Hudson's Bay Company

Annual Report 1991

Company Profile

Hudson's Bay Company is Canada's oldest corporation and one of its largest retailers.

Through its three operating divisions, Hudson's Bay Company covers the Canadian retail market across all price zones and from coast to coast. On a combined basis, it accounts for approximately 8% of Canadian retail sales (excluding food and autos).

The Company aims to develop its human and material resources and capitalize on its experience in merchandising to anticipate and satisfy the needs of customers for the goods and services they seek at fair prices, and thereby earn a satisfactory return for its shareholders.

A Brief History

King Charles II granted, on May 2, 1670, to 18 investors, a Charter incorporating them as the Governor and Company of Adventurers of England trading into Hudson's Bay (HBC). This followed the successful voyage of the ketch "Nonsuch", to trade for furs. During its first century, HBC established forts on Hudson Bay and traded with the Native Peoples.

As competition from the North West Company increased in the 1780's, HBC moved into the interior. The two rival companies amalgamated in 1821 under the Hudson's Bay name.

In 1870, HBC's chartered territory, Rupertsland, was transferred to the Government of Canada in return for farm lands in the prairie provinces which were sold to settlers during the next 85 years.

Early in this century, HBC turned its attention to retailing which became its most important activity. HBC built downtown department stores in each of the major cities of Western Canada (1913 –1968). It moved into eastern Canada through acquisitions (1960 and 1971) and expanded to the suburbs of major Canadian cities beginning in the 1960's. It acquired Zellers in 1978 and Simpsons the following year. Simpsons was merged into the Bay over the period 1986 –1991.

HBC acquired control of Markborough Properties in 1973 and real estate was an important segment of HBC's activities until Markborough was spun-off to HBC shareholders in 1990.

HBC had major investments in oil and gas (Hudson's Bay Oil & Gas, Siebens and Roxy Petroleum) between 1950 and 1987.

In the mid-1980's HBC disposed of a number of "non-strategic" assets including its Northern Stores, Wholesale and Fur divisions.

In 1979, Kenneth R. Thomson and his family interests acquired a 75% controlling interest in HBC.

HBC was continued as a Canadian corporation in 1970.

Financial Highlights

	Year Ended January 31, 1992	1991*
	$ millions	$ millions
Sales and Revenue	**5,032**	4,970
Earnings Before Interest and Income Taxes	**284**	318
Net Earnings	**83**	158
Cash Flow From Earnings	**185**	203
Capital Expenditures	**122**	120
Debt	**1,335**	1,243
Equity	**1,226**	1,172
Debt: Equity Ratio	**1.1:1**	1.1:1

Per Common Share	**$**	$
Net Earnings	**1.61**	2.01**
Cash Flow From Earnings	**3.67**	4.35
Dividends	**0.80**	0.80
Equity	**24.43**	23.53

* Excludes Markborough Properties Inc., which was distributed to shareholders effective August 1, 1990

** $3.34 after non-recurring tax loss recovery

Donald McGiverin

Directors' Report To Shareholders

SUMMARY

"The recession that refused to go away" wreaked havoc on the Canadian retail industry in 1991. Some retailers were forced to close their doors; many more have reported losses for the year. Our results – a 15.8% reduction in "regular" earnings to $82.8 million – were amongst the best in the industry. Our earnings were sustained by a strong performance by Zellers and by a welcome reduction in interest rates.

The outlook for 1992 is for a further small decline in consumer spending. We are prepared for another difficult year, characterized by intense price competition and requiring a continuing priority on expense and inventory management. Despite this, we believe that an improvement in our earnings is achievable.

NOTABLE EVENTS

a) The Recession

Canada entered 1991 in a recession but with some expectation that it might be both mild and short-lived. Indeed, GNP recovered in the second quarter only to fall back again in the second half. Seasonally adjusted unemployment rose from 9.7% in January to 10.3% in December. The recession coincided with the introduction of the Federal Goods and Services Tax in January and with a related increase in cross-border shopping. Together, these factors had a devastating effect on consumer spending in Canada. Sales of "Department Store Type Merchandise" were well below the previous year in every month of 1991 and for the calendar year as a whole were down by 10.7%. As a result, your Company's 1.3% sales increase represented a substantial gain in market share.

The Simpsons merger in July 1991 changed the Toronto shopping landscape. At Scarborough Town Centre the Bay moved into the former Simpsons location and Sears now occupies the former Bay store. The Bay now operates 23 stores in the Toronto market area.

b) Bay/Simpsons Merger

The operations of Simpsons in the Toronto market were merged into the Bay in the summer of 1991 with the exception of stores in malls which already included the Bay. These latter Simpsons locations were sold to Sears Canada for approximately $37 million. The merger of Simpsons into the Bay did not have a material impact on earnings.

Simpsons was acquired by HBC in 1978. Its stores outside the Toronto area were merged into the Bay in 1986 and 1989. It was our intention to operate Simpsons as an upscale traditional department store in the Toronto market. However the recession which has had a disproportionate effect in Ontario, the lowering of expectations for Ontario's long-term growth and the continued failure of Simpsons to meet its profit projections caused management and your Board to conclude reluctantly that we could no longer afford to operate two competing traditional department store groups in the Toronto market. In this report, and in the financial statements, Simpsons results for 1991 and prior years have been merged with those of the Bay.

c) Towers Re-Launch

Forty-seven former Towers stores were re-launched as Zellers stores on April 15, 1991. The Towers stores had been purchased by Zellers in November, 1990. The former Towers stores made a positive contribution to the record earnings achieved by Zellers in 1991 and further improvement in the operations of these stores is anticipated. For further details on the re-launch, see page 12.

George Kosich

BUYING STRATEGIES IN A GLOBAL ECONOMY

The current globalization that is occurring throughout the world demands that our base of business cannot remain insular, but must be more international in vision, scope and activity.

Most industries, including ours, will not survive without the knowledge and resources to acquire either revenue or merchandise and services from outside our domestic market.

This accelerating change has become pervasive because of free trade in North America, Europe and Asia; cross-border shopping; the mobility of the consumer; the expanded knowledge, sophistication and changing attitudes of the consumer; the continual changes in technology; the increased efficiency in transportation and distribution logistics; easier global communications; and the ease and affordability of travel.

We intend to constantly monitor emerging third-world markets, principally in Asia, to ensure our ability to access them rapidly as opportunities arise and, when they do, we will source the product directly to provide the best possible value for our customers.

We will also utilize Europe and the United States to complement our needs for trend-setting fashion products and to provide fashion direction for our Asian and domestic purchases.

Globalization is not a threat to most of our current Canadian suppliers who are efficient, consumer-conscious, technologically-advanced and well-capitalized. It can pose a threat to importers and subsidiaries of U.S. manufacturers. As we strive to give the best values to our customers and ensure that we are competitive with U.S. retailers at our border-towns, we must streamline the distribution cycle. Direct factory-to-stores must be our most effective course of distribution.

Hudson's Bay Company, after 322 years in business, understands very clearly that elimination of manufacturing jobs in Canada can endanger the well-being of Canada and our customers.

We value our contribution to the Canadian heritage and also understand the need for an economically sound Canadian manufacturing sector.

We will always procure a Canadian-made product if the price, quality, fashionability and delivery is the same or better than an imported product.

We are continuing to work very closely with our Canadian vendors who will supply the majority of our merchandise for the foreseeable future. Canadian vendors enjoy the advantages of close proximity to our stores and familiarity with our markets. We have recently introduced linked computers and "Just-In-Time" procurement with many of our suppliers to ensure in-stock positions and continuing growth. We look forward to working in partnership with our Canadian resources to develop marketing plans that will generate new business and mutual benefits.

Our objective is quite clear; to procure goods of the quality and fashionability that our customers desire at prices that represent the best value.

George Kosich

1991 RESULTS

Earnings were $82.8 million ($1.61 per share) in 1991 compared with "regular" retail earnings of $98.3 million ($2.01 per share) the year before. (A tax loss recovery and six months of earnings from Markborough prior to its spin-off increased 1990 reported earnings to $163.3 million or $3.46 per share.)

Earnings before interest and taxes declined to $284.1 million from $317.6 million for HBC Retail in 1990 as increased operating profit at Zellers and a profit on the sale of an investment in a shopping centre failed to offset a substantial decline in operating profit at the Bay.

The Bay in Burlington Mall, acquired from Sears and re-opened in the fall of 1991 as the prototype Bay store for the 1990's, with expanded space for apparel and Market Square departments.

A 19.7% sales increase – primarily due to the addition of Towers – and a marginal improvement in the gross profit rate were the principal factors in the $17.3 million increase in Zellers' operating profit to $217.9 million.

Operating profit at the Bay dropped to $59.4 million from $122.1 million in 1990 because of reduced sales throughout the year and heavy markdowns. These were required to respond to intense competitive price cutting in fashion apparel, including numerous bankruptcy sales during the Christmas season.

The Company realized a pre-tax profit of $15.2 million on the sale of a participating debenture in the Scarborough Town Centre shopping mall in October 1991. The debenture had been acquired by Simpsons on its entry into the Centre in 1973. The opportunity to sell arose as a result of a change in ownership of the Centre.

Interest expense at $144.6 million declined by $10.6 million from the year before, principally because of a reduction of both long and short-term rates. Average debt was higher as growth in assets and a reduction in outstanding preferred shares more than offset an increase in common share equity.

Cash Flow

Cash flow from earnings at $184.8 million was down from $203.2 million in 1990. Cash required for investing activities at $159.0 million was down by $127.2 million from the previous year with the 1990 purchase of Towers accounting for most of the difference. There was an increase in working capital of $90.9 million in 1991 compared with a decrease of $15.8 million the year before.

The net cash outflow of $109.7 million was financed by increases of $94.0 million in debt and $15.7 million in equity.

The debt equity ratio at year-end of 1.1:1 was unchanged from the previous year.

Financial

The decline in interest rates in 1991 – the prime rate fell from 11.75% on February 1, 1991 to 7.5% on January 31, 1992 – provided the Company with an opportunity to refinance part of its debt at lower rates. During the year debt amounting to $88.3 million was redeemed or called for redemption prior to maturity and a further $191.4 million in debt was retired at maturity. In addition, the Company's remaining $97.9 million of outstanding preferred shares which had become more expensive to service than debt, were purchased for cancellation or called for redemption. These debt and preferred share issues have been replaced principally by floating rate debt.

This refinancing activity, together with the sale in March 1991 of three million common shares from Treasury, contributed to the reduction of $10.6 million in interest costs.

For further discussion of the results and financial condition of the Company, please refer to the "Management Discussion and Analysis" section of this annual report beginning on page 15.

OUTLOOK FOR 1992

We expect spending on department store type merchandise will continue to decline in 1992. Department store sales are also expected to decline, but should outperform the rest of the market. While certain economic indicators have begun to turn positive – such as interest rates and housing outlook – consumers remain uncertain about their future job security. Corporate restructuring will keep unemployment levels high in 1992, helping to contribute to the decline in retail spending.

Consumers will put an even higher priority on value. Those retailers who do not have a well understood value offer will lose market share to their competitors.

