

ALGOMA STEEL

ANNUAL REPORT 1987

The Algoma Steel Corporation, Limited

Annual Meeting

The Annual Meeting of Shareholders will be held at the Algoma Steel Club, 89 Foster Drive, Sault Ste. Marie, Ontario, Wednesday, April 13, 1988, at 2:15 p.m. A Notice of Meeting, an Information Circular and a Proxy are mailed with this Annual Report to each shareholder.

Les actionnaires qui désirent recevoir ce rapport en français sont priés d'en faire la demande au Secrétaire, Aciers Algoma Limitée, Sault-Sainte-Marie (Ontario).

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Incorporation

Under the laws of the Province of Ontario

Share Transfer Agents and Registrars

Montreal Trust Company,
Halifax, Saint John, Montreal, Toronto,
Winnipeg, Regina, Calgary and Vancouver
The Bank of Montreal Trust Company,
New York

Shares Listed

Montreal, Toronto and Vancouver
Stock Exchanges

Trustee for Debentures

Montreal Trust Company,
Toronto, Ontario

Registrar for Debentures

Montreal Trust Company,
Halifax, Montreal, Toronto, Winnipeg,
Regina, Calgary and Vancouver

Auditors

Peat Marwick

Valuation Day Values (for Canadian Income Tax Purposes)

Series C Debenture	\$ 94.00
Series D Debenture	\$ 103.50
Common Share	\$ 13.38

Corporate Profile

Algoma Steel was formed in 1901 as a rail producer supplying the rapidly expanding Canadian and United States railroads. The Corporation was reorganized by Sir James Dunn in 1935 and began to expand its range of products. Today, Algoma is a fully integrated steel producer with five principal steel product lines consisting of sheet and strip, plate, seamless tubulars, structural shapes and rails. It also produces and sells steam and metallurgical coal. Algoma employs directly and through its United States subsidiaries approximately 9,000 employees.

The Corporation's steelworks and head office are located in Sault Ste. Marie, Ontario. It has sales offices in Mississauga, Ontario, and Calgary, Alberta, and in two United States locations. Through direct ownership, Algoma can satisfy all its iron ore and the majority of its coal requirements. Iron ore is obtained from mines in Wawa, Ontario, and Ishpeming, Michigan, and coal from mining locations in West Virginia. The United States mining operations and tubular sales are conducted through Algoma's principal subsidiary, Cannelton Industries, Inc.

The Corporation holds ownership interests in downstream operations which finish and process steel into higher valued products.

Canadian ownership of Algoma Steel exceeds 99 per cent. Canadian Pacific Limited, with a 54-per-cent interest, is the principal shareholder.

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The Algoma Steel Corporation, Limited

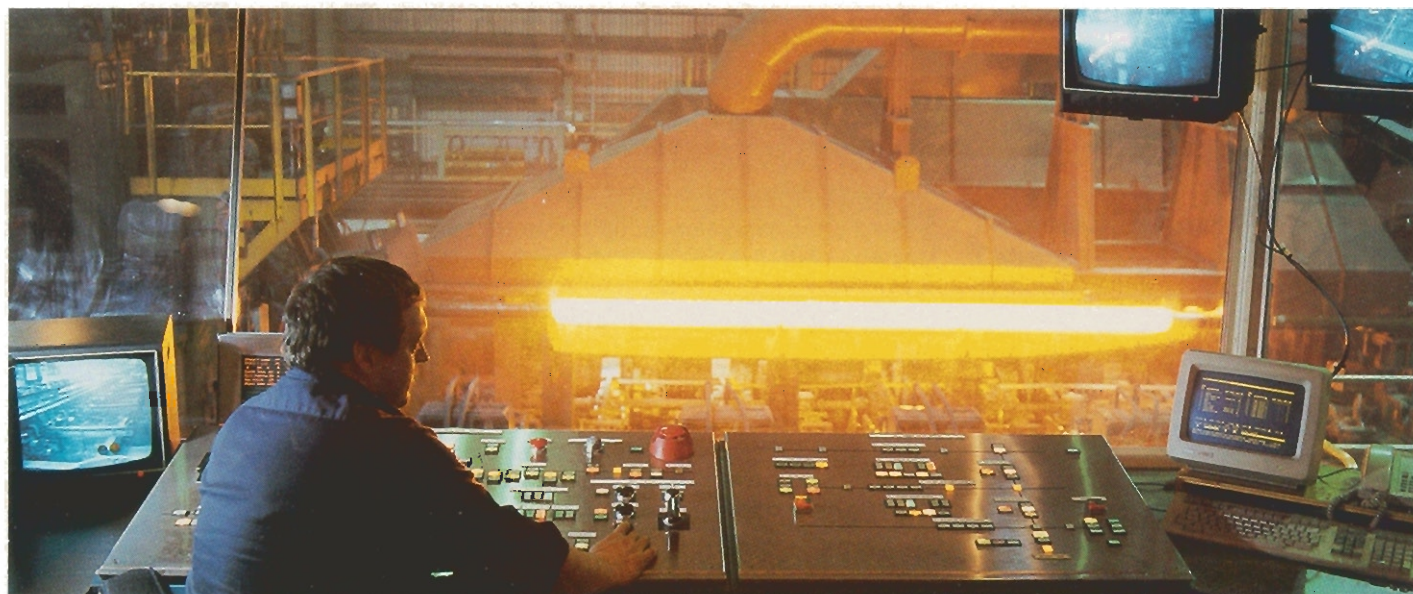
Annual Report 1987

Highlights

Tons and dollars in millions except per share data	1987	1986
Shipments of steel products (tons)	2.125	2.032
Sales	\$ 1,228.0	\$ 1,093.3
Earnings (loss) from operations	\$ 100.3	\$ (9.2)
Earnings (loss) before income taxes and equity in earnings of AMCA International Limited	\$ 48.8	\$ (72.1)
Net earnings (loss)	\$ 40.3	\$ (134.8)
- from integrated steel operations	\$ 30.7	\$ (51.0)
- from AMCA International Limited	\$ —	\$ (2.4)
- from extraordinary gains (losses)	\$ 9.6	\$ (81.4)
Per common share data		
Net earnings (loss)	\$ 1.53 *	\$ (9.93) **
Dividends paid in cash	\$ —	\$ —
Book value	\$ 27.82	\$ 26.31
Cash provided from operations	\$ 133.3	\$ 113.7
Long-term debt as a per cent of capitalization	48%	43%
Return on average total investment	5.4%	(7.2)%
Return on average common shareholders' equity	5.6%	(29.1)%
Closing market price		
- 8% tax deferred preference share	\$ 18.75	\$ 13.63
- class B convertible preference share	\$ 17.00	\$ 14.38
- common share	\$ 15.25	\$ 11.00

* Includes an extraordinary gain of \$0.56 per share.

** Includes an extraordinary loss of \$5.34 per share.



Bob McIntyre casts a watchful eye on a shell from the piercer at the No. 2 seamless tube mill.

MAR 23 1988
M. GILL U.

Report to Shareholders

The Program of Action, announced in April, 1986, was translated into results in 1987. Pretax earnings of \$49 million were a \$121 million turnaround from the \$72-million pretax loss in 1986. Net earnings per common share, after preference-share dividends, were \$1.53, the first positive earnings since 1981.

Algoma's return to profitability was accomplished by the dedicated efforts of many Algoma employees. Most of the improvement came from cost reduction, part of which was volume-related. Also, the average sales return per ton of steel products shipped increased by seven per cent over 1986 as a result of some modest price recovery and an improved product mix. There was a 23-per-cent decrease in interest expense, including capitalized interest in respect of construction of the new tube mill.

Concurrent with the restoration of profitability came an improvement in the Corporation's financial position. Total financial obligations, including debt, retractable preference shares and share of Tilden Mine debt, were reduced from mid-1986 to December 31, 1987, by approximately \$330 million. Year-end long-term debt, including the Tilden long-term debt which was restructured in 1987 and became a direct obligation of the Corporation, was 48 per cent of total capitalization. The retractable preference shares were redeemed in 1987.

The stabilization of Algoma's affairs is a positive development. The Program of Action was a good beginning, but much more remains to be done. The 5.4-per-cent return on investment represented by 1987 results is far from adequate. The cash flow from operations was \$20 million better than 1986, but it must be further increased to support the capital expenditures which are necessary.

A strategic planning program carried out during 1987 with the assistance of skilled advisors has identified specific opportunities to improve the quality and cost competitiveness of Algoma's products and thereby enhance profitability. The opportunities are in almost every area of the Corporation, from the coal and iron ore mines through primary steel production and continuous casting, to the rolling mills and product finishing operations, and on to the overhead charges which must be carried by the Corporation's products. In each instance, work is underway to describe the opportunity, identify the action required, estimate the capital cost and document anticipated benefits. The program is designed to guarantee Algoma's future, increase customer satisfaction, secure the employment base and provide a responsible return to shareholders.

The improved market outlook for all Algoma's products, other than rails, has created a favourable environment for implementation of the Corporation's strategic plan. Actions have already been taken to improve the profit contribution of the West Virginia coal mines and to reduce iron ore costs. Engineering is proceeding for ladle metallurgy facilities in both steelmaking shops which will improve Algoma's ability to meet exacting product specifications and customer expectations in a cost-effective manner. A new continuous round caster is being engineered which will substantially reduce the cost of tubular products and improve tubular quality. It is expected that the ladle metallurgy and continuous-round caster projects will be approved for construction before mid-1988.

