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THE PAGURIAN CORPORATION

ANNUAL REPORT 1988



Board of Directors

Christopher Ondaatje
Chairman and Chief Executive Officer
The Pagurian Corporation Limited
Toronto

Timothy W. Casgrain
Managing Partner
Hees International Bancorp Inc.
Toronto

David J. Hennigar
Chairman
Crownx Inc.
Toronto

John M. Judson, Q.C.
Partner
Shibley, Righton & McCutcheon
Toronto

Willard J. L'Heureux, Q.C.
Managing Partner
Hees International Bancorp Inc.
Toronto

Michael F. B. Nesbitt
President
Montrose Investment Co. Ltd.
Winnipeg

Danesh K. Varma
President and Managing Director
American Resource Corporation Limited
Bermuda

Manfred J. Walt
Managing Partner
Hees International Bancorp Inc.
Toronto

Officers

Christopher Ondaatje
Chairman and Chief Executive Officer

Timothy W. Casgrain
President and Chief Operating Officer

Brian D. Lawson
Vice President Finance

John M. Judson, Q.C.
Secretary

Corporate Information

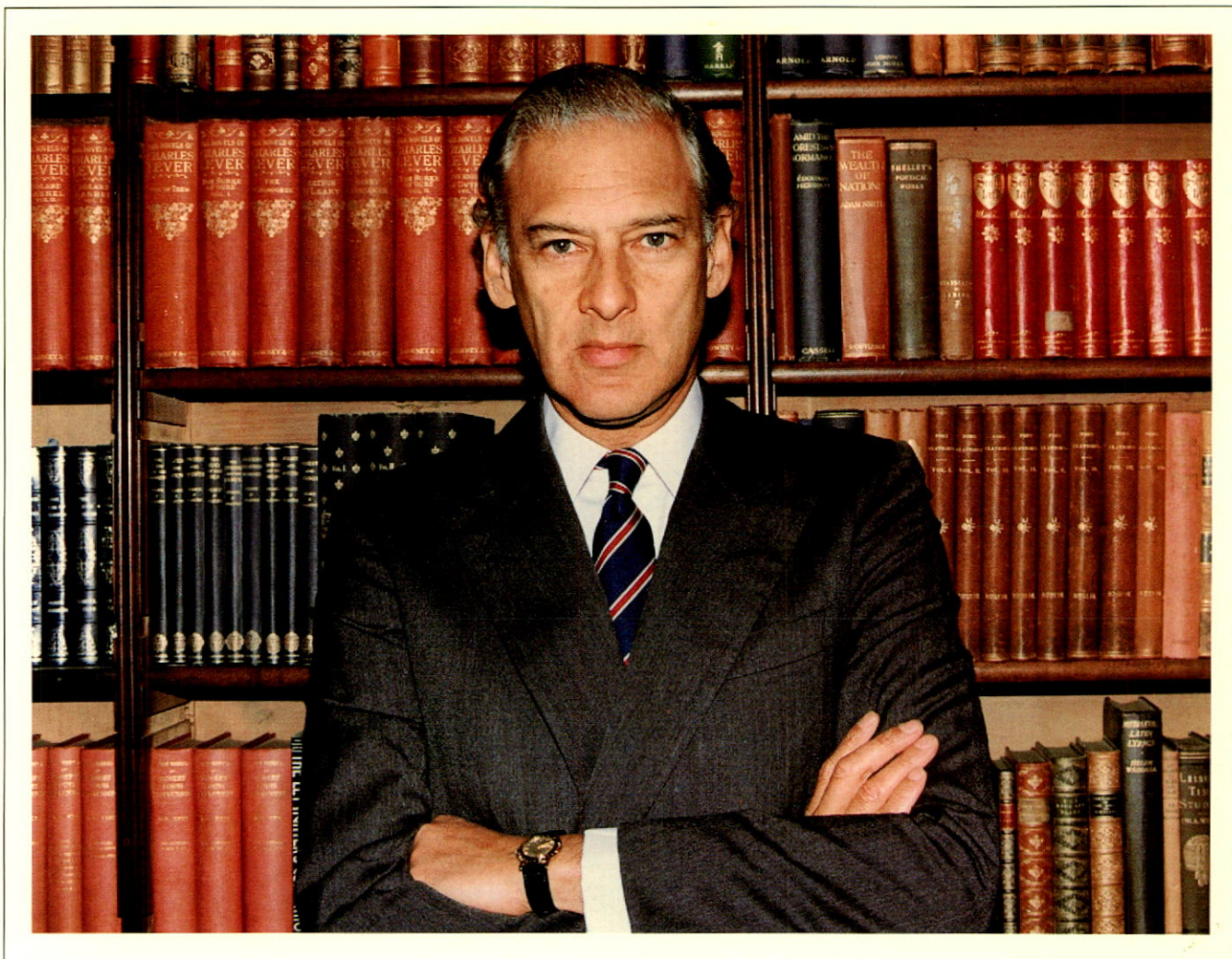
Corporate Office
13 Hazelton Avenue
Toronto, Ontario M5R 2E1
Telephone Number: (416) 968-0255
Facsimile Number: (416) 969-9394

Auditors
Touche Ross & Co.
Toronto, Canada

Exchange Listing
The Toronto Stock Exchange

Registrar and Transfer Agent
The Royal Trust Company
Suite 3900
Royal Trust Tower
Toronto, Ontario M5W 1P9

Annual Meeting
11 a.m., May 23rd, 1989
Commerce Hall
Commerce Court, Concourse Level
King & Bay Streets
Toronto, Ontario



Chairman's Report to Shareholders

Pagurian maintained its twenty-one year record of sustained growth in 1988. Gross revenues for the year ended December 31, 1988 grew to \$107 million from \$100 million and net income was \$89.2 million compared with \$88.5 million in the previous year. Net income per share was \$1.81 in 1988 and \$1.80 per share in 1987.

Your Company's performance for the five years ended December 31, 1988 resulted in average annual compound growth rates in gross revenues, net income and income per share of more than 25% per annum. During the same period, assets grew at the rate of 37% from \$96 million to \$457 million at historical cost and 25% based on market values.

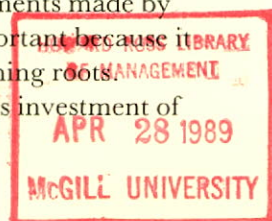
All three of the operating divisions —

communications, merchant banking and corporate finance continued to be profitable and contributed to the growth in income and assets during the year.

OPERATING HIGHLIGHTS

During 1988, your Company added to its communications interests, which include publishing, fine arts and portfolio investments, with the acquisition of all the shares of the internationally acclaimed Canadian publisher Lester & Orpen Dennys Limited. Although small in size when compared with some of the investments made by Pagurian in recent years, it is important because it returns the Company to its publishing roots.

In March 1988, Pagurian sold its investment of



8.3 million common shares and \$15 million preference shares of Hees International Bancorp to Canadian Express Limited in exchange for \$93.5 million preferred shares, a demand note in the sum of \$93.9 million and \$12.3 million cash. By July, Canadian Express had completed a public distribution of 8.3 million warrants, each entitling the holders to purchase one common share of Hees