Recent Federal government initiatives on cross-border shopping should provide some assistance to the retail industry this year. Provincial governments could also be helpful by integrating their sales taxes with the GST and in those provinces where it is now illegal, allowing Sunday shopping.

We believe that we have adjusted every aspect of our business to the harsh realities of the current marketplace and that our results for 1992 should show some improvement.

APPRECIATION

In a recession year there is constant pressure on employees to do more with less. Our employees have responded magnificently to the challenge and we express our grateful appreciation to them.

We also thank our customers, our suppliers and our shareholders for their continuing support.

On behalf of the Board

DONALD S. McGIVERIN,
Governor

GEORGE J. KOSICH,
President

March 12,1992

Zellers store in Fairview Mall, St. Catharines, one of ten new Zellers stores opened in 1991.

the Bay

Results

	(in millions of dollars) This Year	Last Year
Sales and revenue	**2,118.4**	2,322.1
Operating profit	**59.4**	122.1
Assets employed	**1,237.2**	1,293.7

During 1991, the Bay acquired six (net) Toronto-area Simpsons stores when Simpsons operations were discontinued in July. The remaining Simpsons stores, in mall locations where the Bay had existing stores, were sold to Sears Canada and the Bay obtained one store in Burlington, Ontario from Sears Canada.

The continuing severe recession in Canada was marked by sharply reduced consumer spending. This led to intensified competitive pressure, price reductions and lower gross margins.

Consequently, sales and revenue, at \$2.1 billion, fell 8.8% from \$2.3 billion in 1990 and operating profit fell to \$59.4 million from \$122.1 million. The results for 1990 include a full year of Simpsons operations. The results for 1991 include all Simpsons operations for the first six months and results of the merged stores for the second half of the year. Operating results were also reduced by \$10 million due to restructuring costs in the first quarter.

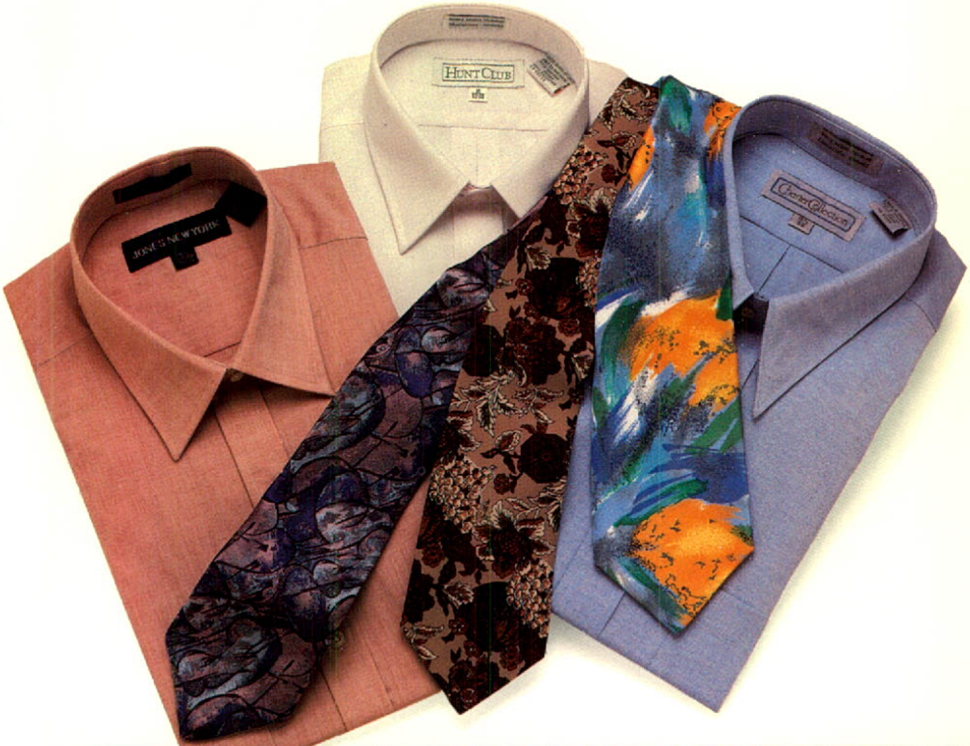
During the year, four new stores were opened; in Burlington, Bedford (Halifax), Rosemere (Montreal) and Metrotown (Burnaby). The former Sears store in Burlington represents the prototype for Bay stores this decade. It features expanded space and contemporary environments for women's, men's and children's apparel, accessories and shoes. In addition, "Market Square" environments for linens, housewares, china, stationery and candy feature a wide range of quality products and attractive shopping experiences.

Replacement stores were opened in the new Hudson's Bay Centre in downtown Edmonton and in the expanded St. Laurent Shopping Centre in Ottawa.

Renovations were completed in Surrey, B.C., St. Albert, Alberta and Londonderry (Edmonton), which created new, contemporary environments throughout the stores with expanded space for fashions and "Market Square" departments.

A new store is scheduled to open in Quebec City in the former Pascal location in the Fleur de Lys Mall this fall.

We expect that the severe economic conditions experienced throughout 1991 will continue well into this year and, perhaps, beyond. These conditions will limit our growth prospects and will require the Bay to continue to streamline its operations, reduce expenses and manage inventories effectively.



Women's sportswear in the new Bay store in Rosemere, north of Montreal.

"Our mission is to be Canada's best fashion department store by offering broad, dominant assortments, quality and value, fashion and trend leadership, a high level of customer service and an unremitting guarantee of performance."

Bob Peter

When the Bay took over the Simpsons Queen Street store, it retained its outstanding distinctions such as the West End Shop, Avon Galleries and The Room, shown here.

Store Profile

The Bay operates 89 department stores from coast to coast in Canada. It competes aggressively in the mid range urban and suburban markets, with a strong franchise in the downtowns of major cities. It provides its customers with superior value by offering fashionable good quality merchandise at popular prices backed by traditional department store guarantees and services. The Bay promotes its own credit card and accepts major bank cards.

Merchandise selection and procurement and sales promotion are centralized. A number of service functions are integrated on a corporate basis to reduce costs and improve performance.

Bay stores are tailored by price level and fashion appeal to fit the communities in which they are located. They vary in size from 21,000 sq. ft. in Banff, Alberta to 890,000 sq. ft. in downtown Toronto with most suburban branches in the 120,000 to 165,000 sq. ft. range.

Store Statistics

(February 1, 1992)	**Stores**	Square Feet (000's)
Nova Scotia	**4**	463
Quebec	**18**	2,800
Ontario	**32**	5,707
Manitoba	**4**	1,044
Saskatchewan	**3**	457
Alberta	**15**	2,125
British Columbia	**13**	2,189
	89	14,785

The Great Downtown Store

Vancouver, men's wear.

Vancouver, a landmark since 1926.

Heather Andrechuk, Manager, Queen Street, Toronto on location in The Room. Ms. Andrechuk knows her flagship stores, having previously managed Winnipeg and Vancouver.

"A company's flagship store is not like any other store anywhere. It's different in size, in layout, in merchandise and, above all, in its quality of visual entertainment."

Rick Sorby, the Bay's Vice-President, Downtown Stores, and Heather Andrechuk, Manager of the Bay's Queen Street store in downtown Toronto, share not only a common view of what a truly great downtown store must be, but also a driving commitment to ever-rising standards of excellence for the Bay's own flagship stores.

"Our Downtown Stores in Vancouver, Calgary, Winnipeg, Toronto and Montreal are on the way to becoming comparable to some of the best department stores in the world; Harrods in London, Nieman Marcus in Dallas, Gallerie Lafayette in Paris, or Seibu in Tokyo".

As in these great stores, quality is the touchstone for success. For the Bay, quality begins with the name Hudson's Bay Company. This quality extends through the range and variety of merchandise assortments, customer service, shopping environments, special events and special promotional activities.

"Great stores market with a difference. They are the fashion leaders with new and unique merchandise and continually changing presentations to add visual entertainment to outstanding value and superior service."

Location is a major determinant of a great downtown store's success. It must be central to a high daytime pedestrian traffic and well served by public transportation. The Bay enjoys direct access to the subway in Montreal and Toronto and to the LRT in Calgary and Vancouver.

Montreal (originally Morgans), women's shoes.

Winnipeg, showing skywalk to Portage Place.

Toronto, Queen Street, Market Square.

"Great Downtown Stores must offer first class ancillary services, such as portrait studios, beauty salons, pharmacies, travel offices, restaurants, optical services and a wide range of other service businesses."

Hudson's Bay Company Downtown Stores are unique blends of tradition and innovation. To help achieve its goal of differentiating itself from all competitors, it conceived a distinct program of sales promotion and event marketing. In April, after two years of planning, all downtown Stores will present a month-long spectacular South East Asian promotion featuring Indonesia, Thailand and the Philippines.

"The strategy for these events is to research profitable new business opportunities and showcase the merchandise with theatre and excitement. The Downtown Stores will be a visual extravaganza of special decor, performing artisans, singers and dancers from all three countries."

The spectaculars will also meet another key objective; provide fashion and merchandise leadership for other stores in the chain with pioneering events and presentations.

"Our large downtown stores have a major strategic and uniquely Canadian advantage. The downtown cores of our principal cities are alive and well — they don't close down at six o'clock in the evening as so many U.S. cities do. Our big cities are still 'downtown' cities."

Zellers

Results

	This Year	Last Year
(in millions of dollars)		
Sales and revenue	**2,788.8**	2,329.9
Operating profit	**217.9**	200.6
Assets employed	**1,169.8**	814.4

Zellers successfully integrated 47 Towers/Bonimart stores in Ontario, Quebec and the Maritimes into its operations during 1991 in addition to opening 10 new Zellers outlets.

Sales and revenue for Zellers' expanded operations during the year rose 19.7% to \$2.8 billion from \$2.3 billion. Operating profit rose 8.6% to \$217.9 million from \$200.6 million.

Zellers' strong gains during the year, despite a deep and continuing national economic recession, reflect the Company's strategy of offering an attractive combination of low prices and outstanding value supported by aggressive marketing and advertising. Substantial market share gains were achieved throughout Canada.

Most merchandise groupings also reported increased market share. In hardlines, housewares and home fashions led the gains and in fashions, men's and children's wear achieved notable sales increases.

The Towers stores acquired during the year complemented existing Zellers locations and have advanced the Company's expansion strategy and in particular have strengthened its position in the Toronto market. For details on the integration of Towers into Zellers, see page 12.

During the year, Zellers also initiated a \$40 million program to replace all point-of-sale systems during the next three years. The upgraded facilities will speed the passage of customers through our checkouts and improve our marketing information.

This year Zellers plans to open at least six new stores. Club Z and Zellers' credit card network will be marketed aggressively in these locations as they are in all our markets. We anticipate vigorous competition during the year but we are confident that our established strategic positioning will continue to enhance our competitive ability.

New Zellers store in Cote Vertu Centre in Montreal. This is one of a number of Zellers stores opened recently in good locations vacated by competitors.

"Our objective is to be the premier discount department store in Canada, as measured by market share and return on investment, and to consistently provide the customer with assurance of value through lowest price and quality."

Paul Walters

Shopping for valentines at a new Zellers store in Markham, Ontario.