Although the timing for total elimination of ingot production has been extended, Algoma remains committed to the objective of continuously casting 100 per cent of its raw steel. Slab caster modifications already underway and planned construction of the tube-round caster will increase production flexibility and expand annual continuous casting capacity to 2.6 million tons by 1991.

The involvement of employees and their union representatives was expanded in 1987 through Employee Involvement Groups and through the Labour/Management Advisory Committee which was established during 1987 negotiations with the United Steelworkers of America. The Committee has been provided with comprehensive information on the Corporation's affairs and there have been wide-ranging discussions on issues that could affect the future of the company and its employees.

Signing of the Canada/U.S. Free Trade Agreement is a positive development for Algoma. Access to traditional U.S. markets and customers is an important element of Algoma's marketing plan. We intend to maintain a responsible and constructive presence in the U.S. market as part of a strategy which has traditionally allowed for approximately one-quarter of our total steel product tonnage to be exported to the U.S. and offshore.

Business arrangements concluded with users and finishers of steel products will be important to Algoma's efforts to stabilize volume and improve margins. Arrangements already in place are described under the Sales and Marketing section of this report. We are actively exploring other opportunities which can provide captive outlets for the Corporation's steel products and increase their value.


We expect 1988 to be another challenging year. Algoma's largest blast furnace must be relined and new labour agreements must be negotiated with Canadian employees. The production output of the new seamless tube mill must be further increased and we must begin construction on priority capital projects. We must continue to market our products in a way that will meet customer needs without compromising Algoma's profit opportunity. We must aggressively and relentlessly continue to reduce production costs. We remain optimistic that these objectives can be achieved and that Algoma can and will be a stronger and better-positioned company at the end of the year than it was at the beginning.

We note with regret the retirement from our Board of Directors of Paul Nepveu who reached the mandatory retirement age in 1987. Mr. Nepveu was a dedicated Director who provided outstanding service to the Corporation during his 14 years on the Board. His sound business sense, wise counsel and friendship will be missed.

Gordon Paterson, Vice President — Engineering and Technical Services, and Sam Ellens, Vice President — Employee Relations, retired during 1987 after 33 and 31 years of service, respectively. They each had long careers with Algoma and made important contributions to the Corporation.

Paul Paciocco was appointed to the position of Vice President — Engineering and Technical Services and Bob Turpin was appointed Vice President — Employee Relations.

The results in 1987 have demonstrated that Algoma can be profitable and that financial stability can be restored. We know that opportunities exist to substantially enhance profits in future years. However, past results could not have been achieved and future opportunities will not be realized without the understanding and participation of employees, customers and suppliers. On behalf of the Board of Directors we express our appreciation and thanks to everyone who has contributed to making 1987 an important year of progress and a stable base from which we can move on to future accomplishments.



Dr. John Macnamara
Chairman and Chief Executive Officer



Peter M. Nixon
President and Chief Operating Officer

Sault Ste. Marie, Ontario
February 3, 1988

Sales and Marketing

Consolidated sales of \$1.2 billion were 12 per cent higher than in 1986. Steel shipments were five per cent above 1986 levels. The markets for sheet, plate, seamless tubular and structural products strengthened significantly in 1987, giving rise to opportunities for some price recovery. An improved product mix and higher volume contributed to more efficient operation of steelmaking and rolling mill facilities.

The automotive market was strong throughout the year, providing good demand for Algoma's hot- and cold-rolled sheet products. Flat-rolled operations were at capacity for most of the year. In 1987, through the Huron Limited Partnership arrangement, the Corporation acquired an equity position in a Windsor-based automotive parts manufacturer. This arrangement will expand the base load for flat-rolled production and assist Algoma in achieving higher sales to the automotive sector.

Effective January 1, 1988, Algoma exercised its option to become a 50-per-cent owner of Ferrum Inc. Ferrum, one of the Corporation's major flat-rolled customers, produces and markets welded tubing and hollow structurals and is projecting a strong year in 1988.

Increased activity in non-residential construction resulted in improved demand for plate and structural products. Markets for plate were expanded during the year, particularly in the mining and heavy equipment sectors, and sales of



Application team members discussing a customer requirement. (l to r): Ron Baic (Superintendent - Cold Mill and Unfinished Parts); Glenn Hogan (Manager - Automotive and Light Manufacturing Sales); Peter Leach (Market Development Engineer - Flat Rolled Products); Jim Barber (Assistant Manager - Flat Rolled Marketing); Dean Casagrande (Senior Market Metallurgist); Alan Crozier (Senior Product Metallurgist - CDAC).

Algoma's higher-value-added, quenched-and-tempered plate products reached record levels. A favourable anti-dumping ruling was obtained in December 1987 against imports of Spanish structurals. Non-residential construction activity is expected to continue its growth pattern in 1988 which should result in strong demand for Algoma's plate and structural products.

Rail demand weakened in 1987 and head-hardened rails took an increased share of the North American market. A decision on the capital investment necessary to manufacture head-hardened premium rails was deferred pending additional review. The federal government's decision to further subsidize Sydney Steel Corporation is a serious negative factor which must be considered.

Recovery in the North American energy sector led to increased drilling activity and greater demand for seamless tubular products. The expanded product range and improved quality made possible by the new seamless tube mill and by modifications to the original mill contributed to a more favourable product mix and the achievement of volume levels that were well above 1986. The Steelpipe arrangement is providing an opportunity to expand sales of Algoma's seamless tubulars in non-oil-country markets. If oil prices remain reasonably stable during 1988 it is expected that sales of seamless tubulars will increase in both Canada and the U.S. The Corporation has entered into a limited partnership which has acquired a tube and casing finishing facility at Edmonton, Alberta. This partnership, the Superior Tube Limited Partnership, provides Algoma with an equity interest in upsetting, threading and other tubular-finishing facilities and gives Algoma an operating presence in Western Canada.

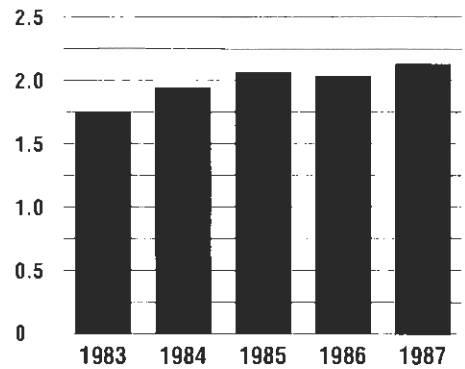
Algoma's Finished Steel Product Shipments by Product Classification

	1987	1986
Plate & Sheet	65%	69%
Structural Shapes	17%	16%
Seamless Tubulars & Skelp	13%	11%
Rails & Fastenings	5%	4%
Total	100%	100%

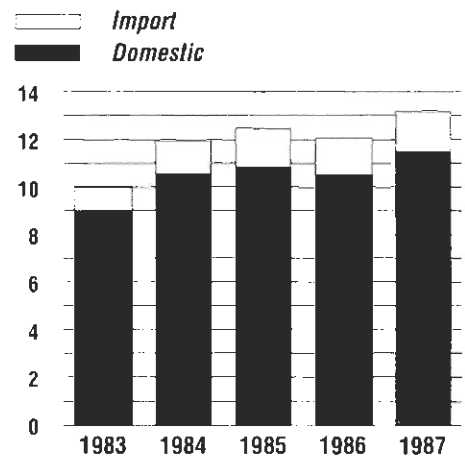
The increased sales volume and modest price recovery in 1987 provided welcome relief for the North American steel industry and for Algoma. Total industry sales may decline slightly in 1988. However, Algoma's products which generally favour the energy and capital goods sectors are well positioned for projected 1988 markets.

In 1988 the Corporation will continue to pursue downstream value-added business opportunities which will enhance the sales and profit potential of its steel products.

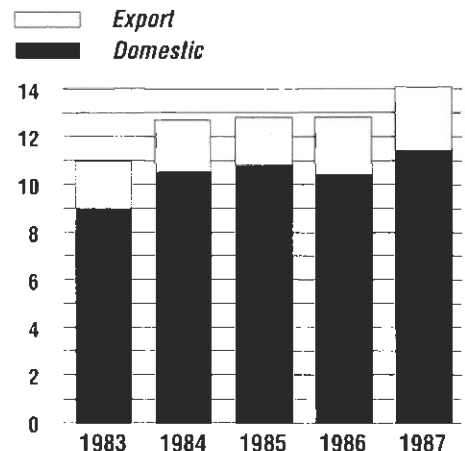
Algoma's Steel Product Shipments
(millions of tons)



Canadian Steel Consumption
(millions of tons)



Canadian Steel Mill Shipments
(millions of tons)



The Algoma Steel Corporation, Limited

Review of Operations

Mining

Algoma's U.S. subsidiary, Cannelton Industries, Inc., expanded its profitable West Virginia steam coal business in 1987. Steam coal shipments increased to 2.4 million tons which was 19 per cent higher than the previous record set in 1986. Cannelton also reduced steam coal production costs. Cannelton's steam coal business will be expanded in 1988 through a contract which provides for the operation of a 75-cubic-yard dragline at the Kanawha surface mine. The dragline is expected to be in operation by mid-1988 and will allow increased steam coal production and sales at lower costs.

Cannelton's metallurgical coal production at 1.5 million tons was slightly lower than in 1986. Cost and quality objectives for the production and shipment of metallurgical coal were achieved or surpassed.

Cannelton steam coal is loaded on the Kanawha River and barged to utility companies in the United States.



The Algoma Ore Division iron ore mine at Wawa, Ontario, achieved record productivity and improved costs in 1987. The freight rate for the transportation of iron ore sinter between Wawa and Sault Ste. Marie was lowered as part of an arrangement between the federal and provincial governments and the Algoma Central Railway.

