	1985
Land	**$ 20,888**	$ 22,565
Buildings	**114,064**	103,371
Equipment	**164,936**	127,468
Leasehold improvements	**39,903**	30,679
	339,791	284,083
Less accumulated depreciation	**126,231**	113,279
	213,560	170,804
Property under capital leases, less accumulated depreciation of $1,023 (1985–$825)	**3,974**	4,172
	$217,534	$174,976

3. Other Assets

	1986	1985
Loans and mortgages receivable	**$ 8,928**	$7,666
Deferred major expansion costs	**5,370**	–
Other	**723**	768
	$15,021	$8,434

In August 1985, the Company acquired 22 Safeway stores in Ontario and 9 Dominion stores and warehouse facilities in Nova Scotia.

Subsequently the Company embarked on a program to upgrade the retail locations and to integrate their operations with those of the Company's other retail facilities.

The costs of this program have been deferred and are being amortized on a straight-line basis over three years commencing in the 1987 fiscal year.

4. Long Term Debt

	1986	1985
Bank indebtedness	**$ 7,770**	$ 7,770
Mortgages and loans payable	**36,490**	35,363
Series A Sinking Fund Debentures	**9,214**	9,790
Obligations under capital leases (note 9)	**4,838**	4,864
	58,312	57,787
Less current portion	**1,394**	1,532
	$56,918	$56,255

Principal Repayments

Principal repayments of long term debt are as follows:

Fiscal year ending in	
1987	$ 1,394
1988	7,902
1989	1,915
1990	1,666
1991	4,482
1992-2011	40,953
	$58,312

Bank Indebtedness

Bank indebtedness bears interest at rates varying from short term money market rates to prime, and provides for principal repayments in 1988, 1989 and 1991.

Mortgages and Loans Payable

These obligations bear interest at an average rate of 10.9% per annum and provide for principal repayments from 1987 to 2009.

Series A Sinking Fund Debentures

These debentures, secured by a floating charge on the undertaking and assets of the Company, bear interest at 9¼% per annum and mature June 15, 1991.

5. Capital Stock

The Class A shares are non-voting, participating and are entitled to a non-cumulative annual dividend of 10 cents per share in priority to the payment of dividends on the Common shares.

Under the optional stock dividend policy, 71,437 Class A shares are available for future issue. During the year, 34,625 Class A shares were issued in lieu of cash dividends.

The Company has reserved 600,000 Class A shares for issuance under the Share Option Plan for Officers and Key Executives 1982. As at January 25, 1986 options for 170,000 Class A shares were outstanding under this plan, exercisable until 1993 at a price of $14 per share. The exercise of these share options would have no material dilutive effect on earnings per share.

6. Interest Expense

	1986	1985
Interest on long term debt	**$5,065**	$5,362
Other interest	**1,911**	1,329
Interest on obligations under capital leases	**894**	989
	7,870	7,680
Less interest capitalized to cost of real estate	**962**	422
	$6,908	$7,258

7. Extraordinary Items

	1986	1985
Reduction of income taxes on application of prior years' losses of certain subsidiaries	**$ 524**	–
Loss on closing Dominion Mushroom division, less income taxes recovered of $417	**(398)**	–
	$ 126	–

8. Effective Income Tax Rate

	1986	1985
Combined basic Canadian and Ontario income tax rate	**52.0%**	51.0%
Inventory allowance	**(4.8)**	(5.1)
Tax reductions due to lower rates in other provinces	**(3.8)**	(2.4)
Sundry items	**(0.8)**	(0.4)
	42.6%	43.1%

9. Leases

Minimum lease payments for store locations, office and warehouse facilities and equipment (exclusive of additional amounts based on percentage of sales, taxes, insurance, and other occupancy charges) under capital and operating leases in future years are as follows:

	Capital Leases	Operating Leases
Fiscal year ending in		
1987	$ 930	$ 31,018
1988	933	26,130
1989	933	23,705
1990	933	22,295
1991	834	20,048
1992-2011	14,943	161,948
Total minimum lease payments	19,506	$285,144
Less imputed interest at an average rate of 18% per annum	14,668	
Obligations under capital leases	$ 4,838	

It is expected that rental revenue of $6,406 will be received in the fiscal year ending January 24, 1987, from locations which have been sublet.

10. Contingent Liability

The Company has guaranteed one-half of any deficiency between net rental income and the payment of principal, interest and taxes required under a mortgage loan having a balance of $7,632 at January 25, 1986. The Company has received an indemnity against any losses which may be suffered under this guarantee.

11. Related Party Transactions

The Company leases a warehouse and six retail outlets from a company owned by certain Officers, Directors and their families. Rentals for the year ended January 25, 1986, amounted to $1,027 (1985 – $1,027).

12. Comparative Figures

Comparative figures have been reclassified, where necessary, to conform with the current year's presentation.