Store Profile

Zellers is the leading national chain of discount department stores. It targets the budget minded customer with the assurance of the lowest price. Excellent values are offered in both national and private brand merchandise and these are communicated aggressively with frequent advertising in both print and electronic media. Zellers is further distinguished by Club Z, its frequent buyer program. Zellers is able to compete successfully in its competitive retail segment by operating with a very low expense rate.

Zellers stores are characterized by self service and central checkout. Zellers markets its own credit card and accepts those of the major banks. Merchandising and sales promotion are centrally directed. Zellers operates 272 stores across Canada mainly in shopping malls. The typical store is 65,000 sq. ft. in size.

Store Statistics

(February 1, 1992)	Stores	Square Feet (000's)
Newfoundland	5	258
Prince Edward Island	4	255
Nova Scotia	15	1,054
New Brunswick	14	855
Quebec	53	3,883
Ontario	112	7,943
Manitoba	8	561
Saskatchewan	12	672
Alberta	25	1,582
British Columbia	24	1,556
	272	18,619

Towers re-launch a big success!

It was a formidable task; to transform 47 active Towers/ Bonimart department stores in Ontario, Quebec and the Maritimes into fully-operational Zellers stores within 11weeks without business interruption.

When Zellers purchased Towers Department Stores Inc. from the Oshawa Group Inc. in November 1990, it knew it had acquired the best possible opportunity to accelerate its growth in eastern Canada. The purchase boosted Zellers total square footage by 30% and would increase its DSS market share by a full four percentage points if it could retain its new Towers customers.

Towers stores were, on average, about 20% larger than Zellers stores; only about 30% of Towers merchandise was the same as, or similar to that of Zellers; Towers enjoyed a solid franchise with its customers.

But Zellers knew that it could offer Towers shoppers lower prices, especially during promotional events, on a similar assortment of merchandise. In addition, it believed that the introduction of the Zellers credit card together with Club Z would attract and build customer loyalty.

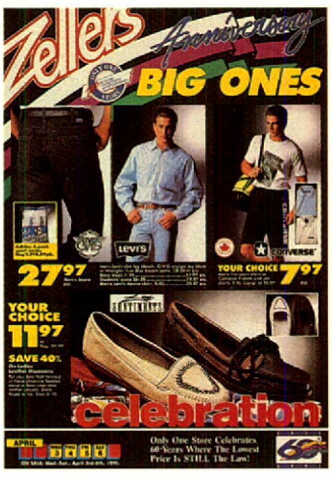
Towers; the old format.

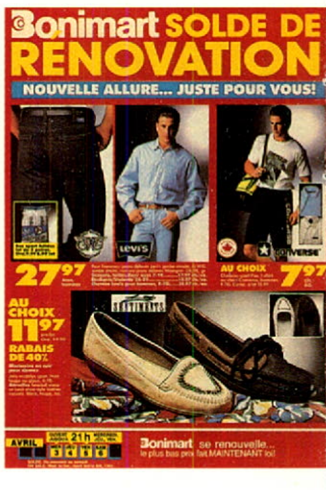
Zellers established a task force, led by John Urie, Executive Vice President, which included Dave Owen, Vice President Stores and Mike Martin, Vice President and Controller.

The first task was to identify and eliminate all duplicate functions within the two organizations. More than 400 positions were eliminated as major Towers operations, including its head office and buying office, were closed. All displaced executives and staff members received salary continuance related to length of service and relocation counselling.

The second task was to eliminate, as stocks were sold, all merchandise in Towers stores not also carried by Zellers and to assign an appropriate Zellers assortment to each acquired store. With increased buying power, the Company was also able to negotiate better terms with its suppliers, increase advertising pene-

The formidable task complete, employees are ready to welcome customers at a relaunched Zellers in Ontario.





tration and reduce costs as a percentage of sales.

New layouts for the Towers stores and leasehold improvements totalling some $40 million were planned. Changes and improvements included new fixturing and 119 exterior neon Zellers signs.

By the end of January 1991 all Towers systems had been replaced by Zellers systems and by February all Towers merchandise had been replaced by Zellers offerings and Zellers and Towers advertising was merged as both companies began to promote the same items at the same prices. Between February and the grand opening in mid-April, Zellers distributed 11 "side-by-side" Towers/Bonimart circulars.

Customer response was positive and although in-store renovations were in progress, customers continued to shop.

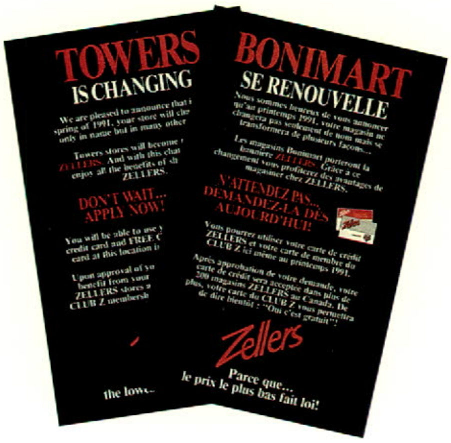
Finally, on April 15 the sign covers and banners were removed and 47 new Zellers stores moved the Company significantly closer to its goal of becoming the largest retailer in Canada.

Multi-media promotion, including a special grand opening circular, newspaper, radio and television advertising, was aimed at building store traffic while in-store excitement was created with giveaways, contests, the Club Z launch and Zeddy Bear for the most comprehensive campaign by Zellers since the launch of Club Z in 1986.

Increasing Zellers credit card penetration was a major undertaking. With no existing credit base to leverage, Zellers employed telemarketing, in-store solicitation, direct mail and staff in an aggressive marketing campaign that resulted in more than 500,000 new Zellers accounts.

Best of all, the whole exercise was successful despite the continuing economic recession. Sales of the former Towers stores were up in 1991 after adjusting for FST. Even more encouraging, operating profit of the 47 stores was ahead of the prior year by a substantial amount.

The integration of Towers management and staff strengthened Zellers greatly and has moved the Company closer to maximum market penetration. It has also reinforced the confidence of management to pursue other greater opportunities in the future.



Zellers; the new format featuring "power walls".

The old, above, and the new, right, at Lawrence and Midland in Toronto.

FIELDS

"Fields' mission is to provide the lowest prices, outstanding values and to be the dominant discount store in small markets across Canada."

Janis Ostling

Results

	(in thousands of dollars) This Year	Last Year
Sales and revenue	**86,408**	91,129
Operating profit	**724**	2,670
Assets employed	**19,118**	21,408

Operating profit in 1991 was $724,000, a decrease of $1.9 million from 1990.

Sales were down by 5.2% to $86.4 million. Strong sales growth in linens and household/seasonal items was offset by a reduction in softgoods sales.

Gross profit declined as a result of high markdowns and the lower sales base. Expenses were well managed and decreased from last year.

During 1991 three Fields stores were opened while eight Fields stores and three PSS stores were closed.

Fields will test market a new concept in the spring of 1992 in ten of its existing stores. They will be converted to highly promotional mini-discount department stores with a 60% hardlines blend. The buying expertise of Zellers will be utilized. Once the new strategy is proven successful, the balance of the Fields stores will be converted to the new format.

The new concept Fields store in Squamish, B.C. on opening day, March 4, 1992.

Store Profile

Fields operates 124 discount family clothing stores in Western Canada, 118 under its own name and six as PSS (Plus Sizes Plus Savings). Merchandise procurement, distribution and support services are centralized in Vancouver, British Columbia. Stores range from 1,100 to 25,400 sq. ft. Typical store is a freestanding unit or in a strip mall, averaging 7,600 sq. ft.

Fields provides outstanding values and the lowest prices in its markets, in family clothing and footwear, linens and household/seasonal commodities. The stores are located in small markets and operate in a convenient, friendly "no frills" atmosphere.

Store Statistics

(February 1, 1992)	Stores	Square Feet (000's)
Saskatchewan	**2**	11
Alberta	**44**	314
British Columbia	**78**	618
	124	943

Management Discussion and Analysis

I. OPERATIONS

a) Retail Environment – 1991

Total spending on "department store type merchandise" (DSTM) declined 10.7% in 1991. The termination of the Federal Sales Tax which was included in 1990 sales represented about 4.0 percentage points of this decline. Department store sales, which are included in DSTM, were down 8.9% in 1991.

The year began on an extremely weak base. The Gulf War, combined with the introduction of the Goods and Services Tax, resulted in a January DSTM sales decline of 19%. Deteriorating economic conditions and corporate restructuring activities drove unemployment levels higher as the year progressed. Bankruptcies reached an all time high. Consumers greatly increased their cross-border shopping trips to the U.S. Several large retail chains, especially those unable to increase market share, could not withstand these conditions and were forced to close their doors after liquidating their inventories at huge discounts. In spite of very high levels of promotional activity, sales levels did not increase in the second half of the year. In the important fourth quarter alone, DSTM in Canada declined 9.3%.

Sales of big ticket durables were particularly hard hit. Statistics Canada reported appliance and furniture sales were down 17%. The apparel market was down over 14%, with sales of men's apparel leading the decline. Fashion basics outperformed most clothing categories. Housewares and linens similarly outperformed the other home categories.

British Columbia and Alberta were the only provinces which did not experience double digit DSTM sales declines.

In 1990 DSTM spending had increased by 2.0% over the previous year. Spending was up by 6.4% in the first quarter but declined over the balance of the year as the Canadian economy slipped into a recession. Rising unemployment reduced consumer purchasing power notably in Ontario and Quebec.

b) Retail Risk Factors

The five elements which combine to produce retail profits are sales, margins, operating expenses, credit earnings and interest expense. The following table shows the principal external and internal risk factors which affect these elements.

Retail Risk Factors

	External	Internal
Sales	The Economy Competition Inflation	Store Openings and Closings Marketing Strategies Customer Service
Margins	Competition Consumer Resistance	Buying/Pricing Control of Inventories Stock Shortages Sales Blend
Operating Expenses	Inflation Taxes and Levies	Occupancy Costs Payroll Advertising
Credit Earnings	Bad Debts Card Competition	Card Promotion Service Charge Rates
Interest	Rates Credit Rating	Amount of Debt

These elements interact and an action taken to stimulate one element often results in an unwanted effect on other elements. For example, store openings will stimulate sales but will also increase occupancy and interest expense. Additional advertising may increase sales but will certainly raise expenses. Cutting selling staff will reduce payroll expense but may also reduce sales and increase stock shortages. Management's responsibility is to achieve an appropriate balance among the factors of risk.

Cross-border shopping is a further external risk factor which had a substantial but unquantifiable impact on sales in 1991. The recent decline in the Canadian dollar, actions of the Canadian government to collect more tax at the border and to eliminate tariffs on some offshore merchandise and the efforts of Canadian retailers to be more competitive are expected to reduce the impact of cross-border shopping in the current year.

c) Earnings

Total net earnings were $83 million in 1991 compared with $163 million and $168 million for the previous two years. These figures require analysis before they can be used to assess the year's performance.