Cost and efficiency improvements were also achieved at the Tilden iron ore mine in Michigan. However, it has become clear to Algoma and its Tilden partners that the existing hematite operation cannot achieve fully competitive cost and quality performance. The potential for converting to a cost- and quality-competitive magnetite mining operation at the Tilden site was identified in 1987. Evaluation of the project was somewhat delayed because of a shareholder proxy dispute involving Cleveland-Cliffs Inc., the mine operator. The dispute was resolved at year-end and a decision on the magnetite project is expected early in 1988.

Diamond drilling on a joint Canamax Resources Inc./Algoma Steel gold property in the Goudreau/Lochalsh area of Northern Ontario showed encouraging results. Further exploration is planned in 1988.

Manufacturing

Although production costs improved substantially during 1987, it was not an easy year. There were a number of disruptions to steelmaking operations caused by problems in ironmaking and an incident in No. 2 steelmaking shop. Algoma's largest blast furnace will be

relined in 1988 and as the furnace approaches the end of its campaign the frequency of delays has increased.

The proportion of raw steel continuously cast increased in 1987 to a record 75 per cent and improvements were achieved in casting rates, yields and quality. A number of projects are underway to further increase continuous casting capacity and achieve added benefits as the Corporation moves towards its goal of 100-per-cent continuous casting.

The plate and strip mill complex ran at high operating rates throughout the year. The plate heat-treating facility operated at record levels as sales of quenched-and-tempered products increased and Algoma moved into new markets, including armor plate. The installation of automatic gauge control on the 106-inch strip mill has provided substantially improved gauge tolerances on hot-rolled sheet products.

The rail and structural mill moved to higher levels of production during 1987 as demand for structurals strengthened. Preliminary engineering is underway to determine how the structural mill might be renovated to improve its cost competitiveness. The study relates not only to the mill itself, but to the production of beam blanks from which wide-flange beams are rolled.

Production steadily increased on both seamless tube mills during 1987. Although there are still some modifications required to the new finishing facilities, it is evident that the new seamless mill can and will meet cost and quality expectations. The acquisition of a 50-per-cent interest in finishing facilities at Edmonton, Alberta, will provide an upsetting capability for tubular products and will add to tubular finishing capacity.

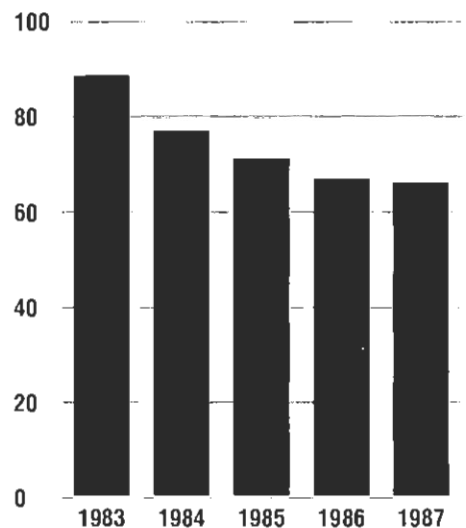
Algoma remains committed to Statistical Process Control and 66 teams were operating throughout the Corporation at year-end. In addition, a number of Employee Involvement Groups were active in the rolling mills during 1987. The SPC and EIG teams have made valuable contributions in cost reduction and quality improvement.

The employee accident frequency was reduced in 1987, but the number of days lost per accident remained at a high level. Pains and strains again accounted for the majority of lost-time accidents. Algoma's Joint Management and Union Health and Safety Committees continue to address safety concerns throughout mining and manufacturing operations with the assistance of various government bodies. Their efforts have contributed to a safer work place which was particularly evident in the cokemaking and mechanical maintenance areas where a significant improvement occurred in 1987.

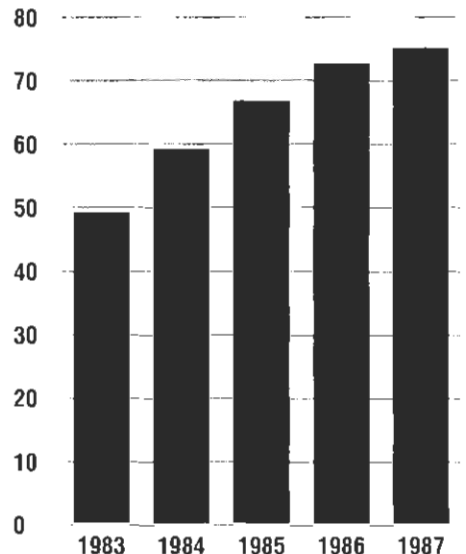
Semi-finished-steel purchases, required in 1987 to supplement Algoma's production, will again be necessary in 1988. Steel production will decrease during the 60-day reline of No. 7 blast furnace planned for the third quarter of 1988. During this period semi-finished-steel production will be supplemented from inventory and purchases.

The operating challenge of 1988 will be to respond to expected strong market demand by co-ordinating steel supply in a manner that will ensure uninterrupted rolling mill operation. At the same time, the favourable trends in productivity and cost reduction must be maintained.

**Index of Man-hours per Ton of Finished Steel Product
1972 = 100**



Percentage of Raw Steel Continuously Cast



Employee Relations

New labour agreements with the unions representing Canadian employees were concluded in late May, well in advance of the July 31, 1987, expiry date of the previous agreements. The new one-year agreements restructured the compensation packages to provide increased pension benefits without increasing hourly employment costs. Provision was made for greater union participation in the Corporation's affairs through establishment of the Labour/Management Advisory Committee. The committee was formed to keep presidents of the local unions and international representatives of the United Steelworkers of America better informed of the Corporation's affairs and allow for constructive input into decisions directly affecting Algoma's work-force.

Major Employment Cost Elements

(millions of dollars)

	1987	1986
Wages and Salaries		
For time worked	\$ 289	\$ 271
For vacation and statutory holidays	49	44
Benefits		
Company pension plans	28	30
Workers' compensation	14	13
Unemployment insurance	7	7
Group insurance plans and other benefits	37	36
	\$ 424	\$ 401

The wages and benefits of salaried employees, reduced in 1986, were restored to their former levels in mid-1987. A plan was introduced under which earnings lost during the period of reduction will be recovered, subject to the Corporation's ongoing profitability.

The combined Canadian and U.S. work-force increased from a total of 8,300 at the end of 1986 to 9,300 at the end of 1987. The increase reflected the higher level of activity in mining and manufacturing operations and particularly an increase in tube mill production. The combination of more people working and a high level of retirements resulted in a substantial recall of laid-off employees and an improved employment picture for the communities in which Algoma operates.

A meeting of the Labour/Management Advisory Committee.



The response of Algoma employees to the 1987/88 United Way campaign was again outstanding with participation in Sault Ste. Marie at 65 per cent and the average employee contribution at \$81, comparing favourably with the best performance of United Way employee campaigns at other Canadian companies. The campaign was co-chaired by Dennis Abernot, President of Local 2251, USWA, and Reg Shaughnessy, Corporate Manager — Quality Control and Research, who, with all employees, can take pride in their accomplishment.

The challenge in 1988 will be to reach new collective agreements with union employees in Canada without any interruption in operations. It will be important to achieve an early agreement to maintain customer confidence and avoid the inevitable loss of business and employment that would otherwise occur.

Algoma's return to profitability is good news for everyone who works for or depends on the Corporation. It remains now to build on this foundation.

The 1987 net earnings of \$40 million mark a positive achievement when compared with the \$135-million net loss in 1986. The return to profitability, which follows five years of losses, has resulted from more favourable markets and the co-ordinated efforts of Algoma employees. Earnings applicable to common shares of \$26 million, \$1.53 per share, compare with a loss of \$151 million, \$9.93 per share, in 1986.

Extraordinary gains in 1987 amounted to \$10 million, \$0.56 per share, whereas 1986 results included an extraordinary loss of \$81 million, \$5.34 per share. The 1987 extraordinary items consisted of a \$5-million (net of taxes) gain on the sale of property, and a \$5-million reduction in income taxes from application of prior years' losses. A pretax gain of \$9 million on the early retirement of the Corporation's share of the Tilden joint venture mortgage notes was offset by the realization of a foreign currency exchange loss on the transaction.

Pretax Earnings (Loss) by Quarter Year

(millions of dollars)

Quarter	1987	1986
1	\$ 8.0	\$ (17.0)
2	14.5	(15.4)
3	8.4	(27.1)
4	17.9	(12.6)
Year	\$ 48.8	\$ (72.1)

The dramatic \$121-million year-over-year improvement in pretax earnings from integrated steel operations was evenly distributed throughout 1987. A five-percent increase in total shipments of steel products, a modest recovery in sales returns and a higher value of the Canadian dollar relative to the U.S. dollar were contributing factors. However, reductions in operating costs contributed most to the Corporation's improved earnings.

The Program of Action announced in April 1986 included an expectation that the Corporation would achieve annual cost reductions of \$80 million to \$100 million when the program was fully implemented. Cost reductions in 1987 attributed directly to the Program of Action amounted to \$95 million. Additional identified reductions will be realized during 1988.

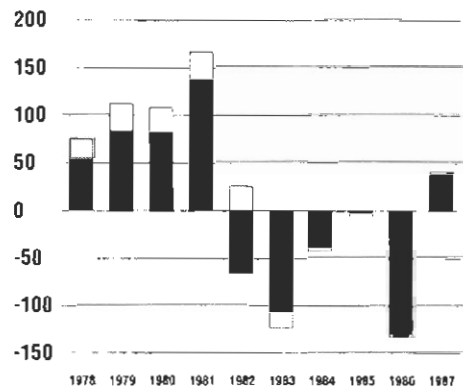
The new No. 2 seamless tube mill commenced commercial production on October 1, 1987, thereby increasing fourth-quarter depreciation and interest expense by approximately \$9 million.

