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ANNUAL REPORT 1987

NOVA Corporation of Alberta

Incorporated in the province of Alberta, NOVA is a major Canadian shareholder-owned energy company headquartered in Calgary. NOVA's areas of business include gas transportation and marketing, petrochemicals, petroleum, manufacturing, consulting and research.

In 1987, the Corporation's assets of $4.7 billion generated $2.3 billion in sales and $179 million in net income. The NOVA companies employ about 7,100 people in Canada, the United States, Europe and Pacific Rim countries.

1987 Operations

- Petrochemical operations increased output significantly and cut production costs as commodity prices improved.
- The Alberta Gas Transmission Division moved a record 2.35 trillion cubic feet in 1987, and our gas marketing subsidiary had total sales of 293 billion cubic feet, up 34% from 1986.

1987 Financial

- Consolidated net income rose to $179 million from $100 million in 1986.
- Fully diluted net income per common share was 67 cents compared with 12 cents in 1986.
- Common equity increased to $1.3 billion as a result of the conversion of preferred shares and warrants to common shares, the issue of convertible debentures, and improved earnings.
- Favourable refinancing arrangements reduced costs to shareholders and pipeline tariffs considerably.

CONSOLIDATED FINANCIAL HIGHLIGHTS

(Thousands of dollars except for share data)

Year Ended December 31	1987	1986	% Change
Financial			
Revenue	$2,322,438	$2,680,966	(13)
Operating Income	$ 528,198	$ 573,221	(8)
Net Income	$ 179,130	$ 100,197	79
Net Income to Common Shareholders	$ 129,834	$ 16,126	*
Net Income Per Common Share			
Basic	$ 0.70	$ 0.12	*
Fully diluted	$ 0.67	$ 0.12	*
Common Shares Outstanding (Thousands)			
At Year End	211,484	141,841	49
Average	185,321	134,655	38
Common Equity**	$1,302,797	$ 648,707	*
Per Share	$ 5.76	$ 4.22	36
Return On Average Common Equity	13.3%	2.7%	*
Dividends Per Common Share	$ 0.40	$ 0.40	—

**Exceeds 100%* ***Includes convertible debentures and warrants*

CONTENTS

THE NOVA LOGO

A-shaped for Alberta

Natural Gas Flame

Natural Gas Pipeline

Petrochemical Flask

Annual Meeting

NOVA Corporation of Alberta's annual meeting will be held on Tuesday, April 26, 1988, at 10:30 a.m. in the Calgary Convention Centre, 120 Ninth Avenue S.E., Calgary, Alberta.

Rapports annuels en français

Veuillez vous adresser au secrétaire de la Compagnie si vous désirez recevoir un exemplaire de la version française de ce rapport.

It is a pleasure to report significant improvement in the Corporation's results for 1987.

Net income rose to $179 million or 67 cents a share, of which $54 million or 20 cents a share was earned in the fourth quarter.

The improvement resulted mainly from higher output and reduced costs throughout the Corporation's main business operations. The recent trend of price recovery for polyethylene, which is the commodity most important to NOVA's financial results, has been a positive factor. All of these favourable trends continue further, in early 1988.

Refinancing initiatives have lowered interest and preferred share dividend expense and have added to the Corporation's readiness to make the best of any foreseeable financial market and economy circumstance. A conservative financial strategy is being followed for the late 'eighties.

While there is genuine concern about worldwide economic conditions during the next few years, our earnings in 1988 are continuing to grow. NOVA gas transmission and petrochemical sectors are well based in Canada, and are very productive and efficient operations. We have a good opportunity to use our large investments in these two sectors to achieve record earnings in 1988, and in future years.

As a company relatively young with a large capital base, we believe that the management of assets is steadily improving.

The quarterly common share dividend, which was maintained at 10 cents per share during our lean earnings period of 1985 through mid-1987, is once again covered more than amply by current earnings and a dividend increase can be considered during 1988.

Pipelines, Petrochemicals and Petroleum

In the 1970s and early 1980s, we built NOVA's assets and revenues by making those investments which were perceived available and best at the time. During that period of aggressive growth, we moved into several new businesses which were seen as related to one another.

Some of those have proved to be highly desirable after several years of experience, while other investments and some project proposals have turned out to be relatively less relevant or timely than we intended and therefore have been disposed of, terminated or in some cases simply deferred for future performance when they may achieve better economic results.

The core business of NOVA itself has developed to be gas pipelines and petrochemicals. In those two businesses our people are experienced and proficient and have shown highly competitive abilities to work successfully in domestic and world markets. In each of those sectors, NOVA has shown that its organization is proficient at each stage including research and analysis, project conception, financing, project management and construction, operations, marketing and sales, and earning profits. Our application and development of new technology and production skills has become well recognized in the demanding and increasingly competitive world marketplace.

So NOVA goes forward in 1988, 1989 and 1990 as basically a pipeline and petrochemical company.

Some of our related and continued business lines such as valve manufacture have proven to be profitable even under the most difficult of industry conditions and will be maintained as supplementary activities. A small amount of our capital structure—but not more than one or two percent of our total assets—continues to be devoted to endeavouring to establish new and balancing business positions such as in NovAtel Communications Ltd.

The one other large investment position which NOVA maintains is its shareholding in Husky Oil Ltd. We see that and our smaller natural gas production investment in Novalta Resources Ltd. as maintaining a good position in the future evolution of Canadian-based oil and natural gas exploration and production, which should be very promising for the 1990s.

Husky is a medium-sized but very aggressive Canadian integrated oil company owned and equally controlled by NOVA and the Hong Kong-based group of companies led by Mr. Li Ka-shing. We believe that we will obtain really good future growth of asset values and financial performance through Husky.

Review of 1987

The earnings improvement in 1987 followed several years of depressed earnings linked mainly to low world petrochemical commodity prices and the start-ups of major investments. NOVA's common share price increased as the markets recognized both improved operating results and the inherent financial strength and stability of NOVA's businesses. Earnings for 1987 slightly exceeded management's 1987 budgeted expectations.

Additional small investments in ethylene and polyethylene facilities yielded significant improvements in production levels in 1987. These gains were augmented by strong operating performance which further exceeded expanded design capacity. Polyethylene operations also benefited from new marketing initiatives in Pacific Rim countries, significant engineering improvements and reduced feedstock costs. A sharp improvement in the price of methanol, which occurred in the second half of the year, allowed the Medicine Hat methanol complex to resume profitable full-scale production.

NOVA's gas transportation and marketing division continued to make steady and substantial contributions to earnings. A record 2.35 trillion cubic feet of natural gas was transported in and across Alberta in 1987, up over 10% from 2.13 trillion cubic feet in 1986. Early in 1988, a new record day receipt of 9.20 billion cubic feet was recorded. These volumes rank among the two or three largest throughput levels for pipeline systems in North America. The Corporation's marketing subsidiary, Pan-Alberta Gas Ltd., led the growth in export volumes among all Canadian marketers.

Late in 1987, NOVA elected to exercise its option to increase its ownership of Husky Oil Ltd. to 42.5% from 24.4% held after completion of the Husky reorganization earlier in the year. Husky was reorganized as a private company governed by a shareholder agreement, with ownership/control held equally by NOVA and a publicly traded Hong Kong company group. We believe this

◀ *From its head office in Calgary, Alberta, NOVA is active worldwide in pipeline transportation, petrochemical production and marketing, oil and gas exploration and development, and related manufacturing ventures.*

A substantial gain in NOVA's 1987 overall performance was due largely to major successes in both operating and marketing initiatives by the Corporation's petrochemical business.

arrangement will enhance our ability to achieve corporate goals and objectives for oil and gas investment.

In September 1987, NOVA completed the corporate restructuring of share equity initiated in the second quarter to provide its shareholders with rights and a share structure reflective of the major corporation NOVA has become. As a result, Class "B" common shares have been redeemed at par value and Class "A" common shares have been designated as common shares with full voting rights. The restructuring also provided for an increase in the number of NOVA directors up to 20, changed the corporate name to NOVA Corporation of Alberta and continued the Corporation under the Alberta Business Corporations Act.

Outlook for 1988

There are good prospects being developed for major investment and earnings growth for the future, some of which may be ready to start in 1988. The first of these could be the "Ethylene III project" which plans a 50% expansion of our ethylene production capacity in Alberta plus investment by NOVA and other international companies in a group of ethylene-using derivative plants in Alberta. The proposed investment, totalling over $1.5 billion by all participants, is subject to satisfactory assurance of ethane supply presently under review by the Energy Resources Conservation Board relating to the Alberta Government's policy. There is also the prospect of another round of major expansion of our natural gas pipeline facilities to transport a new higher level of deliveries of Alberta natural gas to the United States.