Earnings Analysis (in millions of dollars)

	1991	1990	1989
Comparable Operations:			
Operating profits of major retail divisions (see below)	**278**	325	312
Other net revenues (expenses)	**6**	(8)	3
	284	317	315
Interest expense	**(144)**	(155)	(158)
	140	162	157
Income tax on current earnings	**(57)**	(64)	(59)
Comparable net earnings	**83**	98	98
Major Non-comparable Items:			
Recovery of prior years' tax losses	**–**	60	46
Markborough earnings after interest and taxes	**–**	5	24
Total net earnings	**83**	163	168
Total Net Earnings per Common Share	**$1.61**	$3.46	$4.37

After major non-comparable amounts are excluded from prior years' earnings it can been seen that comparable net earnings have declined from a level of $98 million in each of the two preceding years to $83 million in 1991.

"Other net revenues (expenses)" includes items that are not directly attributable to any one of the three operating entities. In each of the three years it includes miscellaneous net earnings from investments and ancillary activities including the operation of the Simpson Tower building, offset by unallocated corporate expenses. In 1991 it also included a non-recurring gain of $15 million from the sale of a participating debenture in the Scarborough Town Centre shopping mall. In 1990 it included $2.3 million of operating profit from Towers Department Stores Inc. between its acquisition on November 4, 1990 and its merger with Zellers on February 1, 1991.

Interest expense at $144 million in 1991 declined by $11 million from the year before entirely because of lower interest rates. Average debt was up by $76 million because of a higher level of working capital in use. However this factor was more than offset by a drop in the average interest rate from 12.1% in 1990 to 10.6% in 1991.

In 1990 interest expense declined by $3 million to $155 million. Debt was lower because of an equity issue in December, 1989 but the average interest rate was higher than the year before.

Earnings per common share figures are not comparable due to significant increases in the number of common shares outstanding, and reductions in preferred shares outstanding, in 1989 and 1991.

The recoveries of prior years' tax losses which were recorded in 1989 and 1990, absorbed the benefit of all such losses which had been carried forward since the 1982 to 1985 period. Projected recoveries had not been recorded in the years in which the losses were incurred as the Company could not, at the time, be certain that they would be realized before their respective expiry dates. As all past losses were recovered by the end of 1990 no similar credits will arise in the future.

After nearly 17 years as a subsidiary of Hudson's Bay Company, Markborough Properties Inc. was spun off to shareholders in August 1990. Results for 1990 include Markborough operations for six months only. Detailed information concerning, or including, Markborough is not given as it is neither comparable nor of use in assessing the future prospects of Hudson's Bay Company.

d) Operating Profits

Operating profits of the retail divisions for the past ten years were as follows:

Operating Profits by Division (in millions of dollars)

	The Bay	Simpsons	Zellers	Fields	Total
1991	**59***	*	**218**	**1**	**278**
1990	119	3	200	3	325
1989	115	14	180	3	312
1988	70	19	142	2	233
1987	64	17	93	1	175
1986	83	6	64	3	156
1985	26	13	51	1	91
1984	10	(51)	40	3	2
1983	29	(29)	47	5	52
1982	10	(34)	31	3	10

*Simpsons included with the Bay in 1991

Operating profits declined in 1991 by $47 million principally because of reduced sales and lower margins at the Bay.

Because sales in the fourth quarter, which includes the Christmas season, are higher than in other quarters while expenses are spread more evenly through the year, a disproportionate share of operating profit is earned in the fourth quarter as shown in the following table.

Operating Profits by Quarter (in millions of dollars)

	1st	2nd	3rd	4th	Total
1991	**(1)**	**60**	**64**	**155**	**278**
1990	22	57	61	185	325
1989	12	53	58	189	312

In 1991 first quarter operating profits were affected by introduction of the GST and by severance costs relating to a restructuring at the Bay; the fourth quarter reduction was the result of lower same store sales and increased markdowns in both Zellers and the Bay.

Factors that determine operating profits are:
i) sales and revenue
ii) gross profit rate
iii) expense rate
iv) credit earnings

i) Sales and Revenue

Sales and revenue of the retail divisions for the past three years were as follows:

Sales and Revenue by Division (in millions of dollars)

	The Bay	Simpsons	Zellers	Fields	Total
1991	**2,118***	*	**2,789**	**86**	**4,993**
1990	1,887	435	2,330	91	4,743
1989	1,859	437	2,149	90	4,535

*Simpsons included with The Bay in 1991

Total sales and revenue increased by 1.3% in 1991 to $5,032 million. However prior year's sales are not comparable because of:

- the purchase of Towers in November 1990
- the disposal of seven (net) Simpsons stores to Sears Canada in July 1991
- the inclusion in 1990 sales figures of the former Federal Sales Tax estimated at approximately 4.0% of the total

Same store sales adjusted for FST were estimated to be down by approximately 3.4% in 1991. Inflation in the general merchandise sector was estimated at zero percent.

Sales of all divisions in 1991 were affected by the general decline in consumer spending caused by the recession, introduction of the GST and the popularity of cross-border shopping.

Sales and revenue at Zellers were up by 20% but, excluding Towers, were down by 1.9%. Fourth quarter sales – up 17% – were below the average gain for the year principally because of intense competitive price-cutting in that period. Sales in the Maritimes, which have suffered high unemployment, were below the national trend.

Sales and revenue at the Bay were down 8.8%. By quarter, sales were weakest in the first quarter which was most directly affected by the GST introduction. By merchandise division, women's wear and Market Square (linens, housewares, etc.) were strongest; shoes and major appliances weakest.

The following table shows the percentage of sales of the Company derived from each of the four regions of Canada for the last three years.

Sales by Region

% of Sales	1991	1990	1989
Maritimes	**7.5**	7.4	7.5
Quebec	**20.0**	20.1	20.0
Ontario	**42.9**	40.2	40.4
Western Canada	**29.6**	32.3	32.1
	100.0	100.0	100.0

The growth in the Ontario share of sales reflects the Towers purchase offset to some extent by the Simpsons merger.

In 1990 sales and revenue increased 8.0% to $4,970 million including $171 million from Towers in the last quarter. Zellers sales were ahead by 8.4%, excluding Towers, while Bay/Simpsons, hurt by the economic downturn in Ontario, were ahead by only 1.1%. Sales momentum slowed during the year as the recession worsened.

ii) Gross Profit Rate

The overall gross profit rate deteriorated in 1991; Zellers was up marginally, the Bay down substantially. Stock shortages were improved in both divisions.

At the Bay, improved markup was more than offset by substantially higher markdowns that were required to respond to intense competitive price-cutting, including specialty store bankruptcy sales, and to clear fashion inventories.

At Zellers, more effective buying resulted in higher markup but markdowns were also higher as Zellers attempted to maintain its low price leadership in a highly promotional marketplace.

In 1990 gross profit rate was down marginally as both Zellers and the Bay had high markdowns in the fourth quarter and a worsening of stock shortages, particularly in the Toronto market area.

iii) Expense Rate

The overall expense rate was higher in 1991 despite effective control in both divisions.

At the Bay total expenses were down, but as the sales decline was proportionally greater, the expense rate was up. Property taxes and utility costs continued to escalate at rates substantially higher than the rate of inflation.

At Zellers higher occupancy costs were the principal cause of an increase in expense rate. These arose from the addition to the group of the former Towers stores which generally had higher occupancy costs than ongoing Zellers stores and from increased taxes and utility costs in both groups.

The expense rate in 1990 was virtually unchanged from the year before, principally due to tight control in every area.

iv) Credit Earnings

Credit earnings before interest were up slightly in 1991 as increased revenues from new accounts, principally at the former Towers stores, more than offset higher expenses for postage, communications and marketing. Bad debt expense was down marginally from the previous year because of tighter control of credit granting and intensified collection activities.

In 1990 credit earnings were virtually unchanged from the year before as higher revenue from new accounts was offset by a sharp increase in bad debt expense.

II. RETAIL PROPERTIES

The number and aggregate gross areas of Hudson's Bay Company's retail stores, by division, at January 31, 1992 were:

	Stores	000's Sq.Ft.
The Bay	89	14,785
Zellers	272	18,620
Fields	124	943
	485	34,348

In addition, the Company operated 12 distribution centres totalling 3,990,000 sq. ft. and 13 clearance centres totalling 311,000 sq. ft.

The Company owns the land and buildings of nine downtown Bay stores, three suburban Bay stores, and 12 Zellers stores. As well, the Company owns the Toronto Queen Street store building and approximately 60% of the related land, and the buildings (on leased land) of 13 suburban Bay stores.

The remaining stores are generally held under long-term leases.

The Company's important non-retail properties are The Simpson Tower, a 32 floor office building in Toronto, and the former Simpsons downtown store in Montreal which is being held for sale or development.

III. FINANCIAL CONDITION

a) Cash Flow, Funding and Capital Spending

Cash inflow from retail operating activities amounted to $94 million in 1991, compared with $219 million in 1990 and $234 million in 1989. The decline in 1991 resulted from an increase in working capital of $91 million whereas the previous two years had produced reductions of $16 million and $44 million respectively. The 1991 working capital change was the result of increased inventory levels attributable to a combination of the sales shortfall, more aggressive buying in women's wear and for promotions, and Simpsons commitments (made before the decision to merge and dispose of seven stores) which could not be cancelled.

Net cash outflow for 1991 was $110 million which is $1 million less than 1990 but that was the year that $142 million was expended on the acquisition of Towers Department Stores (the corresponding 1991 outlay with respect to the Towers acquisition was $36 million). The previous year had an inflow of $131 million.

Capital expenditures (excluding the Towers acquisition) were $122 million in 1991, $120 million in 1990 and $92 million in 1989. Projected capital spending over the next three years averages $115 million per annum and includes 24 additional Zellers stores. Only one new Bay store is committed during this period but both divisions will be renovating and upgrading existing stores where appropriate to maintain or enhance the desired marketing image.

The Company remains committed to continuing its expansion in communities where there are appropriate marketing opportunities.

The following table shows cash flow and funding in the retail business for the past three years.

Cash Flow and Funding

(in millions of dollars)

	1991	1990	1989
From earnings	**185**	203	190
Working capital change	**(91)**	16	44
From Operating Activities	**94**	219	234
Capital expenditures	**(122)**	(120)	(92)
Towers acquisition	**(36)**	(142)	–
Fixed asset dispositions	**20**	–	3
Dispositions of non-core businesses	**–**	–	36
Dividends	**(45)**	(44)	(43)
Other	**(21)**	(24)	(7)
Net Cash (Outflow) Inflow	**(110)**	(111)	131
Funding:			
Debt	**94**	95	(282)
Equity	**16**	16	151
	110	111	(131)

b) Assets Employed and Liquidity

The objectives of the Company with regard to financing are:

- to maintain a debt/equity ratio which allows access to capital markets at all times;
- to maintain a level of leverage appropriate to the retail industry to generate superior returns for shareholders;
- to maintain a mix of debt which will provide adequate liquidity at the lowest cost of capital.

The following summary shows the assets employed at each operating division as financed by debt and equity for the last three years.