An incident in the Corporation's largest steelmaking shop reduced raw steel production and shipments in the fourth quarter. The loss of steel production was partially offset through purchases of semi-finished steel, increased production in the other steelmaking shop and a reduction in inventories. It is expected that repair costs relating to the incident and loss of earnings caused by the disruption will be recovered through insurance.

The graph at right demonstrates, on an index basis (1981 = 100), the unfavourable spread between the selling prices of the Corporation's steel products and the unit cost of production inputs which negatively impacted 1987 earnings from operations by an estimated \$125 million. Consequently, the 1987

Net Earnings (Loss)
(millions of dollars)

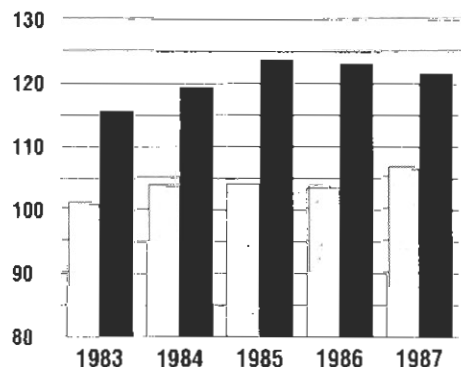
■ Integrated Steel Operation
□ Equity in AMCA International Limited
(Equity interest sold in August 1986)



Sales Return Index Compared with Combined Labour, Materials & Service Price Index
1981 = 100

■ Combined Labour, Materials and Service Price Index

□ Sales Return Index (Including offshore sales and adjusted to a common mix of finished products)



earnings from operations of \$100 million attest to the unrelenting emphasis which has been placed on cost reduction and the positive results which have been achieved.

Cash provided from operations at \$133 million is the highest level since 1981, the Corporation's best year. The Corporation's U.S. \$79-million share of the Tilden joint venture mortgage notes were purchased for U.S. \$71 million, representing a 10-per-cent discount on the amount outstanding.

Pursuant to a retraction provision, all series C and D preference shares were purchased by the Corporation in May and December, respectively, at an aggregate cost of \$80 million. The balance of the 7-3/8-per-cent series C sinking fund debentures in the amount of \$12 million was retired October 1, 1987.

Expenditures on manufacturing and mining facilities amounted to \$45 million, compared with \$131 million in 1986. The Corporation's total financial obligations (debt, retractable preference shares and share of Tilden Mine debt) were reduced by \$117 million during the year and at December 31, 1987, amounted to \$577 million, representing 48 per cent of total capitalization. The reduction in financial obligations since December 31, 1985, has totalled \$300 million.

Effective January 1, 1988, the Corporation acquired the tube mill operations of The Superior Limited Partnership through its acquisition of Canadian Pacific Limited's interest in the partnership. During the term of the arrangement, the partnership provided approximately \$175 million to complete construction of the new seamless tube mill and to upgrade the original tube manufacturing facilities.

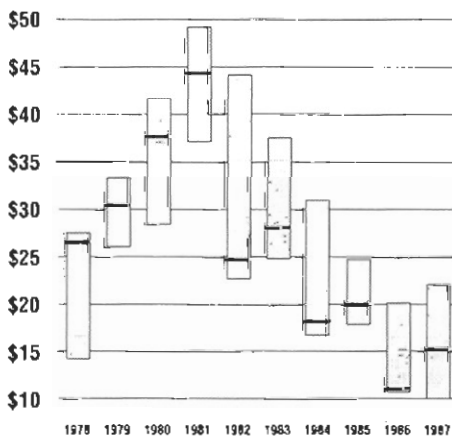
Common Share Price Range for 1987
(dollars)

Quarter	High	Low
1	\$ 16-1/4	\$ 10
2	18-3/4	14-1/2
3	20-1/2	16
4	22-1/4	13-1/2

At December 31, 1987, estimated expenditures to complete capital projects authorized by the Board of Directors and committed by the Corporation were \$18 million. A further \$22 million of expenditures was authorized but not yet committed.

Dividends paid to preference shareholders during 1987 amounted to \$14 million. A common-share stock dividend equivalent to \$.308 per common share was paid in the fourth quarter.

Common Share Price Range
(— closing price)



New accounting and disclosure rules for pension costs were issued by The Canadian Institute of Chartered Accountants effective January 1, 1987. The adoption of the revised standards increased 1987 net earnings by approximately \$3 million as disclosed in Note 10 to the consolidated financial statements.

The Algoma Steel Corporation, Limited

Consolidated Financial Statements

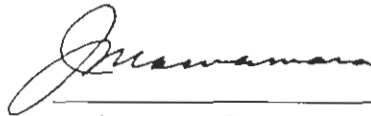
Management's Responsibility for Financial Statements

The consolidated financial statements of The Algoma Steel Corporation, Limited have been prepared in accordance with generally accepted accounting principles and necessarily include some amounts based upon management's estimates and judgments. Algoma's management is responsible to ensure that these statements reasonably reflect the Corporation's business transactions and financial position.

The integrity and reliability of Algoma's reporting systems are achieved through the use of formal policies and procedures, the careful selection of employees and an appropriate division of responsibilities. Internal accounting controls are continually monitored by an internal audit staff through ongoing reviews and comprehensive audit programs. Algoma's Code of Business Conduct policy, which is regularly communicated throughout the organization, requires employees to maintain high ethical standards in their conduct of the Corporation's affairs.

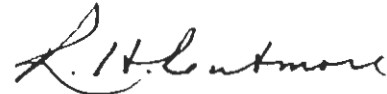
Peat Marwick, Chartered Accountants, the shareholders' auditors, have performed an independent examination and have attested to the fairness of presentation of these statements. Their report appears below.

The Board of Directors annually appoints an Audit Committee comprised of directors, the majority of whom are neither employees of the Corporation nor of companies related to the Corporation. This Committee meets regularly with management, the internal auditors and the shareholders' auditors to review significant accounting, reporting and internal control matters. Both the internal and shareholders' auditors have unrestricted access to the Audit Committee. Following its review of the financial statements and discussions with the shareholders' auditors, the Audit Committee reports to the Board of Directors prior to its approval of the financial statements.



Chairman and Chief
Executive Officer

February 3, 1988



Vice President-
Finance and Accounting

 Peat Marwick

Auditors' Report to the Shareholders

We have examined the consolidated statement of financial position of The Algoma Steel Corporation, Limited as at December 31, 1987 and the consolidated statements of earnings and retained earnings and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the Corporation as at December 31, 1987 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, except for the change in the method of accounting for pension costs as explained in Note 10 to the consolidated financial statements, on a basis consistent with that of the preceding year.

Sault Ste. Marie, Canada
February 3, 1988



Chartered Accountants

The Algoma Steel Corporation, Limited

Consolidated Financial Statements

Summary of Significant Accounting Policies

Principles of Consolidation	<p>The consolidated financial statements include the accounts of all subsidiary companies and The Superior Limited Partnership. Inter-company transactions are eliminated. The investments in the Tilden Mining Company (a joint venture), the Huron Steel group (a limited partnership) and the Superior Tube Limited Partnership are included in long-term investments and are accounted for by the equity method. The Tilden Mining Company is a cost-sharing joint venture producing iron ore pellets for use by the Corporation, and accordingly, costs associated with this operation are included with cost of sales in the statement of Earnings.</p>
Translation of Foreign Currencies	<p>The financial statements of foreign subsidiaries and the joint venture and foreign currency denominated balances of domestic operations are translated using year-end closing exchange rates for cash and short-term investments, accounts receivable, current liabilities, long-term debt and accrued pension cost. Historic exchange rates are used to translate inventories, prepaid expenses, fixed assets and deferred income taxes. Exchange rates in effect at the date of transaction are used to translate revenues and expenses, other than depreciation and amortization which are translated using the same historic rates applied in the translation of the related assets.</p> <p>Exchange gains and losses on translation of long-term debt are deferred and amortized to earnings over the remaining life of the debt. Exchange gains and losses from the translation of other balances together with gains and losses on transactions are included in the statement of Earnings.</p>
Inventories	<p>Finished products and work in process are valued at the lower of cost and net realizable value. Raw materials and supplies are valued at the lower of cost and replacement cost.</p>
Fixed Assets	<p>Property, plant and equipment are recorded at cost. Expenditures for improvements and renewals which extend economic life and for mine development are capitalized. Maintenance and repairs are charged to earnings as incurred excepting expenditures for periodic relines of blast furnaces which are accrued for in advance on a unit of production basis. The provision for such expenditures is included with net fixed assets.</p> <p>Depreciation of manufacturing plant and equipment, which comprises over 80 per cent of fixed assets, is provided using the straight-line method applied to the cost of the assets based on their estimated useful composite life of approximately 20 years commencing with commercial operation.</p> <p>Plant and equipment at raw material properties and mine development costs are either depreciated using the straight-line method at rates intended to amortize the cost of these assets over their estimated economic lives or amortized on a unit of production basis over the estimated recoverable raw material reserves.</p> <p>Interest incurred on funds borrowed to directly finance the development of new raw material properties and the construction of new manufacturing facilities is capitalized during the period of initial development and construction.</p>
Exploration, Research and Start-Up Costs	<p>Expenses in exploring for raw materials, investigating and holding raw material properties and costs of research and start-up of new production facilities are charged to earnings as incurred</p>
Pension Costs and Funding Obligations	<p>The employees of the Corporation are covered under several pension plans providing benefits which vary with the respective employee groups. Defined benefit plans cover all Canadian employees and salaried employees in the United States. Hourly-rated mine employees in the United States receive coverage under a multi-employer plan.</p> <p>The costs of pension benefits earned by employees for the defined benefit plans are determined using the projected benefit method pro rated on service and management's assumptions for the factors required in the calculation. The excess of present value of accrued pension benefits over fund assets and any adjustments arising in the plans are amortized over the expected average remaining service life of the respective employee groups. The pension cost for the multi-employer plan is the employer contribution which is determined using factors negotiated with the union representing the employee group.</p> <p>The funding obligation for defined benefit plans is determined by an independent actuary. The actuary's assumptions for funding may differ from those used by management for determining pension costs and consequently, the pension costs used for financial reporting may differ from amounts funded</p>
Income Taxes	<p>Income taxes are provided for on the deferred tax allocation basis. Since regulations in Canada and the United States permit the deduction of expenses in calculating taxable income which may not coincide with amounts recorded for financial reporting purposes, such differences, principally relating to depreciation, give rise to deferred income taxes in the financial statements.</p> <p>Investment tax credits on qualifying expenditures for production facilities and for research are deducted from such costs provided there is reasonable assurance that the credits will be realized.</p>