Husky Oil Ltd., which had already built a good position in recent years for increased Canadian oil production in the 1990s, is actively investigating additional opportunities for new investment action.

Such new investment expansion prospects could each add materially to further improvement of NOVA's results. However, each NOVA commitment will weigh the effects on current financial results as well as the additions to long-term asset position. NOVA has already earned a bright business future so we will approach with care our further building of a well-balanced, highly competitive and cost-efficient independent Canadian company positioned selectively for international and domestic trade.

Before considering such new prospects, NOVA's consolidated budget for capital expenditures in 1988 is $360 million, which includes $250 million for Alberta gas transmission facilities and $70 million for continuing capital programs to increase production and efficiencies in petrochemical plants.

On January 28, 1988, the Corporation announced its intention to acquire 24.8% of the voting shares of Polysar Energy & Chemical Corporation. The acquisition of these shares reflects the Corporation's assessment of the value of the shares as an investment, based on the earnings of Polysar Limited, a wholly owned subsidiary of Polysar Energy & Chemical Corporation involved in petrochemical production and marketing. On February 22, 1988, the Corporation acquired 13,004,175 shares of Polysar to hold 19,004,175 shares representing approximately 31% of the common shares or 24.8% of the total voting securities of Polysar.

Management Direction

NOVA management highlights the following 1988 objectives:

- To concentrate our investment opportunities in three sectors: pipelines, petrochemicals and through our affiliated company, Husky Oil Ltd., in petroleum.
- To achieve earnings per share in excess of $1 per common share which would result in a return on common equity in excess of 17%, up from 13% for 1987.
- To continue rigorous control of expenses and overhead costs.
- To finance expansion conservatively and maintain or improve the current long-term debt to common equity ratio of 1.9 to 1.
- To improve operations and products with cost-effective applied research and development at a level of at least 5% of after-tax profit.
- To maintain an early lead in pipeline engineering, petrochemical commodities and telecommunications in China and other Asian markets.
- To maintain a high standard of environmental, safety and fair and productive employment practice in all NOVA companies.

Board and Management

Mr. Ronald B. Coleman, consultant, joined the Board in June 1987. In February 1988, the Board received with regret and appreciation of their services the resignations of Messrs. Edward W. Best and John R. McCaig as directors.

The two executive vice presidents of NOVA, Messrs. James H. Butler and William G. Wilson, were appointed to the Board in January 1988. Jim Butler and Bill Wilson have each made important contributions to NOVA's progress in the past year and have broadly increasing responsibilities in its management.

Our hard-earned franchise through Foothills Pipe Lines (Yukon) Ltd. for the current substantial movement of Alberta natural gas to the United States through its prebuild sections and for the future movement of natural gas supply from the northern gas production areas of North America will be even more highly valuable in the next years and has been maintained. These major projects were the responsibility of our president, Bob Pierce, who also chaired the energy sectoral committee advising the Government of Canada for the free trade negotiations with the United States.

The other officers, managers, professionals, technical, operations and office staffs in NOVA have done well again in 1987. They are commended for their many individual specific contributions to the improvements that we have the honour to record in this annual report.

Respectfully submitted on behalf of the Board of Directors,

S. R. Blair
Chairman and Chief Executive Officer

February 23, 1988

H.J.S. Pearson *P.L.P. Macdonnell, C.M.*
A.J.E. Child, O.C. *H.N. Hotchkiss*

S.R. Blair, C.C. — W.A. Howard — R.H. Carlyle — J.J. Healy — R.L. Pierce — J.R. McCaig — W.H. Comrie
F.A. McKinnon — R.B. Coleman — D.K. Seaman — E.W. Best

Edward W. Best
Partner, Foster Research, Calgary, Alberta
(Economic Research)

S. Robert Blair, C.C.
Chairman and Chief Executive Officer
of the Corporation

R. Harold Carlyle
Retired, Calgary, Alberta

Arthur J.E. Child, O.C.
Chairman and Chief Executive Officer,
Burns Foods Limited, Calgary, Alberta
(Food Processor)

Ronald B. Coleman
President, R.B. Coleman Consulting Ltd.,
Calgary, Alberta
(Oil and Gas Consulting)

William H. Comrie
Chairman,
The Brick Warehouse Ltd.,
Edmonton, Alberta
(Home Furnishings Distribution)

J. Joseph Healy
President, Healy Motors Limited,
Edmonton, Alberta (Transportation)

Harley N. Hotchkiss
President, Harman Resources Ltd.,
Calgary, Alberta (Private Investor—
Oil and Gas, Real Estate and Agriculture)

William A. Howard
Senior Partner, Howard, Mackie,
Calgary, Alberta
(Barristers and Solicitors)

Peter L.P. Macdonnell, C.M.
Partner, Milner & Steer,
Edmonton, Alberta
(Barristers and Solicitors)

John R. McCaig
Chairman and Chief Executive Officer,
Trimac Limited, Calgary, Alberta
(Transportation and Resource Services)

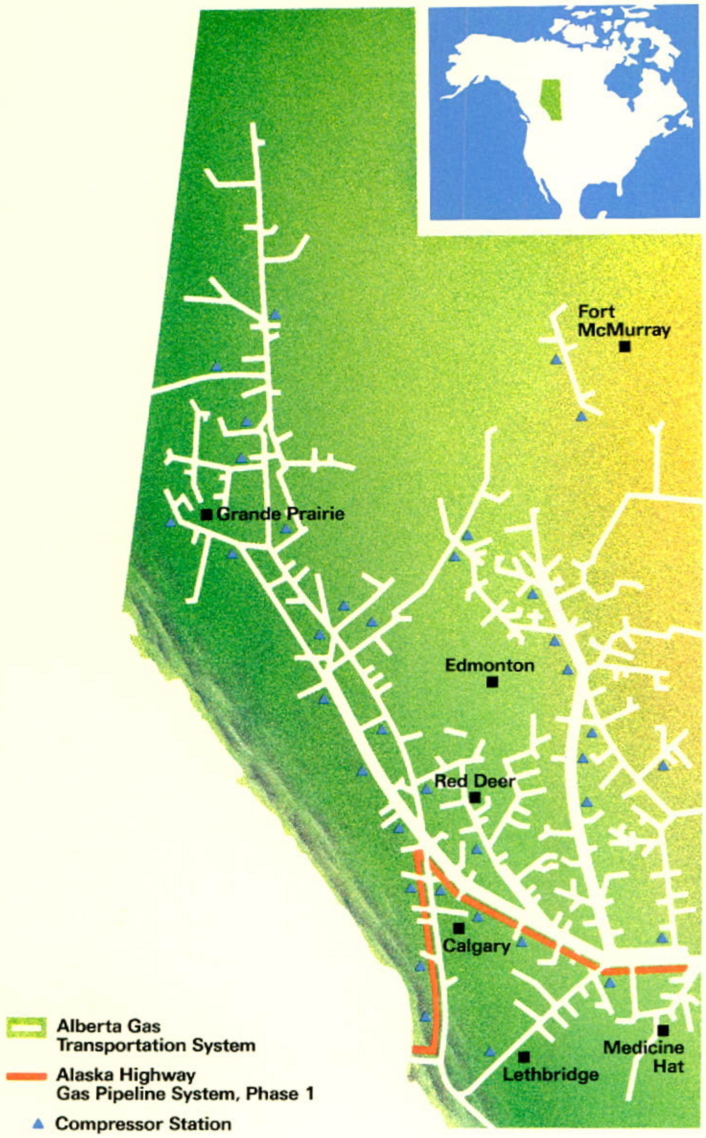
Fred A. McKinnon
Retired, Calgary, Alberta

H.J. Sanders Pearson
Vice Chairman of the Corporation;
Chairman, Century Sales & Service Limited,
Edmonton, Alberta
(Industrial Tools and Fasteners Distribution)

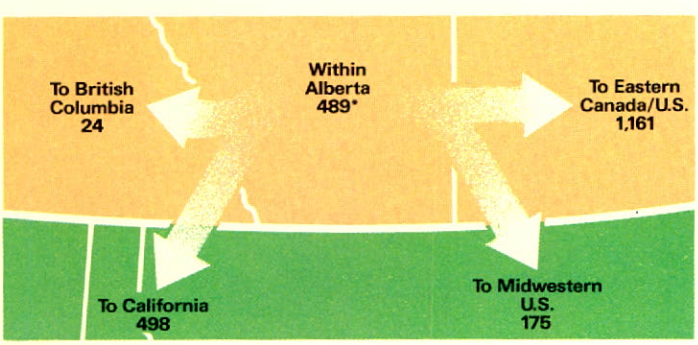
Robert L. Pierce
President of the Corporation

Daryl K. Seaman
Chairman and Chief Executive Officer,
Bow Valley Industries Ltd.,
Calgary, Alberta (Natural Resource
Services, Exploration and Development)

GAS TRANSPORTATION IN ALBERTA



NOVA SYSTEM GAS DELIVERIES
(Billion cubic feet–2,347 total)



**Includes pipeline usage*

Gas Transportation & Marketing

Total marketed Canadian gas production increased about 7% to an estimated 2.7 trillion cubic feet, largely because of increased demand from the United States.