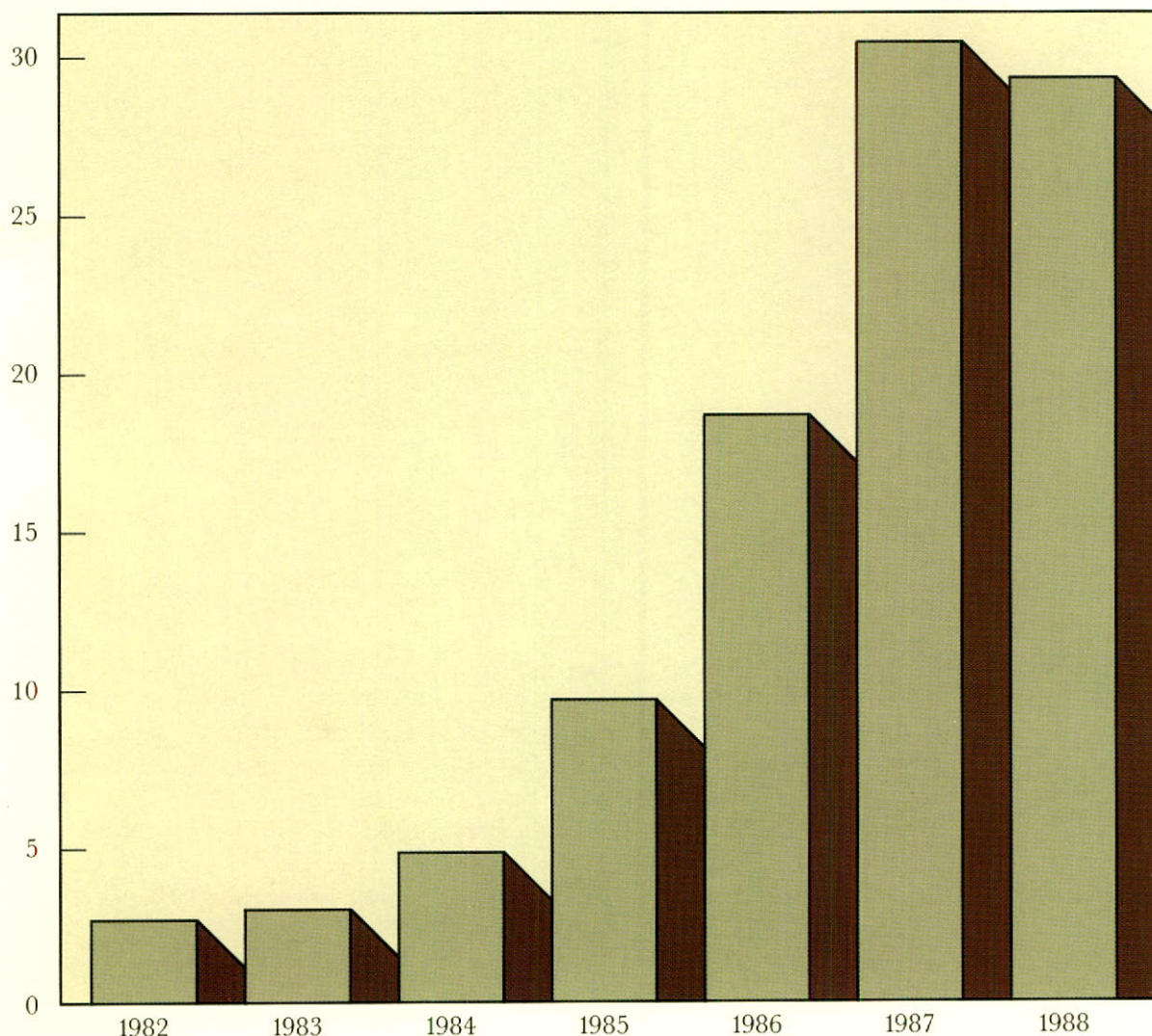
International Bancorp by July 1991 for \$23.50 each. This transaction raised \$46.5 million for Canadian Express' treasury with the expectation of another \$195.1 million being received by July 1991. Annual Hees dividends will continue to be received by Canadian Express until July 1991.

In February, Canadian Express increased its equity interest in American Resource Corporation

THE PAGURIAN CORPORATION LIMITED

\$
(Millions)

Dividend Payout



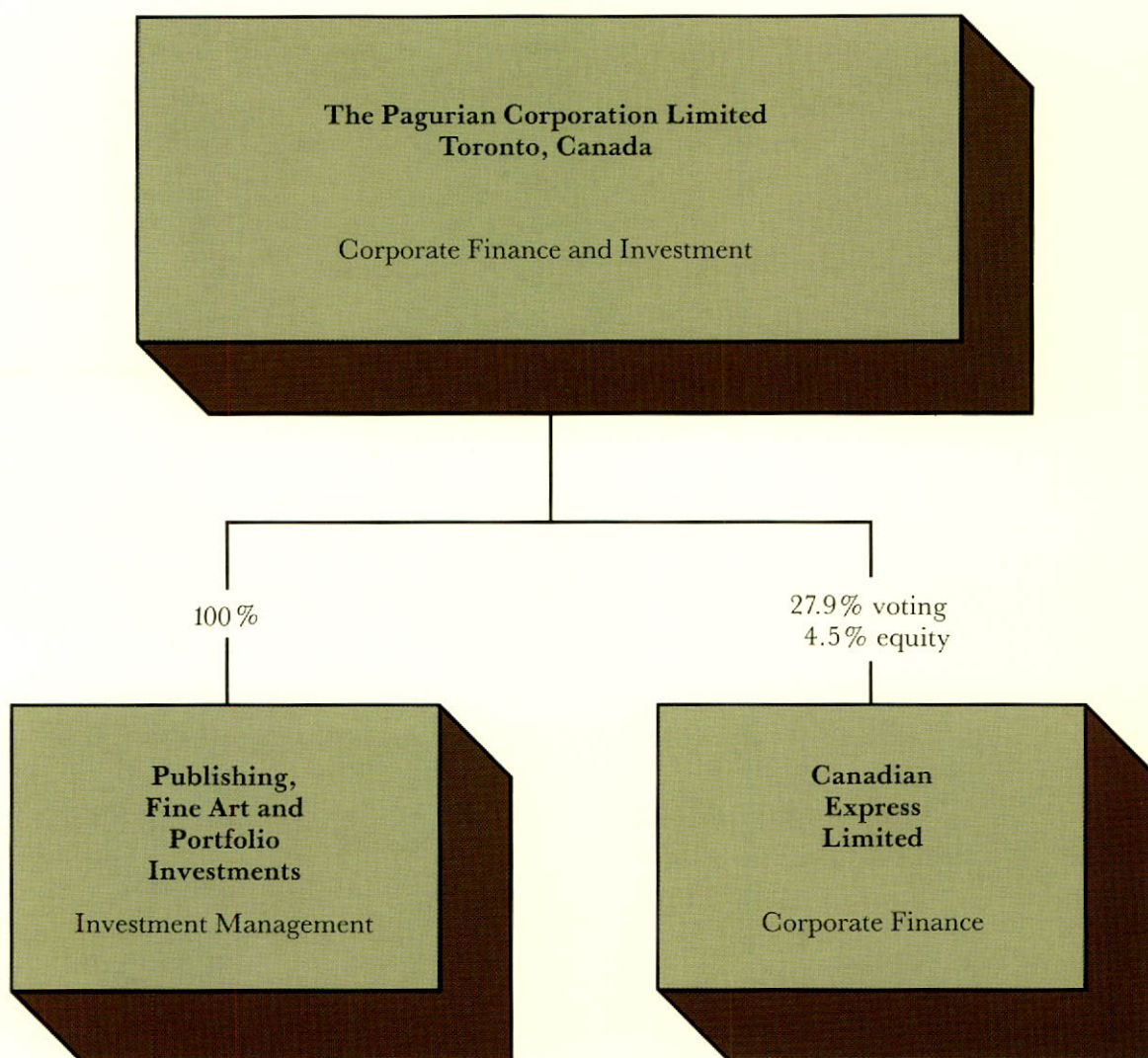
Limited from 34.7% to 96.4% by issuing 54.5 million common shares. By December 31, the minority interest had been reduced to 1.1% by purchasing American Resource Class A shares for cash through the facilities of the Montreal Exchange.