The Algoma Steel Corporation, Limited

Consolidated Financial Statements

Earnings and Retained Earnings

For the years ended December 31

Thousands of Dollars		1987	1986
Revenue	Sales	\$ 1,227,952	\$ 1,093,342
Operating Expenses	Cost of sales	1,071,039	1,048,985
	Depreciation and amortization	56,635	53,520
		1,127,674	1,102,505
	Earnings (loss) from operations	100,278	(9,163)
Financial Expense (Income)	Interest expense (note 1)	51,281	52,617
	Interest and other income	(4,622)	(2,709)
	Exchange loss on foreign currencies	4,811	13,057
		51,470	62,965
Earnings (Loss)	Before income taxes and equity earnings	48,808	(72,128)
	Income taxes - deferred (credit) (note 2)	18,151	(21,137)
	Before equity earnings	30,657	(50,991)
	Equity in earnings (loss) of associated company	—	(2,474)
	Before extraordinary items	30,657	(53,465)
	Extraordinary gains (losses) (note 3)	9,594	(81,380)
Net Earnings (Loss)		\$ 40,251	\$ (134,845)
Earnings per Common Share	Provision for dividends on preference shares	\$ 13,849	\$ 16,368
	Net earnings (loss) applicable to common shares	\$ 26,402	\$ (151,213)
	Per common share		
	Earnings (loss) before extraordinary items	\$ 0.97	\$ (4.59) *
	Net earnings (loss) applicable to common shares	\$ 1.53	\$ (9.93) *
	* restated to reflect shares issued as stock dividend in December 1987		
Retained Earnings	Balance at beginning of year	\$ 326,113	\$ 482,371
	Net earnings (loss)	40,251	(134,845)
	Dividends declared (note 12)	(19,401)	(20,798)
	Expenses relating to issue of common shares, net of income taxes of \$ 493	—	(615)
	Balance at end of year	\$ 346,963	\$ 326,113

See summary of significant accounting policies and notes to consolidated financial statements.

The Algoma Steel Corporation, Limited

Consolidated Financial Statements

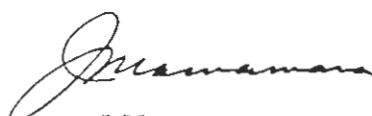
Financial Position

As at December 31

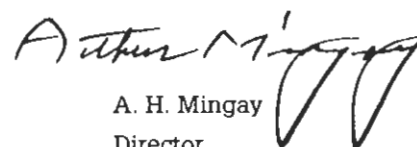
		Thousands of Dollars	
		1987	1986
Current Assets	Cash and short-term investments	\$ 260	\$ 14,074
	Accounts receivable	214,720	202,687
	Inventories (note 4)	321,126	297,895
	Prepaid expenses	5,443	4,656
		541,549	519,312
Current Liabilities	Bank overdraft	16,862	—
	Accounts payable and accrued liabilities	195,662	193,405
	Taxes payable	12,990	13,572
	Long-term debt due within one year	15,514	20,060
		241,028	227,037
Working Capital	Current assets less current liabilities	300,521	292,275
Other Assets	Long-term investments (note 5)	163,877	64,723
	Net fixed assets (note 6)	858,793	877,015
	Unamortized exchange loss on foreign currencies	5,362	21,370
	Unamortized debenture expense	1,929	2,263
		1,029,961	965,371
Total Investment	Working capital plus other assets	1,330,482	1,257,646
Other Liabilities	Long-term debt (note 7)	561,674	481,368
	Accrued pension cost (note 10)	30,350	33,060
	Deferred income taxes	124,238	72,572
			716,262
		\$ 614,220	\$ 670,646
Shareholders' Equity	Capital stock (note 11) Preference shares	\$ 132,570	\$ 215,440
	Common shares	134,687	129,093
	Retained Earnings	346,963	326,113
		\$ 614,220	\$ 670,646

See summary of significant accounting policies and notes to consolidated financial statements.

On behalf of the Board:



J. Macnamara
Director



A. H. Mingay
Director

The Algoma Steel Corporation, Limited

Consolidated Financial Statements

Changes in Financial Position

For the years ended December 31

Thousands of Dollars		1987	1986
Cash Provided From (Used For)			
Operations	Earnings (loss) from operations	\$ 100,278	\$ (9,163)
	Items included in earnings not resulting in an outlay of cash	67,384	56,071
	Decrease (increase) in operating working capital	(34,376)	66,743
		<u>133,286</u>	<u>113,651</u>
Investment Activities	Fixed assets - manufacturing plants	(38,454)	(120,985)
	- raw material properties	(6,904)	(9,641)
		<u>(45,358)</u>	<u>(130,626)</u>
	Long-term investments	(101,226)	(13,371)
	Proceeds from sales of fixed assets	14,816	2,111
	Proceeds from sale of investment in associated company	—	193,411
	Interest and other income	4,622	2,709
		<u>(127,146)</u>	<u>54,234</u>
Financing Activities	Interest on debt	(50,947)	(52,283)
	Dividends	(14,192)	(16,420)
	Reduction of long-term debt	(26,301)	(162,840)
	Preference shares purchased for cancellation	(82,870)	(3,043)
	Pension funding in excess of current expense	(14,293)	(8,192)
	Additional financing		
	Proceeds from issue of common shares	385	21,758
	Funds received for seamless tube mill construction	35,811	70,277
	Proceeds from long-term loans	115,591	—
		<u>(36,816)</u>	<u>(150,743)</u>
Cash (Loan) Position	Increase (decrease) during year	(30,676)	17,142
	Balance at beginning of year	14,074	(3,068)
	Balance at end of year	<u>\$ (16,602)</u>	<u>\$ 14,074</u>
Changes in Operating Working Capital			
	Decrease (increase) in accounts receivable	\$ (12,033)	\$ (21)
	Decrease (increase) in inventories	(23,231)	80,835
	Decrease (increase) in prepaid expenses	(787)	(245)
	Increase (decrease) in accounts payable and accrued liabilities	2,257	(14,907)
	Increase (decrease) in taxes payable	(582)	1,081
	Decrease (increase) in operating working capital	<u>\$ (34,376)</u>	<u>\$ 66,743</u>

See summary of significant accounting policies and notes to consolidated financial statements.

The Algoma Steel Corporation, Limited

Notes to Consolidated Financial Statements

1. Interest Expense	Thousands of Dollars	1987	1986
	Interest and expense on long-term debt	\$ 54,540	\$ 70,759
	Other interest	625	578
	Interest capitalized on loans for seamless tube mill construction	(3,884)	(18,720)
		<u>\$ 51,281</u>	<u>\$ 52,617</u>

2. Income Taxes

The effective income tax rate for the Corporation differs from the composite income tax rate of the various taxing jurisdictions in which it operates. A reconciliation between these rates follows:

	1987	1986
Composite income tax rate	49.3 %	(50.6) %
Increase (decrease) resulting from		
Operating losses of United States subsidiaries not tax effected	—	12.8
Certain exchange (gains) losses on foreign currency not tax effected	(0.9)	4.7
Interest expense on income debentures	6.4	4.6
Manufacturing and processing allowance	(6.1)	4.0
Federal and provincial resource allowances	(17.5)	(4.0)
Inventory allowance	—	(0.6)
Other	6.0	(0.2)
Effective income tax rate	<u>37.2 %</u>	<u>(29.3) %</u>

At December 31, 1987 the Corporation's United States subsidiaries have accumulated operating losses of approximately \$29 million on which tax benefits of \$10 million have not been recorded in the financial statements.

3. Extraordinary Gains (Losses)

Thousands of Dollars	1987	1986
Loss on early retirement of Tilden joint venture mortgage notes (1)		
Amount by which the purchase cost was less than the principal outstanding	\$ 9,005	\$ —
Realization of unamortized foreign currency exchange loss on retirement	(9,110)	—
Net loss on the transaction	(105)	—
Gains on sales of property (net of income taxes of \$3,511)	4,613	—
Reduction in income taxes from application of prior years' losses	5,086	—
Provision for write-down of assets and restructuring of operations (net of income tax credit of \$59,400)	—	(115,000)
Loss from restructuring of operations by associated company	—	(24,000)
Gain on sale of investment in associated company (net of income taxes of \$25,600)	—	57,620
	<u>\$ 9,594</u>	<u>\$ (81,380)</u>

(1) On October 1, 1987 the Corporation purchased, through a wholly-owned United States subsidiary, its share of Tilden Iron Ore Partnership notes thereby retiring the U.S. \$78.9 million principal amount of the indebtedness with the payment of U.S. \$71.0 million. Income taxes of \$3.8 million on the transaction were offset by an income tax recovery from the application of losses carried forward.