Deregulation of natural gas pricing resulted in innovative marketing initiatives and extensive negotiations with end users which contributed to increased export sales of Canadian gas in 1987.

Average prices received by gas producers declined because of surplus supplies and intense competition for natural gas contracts in all markets.

Review of 1987

NOVA's investments in natural gas transportation and marketing include the gas transmission system in Alberta and Novacorp Pipelines Ltd., both 100% owned, and 50% ownership of Foothills Pipe Lines (Yukon) Ltd., Pan-Alberta Gas Ltd. and Trans Québec & Maritimes Pipeline Inc. In 1987, this sector comprised about half of the Corporation's consolidated assets and revenue and over 60% of operating income.

NOVA's Alberta pipeline system carries more than 10% of the gas produced annually in North America and over 75% of all marketed Canadian gas.

Total volumes transported through NOVA's Alberta system during the past calendar year were up over 10%, setting a new record of 2.35 trillion cubic feet. NOVA shipped 2.13 trillion cubic feet of gas in 1986 and 2.25 trillion cubic feet in 1985, the previous record year. Leading the increase were deliveries to the Alberta industrial market and to customers in California and the midwestern states.

Some 1.86 trillion cubic feet were exported from Alberta in 1987, including 497.8 billion cubic feet to California and 175.1 billion cubic feet to the U.S. midwest via the Foothills pipeline system. Deliveries in Alberta totalled 483.5 billion cubic feet, up 5% from 1986.

As a result of higher volumes, reduced financing charges and ongoing cost control, NOVA's transportation service rates for exports from the province averaged 25 cents per thousand cubic feet in 1987, down from 27 cents in 1986.

In August, NOVA reduced its rate of return on its $1.3 billion rate base for Alberta gas transportation operations to 11.49% from 12.91% because of initiatives taken to reduce financing costs. The new rate, set after discussions initiated by NOVA with its customers and other interested groups, incorporates a 13.25% after-tax return on a deemed 32% common equity component. NOVA has reduced its charges to the producing industry four times in as many years.

Pipeline investment in 1987 included expansion and improvements to the existing system, with capital spending of over $70 million. Approximately 123 miles of pipeline and related metering facilities were installed.

At December 31, 1987, NOVA's Alberta system comprised 8,805 miles of pipeline, 36 compressor stations and 825 major receipt and delivery points.

Novacorp Pipelines Ltd., 100% owned, builds, owns and operates pipelines on a contract basis to meet customer requests for service outside the parameters of NOVA's gas transmission system. In 1987, the company completed a 100-mile gas liquids pipeline in the Porcupine Hills area of southern Alberta. Novacorp Pipelines has total pipeline assets of about $30 million.

Phase I of the Alaska Highway Gas Pipeline system, owned and operated by Foothills, delivers Alberta gas to markets in the United States. The pipeline was built as the first phase of a major system to bring Alaska gas to market in the lower 48 states. The system's western leg operated at full capacity of 240 million cubic feet a day in 1987 and the eastern leg, with contracted capacity of 975 million cubic feet a day, operated at about 48% of contracted capacity. Throughput on the eastern leg increased in 1987 by 95%, primarily because of Pan-Alberta Gas marketing initiatives.

At December 31, 1987, the eastern and western legs comprised 528 miles of pipeline, four compressor stations and two meter stations. The rate of return was 10.9% on an average rate base of $631 million, with an after-tax return, excluding an incentive return, of 14.25% on a 25% equity component.

Pan-Alberta Gas, the largest independent Canadian marketer of gas to the United States, had total sales of 293 billion cubic feet in 1987, up 34% from 219 billion cubic feet in 1986. For the third year in a row, Pan-Alberta's customer in California purchased all of the gas allowed under its contract. About 88% of Pan-Alberta's gas sales are to the U.S. market.

Pan-Alberta has about 1,200 contracts with some 420 Alberta producers. During 1987, the company continued its adjustment to the deregulated environment by aggressively seeking new short- and long-term markets for Alberta gas.

Trans Québec & Maritimes Pipeline, which transports gas in the province of Quebec, carried about 93 billion cubic feet in 1987, up slightly from 90 billion cubic feet in 1986. At December 31, 1987, TQM facilities comprised 213 miles of pipeline, 10 meter stations and five sales taps. The rate of return is 13.11% on a rate base of $383 million, with a 13.75% after-tax return on a 25% equity component.

Outlook for 1988

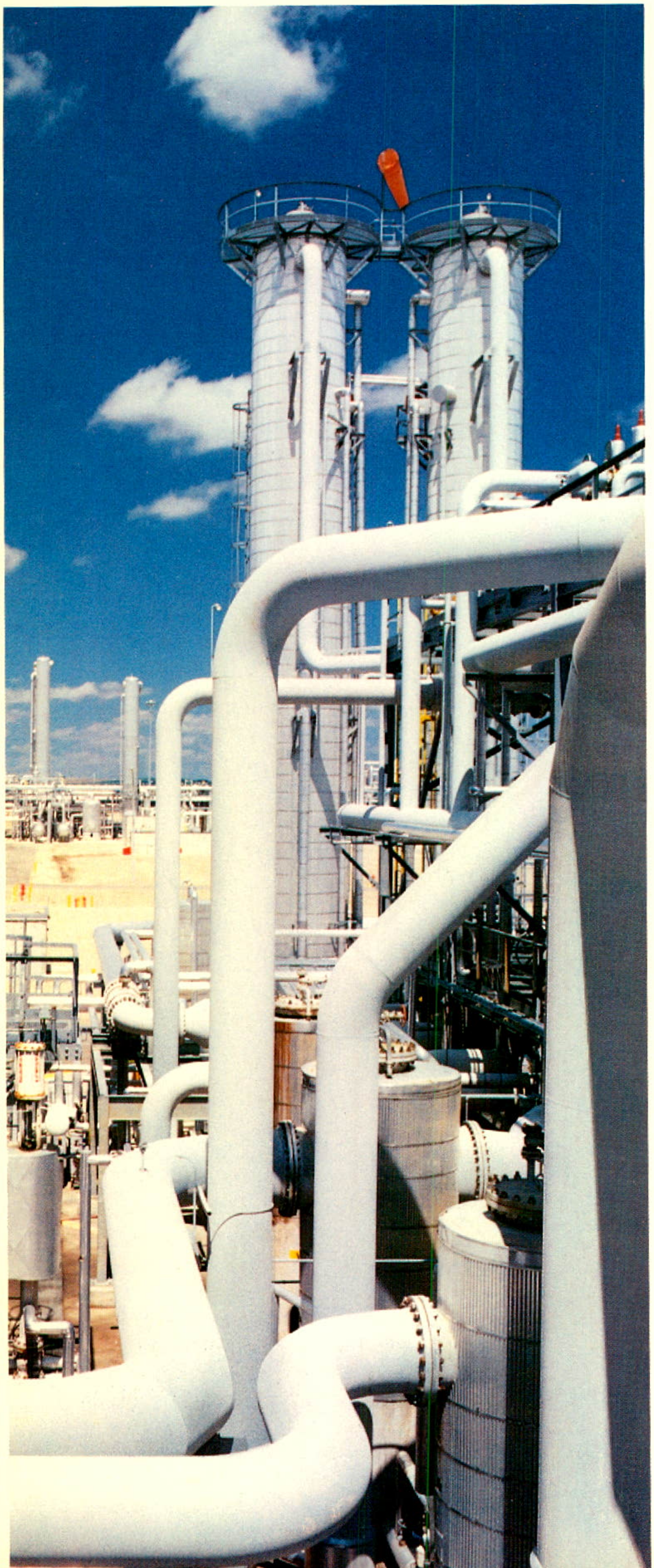
Increased demand for Alberta gas in both Canada and the United States is expected to spur increased gas transmission and marketing volumes for NOVA in 1988, with gas volumes projected to increase over 1987 record levels.

Capital spending on the pipeline system, driven by customer requests for increased capacity, is budgeted at about $250 million in 1988. Deregulation has resulted in continued growth in numbers of customers and contracts for the Alberta system and this trend is expected to continue in 1988.