During 1988, Canadian Express also increased its investment in The Enfield Corporation Limited, a company Pagurian sponsored in 1984, to

approximately 30%. Subsequent to the year end, Enfield completed a private placement of 5 million of its common shares diluting Canadian Express' interest and requiring Canadian Express to acquire a further 2.2 million common shares through open market purchases to maintain Canadian Express' interest in Enfield above the 30 percent level. Enfield's principal investments are controlling

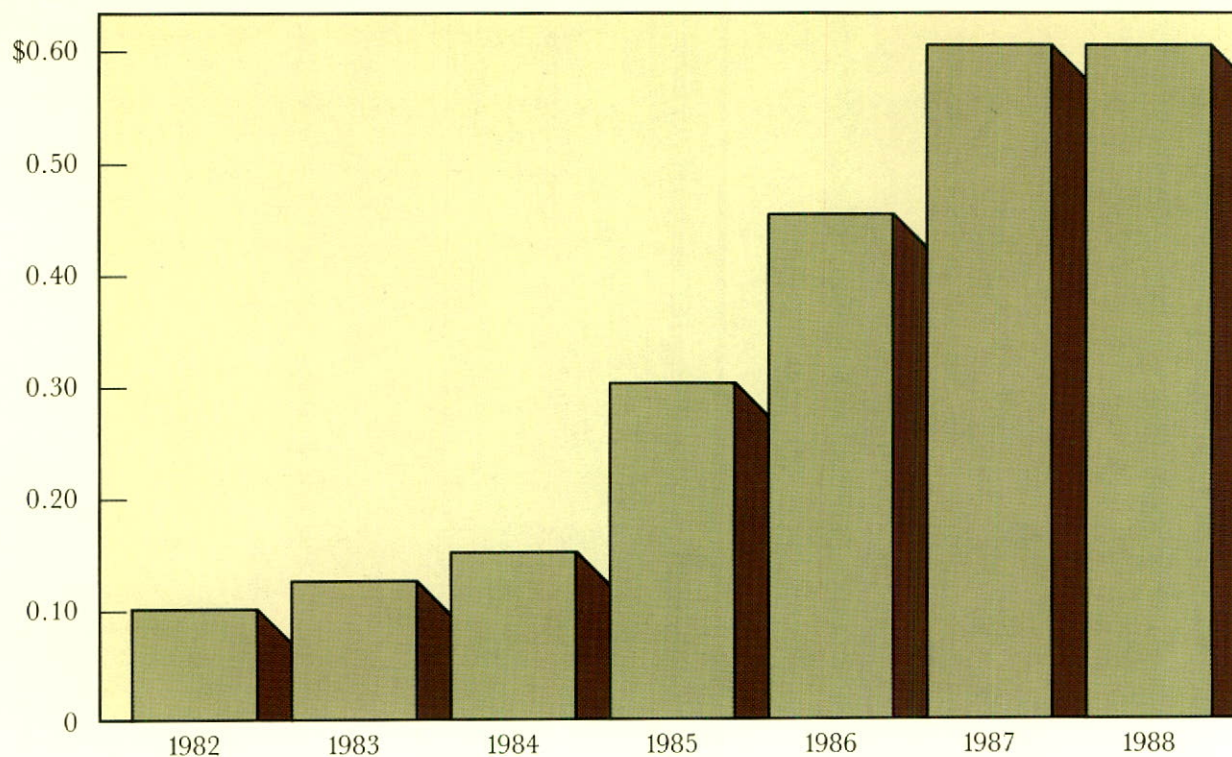
THE PAGURIAN CORPORATION LIMITED

Operating Structure

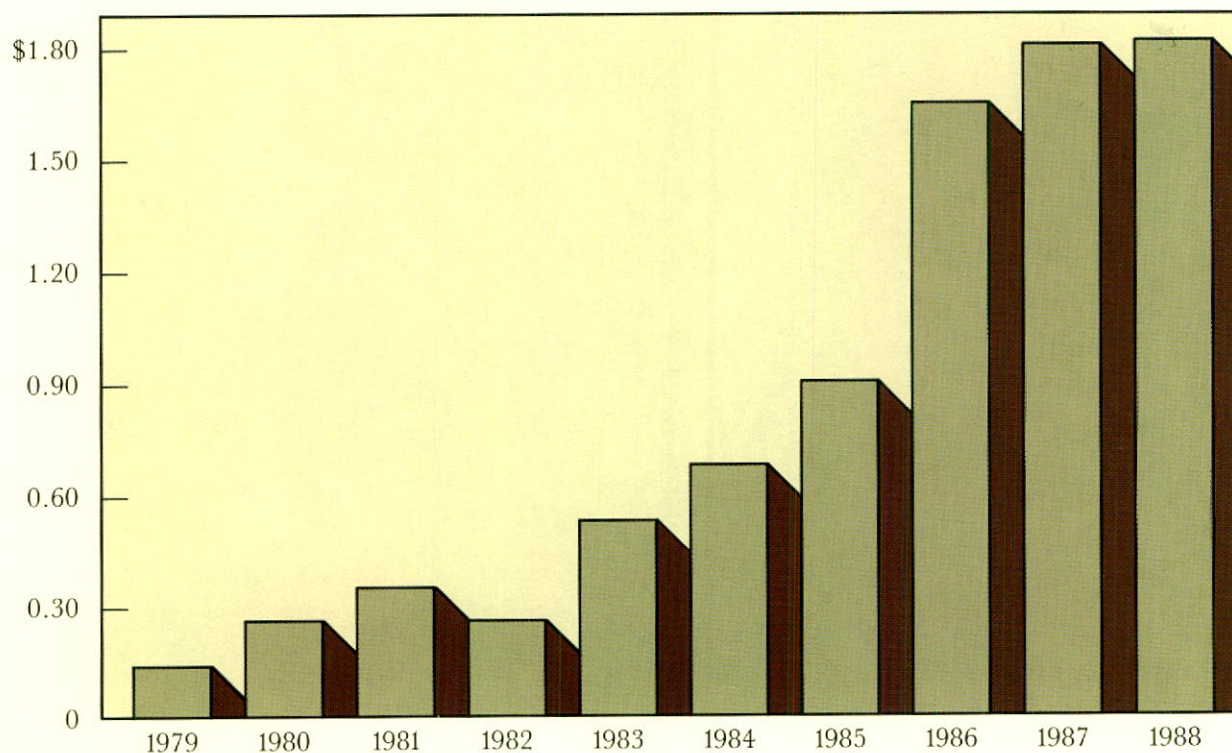


THE PAGURIAN CORPORATION LIMITED

Dividend Per Share



Net Income Per Share*



*Based on weighted average number of shares, net of reciprocal shareholdings.

interests in Consumers Packaging Inc., Federal Pioneer of Canada, Numac Oil & Gas, Complax Corporation and Tarxien Corporation.

PROPOSED RESTRUCTURING

Consideration is being given to exchanging Pagurian's interest in Canadian Express for cash and common shares of Hees International Bancorp. These discussions are at a preliminary stage and will require regulatory and other approvals. This is intended to be a first step in unwinding the interlocking ownership between Pagurian and Canadian Express. In completing this transaction, it is expected that Pagurian will also collect \$167 million on its present loans to Canadian Express.

THE PAST AND THE FUTURE

On December 16, 1988 Hees International Bancorp was invited to become a co-manager of Pagurian, following its acquisition of a half interest in Canadian Corporate Services Limited, a private management services company and a major shareholder of Pagurian.

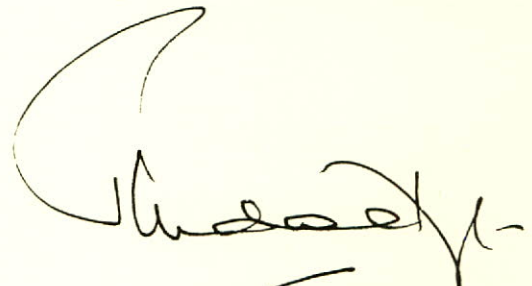
It is a matter of immense personal pride and satisfaction that Pagurian has grown in twenty-two years from assets of \$3,000 to \$457 million and from generating net income of \$2,700 to \$89.2 million. Furthermore, this record has been achieved without the use of debt and by only making nine investments over the period from the cash flow initially generated from the publishing and fine arts businesses. In accordance with a generous dividend policy

established over the years, the annual dividends per share were increased from 5 cents in 1982 to 60 cents in 1988 after adjusting for two 2:1 stock splits in 1980 and in 1985.

Given the substantially increased size of the Company and the new investment climate Pagurian is likely to face in the years ahead, it is imperative that there be a smooth transition in the management of Pagurian. It is these concerns that have led to the new association with Hees International Bancorp, one of the most broadly based merchant banks in North America. It is noteworthy that Pagurian's close association with Hees International Bancorp extends over a number of years and that Pagurian's investment in Hees has contributed approximately one-third of the Company's cumulative earnings and one-half of the total assets of Pagurian during this period.

The growth and evolution of Pagurian has only been possible because of the support of shareholders, Directors and staff. I am extremely grateful for your confidence and loyalty.

On behalf of the Board of Directors

A handwritten signature in black ink, appearing to read 'Christopher Ondaatje', with a large, sweeping initial 'C'.