Assets Employed, Debt and Shareholders' Equity

(in millions of dollars)

	1991	1990	1989
Assets Employed			
The Bay	**1,237**	1,294	1,270
Zellers	**1,170**	814	757
Fields	**19**	21	18
Other	**162**	272	153
HBC Retail	**2,588**	2,401	2,198
Markborough	**–**	–	1,088
	2,588	2,401	3,286
Provided from:			
HBC Retail			
Debt	**1,335**	1,243	1,147
Deferred tax	**27**	(14)	6
Equity			
Preferred	**9**	98	104
Common	**1,217**	1,074	941
	2,588	2,401	2,198
Markborough			
Debt	**–**	–	813
Equity	**–**	–	275
	2,588	2,401	3,286
Debt: Equity Ratio			
HBC Retail	**1.1:1**	1.1:1	1.1:1
Including Markborough	**N/A**	N/A	1.5:1

At 1.1:1 the Company's debt: equity ratio is well within an acceptable range for the retail industry.

c) Debt

Debt at the 1991 year end was $1,335 million, of which $904 million was long term and $431 million was short term. The principal source of short term borrowing in 1991 and 1990 was commercial paper with some borrowings from banks (by way of banker's acceptances and overdrafts). Bank borrowings had been used to a much more significant degree in 1989 before ratings on HBC commercial paper were upgraded. Seasonal upswings in inventory are financed by short term debt.

The Company negotiates lines of credit annually with a number of Canadian banks to provide for short term financial needs. These credit lines are unsecured and uncommitted facilities. Management expects to be able to negotiate lines of credit sufficient to meet its requirements in 1992.

Long term debt coming due in 1992 amounts to $68 million which includes $39 million called for early redemption in February and March. Management is confident that it will be able to refinance this amount and raise any additional long-term funds required.

After release of last year's (1990) operating results, the rating by DBRS on Hudson's Bay Company preferred shares improved from "Pfd 3" to "Pfd 2" and its debentures and those of Hudson's Bay Company Acceptance Limited and bonds of Hudson's Bay Company Properties Limited improved from "BBB high" to "A low". This followed an improvement in commercial paper rating from "R2(mid)" to "R1(low)" the year before.

Debt at 1991 year-end comprised $357 million at fixed rates and $978 million at nominal floating rates. However, rates on $372 million of nominal floating rate debt have been fixed at an average rate of 11.4% through various currency agreements and interest exchange transactions. A further $292 million has been capped at 12.6% LIBOR through various U.S. dollar interest rate agreements.

Foreign exchange and floating rate interest rate risks are limited by hedges, swaps and caps under guidelines established and reviewed periodically by the Board. Debt subject to foreign exchange rate risk amounts to $53 million representing the Canadian dollar equivalent of unhedged U.S. dollar and sterling obligations.

d) Asset Protection

The many programs which are in effect to protect the assets of the Company from loss and from liability claims from third parties are backed by contracts of insurance to cover major losses.

The amount of self insured risk assumed by the Company is reviewed periodically by the Board of Directors.

e) Dividends

The company has been paying annual dividends at the rate of $0.80 per share on the common shares since April 30, 1990 at which time it was increased from $0.60 per share.

Consolidated Statements Of Earnings

	Year Ended January 31, 1992	1991
	$000's	$000's
HBC Retail – Sales and Revenue		
The Bay (Note 2)	**2,118,398**	2,322,077
Zellers	**2,788,756**	2,329,872
Fields	**86,408**	91,129
Other (Note 4)	**38,681**	226,900
HBC Retail – Sales and Revenue	**5,032,243**	4,969,978
Markborough – revenue (Note 3)	**–**	71,755
Consolidated – sales and revenue	**5,032,243**	5,041,733
HBC Retail – Source of Earnings (Note 5)		
Operating profit:		
The Bay (Note 2)	**59,409**	122,086
Zellers	**217,920**	200,583
Fields	**724**	2,670
Other	**6,062**	(7,701)
Earnings Before Interest and Income Taxes	**284,115**	317,638
Interest Expense (Note 6)	**(144,599)**	(155,246)
Earnings Before Income Taxes	**139,516**	162,392
Income Taxes (Note 7)		
Current year's provision	**(56,736)**	64,063)
Recovery of prior years' tax losses	**–**	59,805
HBC Retail – Net Earnings	**82,780**	158,134
Markborough – net earnings (Note 3)	**–**	5,148
Consolidated – net earnings	**82,780**	163,282
Earnings Per Common Share		
HBC Retail		
Earnings before recovery of prior years' tax losses	**$1.61**	$2.01
Recovery of prior years' tax losses	–	$1.33
Markborough	**–**	$0.12
Consolidated	**$1.61**	$3.46

Consolidated Statements Of Retained Earnings

	Year Ended January 31, 1992	1991
	$000's	$000's
Retained Earnings at Beginning of Year	**350,144**	365,793
HBC Retail – Net Earnings	**82,780**	158,134
Markborough – net earnings	**–**	5,148
Dividends Paid		
Preferred shareholders – cash	**(5,031)**	(7,855)
Common shareholders:		
Cash	**(39,434)**	(35,987)
Markborough distribution (Note 3)	**–**	(287,623)
Reduction of Stated Capital of Special Shares (Note 14)	**–**	152,534
Retained Earnings at End of Year	**388,459**	350,144

Consolidated Balance Sheets

	1992	January 31, 1991
	$000's	$000's
Current Assets		
Cash	**5,937**	7,128
Short-term deposits (Note 13)	**6,015**	12,201
Customer accounts receivable	**945,195**	891,678
Other accounts receivable	**146,581**	218,528
Merchandise inventories	**1,074,880**	955,095
Prepaid expenses	**41,583**	32,469
	2,220,191	2,117,099
Secured Receivables (Note 8)	**28,087**	13,879
Investments (Note 9)	**55,992**	53,615
Fixed Assets (Note 10)	**665,400**	624,904
Deferred Charges	**62,198**	57,408
Goodwill (Note 11)	**95,708**	96,073
Pensions (Note 12)	**146,542**	123,277
Deferred Income Taxes	**–**	14,034
	3,274,118	3,100,289
Current Liabilities		
Short-term borrowings (Note 13)	**416,110**	405,151
Trade accounts payable	**313,954**	309,231
Other accounts payable and accrued expenses	**318,002**	323,817
Income taxes payable	**875**	785
Long-term debt due within one year (Note 13)	**67,909**	296,597
	1,116,850	1,335,581
Long-Term Debt (Note 13)	**904,533**	592,661
Deferred Income Taxes	**26,710**	–
Shareholders' Equity		
Capital (Note 14)	**837,566**	821,903
Retained earnings	**388,459**	350,144
	1,226,025	1,172,047
Contingencies (Note 19)		
	3,274,118	3,100,289

On behalf of the Board:

D McGiverin

Director

Marcel Bélanger

Director

Consolidated Statements Of Cash Flow And Funding

	Year Ended January 31, 1992 $000's	1991 $000's
HBC Retail – Operating Activities		
Earnings before income taxes	**139,516**	162,392
Current income tax expense	**(11,088)**	(5,274)
Items not affecting cash flow:		
Amortization	**75,525**	69,679
Pension credits	**(19,198)**	(23,570)
Cash inflow from earnings	**184,755**	203,227
Net effect of changes in operating working capital (Note 15)	**(90,947)**	15,772
Net cash inflow from operating activities	**93,808**	218,999
HBC Retail – Investing Activities		
Capital expenditures	**(122,213)**	(120,409)
Acquisition of Towers Department Stores Inc. (Note 4)	**(35,908)**	(142,432)
Fixed asset dispositions	**20,084**	55
Other	**(20,978)**	(23,424)
Net cash outflow for investing activities	**(159,015)**	(286,210)
HBC Retail – Dividends		
Preferred shareholders	**(5,031)**	(7,855)
Common shareholders	**(39,434)**	(35,987)
Cash outflow for dividends	**(44,465)**	(43,842)
HBC Retail – Net Cash Outflow for Activities and Dividends	**(109,672)**	(111,053)
Markborough – net cash outflow	**–**	(187,107)
Consolidated – net cash outflow for activities and dividends	**(109,672)**	(298,160)
HBC Retail – Funding		
Debt:		
Long-term:		
Increase	**330,197**	97,500
Reduction	**(94,900)**	(387,536)
Increase (reduction) in net short-term debt	**(141,288)**	385,483
	94,009	95,447
Equity:		
Preferred shares	**(85,410)**	(4,642)
Common shares	**101,073**	20,248
	15,663	15,606
HBC Retail – Net Cash Inflow from Funding	**109,672**	111,053
Markborough debt	**–**	187,107
Consolidated – net cash inflow from funding	**109,672**	298,160

Notes to the Consolidated Financial Statements

Years Ended January 31, 1992 and January 31, 1991

1. SIGNIFICANT ACCOUNTING POLICIES

These consolidated financial statements have been prepared by management in accordance with accounting principles generally accepted in Canada and conform in all material respects with the historical cost accounting standards of the International Accounting Standards Committee.

The significant policies are as follows:

a) Consolidation and segmentation
These consolidated financial statements include the accounts of Hudson's Bay Company and of all its subsidiary companies. "HBC Retail" denotes Hudson's Bay Company and its consolidated subsidiaries, excluding Markborough Properties Inc. ("Markborough"), which was a wholly owned subsidiary of the Company prior to its distribution effective August 1, 1990 (see note 3).

With the distribution of Markborough, retailing became the dominant industry segment. Retailing comprises retail stores, including both full-line and promotional department stores. Prior to its distribution, Markborough had represented substantially all of the Company's real estate industry segment.

In order to provide meaningful comparative information in view of the distribution of Markborough, pre-distribution Markborough figures are recorded by the equity accounting method supplemented by an analysis of earnings in note 18.

b) Foreign currency translation
Foreign currency assets and liabilities are translated into Canadian dollars at the exchange rates prevailing at the balance sheet dates and foreign currency earnings are translated into Canadian dollars at approximately the exchange rates in effect at the time they are earned.

c) Capitalization of interest
Interest that relates to properties which are under construction or held for sale or development is capitalized to such assets when their net carrying amount is lower than their estimated net recoverable amount.

d) Earnings per common share
Earnings per common share are determined after deducting preferred dividends paid and accrued during the year and are based on the weighted average number of common shares outstanding during the year.

e) Customer accounts receivable
In accordance with recognized retail industry practice, customer accounts receivable include instalment accounts, of which a portion will not become due within one year.

f) Merchandise inventories
Merchandise inventories are carried at the lower of cost and net realizable value less normal profit margins. The cost of inventories is determined principally on an average basis by the use of the retail inventory method.

g) Investments
Portfolio investments comprising fixed term securities are carried at cost, with discounts or premiums arising on purchase amortized to maturity. Other investments are carried at the lower of cost and estimated realizable value with dividends being reflected in earnings when received.

h) Fixed assets
Fixed assets are carried at cost. The cost of buildings (excluding the office tower noted below), equipment and leasehold improvements in service is amortized on the straight-line method over their estimated useful lives. The amortization periods applicable to the various classes of assets are as follows:

Buildings	20 – 50	years
Equipment	3 – 12½	years
Leasehold improvements	10 – 40	years

Buildings include an office tower which is being amortized on the sinking fund method at a rate of 3% over a 40 year period.

i) Deferred charges
Deferred charges include debt discount and expense, costs associated with certain currency and interest hedging transactions and unamortized exchange gains and losses on foreign currency long-term debt which are amortized on the straight-line method over the terms of the issues to which they relate. The amortization is included with interest expense in the Consolidated Statements of Earnings.