		1987	1986
4. Inventories	Thousands of Dollars		
	Finished products	\$ 64,078	\$ 77,694
	Work in process	84,117	66,178
	Raw materials and supplies	172,931	154,023
		<u>\$ 321,126</u>	<u>\$ 297,895</u>
5. Long-Term Investments	Thousands of Dollars		
	Joint venture	\$ 140,066	\$ 50,591
	Limited partnerships and other	23,811	14,132
		<u>\$ 163,877</u>	<u>\$ 64,723</u>
6. Net Fixed Assets	Thousands of Dollars		
	Property, plant and equipment		
	Manufacturing plants	\$ 1,600,264	\$ 1,566,023
	Raw material properties	232,687	239,432
		<u>1,832,951</u>	<u>1,805,455</u>
	Accumulated depreciation and amortization, and provision for blast furnace relines	974,158	928,440
		<u>\$ 858,793</u>	<u>\$ 877,015</u>
7. Long-Term Debt	Thousands of Dollars		
	Debentures (a)		
	7 3/8% series C maturing 1987	\$ —	\$ 12,000
	8 3/4% series D maturing 1991	17,800	20,727
	10 3/8% series E maturing 1994	31,000	31,072
	11 % series F maturing 1995	40,119	45,300
	17 3/8% series L maturing 1997	43,200	46,600
	Floating rate series G maturing 1999 (b)	60,000	60,000
	Floating rate series I maturing 1994 (b)	51,972	55,220
	11.71 % series M maturing 1990 (c)	129,930	138,050
	Floating rate series N maturing 1995 (d)	110,000	53,805
	Bank loans - secured (d)	19,385	—
	Short-term promissory notes (d)	40,000	—
	9.65% note maturing 2000 (e)	33,782	38,654
		<u>577,188</u>	<u>501,428</u>
	Total amount outstanding	577,188	501,428
	Less due within one year	15,514	20,060
		<u>\$ 561,674</u>	<u>\$ 481,368</u>

Sinking fund and other repayment requirements for each of the next five years, commencing in 1988, are (in millions of dollars) \$15.5, \$28.3, \$151.7, \$28.0 and \$56.9.

- (a) The debentures rank pari passu and are secured by a Trust Indenture containing a first floating charge on all assets of the Corporation in Ontario.
- (b) Series G are income debentures and bear non-taxable interest at 1 1/8% over one-half of the prime lending rate of a Canadian chartered bank. The Corporation is permitted to convert this obligation into series H debentures bearing taxable interest which varies from 3/8% to 3/4% over the prime lending rate of the bank.

Series I are income debentures in the principal amount of U.S. \$40 million and bear non-taxable interest which varies from 1 3/8% to 1 1/2% over one-half of the London Interbank Offering Rate (LIBOR) or, at the option of the Corporation, from 1 1/8% to 1 1/4% over one-half of the U.S. base rate of a Canadian chartered bank on United States dollar demand loans to commercial customers resident in Canada. The debentures are convertible, at the option of the Corporation, into a Canadian currency obligation bearing interest which varies from 1 1/8% to 1 1/4% over one-half of the prime lending rate of the

The Algoma Steel Corporation, Limited

Notes to Consolidated Financial Statements

7. Long-Term Debt, cont'd

bank. The Corporation is permitted to convert this obligation into series J debentures bearing taxable interest at various rates and, at the option of the Corporation, may be in either U.S. or Canadian currency. A United States currency loan would bear interest which varies from 7/8% to 1% over LIBOR or, at the option of the Corporation, from .42% to .55% over the U.S. base rate of the bank on United States dollar demand loans to commercial customers resident in Canada. A Canadian currency loan would bear interest which varies from .42% to .55% over the prime lending rate of the bank.

- (c) Series M debentures in the principal amount of U.S. \$100 million mature in November 1990 and bear interest at an effective rate of 11.71% commencing November 20, 1987. Prior to that date the effective interest rate from date of issue was 14.27%.
- (d) An agreement with three Canadian chartered banks provides a revolving line of credit aggregating \$309 million, in Canadian or equivalent United States funds. The funds available decline annually until maturity at December 31, 1995. Loans outstanding under this line at December 31, 1987 were \$110 million consisting of bankers acceptances. Since the Corporation has the ability to replace short-term debt with term loans under this line of credit, bank loans of \$19.4 million (including U.S. \$5.0 million) and short-term promissory notes of \$40 million are classified as long-term debt.
- (e) The 9.65% note, in the principal amount of U.S. \$26.0 million, is an obligation of a United States subsidiary and is repayable in annual instalments of U.S. \$2.0 million.

8. Commitments

- (a) The Corporation, as a participant in the Tilden Mining Company joint venture, is entitled to receive its 30% share of production and is committed to pay its share of costs including minimum charges for utilities. The Corporation's share of such minimum charges was \$4.6 million in 1987 and will average approximately \$3.5 million annually until 1992 when the commitment ends.
- (b) The estimated amount required to complete approved capital projects is \$40 million. At December 31, 1987 contractual commitments amount to \$18 million in respect of these projects.

9. Long-Term Leases

Rentals under long-term leases amounted to \$10.6 million in 1987. Future minimum rentals will aggregate \$40.6 million and in each of the next five years will be (in millions of dollars) \$7.4, \$6.4, \$5.4, \$4.9 and \$4.6. These rentals are payable principally under leases of steel processing plant and equipment which contain options to purchase and under leases of raw material properties.

10. Pension Costs

Effective January 1, 1987 the Corporation prospectively changed its accounting policy for the determination of pension costs and accrued pension benefits to adopt the revised recommendations of The Canadian Institute of Chartered Accountants. The Corporation's new policy is disclosed in the Summary of Significant Accounting Policies. The adoption of the new policy reduced 1987 pension costs approximately \$5 million, increasing net earnings approximately \$3 million. Pension costs charged to earnings were \$28.2 million in 1987 (\$29.7 million in 1986).

The status of the Corporation's accrued pension benefits at December 31 is summarized as follows:

Millions of Dollars	1987	1986
Present value of accrued pension benefits	\$ 560 (1)	\$ 460
Value of pension fund assets	440	400
Excess of present value of accrued pension benefits over fund assets	\$ 120	\$ 60
Accrued pension costs shown in the statement of Financial Position	\$ 30	\$ 33
Pension costs not recorded	\$ 90	\$ 27

(1) Includes \$61 million respecting pension benefit improvements negotiated in 1987.

11. Capital Stock**(a) Preference Shares**

Authorized - 3,902,800 Preference Shares, which rank prior to Class B Preference Shares and are issuable in series, of which 1,502,800 shares are reserved for conversion of series A shares into series B shares.
 - 12,000,000 Class B Preference Shares, issuable in series.

Thousands of Dollars	Number of Shares 1987	Stated Capital	
		1987	1986
Issued at December 31			
Preference Shares			
8% cumulative redeemable tax deferred series A	1,502,800	\$ 37,570	\$ 40,440
Floating rate cumulative redeemable retractable series C	—	—	50,000
Floating rate cumulative redeemable retractable series D	—	—	30,000
Class B Preference Shares \$2.00 cumulative redeemable convertible series 1	3,800,000	95,000	95,000
		<u>\$ 132,570</u>	<u>\$ 215,440</u>

Series A shares are entitled to annual dividends of \$2.00 per share payable quarterly; commencing with the quarterly payment December 1, 1988, dividends received on that and future quarterly dates will be taxable. They are redeemable at the option of the Corporation at \$25.00 per share and are exchangeable after September 1, 1988 on a share for share basis at the option of the holder into 9 3/4% cumulative redeemable Preference Shares series B on which dividends will be taxable. The Corporation is obligated to purchase in each twelve month period ending May 31 up to 120,000 series A or B shares to the extent that they are available at market prices not exceeding \$25.00 per share. The Corporation purchased for cancellation 114,800 series A shares in 1987 at prices averaging \$17.66 per share.

On May 31, 1987 the Corporation purchased all 2,000,000 outstanding series C Preference Shares at \$25.00 per share pursuant to a retractable feature attached to these shares. Similarly, on December 31, 1987 the Corporation purchased all 1,200,000 outstanding series D Preference Shares at \$25.00 per share.

Class B series 1 shares are entitled to annual dividends of \$2.00 per share payable quarterly. Subject to certain conditions, they are redeemable at the option of the Corporation at \$25.00 per share and a premium of \$1.25 which reduces annually. They are convertible at the option of the holder into .8676 of a common share at any time up to December 1, 1990. Commencing January 1, 1991 the Corporation is obligated to purchase annually 4% of the balance of Class B series 1 shares outstanding at December 2, 1990 to the extent that they are available at market prices not exceeding \$25.00 per share.

(b) Common Shares

Authorized - 30,186,632 shares of which 3,296,880 are reserved for conversion of Class B Preference Shares series 1 into common shares.