Christopher Ondaatje
Chairman and Chief Executive Officer

THE PAGURIAN CORPORATION LIMITED

Consolidated Balance Sheet

AS AT DECEMBER 31, 1988

(thousands of dollars)

Assets

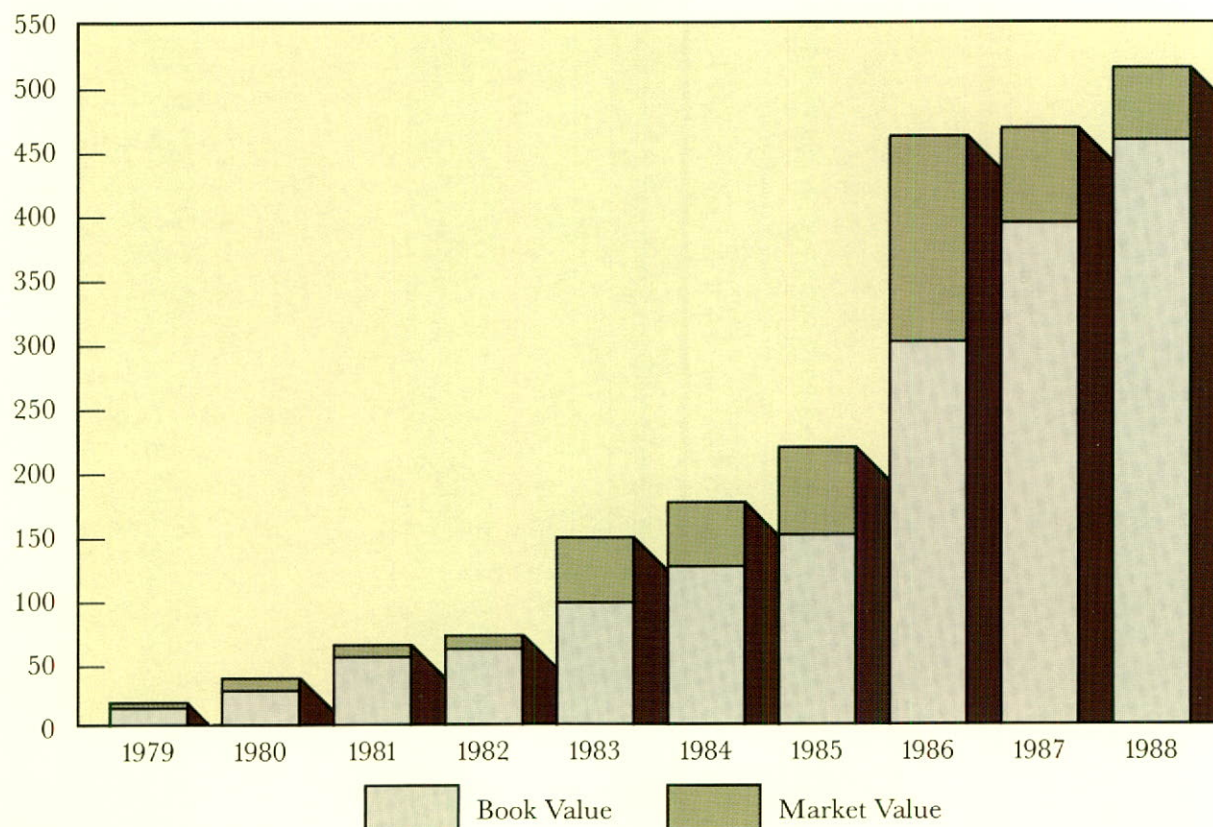
	1988	1987
Cash and securities	\$ 71,762	\$124,751
Loans and accounts receivable (Note 2)	173,486	6,439
Corporate investments (Note 3)	206,620	255,188
Inventories	3,500	2,805
Other	<u>2,056</u>	<u>2,308</u>
	<u>\$457,424</u>	<u>\$391,491</u>

The accompanying notes are an integral part of these consolidated financial statements.

THE PAGURIAN CORPORATION LIMITED

\$
(Millions)

Total Assets



Liabilities

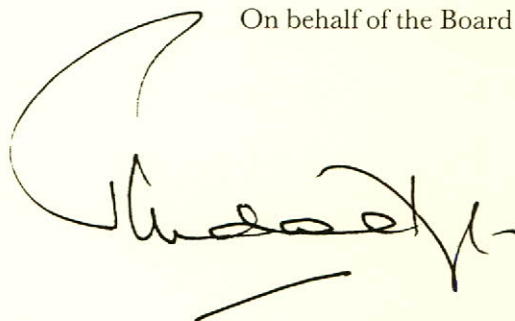
	1988	1987
Accounts payable and other liabilities	\$ 7,253	\$ 2,153
Income taxes payable	<u>4,115</u>	<u>1,500</u>
	<u>11,368</u>	<u>3,653</u>

Shareholders' Equity (Note 5)

<u>446,056</u>	<u>387,838</u>
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<u>\$457,424</u>	<u>\$391,491</u>
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On behalf of the Board



Christopher Ondaatje
Director



Michael F.B. Nesbitt
Director

THE PAGURIAN CORPORATION LIMITED

Consolidated Statement of Income

FOR THE YEAR ENDED DECEMBER 31, 1988

(thousands of dollars except per share data)

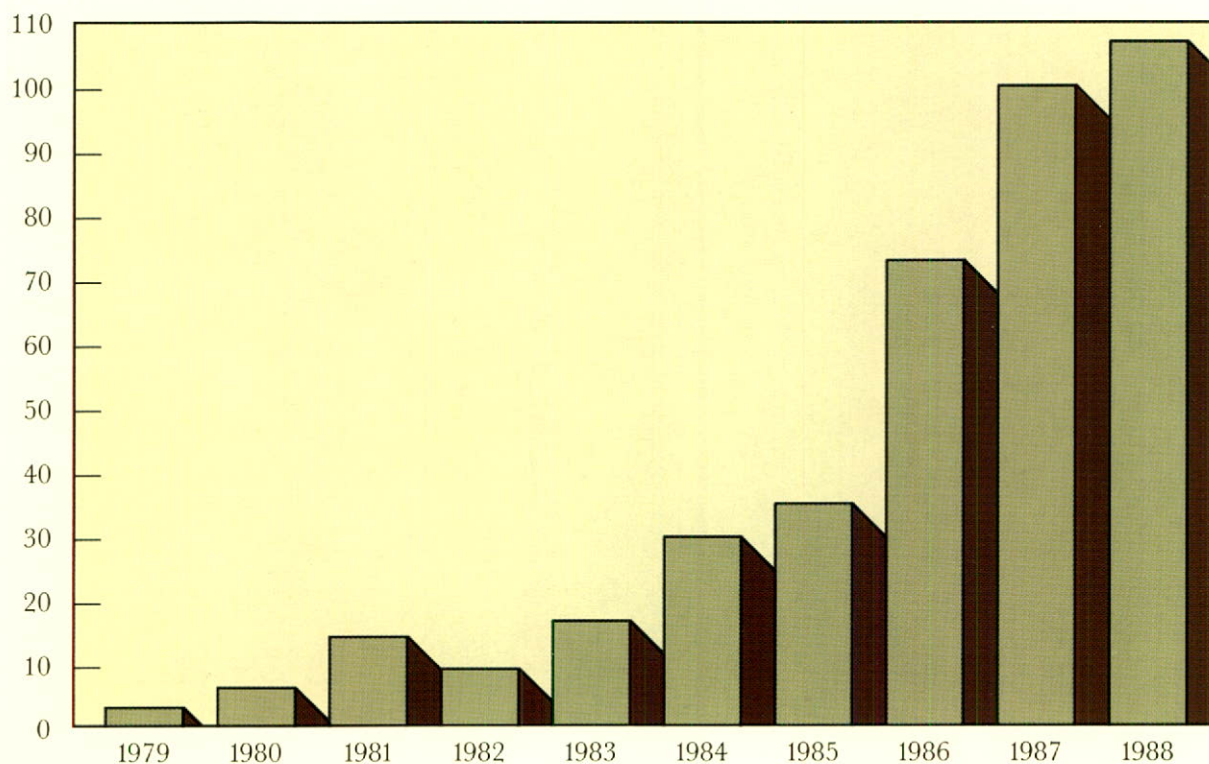
	1988	1987
Revenue		
Publishing and fine art	\$ 1,787	\$ 475
Corporate investments (Note 4)	88,296	82,182
Dividends, interest and other	16,896	17,385
	<u>106,979</u>	<u>100,042</u>
Expenses		
Operating and administrative	8,491	5,299
Income taxes	9,317	6,284
	<u>17,808</u>	<u>11,583</u>
Net income	<u>\$ 89,171</u>	<u>\$ 88,459</u>
Net income per share	<u>\$ 1.81</u>	<u>\$ 1.80</u>

The accompanying notes are an integral part of these consolidated financial statements.

