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2005
Annual Report

The
Jean Coutu
Group (PJC) Inc.

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www.jeancoutu.com

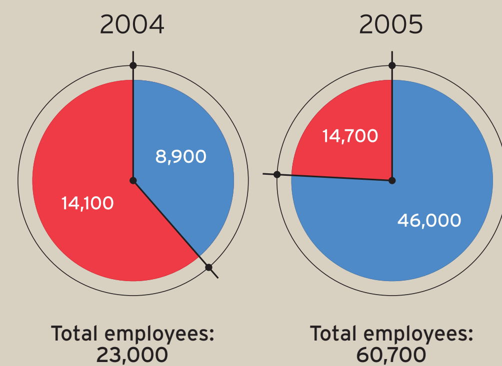
www.brooks-rx.com

www.eckerd.com

ON JULY 31, 2004, THE JEAN COUTU GROUP (PJC) INC., ACQUIRED THE NORTHEASTERN UNITED STATES STORES OF ECKERD PHARMACY. THIS ACQUISITION OF OVER 1,500 DRUGSTORES, THE LARGEST TRANSACTION IN THE HISTORY OF THE COMPANY, BRINGS THE GROUP TO ITS NEXT LEVEL OF DEVELOPMENT AS THE FOURTH-LARGEST DRUGSTORE CHAIN IN NORTH AMERICA AND THE SECOND-LARGEST ON THE EAST COAST.

TODAY, THE JEAN COUTU GROUP EMPLOYS OVER 60,000 PEOPLE AND HAS SYSTEM SALES CLOSE TO $12 BILLION ON A PRO FORMA BASIS. ITS 321 DRUGSTORES IN CANADA ARE FRANCHISED STORES OPERATING UNDER THE JEAN COUTU BANNER, WHILE ITS US NETWORK CONSISTS OF 1,922 CORPORATE-OWNED STORES OPERATING UNDER THE BROOKS AND ECKERD BANNERS.

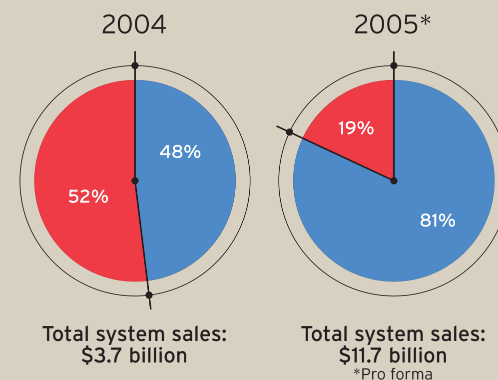
Employees



Total employees: 23,000

Total employees: 60,700

System Sales



Total system sales: $3.7 billion

Total system sales: $11.7 billion
*Pro forma

● Canada ● United States

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General Information

The Jean Coutu Group (PJC) Inc.
530 Bériault Street
Longueuil, Québec
J4G 1S8
(450) 646-9760

The Jean Coutu Group (PJC) USA, Inc.
50 Service Road
Warwick, Rhode Island
U.S.A. 02886
(401) 825-3900

Auditors
Deloitte & Touche, L.L.P.
1 Place Ville-Marie
Suite 3000
Montréal, Québec
H3B 4T9

Transfer agent and registrar
National Bank Trust
1100 University Street
9th floor
Montréal, Québec
H3B 2G7
Tel: (514) 871-7142
1-800-341-1419

Stock market information
Toronto Stock Exchange
Ticker symbol: PJC.SV.A

Internet Sites
The Jean Coutu Group (PJC) Inc.
www.jeancoutu.com

The Jean Coutu Group (PJC) USA, Inc.
www.brooks-rx.com
www.eckerd.com

Annual General Meeting
The Annual General Meeting of Shareholders of The Jean Coutu Group (PJC) Inc. will be held on September 15, 2005 at 9:30 a.m. at the corporate headquarters of the Company, 551 Bériault Street, Longueuil, Québec.

Annual information form
The annual information form for the year ended May 28, 2005 is available upon request. To order, please contact the Corporate Secretary of the Company.