Pan-Alberta expects to increase its sales in 1988 through continued aggressive marketing strategies. To accommodate anticipated volume increases, Foothills is expected to apply to the National Energy Board for permits to expand its eastern leg beyond current capacity of 1.1 billion cubic feet a day. The eastern leg was originally designed to carry 1.8 billion cubic feet a day, and can be expanded to the design capacity at relatively low cost.

Foothills remains committed to the completion of the Alaska Highway Gas Pipeline in the mid-1990s. Ongoing cost studies indicate the pipeline system will cost substantially less than originally envisaged.

NOVA moved record volumes of Alberta natural gas in 1987 as a result of increased demand for exports to the United States.



Petrochemicals

The petrochemical industry experienced a recovery in 1987 after several years of depressed prices linked to oversupply conditions around the world.

Increased demand for polyethylene, ethylene and methanol, NOVA's primary products, resulted in higher sales volumes and prices for these commodities. Polyethylene prices throughout the year were about 23% higher than in 1986. Growth in demand for polyethylene led both ethylene and polyethylene manufacturers to operate at capacity. Methanol prices also increased sharply, exceeding the 1986/87 average by 50% as demand came into balance with supply.

The improved demand results from new markets in developing countries and growth in the use of plastics in industrialized countries.

Review of 1987

NOVA's petrochemical investments include facilities for the production of ethylene, polyethylene and methanol from natural gas, as well as ethane extraction and gathering systems, product pipelines and storage facilities. In 1987, this sector accounted for about a quarter of the Corporation's consolidated assets, 44% of revenue and nearly 40% of operating income. These investments are managed by wholly owned Novacor Chemicals Ltd.

NOVA is the largest producer and marketer of ethylene and polyethylene in Canada, with about 58% of current Canadian ethylene capacity and 41% of polyethylene capacity. Ethylene, the major building block for the petrochemical industry, is made from ethane, which is extracted from natural gas. NOVA upgrades ethylene to produce a full range of polyethylene products. Petrochemical products are marketed in Canada, the United States, China and Pacific Rim countries.

Operating results for the petrochemical division improved substantially in 1987 due to gains in productivity, lower manufacturing costs and a strong upturn in world petrochemical markets.

◀ *Production of ethylene and polyethylene exceeded design capacity at NOVA's facilities near Joffre, Alberta, as the industry experienced strong recovery.*

NOVA's petrochemical investments showed significant improvement in operating results in 1987 and industry conditions are projected to continue strong in 1988.

Price increases for polyethylene—our major product—plus significant technological improvements and lower ethylene costs, allowed Novacor to increase production and cut costs during a period when worldwide product demand achieved balance with industry capacity.

NOVA's annual petrochemical plant capacity now stands at 3 billion pounds of ethylene, 800 million pounds of linear low-density polyethylene, 230 million pounds of high-density polyethylene and 200 million pounds of conventional low-density polyethylene. Two ethylene plants and a linear low-density polyethylene plant are located at Joffre, Alberta. NOVA also owns a polyethylene plant near Sarnia, Ontario.

The ethylene business, conducted under long-term, take-or-pay supply contracts with prices based on cost-related demand/commodity charges, continued to contribute steadily to profit. Production at the Joffre plants exceeded design capacity by an average of 5% in 1987. Higher operating rates allowed NOVA to provide lower cost ethylene to long-term customers.

Since the state-of-the-art ethylene and polyethylene plants were opened, significant cost savings and increases in throughput have been achieved. Ethylene capacity has been increased by 300 million pounds over the original design capacity without major capital investment. Polyethylene production capacity from the original Joffre plant has been increased by 200 million pounds, also at minimum cost, and during 1987, the plant operated at 5% above the new design capacity.

Additional programs are under way to further increase output from the ethylene plants and the Joffre polyethylene plant. At the Sarnia plant, changes to the product mix have yielded more efficient operations and plans are being implemented to increase output of specific polyethylene products.

Also during 1987, Novacor completed and began operating new facilities at Joffre, including a hydrogen plant and an addition for pelletizing polyethylene.

Hydrogen, formerly used as fuel in the ethylene plants, is recovered and sold for use in a nearby ammonia plant. Contracts provide assured return on investment plus coverage of both capital and operating costs. The pelletizing facility allows linear low-density polyethylene, previously available only in granular form, to be produced as a uniform product that can be shipped more cost effectively. Both projects were completed on time and under budget.

The petrochemical industry turnaround also improved operating conditions for NOVA's investments in production and marketing of methanol. NOVA owns 50% of Alberta Gas Chemicals Ltd., which operates three methanol plants at Medicine Hat, Alberta, with a combined design capacity of 2,400 short tons per day.

The most efficient plant, with design capacity of 1,200 short tons per day, continued operations throughout the year. On the strength of price increases late in the year, the other two plants were reopened and all three plants are operating at full production rates.

Outlook for 1988

NOVA's petrochemical interests will reflect a significant improvement in operating results as industry conditions continue to improve in 1988.

Polyethylene prices, which bottomed in mid-1986 then strengthened in 1987, are expected to remain strong and continued growth in demand is forecast. While demand strengthens, no significant new polyethylene capacity will be added to world production levels in 1988 and little new capacity will come on stream over the next four years.

Plans are under way to build a third ethylene plant once feedstock supplies can be assured and sales contracts signed for the plant's planned annual output of 1.5 billion pounds. The third plant could begin operating in 1991. Construction of new ethylene facilities would be based on the dedication of plant output under long-term supply arrangements. Meanwhile, ethylene and polyethylene capacity will be increased through debottlenecking and incremental expansion of existing facilities.

NOVA's investments in methanol production and marketing are also expected to show increased profitability in 1988 because of significant price increases, resulting from increased demand combined with reduced production capacity around the world.

PETROLEUM

The significant decline in world oil prices during 1986 has challenged the petroleum industry to adapt to a new economic environment for energy.

Although crude prices, fiscal conditions and operating efficiencies have improved in 1987, the current pricing environment remains unstable. As a result, the industry must continue to be highly selective in the allocation of capital resources.

Review of 1987

NOVA's petroleum activities are conducted by Husky Oil Ltd., 42.5% owned, and Novalta Resources Ltd., 100% owned.

Husky is an integrated Canadian oil and gas company engaged in exploration, development, production, refining, marketing and transportation of crude oil and natural gas. In addition, Husky continues to position for the future and now has quality exposure in the key Canadian industry segments of heavy oil, in situ oil sands, the Beaufort Sea, East Coast offshore and Alberta's Foothills deep gas area.

In 1987, Husky's light and medium oil and natural gas exploration efforts in the western Canada basin were centred on targets which provide good prospective returns under current prices as well as strong upside economic potential. Husky participated in 23 exploration wells, resulting in 13 oil wells and one gas well.

A particular success during 1987 was Husky's involvement in a significant gas discovery on Husky farm-out lands near Caroline, Alberta. The discovery well tested high sustained rates of natural gas. When fully developed, this field may be the largest of its kind in western Canada. Two step-out wells to the original gas discovery were drilled and tested excellent results, further confirming the potential of this major discovery. Husky is actively pursuing follow-up targets that are based on high technology seismic evaluation.

◀ *NOVA continues to seek quality prospects in oil and gas exploration and production in Canada through its successful petroleum investments in Husky Oil Ltd. and Novalta Resources Ltd.*

Through its petroleum investments, NOVA continues to develop a balanced, quality exposure to key petroleum opportunities.

As part of Husky's evaluation of quality medium- and long-term prospects, heavy oil exploration in 1987 centred on the Caribou Lake block about 120 miles north of Lloydminster, Alberta. This 238,000 acre block contains large deposits of bitumen and the property further integrates and supplements Husky's extensive Lloydminster operations. Since the inception of the Caribou Lake exploration program, about 300 miles of seismic have been shot and 31 wells have been drilled. Results to date are encouraging and support Husky's view that the lands have excellent future production potential.

Husky believes that major oil and gas reserves, capable of contributing significantly to North American energy supply, will most likely be developed from frontier discoveries and international areas. Primary frontier activities in 1987 included further delineation drilling on the Amauligak structure in the Beaufort Sea and delineation drilling on the Whiterose structure on the East Coast offshore.

In the Beaufort Sea, a berm has been built to facilitate drilling and the first well to be drilled from this location, F-24, was spudded on October 1, 1987. With a 17.5% working interest, Husky is the second largest participant in the field. The prospect is currently estimated to contain the largest recoverable oil potential in the Beaufort Sea with estimates ranging from 400-800 million barrels of recoverable oil.

On the Grand Banks off Canada's East Coast, a third Whiterose delineation well, Whiterose E-09, is being drilled. In 1987, additional East Coast exploration activities included the drilling and testing of the North Ben Nevis M-61 delineation well on the Grand Banks, and the drilling of the Bonne Bay C-73, also on the Grand Banks, which was abandoned.