THE PAGURIAN CORPORATION LIMITED

\$
(Millions)

Total Revenue



Consolidated Statement of Retained Income

FOR THE YEAR ENDED DECEMBER 31, 1988

(thousands of dollars)

	1988	1987
Balance at beginning of year	\$166,005	\$112,847
Net income	<u>89,171</u>	<u>88,459</u>
	255,176	201,306
Dividends paid	(29,560)	(30,335)
Premium on shares repurchased	<u>—</u>	<u>(4,966)</u>
Balance at end of year	<u>\$225,616</u>	<u>\$166,005</u>

Consolidated Statement of Changes in Financial Position

FOR THE YEAR ENDED DECEMBER 31, 1988

(thousands of dollars)

	1988	1987
Funds provided from operations		
Net income	\$ 89,171	\$ 88,459
Gains	(58,261)	(51,500)
Equity earnings, net of dividends received	(4,465)	(10,035)
Other	<u>387</u>	<u>1,548</u>
	26,832	28,472
Receivables, inventories and liabilities	<u>7,069</u>	<u>(7,168)</u>
	<u>33,901</u>	<u>21,304</u>
Funds used in financing		
Capital stock, net	<u>(1,393)</u>	<u>37,038</u>
Funds used in investing		
Loans receivable	(167,058)	(1,960)
Corporate investments	105,417	(50,124)
Fixed assets	<u>5,704</u>	<u>(148)</u>
	<u>(55,937)</u>	<u>(52,232)</u>
Dividends	<u>(29,560)</u>	<u>(30,335)</u>
Cash and securities		
Decrease	(52,989)	(24,225)
Balance, beginning of year	<u>124,751</u>	<u>148,976</u>
Balance, end of year	<u>\$ 71,762</u>	<u>\$124,751</u>

The accompanying notes are an integral part of these consolidated financial statements.

Notes to Consolidated Financial Statements

FOR THE YEAR ENDED DECEMBER 31, 1988

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation

Principles of consolidation

These consolidated financial statements include the accounts of the company and its wholly-owned subsidiaries.

Reciprocal shareholdings

These consolidated financial statements are adjusted to reflect the company's interest in its Class A non-voting and Class B voting special shares held by significantly influenced companies.

Net income per share

Net income per share is based on 49,350,000 (1987 – 49,230,000) Class A non-voting and Class B voting special shares being the weighted average number outstanding during the year, net of reciprocal shareholdings.

Comparative figures

Certain comparative figures have been reclassified to conform with current presentation.

Translation of foreign currencies

Foreign currency assets and liabilities are translated into Canadian dollars at rates of exchange prevailing at the balance sheet date except for inventories, investments, fixed assets and shareholders' equity which are translated at historic rates. Revenue and expenses are translated at the average rate of exchange for the year and any resultant translation gains and losses are included in dividends, interest and other revenue.

Cash and securities

Cash and securities are valued at the lower of cost and their estimated market value with any adjustment required charged to dividends, interest and other revenue.

Corporate investments

Corporate investments represent major equity positions acquired with the intention of enhancing their value over time. These investments are accounted for on an equity basis when significant influence is considered to exist and on a cost basis when significant influence is considered not to or

ceases to exist. For equity accounted investments, the difference between the purchase price and the proportionate share of net assets acquired is allocated to the underlying investments and adjusted when appropriate.

Inventories

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

Income taxes

The company provides for income taxes based on accounting income regardless of when such income is subject to taxes under tax law. The carrying value of certain investments acquired from affiliates in exchange for shares issued by the company is in excess of their tax cost base and no provision has been made for potential taxes on this excess which might arise should the company dispose of these investments on a non-tax deferred basis.

2. LOANS AND ACCOUNTS RECEIVABLE

Loans receivable include \$1,910,000 (1987 – \$2,500,000) of accrued dividends, \$165,166,000 (1987 – \$223,000) due on demand from Canadian Express Limited and \$2,202,000 (1987 – \$1,997,000) due under the company's management share purchase plan.

3. CORPORATE INVESTMENTS

	1988 (000's)	1987 (000's)
Canadian Express Limited	\$220,983	\$125,845
Reciprocal shareholdings	(14,363)	(12,970)
	206,620	112,875
Hees International Bancorp Inc.	—	142,313
	<u>\$206,620</u>	<u>\$255,188</u>

Canadian Express Limited

The investment is comprised of 5,000,000 common shares and four series of preferred shares representing a 4.5% equity interest (1987 – 5.7%) and a 27.9% direct voting interest (1987 – 38.5%). At year end, the common shares had a carried value of \$4,658,000 (1987 – \$1,603,000) and a market value of \$4,400,000 (1987 – \$4,750,000). The preferred

shares have a carried value of \$216,325,000 (1987 – \$124,242,000), a par value of \$243,500,000 (1987 – \$150,000,000), are redeemable at par and are convertible into common shares as follows:

Number of Shares	Series	Par Value	Common Shares Issued on Conversion
16,666,667	Series I	\$ 50,000,000	16,666,667
30,769,231	Series II	\$100,000,000	30,769,231
1,000,000	Series III	\$ 38,500,000	35,000,000
1,000,000	Series IV	\$ 55,000,000	not convertible

The dividend rate for the Series I and Series II cumulative preferred shares is 10% and for the Series III and Series IV cumulative preferred shares is based on the prime lending rate with a minimum rate of 8% and a maximum rate of 12%. The Series IV preferred shares participate in common dividends in excess of dividends otherwise receivable based on prime. The participation feature allows for the holder to receive the greater of the dividend based on prime and the dividend on fifty common shares for each preferred share.

Hees International Bancorp Inc.

During the year, the company sold 8,300,000 common shares valued at \$184,675,000 and \$15,000,000 Class AA Preference Shares Series A of Hees to Canadian Express Limited for consideration comprised of cash in the amount of \$12,278,826, a demand note in the amount of \$93,896,174 bearing interest at the prime lending rate and the balance in Series III and Series IV preferred shares of Canadian Express.

A gain of \$52,797,000 was recognized on this transaction and was included in income from corporate investments. In addition, the company included in its income for the year \$4,565,000 (1987 – \$14,760,000) of equity accounted earnings.

4. INCOME FROM CORPORATE INVESTMENTS

Corporate investment income consists of:

	1988 (000's)	1987 (000's)
Disposition and dilution gains	\$53,930	\$51,500
Preferred dividends	23,046	14,880
Loan interest	6,755	797
Equity earnings	<u>4,565</u>	<u>15,005</u>
	<u>\$88,296</u>	<u>\$82,182</u>

5. SHAREHOLDERS' EQUITY

Share capital consists of:

Authorized

Unlimited	Preference shares, issuable in series
Unlimited	Class A non-voting shares
400,000	5% Class B voting preference shares
338,000	Class B voting special shares, convertible on a one-for-one basis into Class A non-voting shares
100	Common shares

Issued

	1988 (000's)	1987 (000's)
50,000,000 Class A non-voting shares	\$234,787	\$234,787
338,000 Class B voting special shares	16	16
Retained income	225,616	166,005
Reciprocal shareholdings	<u>(14,363)</u>	<u>(12,970)</u>
	<u>\$446,056</u>	<u>\$387,838</u>

During the year, 400,000 5% Class B preference shares were redeemed.