Thousands of Dollars	Number of Shares	Stated Capital
Issued		
Balance at January 1, 1987	17,021,108	\$ 129,093
Shares issued for cash to employees under special stock options	23,710	385
Shares associated with stock dividend at \$22.00 per share	236,765	5,209
Balance at December 31, 1987	<u>17,281,583</u>	<u>\$ 134,687</u>

The Algoma Steel Corporation, Limited

Notes to Consolidated Financial Statements

12. Dividends

Dividends were declared as follows:

Thousands of Dollars	1987	1986
Cash dividends		
Preference Shares		
Series A \$2.00 per share in 1987 and 1986	\$ 3,127	\$ 3,371
Series C \$0.79 per share in 1987 and \$1.71 in 1986	1,581	3,416
Series D \$1.54 per share in 1987 and \$1.67 in 1986	1,843	2,009
Class B Preference Shares		
Series 1 \$2.00 per share in 1987 and 1986	7,600	7,600
Common Shares	41 *	24
	<u>14,192</u>	<u>16,420</u>
Stock dividends		
Common Shares		
For each 100 shares held, one and four-tenths shares equivalent to \$.308 per share in 1987, and two and one-half shares equivalent to \$.30 in 1986.	5,209	4,378
	<u>\$ 19,401</u>	<u>\$ 20,798</u>

*Cash in lieu of fractional shares arising from stock dividend.

13. Related Party Transactions

The Corporation is a subsidiary of Canadian Pacific Enterprises Limited which at December 31, 1987 held approximately 54% of the Corporation's outstanding common shares. Canadian Pacific Enterprises Limited is a wholly-owned subsidiary of Canadian Pacific Limited, a diversified corporation with its head office in Montreal, Quebec, and consequently the Corporation is related to the numerous companies in the Canadian Pacific group.

The Corporation holds a 30% interest in the Tilden Mining Company, a 40% interest in the Huron Steel group, comprised of Huron Steel Products and The Mohawk Metal Products Limited Partnerships, and a 50% interest in the Superior Tube Limited Partnership.

In the normal course of business the Corporation sells its products at prevailing market prices and credit terms to its associates and to Canadian Pacific Limited and its subsidiary companies. Similarly, the Corporation regularly purchases iron ore pellets, transportation and other services and capital goods from the related parties. The Corporation has a revolving operating line of credit at competitive rates with Canadian Pacific Securities Limited in the amount of \$75 million.

Transactions with related parties and balances at year end are as follows:

Thousands of Dollars	1987	1986
Transactions during year		
Sales of product	\$ 55,852	\$ 56,027
Purchases, principally iron ore pellets, transportation and capital goods	96,212	95,180
Interest income from short-term investments	7	950
Interest expense on long-term debt	1,875	1,438
Additional investment in Tilden joint venture for retirement of mortgage notes	93,654	—
Funds received for seamless tube mill construction	36,694	78,131
Proceeds from sale of common shares of AMCA International Limited to Canadian Pacific Limited	—	193,411
Balances at December 31		
Accounts receivable	8,285	10,146
Accounts payable	978	739
Short-term promissory notes payable	40,000	—

14. Business Segments Information

Lines of Business

The Corporation is a vertically integrated steel producer which obtains most of its iron ore and coal requirements from properties which it owns, leases or in which it has an interest in Canada and the United States. The Corporation's revenue is derived almost entirely from the sale of rolled steel products and coal. Virtually all of the Corporation's assets are related to integrated steelmaking activities.

Operations by Geographic Area

Thousands of Dollars	1987	1986	1987	1986	1987	1986
	Consolidated		Canada		United States	
Sales						
External	\$ 1,227,952	\$ 1,093,342	\$ 1,055,902	\$ 942,870	\$ 172,050	\$ 150,472
Intra-enterprise sales between geographic areas	208,385	183,128	64,197	53,536	144,188	129,592
	<u>1,436,337</u>	<u>1,276,470</u>	<u>1,120,099</u>	<u>996,406</u>	<u>316,238</u>	<u>280,064</u>
Eliminations	(208,385)	(183,128)	(64,197)	(53,536)	(144,188)	(129,592)
Total	<u>\$ 1,227,952</u>	<u>\$ 1,093,342</u>	<u>\$ 1,055,902</u>	<u>\$ 942,870</u>	<u>\$ 172,050</u>	<u>\$ 150,472</u>
Earnings (loss)						
From operations	\$ 114,390	\$ (32,010)	\$ 89,951	\$ (21,133)	\$ 24,439	\$ (10,877)
Eliminations	(14,112)	22,847	(70)	1,435	(14,042)	21,412
	<u>100,278</u>	<u>(9,163)</u>	<u>\$ 89,881</u>	<u>\$ (19,698)</u>	<u>\$ 10,397</u>	<u>\$ 10,535</u>
Interest expense	(51,281)	(52,617)				
Other income	4,622	2,709				
Exchange loss on foreign currencies	(4,811)	(13,057)				
Income taxes - (deferred) credit	(18,151)	21,137				
Equity in earnings (loss) of associated company	—	(2,474)				
Earnings (loss) before extraordinary items	<u>30,657</u>	<u>(53,465)</u>				
Extraordinary items	9,594	(81,380)				
Net earnings (loss)	<u>\$ 40,251</u>	<u>\$ (134,845)</u>				
Identifiable assets at December 31	<u>\$ 1,571,510</u>	<u>\$ 1,484,683</u>	<u>\$ 1,333,877</u>	<u>\$ 1,329,604</u>	<u>\$ 237,633</u>	<u>\$ 155,079</u>

Intra-enterprise sales between geographic areas are at market prices for similar products. Canadian operations include export sales of approximately \$241 million in 1987 (\$199 million in 1986).

The Algoma Steel Corporation, Limited

Ten-Year Summary of Operating and Financial Data

	Tons in thousands and dollars in millions excepting per share data	1987	1986
Operations	Production - Iron Ore (1)	G.T. 2,939	2,394
	- Coal (2)	N.T. 3,996	3,567
	- Coke	N.T. 1,248	1,139
	- Iron	N.T. 2,428	2,184
	- Raw Steel	N.T. 2,590	2,422
	Shipments - Steel Products	N.T. 2,125	2,032
Earnings and Related Statistics	Sales	\$ 1,228.0	1,093.3
	Earnings From Operations	\$ 100.3	(9.2)
	Earnings Before Income Taxes and Equity Earnings	\$ 48.8	(72.1)
	Income Taxes	\$ 18.2	(21.1)
	Equity in Earnings of Associated Company	\$ —	(2.4)
	Net Earnings	\$ 40.3 (12)	(134.8) (14)
	Applicable to Preference Shares	\$ 13.8	16.4
	Applicable to Common Shares	\$ 26.4 (12)	(151.2) (14)
	Dividends Paid in Cash		
	On Preference Shares	\$ 14.2	16.4
	On Common Shares	\$ —	—
	Earnings Retained in Business	\$ 20.9	(156.3)
	Cash Provided from Operations	\$ 133.3	113.7
	Per Common Share		
	- Net Earnings (3) and (4)	\$ 1.53 (12)	(9.93) (14)
	- Cash Provided from Operations (3) and (4)	\$ 6.92	6.39
	- Dividends Paid in Cash	\$ —	—
	Net Earnings as per cent of		
	- Sales	% 3.3	(12.3)
	- Average Common Shareholders' Equity (5)	% 5.6	(29.1)
	- Average Total Investment (6)	% 5.4	(7.2)
	Cost of Products Sold as per cent of Sales	% 85.2	93.5
	Depreciation and Amortization	\$ 56.6	53.5
Capital Expenditures	Manufacturing Plants	\$ 38.5	121.0
	Raw Material Properties	\$ 6.9	9.6
	Total	\$ 45.4	130.6
Long-Term Debt	Borrowings - Debentures	\$ —	—
	- Other	\$ 115.6	—
	- Total	\$ 115.6	—
	Repayments	\$ 26.3	162.8
	Increase (Decrease) Due to Change in Exchange Rate	\$ (13.5)	(5.5)
	Interest and Expense	\$ 50.7 (13)	52.0 (13)
Financial Position at Year-End	Current Assets	\$ 541.5	519.3
	Current Liabilities	\$ 241.0	227.0
	Working Capital	\$ 300.5	292.3
	Operating Working Capital (7)	\$ 332.6	298.3
	Long-Term Investments	\$ 163.9	64.7
	Net Fixed Assets	\$ 858.8	877.0
	Total Assets	\$ 1,571.5	1,484.7
	Total Investment (8)	\$ 1,330.5	1,257.6
	Long-Term Debt (9)	\$ 561.7	481.4
	Preference Shares	\$ 132.6	215.4
	Common Shareholders' Equity	\$ 481.7	455.2
	Number of Common Shares Issued (000) (10)	No. 17,282	17,258
	Common Shareholders' Equity Per Share (11)	\$ 27.82	26.31
	Number of Common Shareholders	No. 4,093	4,415

Notes

- (1) Includes mines operated by the Corporation and its share of production from joint ventures.
- (2) Metallurgical and steam coal.
- (3) After provision for dividends on preference shares.
- (4) Based on weighted average number of common shares outstanding during the year restated for stock dividends declared in 1983, 1984, 1985, 1986 and 1987.
- (5) Net earnings are after deduction of amount applicable to preference shares.
- (6) Net earnings are before deduction of interest on long-term debt net of income taxes, and total investment is before deduction of long-term debt due within one year.
- (7) Includes accounts receivable, inventories and prepaid expenses, less accounts payable and accrued liabilities, and taxes payable.