Investor Relations
(450) 646-9611, ext.1068
IR@jeancoutu.com

Pour obtenir la version française de ce rapport, veuillez écrire à :

Le Groupe Jean Coutu (PJC) inc.
à l'att. de : Secrétariat corporatif
530, rue Bériault
Longueuil (Québec) J4G 1S8

ou transmettez-nous un message électronique à l'adresse suivante : IR@jeancoutu.com

(in thousands of US dollars, except per share data and ratios)	52 weeks ended May 28, 2005 $	2004 $	Years ended May 31, 2003 $	2002 $	2001 $
Financial Performance					
Revenues[1]					
Canada	1,406,139	1,235,757	884,854	902,619	841,137
United States	8,211,224	1,807,210	1,761,815	1,305,324	1,017,966
Total	9,617,363	3,042,967	2,646,669	2,207,943	1,859,103
Operating income before amortization (OIBA)	452,740	249,722	207,475	171,511	147,584
Earnings before income taxes	91,795	193,754	150,880	130,640	107,175
Net earnings	104,378	132,683	104,784	86,874	69,493
Financial Position					
Capital assets	1,492,499	544,174	502,241	415,065	263,904
Total assets	5,694,926	1,343,754	1,252,020	1,084,152	797,043
Total indebtedness	2,561,432	207,175	269,028	263,789	111,475
Shareholders' equity	1,412,103	853,443	738,078	615,829	538,193
Per Share Data[2]					
Net earnings (basic)	0.41	0.58	0.46	0.39	0.32
Dividends in Canadian dollars	0.12	0.12	0.12	0.09	0.08
Shareholders' equity	5.40	3.76	3.26	2.73	2.39
Financial Ratios					
Net debt/Book capitalization	62.5%	18.4%	26.7%	30.0%	1.0%
Net debt/LTM OIBA[3]	4.8	0.8	1.3	1.5	0.7
LTM OIBA/Interest[3]	2.6	17.2	11.6	15.7	15.9
Network Performance – Retail Sales[4]					
Canada	2,173,428	1,939,637	1,588,364	1,443,556	1,363,197
United States	8,200,445	1,802,585	1,757,035	1,301,720	1,013,287
Total	10,373,873	3,742,222	3,345,399	2,745,276	2,376,484
Share Information in Canadian dollars[2]					
High	21.39	19.79	20.00	19.72	13.97
Low	14.66	14.15	13.25	11.82	8.55
Close	19.59	18.95	15.71	19.12	13.22
Volume	111,710,543	63,944,389	38,986,287	40,391,246	39,117,562

(1) Revenues comprise sales and other revenues.
(2) On September 29, 2000 and September 25, 2002, the Company declared a 2-for-1 split of its Class A subordinate shares and Class B shares. The share figures have been calculated taking into consideration these stock splits.
(3) Pro forma in fiscal 2005, Eckerd and related financing on a 52-week basis.
(4) Franchised outlets retail sales are not included in the Company's Financial Statements.

MY MOTTO HAS ALWAYS BEEN TO CONDUCT SERIOUS BUSINESS WITH A SMILE. AFTER ALL, OUR BUSINESS IS ALL ABOUT PEOPLE. WE ARE HERE TO PROVIDE SERVICE. AT THE JEAN COUTU GROUP, OUR GOAL IS TO OFFER CUSTOMERS ALL THE ADVANTAGES OF A LARGE DRUGSTORE CHAIN WHILE STILL RETAINING THE PERSONALIZED SERVICE OFFERED BY A LOCAL PHARMACIST.

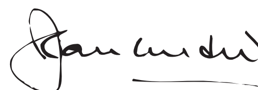
In fact, even though we have grown to be a leading North American drugstore chain, I still take pride in referring to myself as a neighborhood pharmacist, as I was when I opened our first store in 1969. To me, a neighborhood pharmacist takes responsibility for making sure customers and employees are satisfied, while at the same time ensuring that the business grows profitably.

In the past year, the Company took a major step forward with the acquisition of over 1,500 Eckerd drugstores. The integration process is substantially complete. However, the real opportunity will come from instilling our neighborhood pharmacist values of service, excellence and accountability throughout a much larger organization. As we have learned from many previous acquisitions, this process takes time. It involves meeting with our employees, listening to them, building their trust, and providing them with the tools to help them do their job as best they can.

The response of the new Eckerd employees to our approach has been immediate and positive. These are good people and we have a lot in common, including their long-term commitment to the Company's success. Combine that with our expertise in running a successful drugstore chain, and I believe that we have a winning combination for long-term growth, just as we have accomplished with acquisitions in the past.

The real opportunity with Eckerd will come from instilling our neighborhood pharmacist values of service, excellence and accountability throughout a much larger organization.

Our values of service, excellence and accountability have served us well over the past 35 years. We are extremely grateful to our 60,700 people – now located as far south as Georgia to as far north as Québec – for translating these corporate values into action. Together, we have set the stage for future growth and, most importantly, for bringing smiles to people's faces.