6. OTHER INFORMATION

The effective tax rate of the company differs from the combined federal and provincial tax rate as follows:

	1988 %	1987 %
Combined federal and provincial income tax rate	48.0	52.1
Non-taxable equity earnings and gains	(28.4)	(36.6)
Non-taxable dividend income	(11.3)	(8.9)
Other	<u>1.1</u>	<u>—</u>
	<u>9.4</u>	<u>6.6</u>

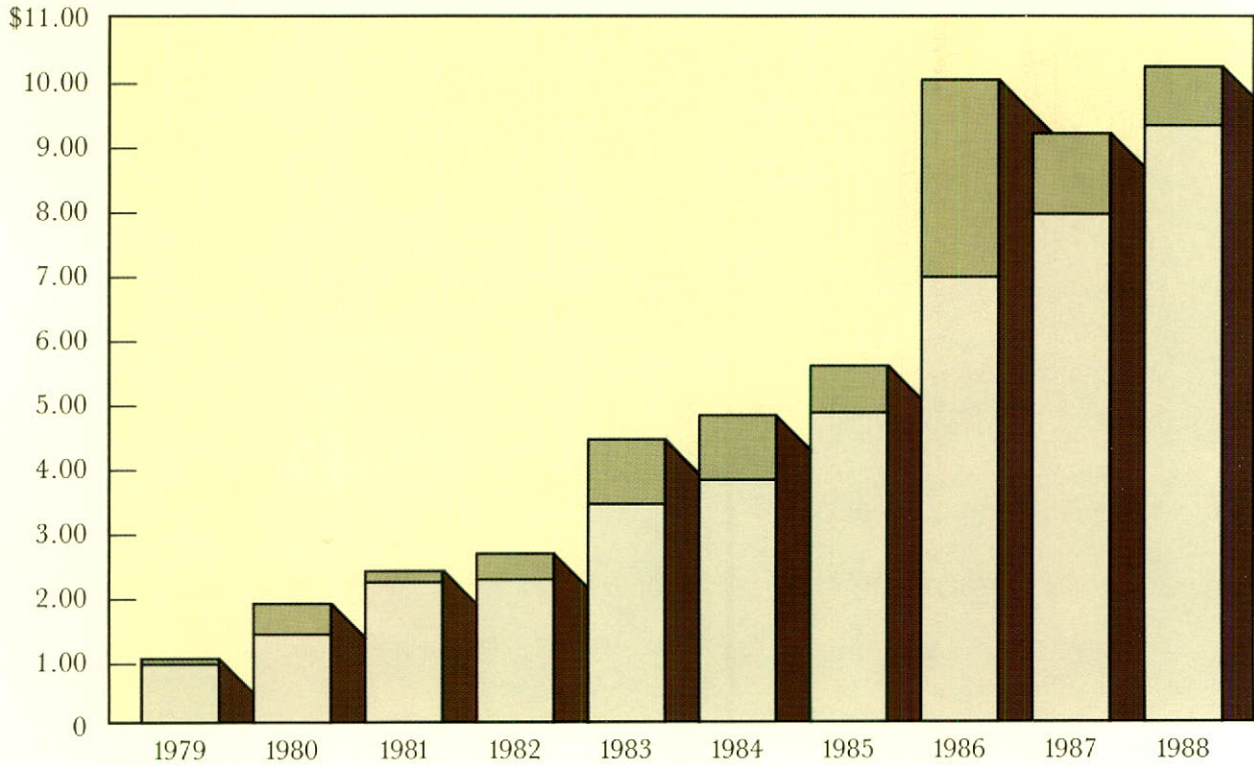
The business affairs of the company are managed by Canadian Corporate Services Limited ("CCSL") for a fee of up to 5 percent of the consolidated pre-tax net income of the company. CCSL holds a 66% voting interest and an 8% equity interest in the company.

Cash and securities have a market value which approximates their cost of \$71,762,000 at December 31, 1988 (1987 – \$124,751,000).

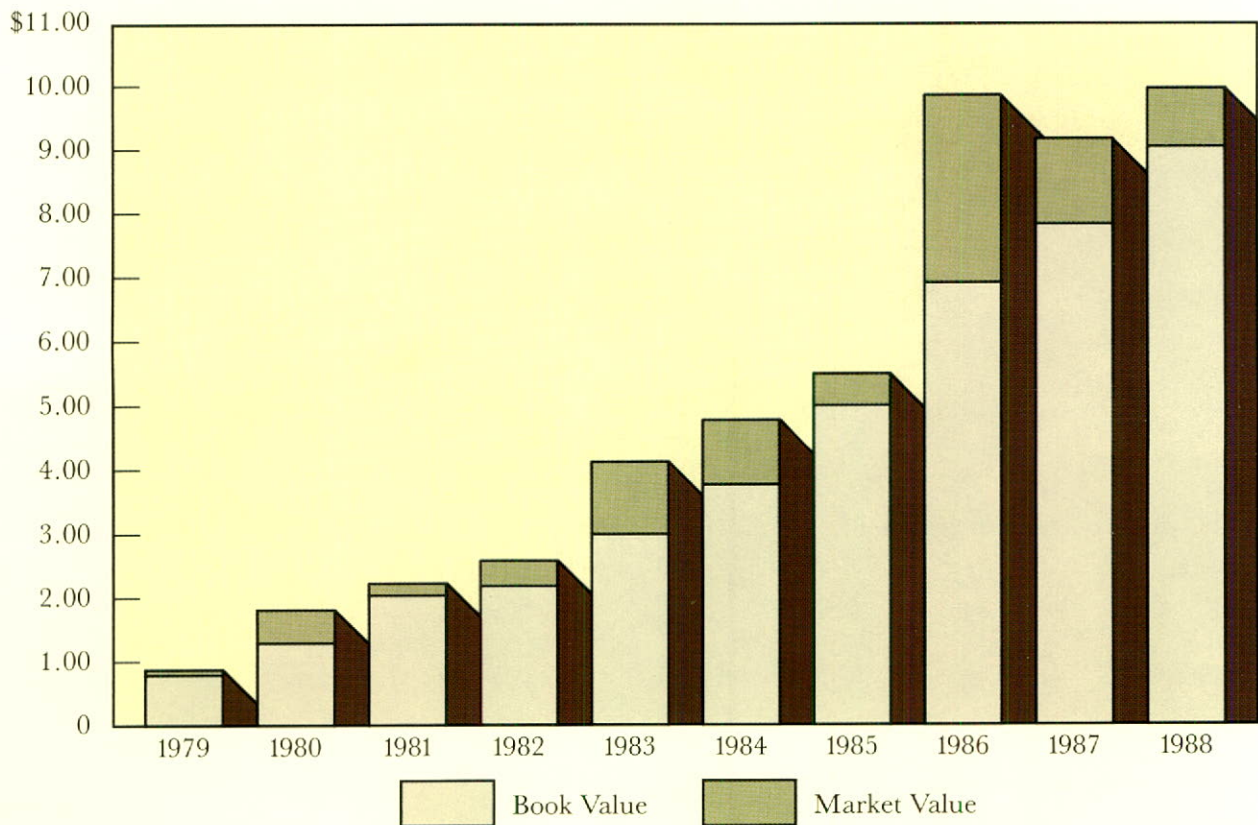
In the ordinary course of business the company carries on transactions with its affiliates which are at normal market terms. At December 31, 1988, cash and securities included \$50,000,000 (1987 – \$Nil) of securities of affiliates. Income from loans to affiliates amounted to \$6,610,000 (1987 – \$423,000).