Deferred charges also include long-term prepaid rent, post employment benefits other than pensions and merchandise systems development costs, which are amortized on the straight-line method over periods of up to 15 years, 10 years and three years, respectively.

j) Goodwill
Goodwill comprises the unamortized balance of the excess of the cost to the Company over the fair value of its interest in the identifiable net assets of Zellers Inc. and the former Towers Department Stores Inc. (subsequently amalgamated with Zellers Inc. – see note 4), at their respective dates of acquisition, and is amortized on the straight-line method over periods of 40 years and 20 years, respectively.

k) Pension costs
The costs of pension plans are calculated under the accrued benefit method and are charged to earnings as incurred. The excess of the value of pension plan assets over the actuarial present value of accrued pension plan obligations as of February 1, 1986, together with adjustments arising from plan amendments, experience gains and losses and changes in actuarial assumptions since that date, are amortized to earnings over the expected average remaining service lives of the respective employee groups (see note 12).

2. SIMPSONS MERGER AND SALE TO SEARS CANADA INC. ("SEARS")

Effective July 27, 1991 the Company merged its Simpsons division with The Bay. In connection with this merger, the Company entered into agreements with Sears under which Sears acquired six Simpsons stores and two Bay stores and the Company acquired one Sears store. The Company received cash proceeds of $37,000,000 from Sears, which marginally exceeded the book value of assets transfered and other costs related to the transfer. The excess has been included in other earnings in the Consolidated Statement of Earnings.

Sales and operating profit of Simpsons prior to the date of merger have been reclassified as The Bay.

3. MARKBOROUGH DISTRIBUTION

On August 1, 1990, in accordance with an Arrangement approved by ordinary shareholders of the Company at a special meeting held on July 26, 1990, the Company distributed its investment in Markborough, which until that date had been a wholly owned subsidiary, to the holders of its ordinary shares. The Arrangement resulted in holders of ordinary shares receiving one Markborough common share for each of the Company's ordinary shares (subsequently redesignated common shares – see note 14) held by them.

Markborough's revenue and earnings to July 31, 1990 (see note 18) have been shown separately in the Consolidated Statements of Earnings.

The amount of the Markborough distribution as shown in the Consolidated Statement of Retained Earnings for the year ended January 31, 1991, $287,623,000, represents the net carrying cost of the Company's investment in Markborough immediately preceding the distribution plus costs of approximately $2,500,000 incurred in implementing the Arrangement.

4. ACQUISITION OF TOWERS DEPARTMENT STORES INC. ("TOWERS")

Effective November 4, 1990, under the terms of an agreement dated October 21, 1990, the Company acquired 1,000 common shares of Towers, representing all of the outstanding shares. At the time of the acquisition Towers operated 51 promotional department stores, of which 47 have since been converted to Zellers stores, three have been closed and one has been converted to a Bay store. At January 31, 1991 the costs of acquisition, including cash payments to the former owners, professional fees, employee terminations and disposal costs of stores, offices, contracts, assets and computer systems, were estimated to be $181,524,000. Of this amount, $39,092,000 had not been paid as of January 31, 1991, resulting in a cash outflow of $142,432,000 for the acquisition in the three month period then ended. During the year ended January 31, 1992 the Company agreed on a final settlement with the former owners. The total cost of the acquisition was determined to be $189,563,000 and the related cash outflow in the year ended January 31, 1992 amounted to $35,908,000.

From the date of acquisition until January 31, 1991 sales and operating profit of Towers, amounting to $170,788,000 and $2,378,000, respectively, were included in "other" in the Consolidated Statement of Earnings. On February 1, 1991 Towers and Zellers Inc. were amalgamated and, since that date, sales and operating profit derived from the former Towers stores have formed an integral part of the Zellers operation and accordingly are included in the "Zellers" figures.

The cost of acquisition, accounted for by the purchase method, was allocated as follows:

	$000's
Merchandise inventories	**133,026**
Other current assets	**18,294**
Current liabilities	**(84,373)**
Fixed assets	**24,232**
Deferred charges (prepaid rent)	**39,363**
Goodwill	**39,879**
Deferred income taxes	**19,142**
	189,563

5. AMORTIZATION

In the Consolidated Statements of Earnings, amortization of HBC Retail fixed assets, deferred charges and goodwill is included as follows:

	Year Ended January 31,	
	1992	1991
	$000's	$000's
Deducted in arriving at earnings before interest and income taxes	**78,038**	62,927
Included in interest expense (amortization of deferred charges (see note 1 i)	**(2,513)**	6,752
	75,525	69,679

6. INTEREST EXPENSE

HBC Retail interest expense may be analyzed as follows:

	Year Ended January 31,	
	1992	1991
	$000's	$000's
On long-term debt	**106,229**	104,670
On net short-term debt (see note 13)	**39,390**	54,938
	145,619	159,608
Less amount capitalized (see note 1 c)	**(1,020)**	(4,362)
HBC Retail interest expense	**144,599**	155,246

7. INCOME TAXES

The HBC Retail average statutory Canadian income tax rate for the years ended January 31, 1992 and January 31, 1991 were 42.6% and 42.2%, respectively. The following schedule reconciles nominal tax provisions for HBC Retail at these rates with the amounts provided in the Consolidated Statements of Earnings.

	Year Ended January 31,	
	1992	1991
	$000's	$000's
HBC Retail earnings before income taxes	**139,516**	162,392
HBC Retail nominal income tax provision at statutory Canadian income tax rates	**59,434**	68,529
Increase (decrease) in HBC Retail income taxes resulting from:		
Large corporations tax	**5,048**	4,127
Tax rates in other jurisdictions	**(3,557)**	(4,697)
Capital gains and losses	**(6,917)**	(5,952)
Adjustments to prior years' taxes	**(843)**	(1,603)
Non deductible costs	**4,150**	3,659
Transactions with affiliate (see note 17)	**(579)**	–
Provision for HBC Retail income taxes per Consolidated Statements of Earnings	**56,736**	64,063

In the year ended January 31, 1991 the Company realized previously unrecorded tax benefits relating to losses incurred in prior years of $59,805,000. Since January 31, 1991 there have been no unrecorded tax loss benefits.

8. SECURED RECEIVABLES

Secured receivables comprise the following:

	1992	January 31, 1991
	$000's	$000's
Mortgages	**21,935**	5,614
Employee share ownership plan loans	**6,953**	6,741
Other	**–**	2,231
Total secured receivables	**28,888**	14,586
Less amounts due within one year classified as other accounts receivable	**(801)**	(707)
	28,087	13,879

Maturities during the five years ending January 31, 1997 are as follows:

1993 – $ 801,000; 1994 – $1,450,000; 1995 – $13,188,000; 1996 – $1,111,000; 1997 – $1,184,000.

Under certain conditions, the amounts due may be paid prior to maturity.

9. INVESTMENTS

Investments comprise the following:

	1992	January 31, 1991
	$000's	$000's
Portfolio investments (see note 13)	**47,476**	39,526
The North West Company Inc.	**8,050**	8,050
Other	**466**	6,039
	55,992	53,615

Portfolio investments are bonds held primarily to support funding obligations and generally will be held until, and replaced upon, maturity. The investment in The North West Company Inc. consists of 1,442,000 common shares which represent 10.9% of all the common and class A voting shares outstanding at January 31, 1992. At January 31, 1992 the closing price of common shares of The North West Company Inc. on The Toronto Stock Exchange was $16.125 per share.

10. FIXED ASSETS

Fixed assets comprise the following:

	1992	January 31, 1991
	$000's	$000's
Cost:		
Land	**72,944**	72,954
Buildings	**267,433**	242,037
Equipment	**712,287**	686,692
Leasehold improvements	**90,854**	70,066
Property for sale or development	**37,056**	37,056
	1,180,574	1,108,805
Accumulated amortization:		
Buildings	**(119,266)**	(107,044)
Equipment	**(376,118)**	(362,149)
Leasehold improvements	**(19,790)**	(14,708)
	(515,174)	(483,901)
	665,400	624,904

11. GOODWILL

Goodwill comprises the following:

	1992	January 31, 1991
	$000's	$000's
Cost:		
Zellers	**82,258**	82,258
Towers (see note 4)	**39,879**	36,366
	122,137	118,624
Accumulated amortization	**(26,429)**	(22,551)
	95,708	96,073

Of the unamortized balance, $58,102,000 will be amortized over the next 29 years and $37,606,000 will be amortized over the next 19 years.

12. PENSIONS

At January 31, 1992 the aggregate actuarial present value of accrued pension plan benefits is $419,000,000 and the aggregate market value of pension plan assets is $650,000,000.

"Pensions" in the Consolidated Balance Sheets represents the recorded portion of the excess of pension plan assets over accrued pension plan benefits net of other obligations to retired employees.

13. DEBT

Total debt may be analyzed as follows:

	1992	January 31, 1991
	$000's	$000's
Short-term borrowings (a)	**416,110**	405,151
Long-term debt due within one year (b)	**67,909**	296,597
Less short-term deposits	**(6,015)**	(12,201)
Less portfolio investments (see note 9)	**(47,476)**	(39,526)
Net short-term debt	**430,528**	650,021
Long-term debt (b)	**904,533**	592,661
	1,335,061	1,242,682

Long-term debt comprises the following:		
Secured on property:		
Hudson's Bay Company Properties Limited		
7½% first mortgage bonds series B due 1991	**–**	4,954
11½% first mortgage bonds series C due 1995 (c)	**–**	15,832
9⅞% first mortgage bonds series D due 1997	**28,826**	28,826
10% first mortgage bonds series E due 1998	**23,408**	23,410
	52,234	73,022

	1992	January 31, 1991
	$000's	$000's
Secured on accounts receivable:		
Hudson's Bay Company Acceptance Limited		
8¾% debentures series D due 1991	–	20,000
8¼% debentures series E due 1993	20,000	20,000
10½% debentures series F due 1996 (c)	16,605	19,028
11.56% debentures series N due 1996	25,000	–
11.23% debentures series N due 1996	25,000	–
13¾% debentures series G due 2001	44,544	44,544
Floating rate debt: (b)		
Term loan due 1994	25,000	25,000
Term loan due 1995	50,000	50,000
Term loans due 1996	55,000	–
Simpsons Acceptance Company Limited		
8⅜% debentures series F due 1992	10,000	10,000
8⅜% debentures series G due 1992	15,000	15,000
9⅞% debentures series H due 1997	12,108	12,308
	298,257	215,880
Secured by floating charge on assets of subsidiary:		
Zellers Inc.		
10¼% sinking fund debentures series 1974 due 1994 (c)	–	4,967
Total secured	350,491	293,869
Unsecured:		
Hudson's Bay Company		
10% notes due 1991	–	86,768
10 3/4% notes due 1991	–	80,000
11% notes due 1993	25,000	25,000
Dual currency bonds due 1993 (U.S. $66,393,000 and U.S. $86,208,000, respectively) (d)	77,680	100,001
10% debentures due 1994 (U.S. $18,954,000 and U.S. $19,738,000, respectively) (c)	22,528	22,896
15.36% term loan due 1995-1997 (£5,592,000)	11,743	12,806
Floating rate debt (b)(e)	485,000	260,000
Simpsons Limited		
8 3/8% debentures series H due 1993 (c)	–	2,740
9 1/8% debentures series I due 1994 (c)	–	1,868
11 3/4% debentures series J due 1995 (c)	–	2,864
	621,951	594,943
Subordinated:		
Zellers Inc.		
5½% convertible subordinated debentures series 1971 due 1991 (f)	–	446
	972,442	889,258
Less amounts due within one year	(67,909)	(296,597)
	904,533	592,661

(a) Short-term floating rate borrowings at January 31, 1992 were $416,110,000. Of this amount, $56,343,000 has been fixed at 10.6% through an interest rate swap agreement, and $292,500,000 has been capped at 12.6% LIBOR, through various U.S. dollar interest rate cap agreements.
(b) Long-term debt (including amounts due within one year) at January 31, 1992 includes floating rate debt amounting to $615,000,000. Of this amount, $315,950,000 has been fixed at 11.53% through various currency and interest exchange agreements.
(c) During the year ended January 31, 1992 $26,675,000 of debt was called for early redemption and notice of early redemption in February and March 1992 was given on a further $39,133,000 of debt.
(d) The dual currency bonds bear interest at 8.0% based on a notional principal amount of 110,655,000 Swiss Francs at January 31, 1992. The effective Canadian interest rate on these bonds is 9.3%.
(e) The Company's floating rate debt comprises term loans and notes with several financial institutions.
(f) Until their maturity on September 15, 1991, the holders of Zellers Inc. 5 1/2% convertible subordinated debentures series 1971 had the right to exchange those debentures for common shares of Hudson's Bay Company at the rate of 45.82 common shares per $1,000 of debenture principal.