13. Segmented Information

	Food		General Merchandise		Real Estate		Consolidated	
	1986	1985	**1986**	1985	**1986**	1985	**1986**	1985
Sales and other revenue								
Outside	**$2,589,526**	$2,185,813	**$ 503,672**	$ 471,146	**$ 9,249**	$ 8,815	**$3,102,447**	$2,665,774
Inter-segment	**46,920**	45,436	**–**	–	**5,078**	4,986	**–**	–
	$2,636,446	$2,231,249	**$ 503,672**	$ 471,146	**$ 14,327**	$ 13,801	**$3,102,447**	$2,665,774
Segment profit	**$ 57,294**	$ 52,181	**$ 12,375**	$ 9,818	**$ 5,315**	$ 5,148	**$ 74,984**	$ 67,147
Corporate investment income							**3,089**	3,710
Interest							**(6,908)**	(7,258)
Income taxes							**(30,305)**	(27,420)
Earnings before extraordinary items							**40,860**	36,179
Extraordinary items							**126**	–
Net earnings							**$ 40,986**	$ 36,179
Assets								
Segment	**$ 360,463**	$ 254,252	**$ 118,679**	$ 114,097	**$ 75,595**	$ 74,544	**$ 554,737**	$ 442,893
Corporate							**12,947**	41,029
Total							**$ 567,684**	$ 483,922
Capital expenditures								
Segment	**$ 56,556**	$ 20,721	**$ 4,272**	$ 5,279	**$ 3,879**	$ 3,665	**$ 64,707**	$ 29,665
Corporate							**180**	378
Total							**$ 64,887**	$ 30,043
Depreciation								
Segment	**$ 11,825**	$ 9,625	**$ 3,869**	$ 3,696	**$ 1,754**	$ 1,737	**$ 17,448**	$ 15,058
Corporate							**124**	131
Total							**$ 17,572**	$ 15,189

14. Subsequent Event

Subsequent to the year end, the Company entered into an agreement to sell its shopping centre in Sudbury, Ontario, for $33,000 of which $19,139 will be received in cash with a mortgage payable of $13,861 being assumed by the purchaser. The transaction is scheduled to close in April 1986, and will result in an extraordinary gain in the year ending January 24, 1987.

6 Year Comparative Summary

(in thousands of dollars except per share)

Income Statement	Sales
	Salaries, wages, benefits
	Depreciation
	Interest expense
	Income taxes
	Earnings before extraordinary items
	Net earnings
Balance Sheet	Total assets
	Current assets
	Current liabilities
	Working capital
Financing	Shareholders' equity
	Long term debt
Cash Flow	Cash flow from operations
	Capital expenditures
	Re-invested in business
	Dividends paid
Key Financial Ratios	Current ratio
	Return on opening equity
	Earnings before extraordinary items as a % of sales
Per Share Data	Earnings before extraordinary items***
	Net earnings***
	Dividends paid
	Shareholders' equity***
	High-low stock price
	Average number of shares*
	Number of shares at year-end*
	Number of full and part time employees at year-end

*Combined Class A and Common
**Dividends declared on January 25, 1980 of 11½¢ per share were paid March 10, 1980
***Earnings per share have been calculated on the average number of shares outstanding during the year.
Shareholders' equity per share has been calculated on the shares outstanding at the end of the year.
Figures for previous years have been adjusted for the two-for-one stock split of July 6, 1984.

1986 January 25	1985 January 26	1984 January 28 (53 weeks)	1983 January 22	1982 January 23	1981 January 24
$3,102,447	$2,665,774	$2,434,985	$2,118,285	$1,896,569	$1,648,188
277,042	241,433	226,144	201,389	177,235	154,863
17,572	15,189	14,287	13,186	12,020	10,590
6,908	7,258	11,066	16,219	16,020	13,332
30,305	27,420	19,643	11,465	11,503	10,443
40,860	36,179	25,895	16,912	15,310	13,486
40,986	36,179	25,895	18,327	15,417	16,523
567,684	483,922	435,631	393,825	380,026	344,583
335,129	300,512	263,448	226,327	217,402	197,857
233,148	189,505	170,946	151,502	157,234	139,345
101,981	111,007	92,502	74,825	60,168	58,512
260,381	226,084	195,223	142,774	127,825	115,605
56,918	56,255	58,202	88,051	84,820	84,410
63,591	52,186	39,944	31,449	32,254	25,786
64,887	30,043	19,439	19,143	27,194	26,673
33,348	29,756	21,341	14,211	11,504	14,122
7,638	6,423	4,554	4,116	3,913	3,177**
1.44:1	1.59:1	1.54:1	1.49:1	1.38:1	1.42:1
18.07	18.53	18.14	13.23	13.24	13.34
1.32	1.36	1.06	0.80	0.81	0.82
2.57	2.28	1.83	1.23	1.12	1.00
2.58	2.28	1.83	1.33	1.13	1.22
48¢	40½¢	33¢	30¢	28¾¢	23½¢**
16.35	14.22	12.33	10.36	9.34	8.51
35-23⅛	25-15½	17¼-10⅝	12⅛-6½	8¼-5¾	7⅛-3⅜
15,915,525	15,865,953	14,135,386	13,730,608	13,623,818	13,529,558
15,928,371	15,893,746	15,835,492	13,776,572	13,678,546	13,576,722
17,819	15,031	14,643	14,806	15,000	14,232