THE PAGURIAN CORPORATION LIMITED

Assets/Share



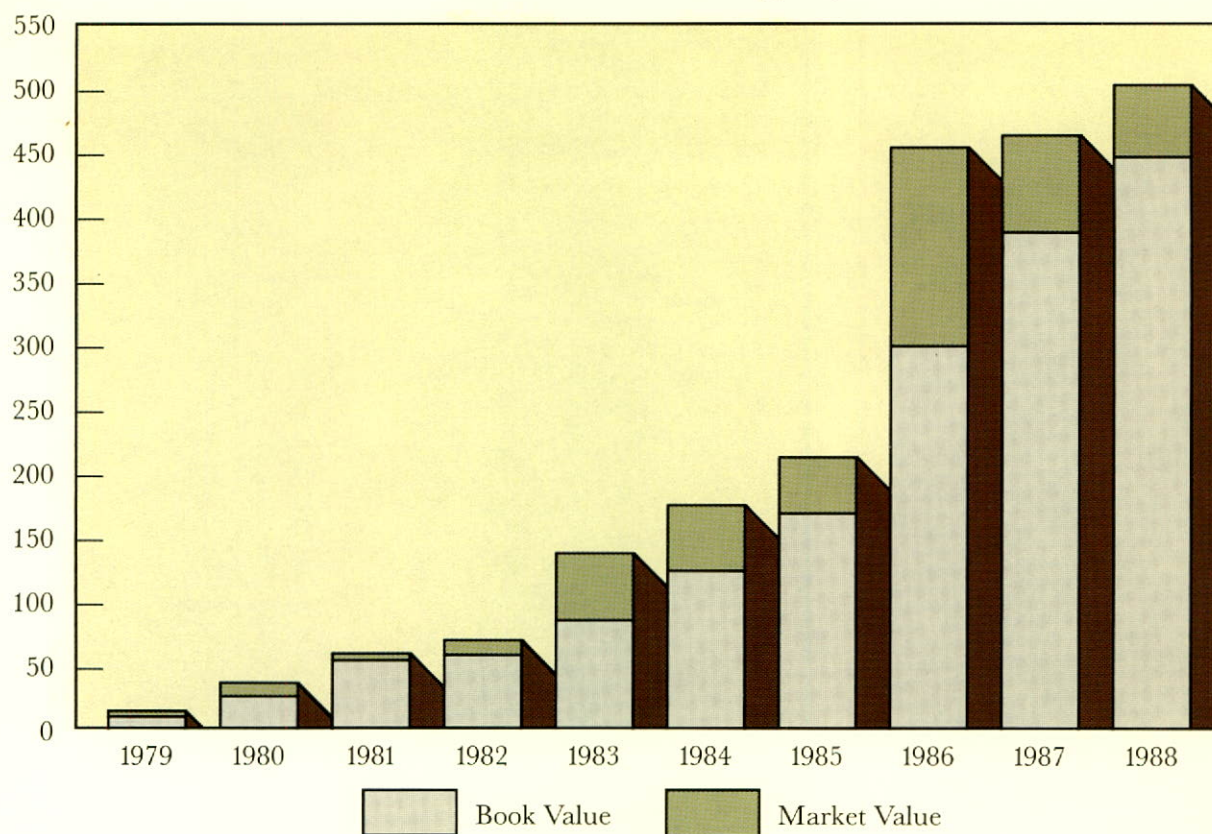
Equity/Share



THE PAGURIAN CORPORATION LIMITED

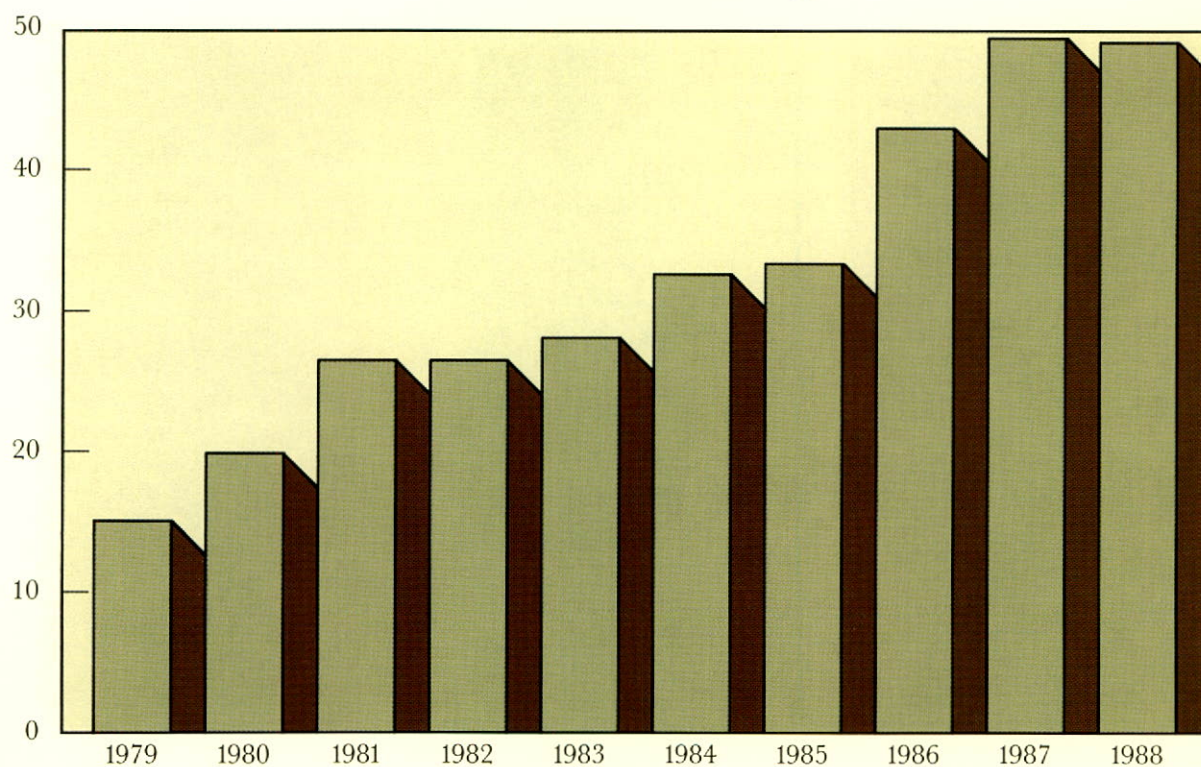
\$
(Millions)

Shareholders' Equity



(Millions)

Shares Outstanding*



*Based on outstanding shares at year-end, net of reciprocal shareholdings.

THE PAGURIAN CORPORATION LIMITED
(and Predecessor Companies Including
Pagurian Press Limited)