In 1987, total gross production of crude oil and natural gas liquids averaged 41,700 barrels per day; light and medium crude oil and natural gas liquids averaged 13,600 barrels per day; and heavy oil production averaged 28,100 barrels per day. Natural gas sales averaged 61.2 million cubic feet per day.

Husky is involved in all aspects of downstream petroleum operations, continuing a program of modest long-term growth. Refined product sales in 1987 averaged 13,200 barrels per day of light oil and 8,200 barrels per day of asphalt and residuals, which are comparable to 1986 sales. Blended crude oil sales of 96,200 barrels per day provided steady contributions to downstream profit.

Novalta Resources is engaged in oil and gas acquisition, exploration, development and production, and gas marketing, with activities centred in Alberta. Novalta increased its gas sales by 25% in 1987, and reached a new record peak day sales rate of 70 million cubic feet per day in December. Novalta also manages deliveries to various industrial markets in Alberta and moved a record 110 million cubic feet per day in December. Market growth included the initiation of deliveries to a hydrogen off-gas project at Joffre, Alberta.

Consistently successful since its formation in the mid-1970s, Novalta continued to show an operating profit in 1987 despite generally poor industry conditions.

Gas production averaged 41 million cubic feet per day, compared with 32 million cubic feet per day in 1986. Oil and natural gas liquids production averaged 942 barrels per day, compared with 692 barrels per day in 1986. Landholdings total 1.1 million gross (550,000 net) acres.

Outlook for 1988

Through its petroleum interests, NOVA continues to pursue quality investments which include conventional oil and gas exploration and development, and further evaluation of quality long-term petroleum prospects.

Husky has successfully adjusted to the fundamental changes in the operating environment and will continue to pursue and capitalize on short- and medium-term investments while furthering efforts to position itself for long-term opportunities.

Novalta Resources will continue to direct its expansion efforts to the enhancement of its natural gas supply capability to serve selected markets, most particularly as a supplier to the Alberta industrial sector, including NOVA's petrochemical businesses. Under the careful direction of management, capital spending will increase modestly in 1988 as Novalta positions itself for anticipated improvement in the profitability of the natural gas producing sector.

Other Businesses

In addition to its primary businesses, NOVA has interests in international consulting, energy-related manufacturing, telecommunications, and research and development.

International consulting and manufacturing activities remained stable, although new opportunities related to pipeline construction continued to be restrained by reduced energy development.

Markets for pipeline consulting and products in North America are generally related to increasing system efficiency and safety. This situation is also prevalent internationally, although there are a few pipeline projects directed toward increased use of indigenous resources, industrial development and environmental considerations.

The telecommunications business continued to expand in 1987 as demand for cellular systems and telephones strengthened in major markets.

Review of 1987

Novacorp International Consulting Ltd., 100% owned, provides engineering, technical and operating consulting services in pipeline transportation and markets specialized pipeline products. Novacorp's expertise and products are based on experience related to project management, construction and operation of NOVA's gas transportation system, which is recognized as one of the most technologically sophisticated in the world.

In 1987, Novacorp continued to provide project management and engineering expertise in Malaysia and Turkey on two of the world's major pipeline projects currently in progress. Novacorp is also involved in pipeline development in several other countries, including China, Australia, Finland and Colombia. Novacorp has focused its marketing activity on selected key areas and increased its emphasis on specialty products such as mechanical dry seals and magnetic

NOVA continues to improve its operations and products with cost-effective applied research and development activities conducted by Calgary-based NOVA HUSKY Research Corporation Ltd. and through commitments to other research organizations.

NOVA's other businesses will contribute increased profits in 1988 as a result of cost-conscious management and closely targeted marketing programs.

bearings based on its extensive knowledge of the international pipeline industry.

Novacorp was awarded 41 contracts in 16 countries in 1987 and is bidding and negotiating on other projects around the world.

Grove Italia S.p.A., 100% owned, manufactures pipeline valves and flow control products in the United States and Italy for worldwide sale to the energy industry. The valve group maintained its consistent profitability last year in an industry where virtually every other major participant operated at a loss. Financial results were positive despite a slight decline in revenue and continued pressure on margins from international sales. The company eliminated debt and continued cost-conscious management practices to reflect current market realities and position itself for improved performance.

NovAtel Communications Ltd., 50% owned, is the only manufacturer of cellular systems and telephones in Canada. Formed in 1983, it has grown rapidly despite strong competition from established international telecommunication companies. NovAtel, headquartered in Calgary, also has offices in Toronto, Montreal and the United Kingdom.

Revenue increased by over 60% in 1987, with NovAtel strengthening its position as one of the largest suppliers of cellular telephones to the United States market, where sales accounted for 55% of revenue. NovAtel also installed and contracted for 16 cellular telephone systems in the United States during 1987. Other systems were installed in western Canada, the Northwest Territories and Chongqing, China. The company also markets its products in the United Kingdom, Australia, New Zealand, Bermuda and Costa Rica.

NovAtel's strong emphasis on quality control produces highly reliable and durable products. In addition, the company continues to support ongoing research and development programs that supplement its position on the leading edge of telecommunications technology. In September 1987, NovAtel was awarded a gold medal in the annual Canada Awards for Business Excellence, winning top honours in the category of industrial design for its 8300/9300 series of cellular telephones.

NOVA's business objectives are supported by the work of NOVA HUSKY Research Corporation Ltd., which continues to pursue research and development activities for its owners and their affiliates. Research focuses on pipeline, petrochemical and petroleum technology. Areas under study in 1987 included natural gas dynamics, enhanced recovery and upgrading of heavy oil, and improved production of a wider range of petrochemical products.

NHRC is currently conducting nearly 100 research projects. Five patent applications for new technology were filed in 1987. New products include a dew point monitor to measure automatically the temperature at which dew forms in a pipeline and a remote terminal unit that facilitates data collection. Research by NHRC was instrumental in increasing polyethylene production at NOVA's petrochemical facilities.

Outlook for 1988

Novacorp, established as a reputable and reliable engineering consulting company, will focus its marketing efforts on specialized products and consulting services in North America and on large pipeline developments in targeted international areas.

Grove Italia expects the U.S. market for valves and flow control products to improve in 1988. The international market will continue to fluctuate according to the rate of energy industry activity. Grove will remain profitable and continue to position itself for increased growth as the industry recovers.

NovAtel expects to increase sales of both terminals and cellular systems as a result of aggressive marketing programs around the world. Quality and cost control and development of new technology will continue to be a high priority.

NHRC will continue to participate in new product development and efforts to enhance the productivity of assets in petrochemical, gas transmission and petroleum operations.

NOVA is committed to providing a safe, productive business environment for its employees, customers and the general public.

To accomplish this corporate objective, NOVA has established policies and programs dedicated to community and employee relations in such areas as corporate contributions, occupational health and safety, environmental affairs, and employee motivation and development.

We believe shareholders have a special interest in corporate policies and practices. Because some of these assumed a particularly important role in 1987, we have chosen to comment on them in this report.

Corporate Contributions

As a major part of our ongoing program of corporate support for non-profit community-based organizations where NOVA has business operations, NOVA participated as a corporate sponsor of the XV Olympic Winter Games, held in Calgary in February 1988.

NOVA agreed to sponsor the games because the Corporation is one of the few major Canadian companies headquartered in Calgary. We believe it fitting that an international event of this high calibre be supported by a company that prides itself on its Alberta base and international scope of operations.

Our sponsorship obligations were met through support that NOVA was uniquely positioned to provide. Allotment of space in NOVA facilities, provision of goods and services, and secondment of several key technical staff members to groups responsible for organizing and managing the games were the main components of NOVA's sponsorship. Another major contribution was the underwriting of novaplayRites'88, part of the Olympic Arts Festival, which provided a Calgary-based theatre group with the opportunity to produce five new Canadian plays. On their own time, NOVA employees also provided support as volunteers, some playing major roles in the organization and staging of the games.

NOVA employees supported the XV Olympic Winter Games, held in Calgary during February 1988, by providing their time and expertise on a volunteer basis to the groups responsible for organizing and staging the games.

NOVA's corporate contributions program is planned, organized and implemented by a committee of NOVA employees which allocates donations in five major areas: health and welfare, education, arts and culture, community relations and recreation.

In 1987, particular emphasis was placed on health and welfare donations to local and provincial organizations which experienced a high demand for services at a difficult time in Alberta's economy. As a second priority, NOVA also provided long-term support to Alberta and other educational institutions for faculties of management, engineering, native education and medicine. This support is intended to help develop important human resource skills for Alberta and Canada.

Funding of projects in smaller communities where NOVA has a presence considers the input of local management and employees who are closely involved in these communities. In addition, NOVA continues to support the substantial involvement of its employees in charitable causes that benefit the communities in which they reside.