Several of the long-term debt issues are subject to redemption at the option of the issuers at various times or under certain conditions. For the most part, redemption earlier than within three or four years of maturity would require the payment of redemption premiums.

Aggregate maturities and sinking fund requirements during the five years ending January 31, 1997 are as follows:
1993 – $ 67,909,000; 1994 – $156,371,000; 1995 – $274,650,000; 1996 – $282,292,000; 1997 – $120,498,000.

14. CAPITAL

The authorized classes of shares of the Company consist of unlimited numbers of preferred shares and common shares (designated ordinary shares prior to August 1, 1990), all without nominal or par value. Of the preferred shares, 11,750,000 are designated as "$1.80 cumulative redeemable preferred shares series A" with a stated capital of $22.50 each, 800,000 are designated as "variable rate, cumulative redeemable preferred shares series C" with a stated capital of $25.00 each and 10,000,000 are designated as "$1.875 cumulative redeemable convertible preferred shares series H" with a stated capital of $25.00 each.

Capital comprises issued and outstanding shares and additional paid-in capital as follows:

	1992		January 31, 1991	
	Number of shares	$000's	Number of shares	$000's
Capital stock:				
Preferred shares				
Series A	–	–	3,675,418	82,697
Series C	347,939	8,699	608,868	15,222
		8,699		97,919
Common shares	49,827,961	811,210	45,597,995	710,137
		819,909		808,056
Additional paid-in capital		17,657		13,847
		837,566		821,903

The changes in shares issued and outstanding during the two years ended January 31, 1992 are as follows:

	Number of shares	$000's
Preferred shares series A:		
Issued and outstanding at January 31, 1990	3,859,618	86,841
Purchased for cash and cancelled	(184,200)	(4,144)
Issued and outstanding at January 31, 1991	3,675,418	82,697
Purchased for cash and cancelled:		
Pursuant to offer (see below)	(2,045,029)	(46,013)
Open market	(150,300)	(3,382)
Redeemed	(1,480,089)	(33,302)
Issued and outstanding at January 31, 1992	–	–

	Number of shares	$000's
Preferred shares series C:		
Issued and outstanding at January 31, 1990	648,867	16,222
Redeemed	(39,999)	(1,000)
Issued and outstanding at January 31, 1991	608,868	15,222
Purchased for cash and cancelled	**(220,931)**	**(5,523)**
Redeemed	**(39,998)**	**(1,000)**
Issued and outstanding at January 31, 1992	**347,939**	**8,699**
Common shares:		
Converted from ordinary shares on August 1, 1990	45,013,026	700,176
Issued:		
Under the executive stock option plan	143,909	1,864
Under the dividend reinvestment plan	442,207	8,117
On conversion of Zellers Inc. 5½% convertible subordinated debentures series 1971	162	5
Purchased for cash and cancelled	(1,309)	(25)
Issued and outstanding at January 31, 1991	45,597,995	710,137
Issued:		
Under the employee share ownership plan	**147,520**	**2,877**
Under the executive stock option plan	**481,421**	**7,603**
Under the dividend reinvestment plan	**583,531**	**17,692**
On conversion of Zellers Inc. 5½% convertible subordinated debentures series 1971	**17,494**	**382**
To a Canadian underwriting group	**3,000,000**	**72,519**
Issued and outstanding at January 31, 1992	**49,827,961**	**811,210**
Weighted average number of common shares outstanding during the year ended January 31,1992	**48,955,538**	
Ordinary shares:		
Issued and outstanding at January 31, 1990	44,608,986	842,405
Issued:		
Under the executive stock option plan	131,275	2,410
Under the dividend reinvestment plan	271,372	7,852
On conversion of Zellers Inc. 5½% convertible subordinated debentures series 1971	1,393	43
Converted on August 1, 1990:		
Into common shares	(45,013,026)	(700,176)
Into special shares		(152,534)
Issued and outstanding at August 1, 1990	–	–
Special shares:		
Converted from ordinary shares on August 1, 1990	45,013,026	152,534
Reduction of stated capital to $1	–	(152,534)
Purchased for cash of $1 and cancelled	(45,013,026)	–
Issued and outstanding at August 1, 1990	–	–

Between February 19, 1991 and March 15, 1991, pursuant to an offer dated February 19, 1991 to the holders thereof, the Company purchased for cancellation 2,045,029 series A shares at $20.75 per share for an aggregate cost, including expenses, of $42,481,000.

The funds borrowed to purchase these shares were repaid from the net proceeds of $72,519,000 from the sale on March 5, 1991 to a Canadian underwriting group of 3,000,000 common shares issued at a price of $25.15 per share, less commission. All remaining outstanding series A shares were redeemed on January 17, 1992 at a redemption price of $22.50 per share plus accrued dividends.

All remaining series C shares have been called for redemption on March 15, 1992 at a redemption price of $25.00 per share. Holders are entitled to receive dividends at a rate of 7.12% until redemption.

At January 31, 1992 3,874,670 common shares are reserved for issuance under the Executive Stock Option Plan and the Senior Executive Share Purchase Plan and options are outstanding with a number of employees to purchase, in aggregate, up to 3,509,151 common shares at an exercise price equivalent to their market price per share immediately preceding the respective dates on which the options were granted. The outstanding options expire at various dates between May 1992 and December 2001 and have a weighted average issue price of $20.84 per share. Both the number of options outstanding and the exercise prices were adjusted as a result of amendments to the plan necessitated by and incorporated in the Arrangement for the distribution of Markborough (see note 3). At January 31, 1992 365,519 options were unallocated.

At January 31, 1992 the holders of approximately 45.3% of the common shares were participating in the Dividend Reinvestment Plan which provides a means for eligible holders of common shares to reinvest dividend proceeds in common shares at 95% of their weighted average market price per share for a three day period immediately preceding the dividend payment date.

During the year ended January 31, 1991 in connection with the Arrangement for the distribution of Markborough (see note 3), all issued and outstanding ordinary shares were converted into special shares and common shares on the basis of one special share and one common share for each ordinary share. The paid-up capital allocated to the special shares was $152,534,000 and was subsequently reduced to $1. On August 1, 1990 all issued and outstanding special shares were purchased for cash and cancelled.

The cost of shares redeemed or reacquired at amounts other than book value in each of the two years ended January 31, 1992 has been allocated as follows:

	Cost	Allocated to	
		Capital stock	Additional paid-in capital
	$000's	$000's	$000's
In the year ended January 31, 1992:			
Preferred shares series A	**78,959**	**82,697**	**(3,738)**
Preferred shares series C	**5,451**	**5,523**	**(72)**
	84,410	**88,220**	**(3,810)**
In the year ended January 31, 1991:			
Preferred shares series A	3,642	4,144	(502)

15. CONSOLIDATED STATEMENTS OF CASH FLOW AND FUNDING

The "net effect of changes in operating working capital" appearing in the HBC Retail operating activities section of the Consolidated Statements of Cash Flow and Funding comprises the following:

	Year Ended January 31, 1992	1991
	$000's	$000's
Decrease (increase) in:		
Cash	**1,193**	743
Customer accounts receivable	**(53,517)**	(17,925)
Other accounts receivable	**72,277**	(77,017)
Merchandise inventories	**(119,785)**	120,190
Prepaid expenses	**(9,099)**	(2,536)
Increase (decrease) in:		
Trade accounts payable	**4,723**	27,593
Other accounts payable and accrued expenses	**13,246**	(36,043)
Income taxes payable	**15**	767
	(90,947)	15,772

16. LEASES

a) As lessee

HBC Retail conducts a substantial part of its operations from leased stores in shopping centres. All leases involving the Company as lessee have been accounted for as operating leases.

HBC Retail rental expenses charged to earnings in the years ended January 31, 1992 and January 31, 1991 were $139,000,000 and $127,000,000, respectively.

The future minimum rental payments required under leases having initial or remaining noncancellable lease terms in excess of one year are summarized as follows:

	$000's
Year ending January 31, 1993	**110,300**
1994	**109,100**
1995	**101,400**
1996	**94,700**
1997	**89,600**
Thereafter	**986,900**
Total minimum lease payments	**1,492,000**

In addition to these rental payments (and, in a few cases, relatively minor contingent rentals), most of the leases generally provide for the payment by the Company of real estate taxes and other related expenses.

b) As lessor

Fixed assets in the Consolidated Balance Sheets at January 31, 1992 and January 31, 1991 include an office tower leased to others under operating leases, with a cost of $21,800,000 at both dates and accumulated amortization of $6,500,000 and $6,200,000, respectively. HBC Retail sales and revenue for the years ended January 31, 1992 and January 31, 1991 include rentals from this property of $7,900,000 and $8,400,000, respectively.

17. RELATED PARTY TRANSACTIONS

a) Tax benefits

During the year ended January 31, 1992 the Company received a net income tax benefit of $579,000 (see note 7) from transactions between a wholly-owned subsidiary and the Company's ultimate holding company which had the effect of accelerating the recovery of tax losses incurred by the latter.

This benefit was obtained through the issuance of taxable interest bearing debt and the concurrent purchase of a similar amount of non-taxable dividend earning preferred shares. These transactions reduced current income taxes otherwise payable by the subsidiary by $4,043,000, of which $3,464,000 is payable to the ultimate holding company as reimbursement for the tax losses transferred. The net amount has been recorded as a reduction of income tax expense.

Both parties have a legally enforceable right to extinguish, by set off at any time, the loan and the preferred shares and settlement will in due course be effected by concurrent repayment of the debt and redemption of the preferred shares. Consequently the corresponding asset and liability as well as the pre-tax income and expense arising therefrom have been offset in the Consolidated Balance Sheet and the Consolidated Statement of Earnings, respectively.

b) Other

The Company is involved in numerous transactions with related parties in the ordinary course of its business. None of these transactions is significant in relation to these consolidated financial statements.