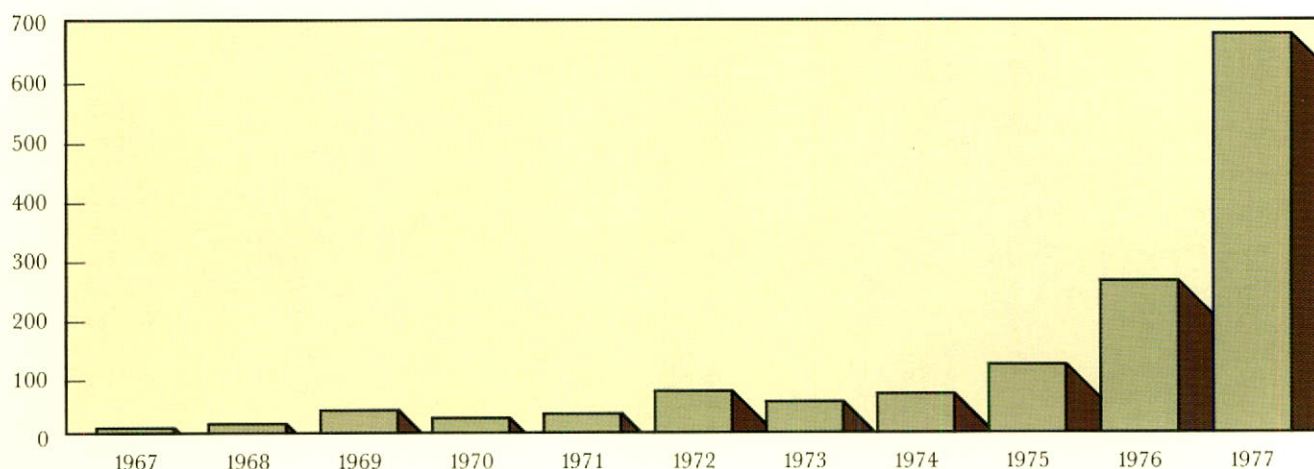
Statistical Review of Operations

AUGUST 17, 1967 TO DECEMBER 31, 1988

	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976	1977
Publishing and fine art											
Revenue	\$ 29,321	\$ 49,095	\$ 43,592	\$ 73,165	\$ 79,738	\$ 194,197	\$ 213,424	\$ 420,823	\$ 472,774	\$ 788,729	\$ 771,539
Direct expenses	24,820	35,773	22,866	50,043	54,755	126,600	141,277	306,323	371,749	551,123	572,749
Gross profit	4,501	13,322	20,726	23,122	24,983	67,597	72,147	114,500	101,025	237,606	198,790
Investments											
Realized gains		5,432	11,583	21,965	18,726	12,826		15,384	60,627	186,869	622,512
Dividend and interest income	87	1,034	1,006	4,818	4,844	875	5,139	28,348	36,883	143,626	152,202
	87	6,466	12,589	26,783	23,570	13,701	5,139	43,732	97,510	330,495	774,714
Interest expense			110	60	133					69,548	73,022
	87	6,466	12,479	26,723	23,437	13,701	5,139	43,732	97,510	260,947	701,692
	4,588	19,788	33,205	49,845	48,420	81,298	77,286	158,232	198,535	498,553	900,482
Administrative expenses	658	2,374	4,949	5,873	7,061	12,504	22,627	70,193	84,177	165,491	239,116
	3,930	17,414	28,256	43,972	41,359	68,794	54,659	88,039	114,358	333,062	661,366
Income taxes	1,244	4,700	6,700	12,300	8,800	21,777	14,858	26,606	35,543	75,230	(12,168)
	2,686	12,714	21,556	31,672	32,559	47,017	39,801	61,433	78,815	257,832	673,534
Corporate investments											
Greywood Publishing			17,078	(4,578)	963	(415)	(25,631)	5,583			
Modern Canadian Library						25,973	39,424	673	36,706		
Black Photo Corporation											
Westdale Oil & Gas											
American Resource Corporation											
Hees International Bancorp											
Enfield Corporation											
Canadian Express (International)											
Canadian Express Limited											
Net income	\$ 2,686	\$ 12,714	\$ 38,634	\$ 27,094	\$ 33,522	\$ 72,575	\$ 53,594	\$ 67,689	\$ 115,521	\$ 257,832	\$ 673,534

\$
(Thousands)

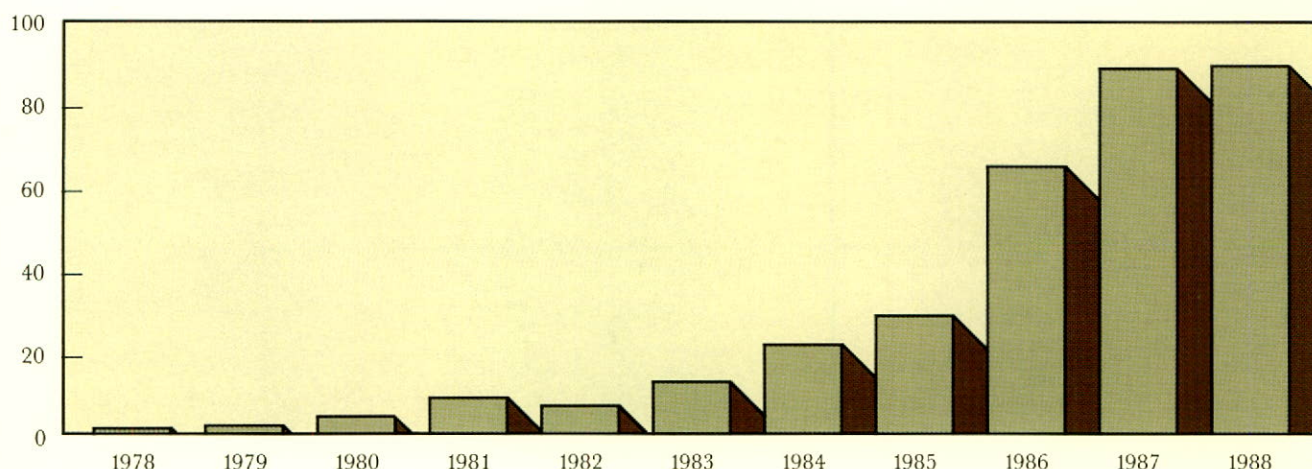
Net Income



<i>1978</i>	<i>1979</i>	<i>1980</i>	<i>1981</i>	<i>1982</i>	<i>1983</i>	<i>1984</i>	<i>1985</i>	<i>1986</i>	<i>1987</i>	<i>1988</i>
\$ 838,038	\$ 399,286	\$ 225,156	\$ 568,423	\$ 306,519	\$ 184,748	\$ 305,592	\$ 346,080	\$ 646,198	\$ 475,030	\$ 1,787,302
706,270	250,106	153,152	328,554	214,119	182,552	244,059	246,912	573,037	415,765	1,755,050
131,768	149,180	72,004	239,869	92,400	2,196	61,533	99,168	73,161	59,265	32,252
934,055	1,725,349	3,959,636	8,789,464	3,714,178	11,844,053	11,559,717	15,657,703	4,404,547	5,997,983	4,488,113
346,269	165,630	730,763	4,149,513	2,958,066	3,450,983	6,114,083	7,367,692	16,421,638	27,064,025	40,739,051
1,280,324	1,890,979	4,690,399	12,938,977	6,672,244	15,295,036	17,673,800	23,025,395	20,826,185	33,062,008	45,227,164
130,114	242,940	435,927	1,000,000		189,786	3,832,734	40,008			
1,150,210	1,648,039	4,254,472	11,938,977	6,672,244	15,105,250	13,841,066	22,985,387	20,826,185	33,062,008	45,227,164
1,281,978	1,797,219	4,326,476	12,178,846	6,764,644	15,107,446	13,902,599	23,084,555	20,899,346	33,121,273	45,259,416
263,713	230,160	219,275	435,055	897,104	1,265,779	1,763,936	1,705,886	3,634,402	4,883,010	5,266,146
1,018,265	1,567,059	4,107,201	11,743,791	5,867,540	13,841,667	12,138,663	21,378,669	17,264,944	28,238,263	39,993,270
(45,276)	201,646	898,577	3,451,447	1,086,966	2,527,271	2,123,018	4,300,011	4,042,766	6,284,000	9,317,000
1,063,541	1,365,413	3,208,624	8,292,344	4,780,574	11,314,396	10,015,645	17,078,658	13,222,178	21,954,263	30,676,270
	723,632	1,341,417	152,209							
			135,994	14,995						
			372,972	2,121,335	1,269,195	173,024				
						11,156,000	7,709,300	13,535,650	14,760,000	55,945,000
						452,000	3,487,974	20,249,785	51,500,000	
							525,000	1,880,050		
								15,985,344	245,000	2,550,000
\$ 1,063,541	\$ 2,089,045	\$ 4,550,041	\$ 8,953,519	\$ 6,916,904	\$ 12,583,591	\$ 21,796,669	\$ 28,800,932	\$ 64,873,007	\$ 88,459,263	\$ 89,171,270

\$
(Millions)

Net Income



Auditors' Report
TO THE SHAREHOLDERS OF
THE PAGURIAN CORPORATION LIMITED

We have examined the consolidated balance sheet of The Pagurian Corporation Limited as at December 31, 1988 and the consolidated statements of income, retained income 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 company as at December 31, 1988 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.

Toronto, Canada
March 31, 1989



Chartered Accountants

About the Front Cover



THE DEATH OF WOLFE

after Benjamin West, oil on canvas, c. 1815

96.5 cm. by 132.1 cm., from the Pagurian Collection

George III wished to buy it, but had to be content with the second version. Sir Joshua Reynolds criticised it at first, but later confessed “....I foresee that this picture will not only become one of the most popular, but will occasion a revolution in art.”

Reynolds was correct. *The Death of Wolfe* by Benjamin West, for all its inaccuracies and departure from tradition, has become one of the best known paintings of an historical event. With this picture West's future and fortune were assured. He was commissioned to paint six other versions, and was appointed History Painter to the King.

The subject matter, and the manner in which the scene is depicted, are in themselves unusual. West broke with tradition when he chose to show an historical event in which the characters wear contemporary attire. It was customary to depict such events with the participants clad in the guise of Classical heroes. But it is more startling that the scene, as

revealed by West, was a total creation of his imagination, even to the curious fact that the portrait of the dying general is no portrait at all.

The truth of the matter is that Wolfe died attended by two soldiers, a Lieutenant Browne and Volunteer Henderson of the Louisbourg Grenadiers, and Hewit, a surgeon's mate. Such a scene was neither romantic nor dramatic enough for the death of a young general at the point of victory. So West surrounded the hero with most of the prominent officers of the campaign, mourning soldiers, runners bearing news of victory, and an Indian.

Such criticism aside, the painting was, as predicted by Reynolds, a startling success and the demand for copies or prints was great. One such copy, painted by an unknown hand in the early 19th century, is from the Collection of Historical Canadian Paintings assembled by The Pagurian Corporation. It is a fine example, and is a faithful rendition of the original.