NOVA's long-term success is supported by its willingness and ability to benefit and enrich communities in which operations are located.

Occupational Health, Safety and Environmental Affairs

NOVA's operations are characterized by an ongoing commitment to occupational health and safety and to preservation of the environment.

The NOVA group of companies has a very low accident rate relative to other companies and industries in Canada. The Corporation maintains occupational health and safety and environmental affairs departments staffed with professionals and our experience and professionalism has earned NOVA a positive reputation for environmental management. All levels of NOVA management promote and encourage safe work practices and environmental responsibility as productive management practices.

Trained personnel play a key role in all aspects of construction and operation of facilities to ensure that new plants and operations meet high health, safety and environmental standards for employees and the general public. Occupational health and safety activities include periodic health assessments, ongoing review of working environments, treatment, diagnosis, health education and counselling through a wide range of programs. Environmental activities include conducting impact studies, obtaining construction permits, ensuring that reclamation programs are implemented when projects are completed, and monitoring operations. Research and development studies on issues such as soil conservation and chemical usage are an integral part of environmental planning.

Human Resources

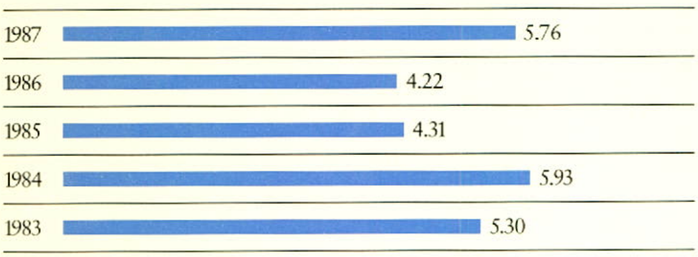
The Corporation's central human resource objective is to create and maintain an environment in which employees optimize talents and skills in the most productive manner possible, to the mutual benefit of the employee and the Corporation.

NOVA has long-standing policies in support of non-discriminatory hiring, compensation and employee development which reinforce performance as the key to career development. By integrating operating plans of NOVA companies with employee performance and development assessment, employees are exposed to diverse career opportunities. The depth of talent in NOVA companies and the emphasis on performance-based human resource management support a high level of productivity and career development.

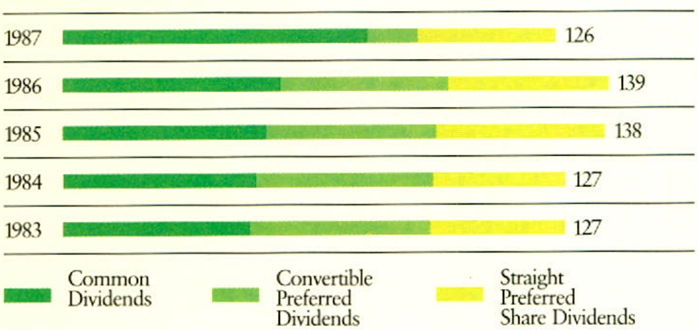
We are proud of the very positive employee relations which NOVA enjoys and of the pride that NOVA employees take in representing the Corporation. Considerable achievements in reducing costs and improving productivity in 1987 are a reflection of the capability, motivation and commitment of NOVA's employees. In addition to these accomplishments in 1987, NOVA employees have again achieved recognition professionally and internationally as individuals and in bringing awards to NOVA companies.

For 1988 the Corporation will continue efforts to develop employees through management and skill training geared to the attainment of corporate goals.

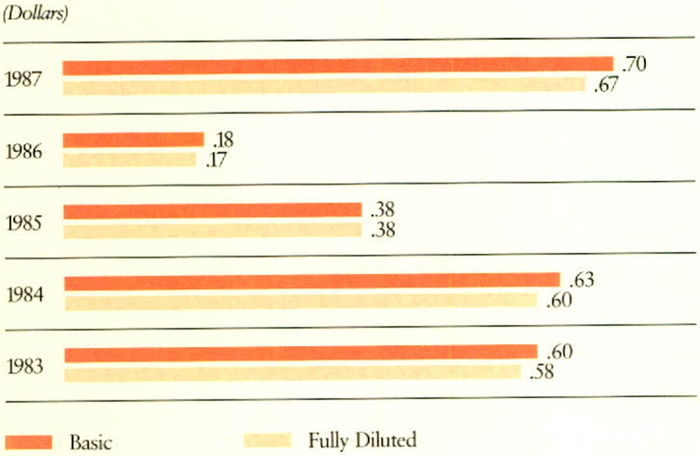
COMMON EQUITY PER SHARE AT YEAR END
(Dollars)



DIVIDENDS FOR THE YEAR
(Millions of dollars)



NET INCOME PER COMMON SHARE FOR THE YEAR*
(Dollars)



**Before extraordinary items*

SHAREHOLDER INFORMATION

NOVA welcomes questions from shareholders and potential investors, which may be directed to senior officers or to the corporate finance department by writing or telephoning the Corporation's head office. NOVA's toll-free number (800) 661-8686 may be used by Canadian callers outside of Calgary.

Literature on various aspects of the Corporation's business is also available and may be obtained by writing to our head office address or by calling our toll-free number.

Share Issues

NOVA shares are listed on the Toronto, Montreal and Alberta stock exchanges. The Corporation's common shares, which are widely held by private sector investors, are among the most actively traded securities in Canada. In 1987, more than 132.3 million shares were traded, representing a total dollar value of about $1.2 billion.

At December 31, 1987, a total of 211.5 million common shares were outstanding. In addition, eight preferred share issues were outstanding.

Share Registration

Common shares are registered with the Vancouver, Edmonton, Calgary, Regina, Winnipeg, Toronto and Montreal offices of National Trust Company. Preferred shares are registered as follows: Canada Trust Company in Vancouver, Calgary, Edmonton, Regina, Winnipeg, Toronto and Montreal for all share issues; and Canada Trust Company in Halifax (7.60%, 6-3/8%, 11.24%, 9-1/8% preferred shares only). The 1996 warrants are registered with the Vancouver, Edmonton, Calgary, Regina, Winnipeg, Toronto, Montreal and Halifax offices of Montreal Trust Company.

Holders of NOVA securities may receive more than one copy of our annual and quarterly reports. Duplication cannot always be avoided because our common shares and preferred shares are registered with two transfer agents. Holders of common shares who receive more than one document due to differences in registered names or addresses should contact National Trust to have their holdings consolidated. Those holders of any issue of preferred shares in the same situation should make similar arrangements with Canada Trust.

Share Designations

NOVA's share issues are designated in newspaper listings as follows:

Nova Cor	f	Common
Nova C	p	4-3/4% Series C Preferred
Nova E	p	7-3/4% Preferred
Nova F	p	9-3/4% Preferred
Nova G	p	9.76% Preferred
Nova H	p	7.60% Preferred
Nova J	p	6-3/8% Second Preferred
Nova N	p	11.24% Preferred
Nova O	p	9-1/8% Preferred
Nova W		1996 Warrants

Dividend Reinvestment Plan

NOVA's dividend reinvestment and share purchase plan provides a convenient method for shareholders to reinvest dividends automatically on all or some of their NOVA common and preferred shares at the weighted average of the selling price of common shares on The Toronto Stock Exchange for the five trading days prior to the dividend payment date. It also allows shareholders to make cash payments of $50 to $5,000 per quarter to buy common shares at the same average price.

Both options are offered to shareholders without brokerage or administrative fees attached. The plan is not available to residents of the United States. Additional information may be obtained from the transfer agent charged with plan administration: National Trust Company, Corporate Trust Services, Suite 1008, 324 Eighth Avenue S.W., Calgary, Alberta, T2P 3B2. Information may also be obtained from NOVA's corporate finance department.

The Corporation's annual meeting will be held on Tuesday, April 26, 1988, at 10:30 a.m. in the Calgary Convention Centre, 120 Ninth Avenue, S.E., Calgary, Alberta.

NOVA Group Officers

Corporate Officers

S. Robert Blair
Chairman and Chief Executive Officer

H. J. Sanders Pearson
Vice Chairman of the Board

Robert L. Pierce
President

William G. Wilson
Executive Vice President and Chief Financial Officer

James H. Butler
Executive Vice President

Bruce W. Simpson
Senior Vice President

Richard C. Milner
Vice President, Treasurer and Corporate Secretary

John W. F. Cowell
Vice President

Alex W. Kabatoff
Vice President

Brian F. Olson
Vice President

Joan A. Dennis
Assistant Secretary and Secretary to the Board

Thomas G. Milne
Assistant Treasurer

Alberta Gas Transmission Division

Donald G. Olafson
Division Senior Vice President

Robert B. Snyder
Division Senior Vice President

Principal Subsidiaries and Affiliates

James H. Butler
Chairman and Chief Executive Officer, Novacor Chemicals Ltd.