1985	1984	1983	1982	1981	1980	1979	1978
2,978	2,866	2,424	1,983	3,643	3,732	4,125	4,109
3,449	2,918	2,490	2,488	2,732	2,907	2,868	2,069
1,334	1,246	1,042	1,009	1,411	1,470	1,546	1,424
2,506	2,307	2,155	1,809	2,907	3,039	3,374	3,148
2,742	2,528	2,306	1,899	3,017	3,179	3,528	3,317
2,063	1,951	1,757	1,472	2,519	2,415	2,597	2,456
1,176.7	1,104.3	859.5	874.2	1,426.4	1,149.1	1,081.2	864.2
52.1	14.9	(123.9)	(83.9)	234.7	146.4	144.5	83.9
(17.4)	(61.8)	(186.4)	(123.8)	225.8	121.2	120.2	57.7
(10.3)	(21.6)	(79.4)	(57.7)	93.4	38.8	35.3	10.7
(2.7)	(5.5)	(19.7)	25.7	26.8	26.8	27.0	22.6
(3.0) (15)	(45.7)	(126.6)	(40.4)	159.2	109.2	111.9	77.1 (16)
16.7	17.2	10.1	12.3	12.8	11.6	10.7	9.5
(19.7) (15)	(62.9)	(136.8)	(52.7)	146.4	97.6	101.2	67.6 (16)
16.8	16.7	10.0	12.5	12.6	11.6	10.6	9.4
—	—	—	14.0	15.4	12.3	8.2	—
(24.2)	(66.3)	(140.8)	(66.9)	131.2	85.3	93.1	67.7
102.4	73.6	(56.7)	59.6	207.2	155.0	154.9	93.0
(1.30) (15)	(4.14)	(9.01)	(3.47)	9.64	7.59	8.00	5.35 (16)
5.64	3.72	(4.40)	3.11	12.81	11.15	11.40	6.61
—	—	—	1.00	1.10	1.00	.70	—
(0.3)	(4.1)	(14.7)	(4.6)	11.2	9.5	10.3	8.9
(3.3)	(9.9)	(18.6)	(6.3)	18.2	14.8	19.0	15.0
2.0	(1.4)	(5.7)	(0.9)	13.2	11.0	13.2	10.5
88.8	91.5	105.4	100.5	78.2	81.2	80.9	84.1
54.1	55.5	55.4	53.5	49.7	47.3	39.9	35.7
128.8	12.0	25.1	175.5	246.6	82.4	65.2	24.2
14.4	12.4	6.5	9.9	18.1	24.8	24.1	15.0
143.2	24.4	31.6	185.4	264.7	107.2	89.3	39.2
—	—	—	172.4	—	—	106.9	—
76.5	36.4	55.7	34.3	—	35.0	0.3	3.5
76.5	36.4	55.7	206.7	—	35.0	107.2	3.5
9.0	22.3	7.9	—	3.2	39.9	62.7	17.1
16.5	18.2	—	—	—	—	—	—
53.4 (13)	66.8	63.4	40.2	29.8	27.5	27.6	24.8
585.8	535.4	514.6	492.1	608.6	562.1	435.5	362.4
234.2	212.3	194.7	173.9	235.8	157.2	150.9	155.5
351.6	323.1	319.9	318.2	372.8	404.9	284.6	206.9
365.0	331.3	321.6	309.3	377.0	319.8	279.8	238.5
194.3	190.5	205.7	242.2	227.3	212.1	197.2	134.2
967.8	895.3	944.7	990.8	879.5	644.8	587.0	549.8
1,784.1	1,646.8	1,668.2	1,728.7	1,718.2	1,422.1	1,224.1	1,050.8
1,549.9	1,434.5	1,473.5	1,554.8	1,482.4	1,264.9	1,073.2	895.3
659.5	576.8	533.8	489.6	290.6	293.7	298.6	248.7
218.5	219.6	222.7	130.5	133.5	136.5	139.8	140.0
584.2	604.0	666.5	805.3	872.2	741.0	578.7	485.4
15,183	15,183	15,183	15,183	15,183	12,866	12,650	12,632
38.40	39.70	43.84	52.99	57.39	57.54	45.69	38.37
4,929	5,188	5,701	6,489	7,142	7,812	8,748	9,369

(8) Total assets less current liabilities.

(9) Excludes long-term debt due within one year.

(10) At December 31 restated for stock dividends declared in 1983, 1984, 1985, 1986 and 1987.

(11) Based on common shares issued at December 31 restated as in Note (10).

(12) Includes an extraordinary credit of \$9.6 million amounting to \$.56 per common share.

(13) Excludes capitalized interest of \$3.9 million, \$18.7 million and \$13.5 million for 1987, 1986 and 1985, respectively.

(14) Includes an extraordinary charge of \$81.4 million amounting to \$.534 per common share.

(15) Includes an extraordinary credit of \$6.8 million amounting to \$.45 per common share.

(16) Includes an extraordinary credit of \$7.5 million amounting to \$.59 per common share.

The Algoma Steel Corporation, Limited

<i>Directors</i>	<i>Principal Officers</i>	<i>Corporate Information</i>	<i>Products and Sales Office Locations</i>
<p>Russell S. Allison Montreal, Quebec President CP Rail</p> <p>* Robert W. Campbell Calgary, Alberta Chairman Canadian Pacific Limited</p> <p>† Stuart E. Eagles Toronto, Ontario Vice-President Corporate Canadian Pacific Limited</p> <p>*§ James F. Hankinson Calgary, Alberta Group Vice-President Canadian Pacific Limited</p> <p>§ Charles H. Hantho Islington, Ontario Chairman and Chief Executive Officer C-I-L Inc.</p> <p>* John Macnamara Sault Ste. Marie, Ontario Chairman and Chief Executive Officer The Algoma Steel Corporation, Limited</p> <p>§ Arthur H. Mingay Toronto, Ontario Former Chairman Canada Trust</p> <p>* Peter M. Nixon Sault Ste. Marie, Ontario President and Chief Operating Officer The Algoma Steel Corporation, Limited</p> <p>† Leonard N. Savoie Sault Ste. Marie, Ontario President and Chief Executive Officer Algoma Central Railway</p> <p>Robert J. Theis Sr. Syracuse, New York President Westover Holding Corp.</p> <p>*† Adam H. Zimmerman Toronto, Ontario Chairman and Chief Executive Officer Noranda Forest Inc.</p>	<p>THE ALGOMA STEEL CORPORATION, LIMITED</p> <p>John Macnamara Chairman and Chief Executive Officer</p> <p>Peter M. Nixon President and Chief Operating Officer</p> <p>Robert N. Robertson Senior Vice President – Commercial</p> <p>Ross H. Cutmore Vice President – Finance and Accounting</p> <p>Gary S. Lucenti Vice President – Manufacturing</p> <p>Gerry B. Hudson Vice President – Sales</p> <p>James T. Melville Vice President, Treasurer and General Counsel</p> <p>Paul J. Paciocco Vice President – Engineering and Technical Services</p> <p>Robert Turpin Vice President – Employee Relations</p> <p>Paul C. Finley Secretary</p> <p>William J. Reed Controller – Steel and Iron Ore Operations</p> <p>CANNELTON INDUSTRIES, INC.</p> <p>Allen S. Pack President and Chief Executive Officer</p> <p>Naaman G. Clonch Vice President – Assistant to the President</p> <p>A. Douglas Tolley Vice President – Operations</p>	<p>EXECUTIVE OFFICES Sault Ste. Marie, Ontario</p> <p>MANUFACTURING AND MINING FACILITIES (Wholly Owned)</p> <p>Canada</p> <p>Sault Ste. Marie, Ontario The Algoma Steel Corporation, Limited Steelworks Division Marine Division Welded Beam Division Tube Division</p> <p>Wawa, Ontario Algoma Ore Division</p> <p>United States</p> <p>West Virginia Cannelton Industries, Inc. Kanawha Division, Cannelton Pocahontas Division, Superior Indian Creek Division, Peytona</p> <p>Maple Meadow Mining Company, Fairdale</p> <p>(Partnerships and Joint Ventures)</p> <p>Canada</p> <p>Brampton, Ontario * Ferrum Inc. (50%)</p> <p>Windsor, Ontario Huron Steel Products, an Ontario Limited Partnership (40%) The Mohawk Metal Products Limited Partnership (40%)</p> <p>Edmonton, Alberta Superior Tube Limited Partnership (50%)</p> <p>United States</p> <p>Ishpeming, Michigan Tilden Mine Joint Venture (30%)</p> <p>* Effective January 1, 1988, subject to final documentation.</p>	<p>PRODUCTS</p> <p>Sheet</p> <p>Hot Rolled and Cold Rolled Coils and Cut to Length</p> <p>Cold Rolled Sheet for Motor Laminations</p> <p>Plate</p> <p>Hot Rolled Sheared and Gas Cut Floor (Pattern)</p> <p>Heat Treated Normalized Quenched and Tempered</p> <p>Seamless Tubular Products</p> <p>Casing</p> <p>Tubing</p> <p>Line Pipe</p> <p>Standard Pipe</p> <p>Mechanical Tubing</p> <p>Couplings and Coupling Stock</p> <p>Structurals</p> <p>Wide Flange</p> <p>Bearing Pile Shapes</p> <p>Standard Angles, Channels and Beams</p> <p>Welded Wide Flange Shapes</p> <p>Welded Special Shapes</p> <p>Rails and Tie Plates</p> <p>SALES OFFICES</p> <p>Head Sales Office Mississauga, Ontario</p> <p>Regional Sales Office Calgary, Alberta</p> <p>Algoma Tube Corporation Houston, Texas Denver, Colorado</p>

* Member of Executive Committee

† Member of Compensation Committee

§ Member of Audit Committee



THE ALGOMA STEEL CORPORATION, LIMITED • SAULT STE. MARIE, ONTARIO, CANADA