18. MARKBOROUGH EARNINGS

Markborough earnings for the six months ended July 31, 1990 comprised the following:

	$000's
Operating profit including equity in earnings of joint ventures (after deducting amortization of $3,011,000)	23,764
Interest expense (excluding amount capitalized of $26,821,000)	(12,070)
Earnings before income taxes	11,694
Income taxes	(6,546)
Net earnings	5,148

19. CONTINGENCIES

As of January 31, 1992 there are a number of claims against the Company in varying amounts and for which provisions have been made in these consolidated financial statements as appropriate. It is not possible to determine the amounts that may ultimately be assessed against the Company with respect to these claims but management believes that any such amounts would not have a material impact on the business or financial position of the Company.

Included among these claims is one, which the Company has denied, for $85,000,000 in damages in respect of an alleged breach of an agreement to which Towers was a party at the time of its acquisition (see note 4). In the unlikely event that this claim does succeed in a material amount it would be accounted for in the year of settlement as a prior period adjustment.

Settlements arising from other claims would be recorded against income of the periods in which they occur.

Management's Report to the Shareholders

Gary Lukassen

The management of Hudson's Bay Company is responsible for the preparation and integrity of the consolidated financial statements contained on pages 19 to 27 of this Annual Report and of financial information, discussion and analysis presented on other pages. The accounting principles which form the basis of the consolidated financial statements and the more significant accounting policies applied are described in note 1 on page 22. Where appropriate and necessary, professional judgments and estimates have been made by management in preparing the consolidated financial statements.

In order to meet its responsibility, management maintains accounting systems and related internal controls designed to provide reasonable assurance that assets are safeguarded and that transactions and events are properly recorded and reported. An integral part of these controls is the maintenance of programs of internal audit coordinated with the programs of the external auditors.

Ultimate responsibility for financial reporting to shareholders rests with the Board of Directors. The Audit Committee of the Board, a majority of whom are outside directors, meets quarterly with management and with internal and external auditors to review audit results, internal accounting controls and accounting principles and procedures. The Audit Committee reviews consolidated financial statements with management and the external auditors and reports to the directors prior to the approval of the audited consolidated financial statements for publication.

Peat Marwick Thorne, independent auditors appointed by the shareholders, express an opinion on the fair presentation of the consolidated financial statements. They meet regularly with both the Audit Committee and management to discuss matters arising from their audit, which includes a review of accounting records and internal controls. The Auditors' Report to the Shareholders appears on the following page.

President and Chief
Executive Officer

Executive Vice-President and
Chief Financial Officer

Toronto, Canada
March 12, 1992

KPMG Peat Marwick Thorne

Auditors' Report to the Shareholders

We have audited the consolidated balance sheets of Hudson's Bay Company as at January 31, 1992 and January 31, 1991 and the consolidated statements of earnings, retained earnings and cash flow and funding for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at January 31, 1992 and January 31, 1991 and the results of its operations and the changes in its financial position for the years then ended in accordance with generally accepted accounting principles.

Peat Marwick Thorne

Chartered Accountants

Toronto, Canada
March 12, 1992

Directors

Ian A. Barclay, Vancouver ■
Associate, McQuaid & Associates Consulting Ltd. Mr. Barclay is a former Chief Executive Officer of a major forest products company.
Elected 1975

Marcel Bélanger, Quebec * ■
President, Gagnon et Bélanger Inc., Management Consultants. Mr. Bélanger is a former President of the Canadian Institute of Chartered Accountants.
Elected 1976

W. Michael Brown, New York
President, The Thomson Corporation, an information, publishing and leisure travel company which is associated with the controlling shareholder of Hudson's Bay Company.
Elected 1985

Gurth C. Hoyer Millar, London, England
Chairman, City Renaissance PLC
Elected 1976

George J. Kosich, Toronto *
President and Chief Executive Officer, Hudson's Bay Company; 32 years service with the company.
Elected 1985

Gary J. Lukassen, Toronto *
Executive Vice-President, and Chief Financial Officer, Hudson's Bay Company; 17 years service with the company.
Elected 1987

Donald S. McGiverin, Toronto ■
Governor, Hudson's Bay Company; 23 years service with the company.
Elected 1969

Dawn R. McKeag, Winnipeg ■
President, Walford Investments Ltd. Mrs. McKeag is a director of a number of major companies.
Elected 1975

Peter W. Mills, Toronto
Senior Vice-President and General Counsel, The Woodbridge Company Limited. Mr. Mills is an officer and director of a number of companies associated with the controlling shareholder of Hudson's Bay Company.
Elected 1985

David E. Mitchell, Calgary
President, Alberta Energy Company Ltd., a diversified company investing in energy resources and industrial development.
Elected 1984

David K. R. Thomson, Toronto
Deputy Chairman, The Woodbridge Company Limited. Mr. Thomson is an associate of the controlling shareholder of Hudson's Bay Company.
Elected 1987

Kenneth R. Thomson, Toronto *
Chairman, The Thomson Corporation. Mr. Thomson is, beneficially, the controlling shareholder of Hudson's Bay Company.
Elected 1979

John A. Tory, Toronto * ■
Deputy Chairman, The Thompson Corporation. Mr. Tory is a director and officer of a number of companies associated with the controlling shareholder of Hudson's Bay Company.
Elected 1979

Neil R. Wood
President, Markborough Properties Inc., a real estate development company which is associated with the principal shareholder of Hudson's Bay Company.
Elected 1987

* Member Executive Committee

■ Member Audit Committee

Officers

Donald S. McGiverin
Governor

George J. Kosich
President and
Chief Executive Officer

Gary J. Lukassen
Executive Vice-President,
and Chief Financial Officer

N.R. (Bob) Peter
Executive Vice-President

Paul S. Walters
Executive Vice-President

Robert N. D. Hogan
Senior Vice-President,
Credit and Financial Marketing
Services

David J. Crisp
Vice-President,
Human Resources

John M. Cunningham
Vice-President,
Operations

Brian C. Grose
Vice-President and
Controller

J.G. (Jerry) Hartman
Vice-President,
Research and Development

A. Rolph Huband
Vice-President and Secretary

R.P. (Ron) Hughes
Vice-President and
Managing Director,
Asian Operations

Raymond J. McDonald
Vice-President,
Distribution

Donald C. Rogers
Vice-President,
Real Estate and Development

Larry W. Rowe
Vice-President,
Information Services

Sheila K. Walters
Vice-President,
Store Planning and
Construction

Kenneth C. Wong
Assistant Treasurer

Principal Subsidiaries/Divisions

The Bay
N.R. (Bob) Peter
President

Zellers Inc.
Paul S. Walters
President

Fields Stores
Janis R. Ostling
President

Corporate Information

Auditors
Peat Marwick Thorne

Registered Office
401 Bay Street,
Toronto, Ontario M5H 2Y4

Principal Bankers
Bank of Montreal
Canadian Imperial Bank of Commerce
The Bank of Nova Scotia
The Royal Bank of Canada
The Toronto-Dominion Bank

Annual Meeting
The 323rd Annual Meeting of Shareholders will be held at the Arcadian Court, 8th Floor, 401 Bay Street (Queen Street store) Toronto, on May 21~~, 1992 at 3:00~~ p.m.

[redacted]

Registrars and Transfer Agents
The R-M Trust Company,
Calgary, Montreal, Toronto, Vancouver,
Winnipeg and London, England

Stock Exchange Listings
Common Shares are listed on the
Montreal and Toronto Exchanges

Comparative Financial Summary

	1991	1990*	1989*	1988*	1987*
Operations (in millions of dollars)					
Sales and revenue:					
The Bay	**2,118**	2,322	2,296	2,334	2,356
Zellers	**2,789**	2,330	2,150	2,011	1,845
Fields	**86**	91	90	88	88
Other	**39**	227	68	58	56
Total sales and revenue	**5,032**	4,970	4,604	4,491	4,345
Earnings:					
Operating profit:					
The Bay	**59**	122	129	89	81
Zellers	**218**	200	180	142	93
Fields	**1**	3	3	2	1
Other	**6**	(8)	3	(5)	6
Earnings before interest and income taxes	**284**	317	315	228	181
Interest expense	**(144)**	(155)	(158)	(171)	(168)
Earnings before income taxes	**140**	162	157	57	13
Income taxes:					
Current year's provision	**(57)**	(64)	(59)	(20)	–
Recovery of prior years' tax losses	**–**	60	46	–	–
Earnings before extraordinary items	**83**	158	144	37	13
Extraordinary items	**–**	–	–	(27)	(18)
Net earnings	**83**	158	144	10	(5)
Preferred dividends paid	**(5)**	(8)	(22)	(27)	(28)
Earnings for common shareholders	**78**	150	122	(17)	(33)
Common dividends paid	**40**	36	21	18	18
Cash flow:					
From earnings	**185**	203	190	104	119
From changes in operating working capital	**(91)**	16	44	44	(134)
From operations	**94**	219	234	148	(15)
Capital expenditures	**(122)**	(120)	(92)	(36)	(30)
Investment in Towers	**(36)**	(142)	–	–	–
Dividends	**(45)**	(44)	(43)	(45)	(46)
Other	**(1)**	(24)	32	17	71
Total cash inflow (outflow)	**(110)**	(111)	131	84	(20)
Funding of Assets Employed (in millions of dollars)					
Debt:					
Long-term	**905**	593	893	996	1,069
Net short-term	**430**	650	254	445	480
Deferred income taxes	**27**	(14)	6	(1)	(42)
Shareholders' equity:					
Preferred shareholders (including accrued dividends)	**9**	98	104	344	357
Common shareholders	**1,217**	1,074	941	447	524
Assets employed	**2,588**	2,401	2,198	2,231	2,388
Debt: Equity Ratio	**1.1:1**	1.1:1	1.1:1	1.8:1	1.8:1
Per Common Share (in dollars)					
Earnings before extraordinary items	**1.61**	2.01**	2.26**	.32	(0.51)
Cash flow from earnings	**3.67**	4.35	5.02	2.53	3.05
Dividends	**0.80**	0.80	0.60	0.60	0.60
Equity	**24.43**	23.53	21.09	14.41	16.33
Shareholders					
Number of registered common shareholders	**7,000**	7,400	7,800	8,900	9,300
Common shares outstanding (in thousands):					
Year End	**49,828**	45,598	44,609	30,993	30,187
Average	**48,956**	44,959	33,489	30,556	29,801
Range in common share price (in dollars):					
After Markborough distribution	**37–23⅞**	24¼–16			
Before Markborough distribution		34–27⅝	38–24¾	26¼–18½	29½–18⅛
The Economy (% increase)					
Gross domestic product	(1.5)	0.8	3.1	4.5	4.0
Consumer price index	5.6	4.9	5.0	4.1	4.4
Department store type merchandise sales	(10.7)	1.5	9.2	7.8	8.1

* Excludes Markborough Properties Inc., whic[redacted]

** Earnings per share before extraordinary ite[redacted] in 1990 and $3.64 in 1989.

Note: Where appropriate and significant, fi[redacted]

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