Gordon W. Cameron
President and Chief Executive Officer, Pan-Alberta Gas Ltd.

John E. Feick
President, Novacor Chemicals Ltd.

Luigi Fiore
Chairman, Grove Italia S.p.A.

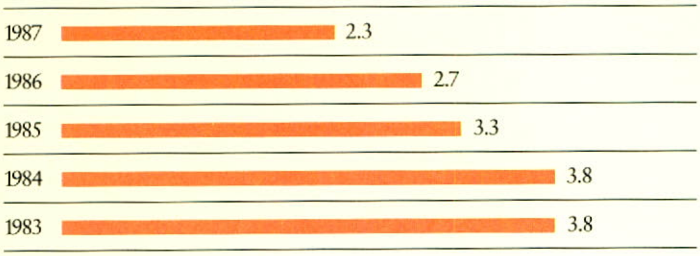
C. Kent Jespersen
President, Foothills Pipe Lines (Yukon) Ltd.

Del Lippert
President and Chief Executive Officer, NovAtel Communications Ltd.

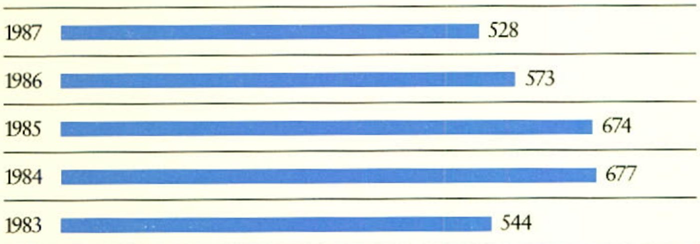
Donald G. Olafson
President, Novacorp International Consulting Inc.

Arthur R. Price
President and Chief Executive Officer, Husky Oil Ltd.

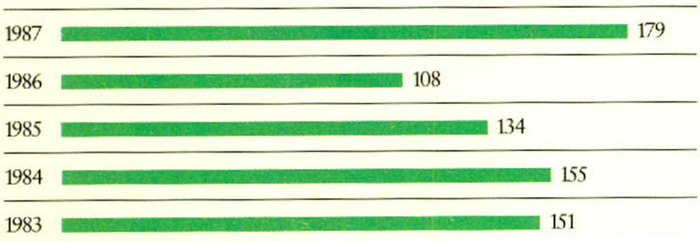
CONSOLIDATED REVENUE FOR THE YEAR
(Billions of dollars)



CONSOLIDATED OPERATING INCOME FOR THE YEAR
(Millions of dollars)



CONSOLIDATED NET INCOME FOR THE YEAR*
(Millions of dollars)



**Before extraordinary items*

NOVA's strong financial performance in 1987 was highlighted by a major increase in common equity and the achievement of a new record in net income to common shareholders.

Consolidated Net Income

Consolidated net income was $179.1 million, up from $100.2 million in 1986. Fully diluted net income per common share was 67 cents compared with 12 cents per common share in 1986. Basic net income per common share was 70 cents on a total of 185.3 million average common shares outstanding, compared with 12 cents on 134.7 million average common shares in 1986. The large increase in the number of outstanding common shares resulted from conversion of convertible preferred shares and warrants as the market price of the common shares increased during 1987.

The largest increase in net income was contributed by NOVA's petrochemical business which achieved higher sales volumes, reduced operating and manufacturing costs and improved prices. Cost-of-service income in gas transportation and petrochemical operations declined slightly due to lower rate bases and reduced returns in some operations. In petroleum, higher crude oil prices in upstream operations were offset by lower margins from downstream operations and lower natural gas prices.

The return on average common equity was 13.3% in 1987.

1986 Compared to 1985

Consolidated income before extraordinary items was $108.0 million, down from $134.1 million in 1985. Improved earnings in petrochemicals through better prices and increased production of polyethylene were more than offset by the effect of lower crude oil prices; lower rates of return and rate bases for certain gas transportation operations; and a decline in contribution from the valve manufacturing operations.

As a result of writing down the portion of NOVA's investment in Husky held for sale to net realizable value, an extraordinary loss of $7.8 million reduced consolidated net income for 1986 to $100.2 million or 12 cents per common share fully diluted.

In 1985 extraordinary items of $216.5 million

Year Ended December 31 (Millions of dollars)	1987	1986	1985
Revenue			
Gas Transportation & Marketing	$1,167.6	$1,245.4	$1,529.9
Petrochemicals	1,021.4	724.8	756.8
Petroleum	49.9	626.2	978.9
Manufacturing	103.5	105.9	97.4
Intersegment Eliminations	(20.0)	(21.3)	(15.8)
	$2,322.4	$2,681.0	$3,347.2
Operating Income			
Gas Transportation & Marketing	$ 320.2	$ 338.7	$ 345.5
Petrochemicals	202.9	73.6	48.1
Petroleum	(2.3)	158.2	266.5
Manufacturing	7.4	2.7	13.5
	$ 528.2	$ 573.2	$ 673.6

caused NOVA to report a net consolidated loss of $82.4 million or $1.31 per common share fully diluted.

Revenue and Operating Income

Significant trends in revenue and operating income are illustrated above and discussed by major business segment as follows.

Gas Transportation & Marketing

Revenue was down 6% in 1987 due to lower prices for natural gas marketed to the United States. The marketing of natural gas has little impact on operating income since the margins in this business yield only a small profit contribution. Lower rates of return and declining rate bases combined with reduced billings for income taxes and carrying costs related to the capital structure of certain cost-of-service operations caused the decline of 5% or $18.5 million in operating income. These factors reduced earnings attributable to common shareholders by $2.2 million.

1986 Compared to 1985

Revenue was down 19% due to lower prices and reduced volumes of natural gas marketed to the United States. Lower rates of return and declining rate bases in certain cost-of-service operations caused a decline of $6.8 million or 2% in operating income.

Petrochemicals

Revenue was up $296.6 million or 41% in 1987 due to increased volumes and improved prices in NOVA's polyethylene business. At the Joffre linear low-density polyethylene plant, sales volumes increased by 35% and average selling prices were up 23%. New revenue was contributed from the linear low/high-density polyethylene plant near Sarnia, Ontario, which was acquired in mid-February 1987.

Operating income was up $129.3 million, more than double the amount reported in 1986. The polyethylene business contributed most of this increase with higher sales volume and improved selling prices combined with reduced operating and manufacturing costs. The contribution from the Corporation's methanol business, which is discussed under equity in earnings (losses) of affiliated companies, also improved in 1987.

1986 Compared to 1985

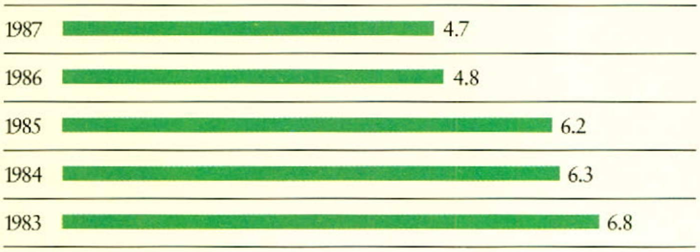
Revenue was down $32.0 million or 4%. The increased revenue for polyethylene was more than offset by reduced by-product sales from the ethylene plants as well as reduced price and demand for ethane. While revenue was down slightly in 1986 compared with 1985, operating income in 1986 improved by $25.5 million or 53% over 1985 due to improved prices and higher volumes for polyethylene.

Petroleum

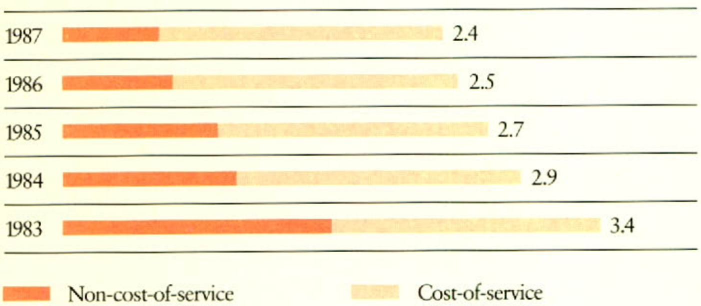
In 1987 NOVA's investment in Husky has been accounted for under the equity basis of accounting. Under this method NOVA's share of Husky's income is included as equity in earnings of affiliates. In 1986 NOVA consolidated Husky's accounts for eleven months and accordingly included in the 1986 revenue and operating income figures are

Net income increased by 79% in 1987 as NOVA's petrochemical business benefited from a strong recovery in operating and marketing conditions.