Directors, Officers

Max Wolfe
Honorary Chairman
of the Board

Directors

William L. Atkinson
Philip F. Connell, F.C.A.*
Allister P. Graham
Charles Perrault, M.Eng.*
Arthur J. R. Smith, Ph.D., D.U.C., LL.D.*
Harold J. Wolfe
Harvey S. Wolfe
Jack B. Wolfe
Jonathan A. Wolfe
Ray D. Wolfe, C.M.
*Audit Committee

Officers

Ray D. Wolfe, C.M.
Chairman and Chief
Executive Officer

Allister P. Graham
President and Chief
Operating Officer

Philip F. Connell, F.C.A.
Senior Vice President and
Chief Financial Officer

Leonard Eisen, F.C.A.
Treasurer

Harold J. Wolfe
Secretary

Corporate Management

Ray D. Wolfe, C.M.
Chairman and Chief
Executive Officer

Allister P. Graham
President and Chief
Operating Officer

Philip F. Connell, F.C.A.
Senior Vice President and
Chief Financial Officer

William L. Atkinson
Group Vice President
General Merchandise

Jack B. Wolfe
Group Vice President
Food Service and Produce
Companies

E. Leonard Besler, C.A.
Corporate Controller

Sam Crystal
Vice President Public
Affairs

Leonard Eisen, F.C.A.
Treasurer

Murray C. Goldman
Vice President
Development

Matilda M. Manojlov
Vice President Profit
Improvement

Paul B. Nielsen
Vice President Industrial
Relations

Sidney Pasoff
Vice President Management
Information Services

Donald A. Smith
Vice President
Human Resources

Harold J. Wolfe
General Counsel

Operating Divisions

Food

Bolands Limited
Dartmouth, Nova Scotia
Leif Christensen
President and
General Manager

Codville Distributors
Winnipeg, Manitoba
Max J. Hatch
President and
General Manager

Dutch Boy Food Markets
Kitchener, Ontario
Barry Humphrey
General Manager

Elliott Marr and Company Limited
London, Ontario
Michael Smith
General Manager

Hudon et Deaudelin limitée
Montreal, Quebec
Pierre Croteau
President and
General Manager

Oshawa Foods
Toronto, Ontario
Jonathan A. Wolfe
President and
General Manager

Food Service and Produce Companies

General Manager Produce
John F. Brown, Ph.D.

The Ontario Produce Company
Toronto, Ontario
Myron J. Wolfe
Vice President

The Ontario Produce Company
Bradford, Ontario
H. Glen Henderson
Manager

The White and Company
Toronto, Ontario
Vance Graham
Manager

General Manager Food Service
Gary R. Adams

Beverage Dispensers
Toronto, Ontario
Robert C. Kelly
General Manager

Hickeson-Langs Supply Company
Toronto, Ontario
Charles J. Davies
President and
General Manager

Langs Cold Storage
Hamilton, Ontario
Kenneth R. Edworthy
General Manager

Model Laundry
Toronto, Ontario
Wilfred M. Dawe
General Manager

General Merchandise

Kent Drugs Limited
Toronto, Ontario
Ab Flatt
President

Restaurants
Toronto, Ontario
Larry J. Crystal
General Manager

Towers Department Stores Inc.
Toronto, Ontario
William L. Atkinson
President and Chief
Executive Officer

Real Estate
Murray C. Goldman
Vice President
Development

Corporate Data

Registrar and Transfer Agents
Class A Shares and Series A Debentures
The Canada Trust Company
Toronto, Montreal, Calgary, Regina and Vancouver

Auditors
Wm. Eisenberg & Co.,
Toronto

Bankers
Canadian Imperial Bank of Commerce
Bank of Montreal
Bank of Nova Scotia
Toronto Dominion Bank
National Bank of Canada

Listed on
Toronto Stock Exchange
Montreal Exchange
Stock Symbol: OSH.A

Investor Information:
Philip F. Connell, F.C.A.

Head Office
302 The East Mall,
Islington, Ontario,
Canada M9B 6B8
(416) 236-1971
Telex: 06-984631

Annual Meeting
The annual meeting of shareholders will take place at 10 a.m., Thursday, June 12th, 1986 in the Tudor Room 8 and 9, Royal York Hotel, Toronto.

Printed in Canada

Oshawa The Oshawa Group Limited