Jean Coutu
Founder and Chairman

To the Next Level

IN FISCAL 2005, THE JEAN COUTU GROUP EMBARKED ON ITS NEXT LEVEL OF DEVELOPMENT BY ACQUIRING OVER 1,500 ECKERD DRUGSTORES LOCATED IN NORTHEASTERN UNITED STATES. THIS ACQUISITION MARKS A TRANSFORMATIONAL STEP FORWARD FOR THE JEAN COUTU GROUP, MAKING US THE FOURTH-LARGEST DRUGSTORE CHAIN IN NORTH AMERICA.

Ideal Opportunity

The Eckerd acquisition was an ideal opportunity for us to expand in a growing industry that we know well. Established in 1898, Eckerd is a well-established banner on the East Coast of North America. In addition, it provided us with an instant leadership position in a contiguous geographic area stretching from Georgia to Vermont. Eckerd also has a modern store network with 65% of its stores opened, reconfigured or relocated in the three years prior to the acquisition.

Value was another important consideration in this transaction. The purchase price of $2.5 billion represented a multiple of 6.9 times OIBA (operating income before amortization) and 0.3 times revenues versus an average of 10.7 times OIBA and 0.7 times revenue for comparable transactions over the last ten years.

Above all, we saw the significant value that we could add to the Eckerd network through integration cost savings and by applying our proven business practices, emphasizing pharmacy and customer care.

Strong Base for US Expansion

The Jean Coutu Group has been building a strong US network since it entered that market in 1987. Our US stores have operated under the Brooks Pharmacy banner since 1994, when the Company acquired 220 Brooks stores in the New England area. Within two years, Brooks' operating income doubled.

Our US operations have continued to grow profitably through operational improvements and a total of four acquisitions of US drugstore chains. We believe that much of this growth has been the result of our strong corporate values, combined with the sharing of know-how and systems developed by the Company over the past 35 years.

Our US operations therefore provide a solid backbone for the integration of the Eckerd operations. In addition to an excellent track record, Brooks Pharmacy has been re-branded for the quality of its customer care. In 2004, Brooks was recognized by consumers as the Regional Drug Store Chain of the Year, and received the National Pharmacy Satisfaction Award at the Retail Excellence Awards sponsored by *Drug Store News*.

Solid Execution of the Integration

The integration of the Eckerd and Brooks operations is essentially complete and the network is performing as expected. Margins have improved in fiscal 2005; at Eckerd, we now have positive trends in pharmacy sales and are gaining market share in key categories of pharmacy and health and beauty products. Most importantly, service levels have improved noticeably in front-end and pharmacy care.

Over the past year, our main focus has been on integrating the head offices and systems, reorganizing the combined network into four operating groups to increase accountability, and improving overall network performance. That involved initiatives such as implementing our 15-minute expectation for prescription fills, improving inventory management and re-emphasizing Eckerd's private label products. In fiscal 2006, we will begin the roll-out of our pharmacy system into the Eckerd stores, along with further initiatives to improve network performance.

We treat our employees as we want them to treat our customers. Our people-oriented approach is the right one for a long-term investor. This approach has worked well for us in the past and we know that, over time, it will reward us in many ways, including in our financial performance.

One of the main challenges of any business integration, particularly one of this size, is the human side. As a people-focused company, this aspect of the integration was of utmost importance to us. Within 24 hours of signing the purchase agreement, senior executives met with Eckerd's senior managers at its Florida head office. They may not have liked what we had to say, but they appreciated our frankness and respect. Whether they were staying with us or moving on, we needed their support to assist us with the integration of our US headquarters in Rhode Island. We are very proud to say that the integration team performed above all expectations and the transfer went well.

We also sought to build the trust of Eckerd employees in the stores and warehouses. Over the course of the year, senior management visited over 1,000 stores, hosted group meetings, broadcast to all the stores, and held presentations in Eckerd's distribution centers – all with one main purpose in mind – to become partners with our new employees and help them do their job better. The response we received was highly positive.

Canadian Operations

In fiscal 2005, our Canadian network continued to out-perform the industry, despite increased competition from many newcomers in the sector. The Canadian franchise network showed a 5.9% increase in sales compared with last year.

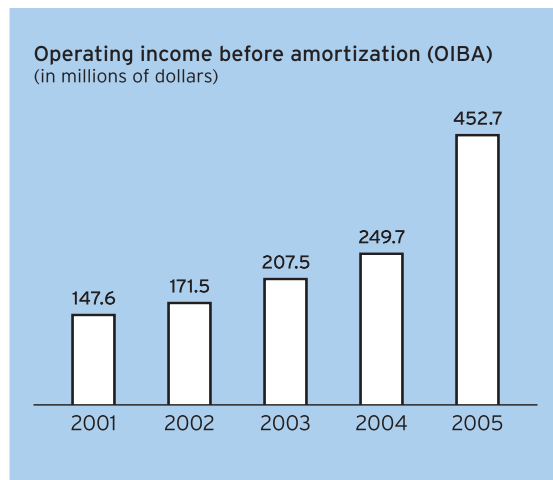
Management attributes the Company's strong Canadian performance primarily to its leading market position, strategically located stores, superior customer service, as well as initiatives like an increased advertising and promotion program in fiscal 2005.