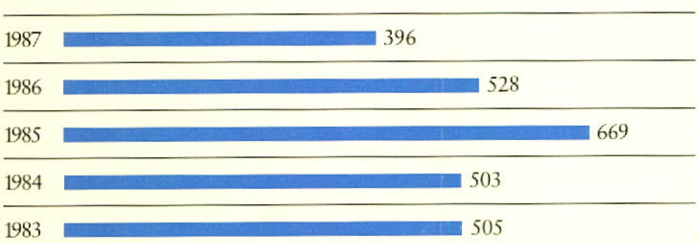
CONSOLIDATED ASSETS AT YEAR END
(Billions of dollars)



CONSOLIDATED LONG TERM DEBT AT YEAR END
(Billions of dollars)



CASH FROM OPERATIONS FOR THE YEAR
(Millions of dollars)



$591.9 million and $162.6 million respectively related to Husky.

The remaining petroleum investments consist of Novalta Resources, a wholly owned intermediate oil and gas company, and NOVA's consulting and engineering business. Novalta Resources maintained 1986 revenue levels despite the drop in natural gas prices; however, higher depletion charges, the result of increased production, reduced the net contribution. The consulting and engineering business, which had a $15.6 million increase in revenue from several new contracts, reported a small loss in both 1987 and 1986.

1986 Compared to 1985

Revenue was down 36% and operating income was down 41% principally due to the significant decrease in oil prices in the year. Lower volumes were experienced in the production of light and medium crudes which was a result of market and pipeline constraints.

Petroleum and gas revenue tax ("PGRT") decreased $78.5 million in 1986 due to the lower production volumes and selling price for crude oil. In addition, an agreement was reached by Husky during 1986 which resulted in PGRT exemptions and recoveries of $36.0 million.

Manufacturing

Revenue of $103.5 million remained relatively unchanged compared with 1986. Improved margins and reduced operating costs contributed to a $4.7 million improvement in operating income.

1986 Compared to 1985

Revenue in 1986 was up 9% compared with 1985; however, operating income declined 80%. The effect of lower crude oil prices contributed to substantial declines in oilfield-related activities and in turn to the decline in product margins in the valve group of companies, which are largely dependent on oil and gas activities.

Interest

Net interest expense was down 15% compared with 1986 due to a lower level of outstanding debt, arising principally from the proceeds received in May 1987 on the disposition of a part of the Husky investment, and lower levels of interest rates generally.

1986 Compared to 1985

Net interest expense was down 10% compared with 1985 due to a lower level of outstanding debt arising from the application of the proceeds received on the sale of NOVA's head office building.

Equity in Earnings (Losses) of Affiliated Companies

NOVA's share in earnings (losses) of affiliates, before non-operating items, was $12.8 million compared with a loss of $15.2 million in 1986. Most of the increase came from NOVA's investment in Husky which contributed $22.1 million ($14.4 million after interest of others in income of subsidiaries) in 1987. Husky benefited from higher crude oil prices but this was offset by lower margins in refining and marketing. In 1986 NOVA equity accounted for Husky for only one month and its contribution was $2.4 million. Earnings from NOVA's investment in the methanol business of $2.9 million were up $5.5 million, the result of increased sales volumes and reduced manufacturing costs. Methanol prices strengthened in the latter part of 1987 and this is expected to continue into 1988. Losses from manufacturing affiliates of $12.2 million improved by $2.8 million in the year. Losses are still being experienced in NOVA's telecommunication investment.

1986 Compared to 1985

NOVA's share in losses of affiliates in petrochemicals and manufacturing was $17.6 million in 1986 compared with $7.2 million in 1985. World methanol markets were depressed while the demand for heavy trucks remained weak. NOVA's telecommunication investment continued to face stiff competition in the cellular telephone market and lower crude oil prices significantly affected the marketing of compressed natural gas conversion equipment. Equity earnings from Husky were $2.4 million in 1986.

Loss on Investments

In 1987 NOVA recorded a net gain of $10.0 million on the sale of investments and recorded a net loss of $3.7 million on the sale of supply vessels. In addition NOVA discontinued the business of CNG Fuel Systems. The write-down of the investment resulted in a net loss of $21.7 million.

1986 Compared to 1985

In 1986 NOVA recorded its share of certain non-operating expenses incurred by affiliates accounted for by the equity method. These consisted of a $23.1 million loss in Husky, related to the write-downs of certain Canadian frontier and international oil and gas properties and a loss on the sale of a semi-submersible drilling vessel, and a loss of $7.0 million on the sale of a methanol plant in New Zealand.

Miscellaneous Income and Other (Deductions)

The increase in other expenses during 1987 and 1986 compared with 1985 is mainly due to rent for NOVA's head office building which was sold and leased back in December 1985.

Income Taxes

Income tax expense was up $12.7 million compared with 1986 principally as a result of higher earnings in petrochemical operations as offset by $35.7 million on the utilization of losses for tax purposes. The 1986 figure includes income taxes of $32.7 million provided by Husky.

1986 Compared to 1985

Income tax expense was down $94.3 million compared with 1985 principally as a result of lower earnings in the petroleum operations. Income tax expense for 1986 was reduced by $34.8 million by applying losses for tax purposes to income on which taxes had been previously paid or provided.

Liquidity and Capital Resources

Cash flow from operating activities totalled $395.6 million in 1987. After removing the effect of Husky ($223.0 million) from the 1986 figure of $527.9 million, the 1987 cash flow from ongoing consolidated operations was up $90.7 million. This improvement came principally from the petrochemical business.

Investment activities resulted in a net cash outflow of $146.6 million in 1987, down $47.1 million from 1986. Capital expenditures on plant, property and equipment were down $126.6 million principally as a result of the deconsolidation of Husky, which had capital expenditures of $173.0 million in the comparative period of 1986. NOVA's consolidated capital expenditure program for 1988 is currently estimated to be about

$350.0 million with $250.0 million of this related to expansion and improvement to the Alberta Gas Transmission Division gas gathering and delivery system.

In May 1987 NOVA received $359.0 million on the completion of the sale of a portion of its investment in Husky. In December 1987, as a result of improved long term opportunities, NOVA acquired, for about $215.2 million, additional common shares of Oil Term Holdings Ltd. ("Holdings"), a company whose only asset consists of a 43% interest in the common shares of Husky. As a result of the purchase NOVA became the beneficial owner of approximately 99% of Holdings and increased its indirect ownership of Husky common shares from 24.4% to 42.5%.

Financing activities in 1987 included the issuance of $31.2 million in common shares, $218.2 million of long term debt and the agreement to issue $150.0 million of convertible debentures in early 1988. Repayment of long term debt amounted to $118.1 million and the purchase of preferred shares (both the Corporation's and those of subsidiaries) amounted to $215.0 million. Dividends paid to common and preferred shareholders of the Corporation amounted to $126.3 million compared with $138.5 million in 1986.

At December 31, 1987, NOVA had consolidated working capital amounting to $79.8 million compared with $324.8 million in 1986. Included in working capital at the end of 1986 was $359.0 million representing the anticipated cash proceeds from the sale of a portion of the Husky investment which were received on May 1, 1987.

During 1987 common equity of the Corporation increased to $1.3 billion, almost double the 1986 figure, as a result of the conversion of preferred shares, the exercise of warrants, the issue of convertible debentures and improved earnings. The common equity per common share at year end increased to $5.76 from $4.22 at the end of 1986.

NOVA has access to additional credit facilities with several Canadian chartered banks. These are subject to routine review and, based on current discussions with NOVA's banks and other lenders, additional credit facilities would be available if required.

1986 Compared to 1985

Cash flow from operating activities totalled $527.9 million in 1986, down $141.5 million principally due to reduced petroleum results.

Investment activities resulted in a net cash outflow of $193.6 million in 1986, down $248.1 million from 1985. Expenditures on plant, property and equipment were down $60.9 million principally as a result of a planned reduction in production development activities which was implemented by Husky in late 1985 and early 1986 in anticipation of low crude oil prices. As well NOVA received $157.5 million in 1986 on the sale of its head office building.

Financing activities in 1986 included the issuance of $97.9 million of warrants and common shares of the Corporation as well as $100.2 million in additions to long term debt. Repayments of bank indebtedness and long term debt amounted to $328.5 million. Dividends paid to shareholders of the Corporation amounted to $138.5 million.

At December 31, 1986, NOVA had consolidated working capital amounting to $324.8 million compared with $33.0 million at the end of 1985. Included in working capital at the end of 1986 was $359.0 million representing the anticipated cash proceeds from the sale of a portion of the Husky investment.

Consolidated assets of NOVA at the end of 1986 were $4.8 billion, down from $6.2 billion in 1985 due to the effect of the deconsolidation of Husky.