Financial Performance

For the fiscal year ending May 28, 2005, revenues increased substantially to $9.6 billion from $3.0 billion in the previous fiscal year. Operating income before amortization (OIBA) amounted to $452.7 million against $249.7 million in the previous year.

While revenues benefited significantly from the addition of the Eckerd operations, operating results were negatively impacted by the costs of running several head office infrastructures. Furthermore, general and operating expenses costs were substantially higher due to transition costs incurred following the Eckerd acquisition.

Our focus is to drive sales growth profitably. Over the year, and principally due to the Eckerd acquisition, the Company's gross margin improved significantly and at 24.9%, the US margin is ahead of pre-acquisition levels. Most of this improvement was due to increased sales of generics and health and beauty products, as well as control over pricing, mix and promotions. In fiscal 2006, we expect further improvement in our gross margin as a result of a variety of initiatives, including a reduction in Eckerd's inventory shrinkage.



Significant progress continues to be made at our US operations to restore profitability to pre-acquisition levels. Our stated objective is to improve the OIBA margin of our combined US operations to our pre-acquisition level of 6.3%. In fiscal 2005, the OIBA margin for our US operations was 3.7%. Operating results will improve in fiscal 2006 as a result of network operational improvements and the completion of head office and systems integration in the first quarter.

Debt Reduction: A Priority

The Eckerd acquisition was financed through a combination of debt and equity. At year-end, our leverage ratio of Net Debt to pro forma OIBA was 4.8 times. Management's stated objective is to reduce this ratio to less than 3.5 within 24 months of closing the acquisition. This continues to be a high priority.

Looking Forward

Demographic trends are excellent for the North American drugstore industry. As the population ages, demand for prescription drugs is expected to continue to increase at a high single-digit rate. Few industries have such steady organic growth. With rising healthcare costs, the neighborhood pharmacist – the most accessible healthcare professional around – is becoming an even more integral and valued part of the healthcare system.

Concluding the integration of our US operation was our top priority in fiscal 2005. It was based on solid execution at the store level and throughout our network. While the Eckerd acquisition was by far our largest to date, we have a proven track record of integrating acquisitions successfully and using capital judiciously to maximize returns.

It is our goal and full expectation that Eckerd Pharmacy will also become the destination pharmacy in its communities, just like the Jean Coutu and Brooks Pharmacies. We are putting all the elements in place to make that a reality.

In addition to the Company's history of performance, we continue to receive a vote of confidence from our customers and peers. Early this year, the Jean Coutu Group was named to the Top 25 Honour Roll of Canada's Most Respected Corporations by a survey of CEOs. We were again named the Most Admired Company in the Province of Québec for the fourth time in eight years. Brooks Pharmacy also continues to win industry awards year after year.

We wish to thank all of our employees for their tireless efforts in meeting the challenges of the integration and for consistently exceeding objectives. To our shareholders, customers, employees and franchisees, thank you for your continued enthusiasm and support. We believe that we have only just begun to capitalize on the strengths of our North American network. We look forward to reporting on our performance improvements over the coming fiscal quarters and years.

François J. Coutu
President and Chief Executive Officer,
The Jean Coutu Group (PJC) Inc.

Michel Coutu
President and Chief Executive Officer,
The Jean Coutu Group (PJC) USA, Inc.

A North American Leader

Canada
321 franchised stores

New England Region
405 corporate stores

Northeast Region
440 corporate stores

Metropolitan Region
446 corporate stores

Mid-Atlantic Region
631 corporate stores

Your Convenient Neighborhood Drugstore

Our drugstores are anchors in their communities on the East Coast of North America. They are designed to be a one-stop pharmacy destination, so customers can fill their health and beauty needs within a few minutes, including the time it takes to walk to and from their car.

In selecting a store location, attention is paid to good visibility, to ensuring easy access through parking or public transit, to shopability, by providing the right size and configuration for the neighborhood, and to proximity to health clinics, as well as to the areas where people live and like to shop. In Canada, approximately 39% of our drugstores are located adjacent to a medical center.

Our average store size is almost 8,000 selling square feet in Canada and about 9,000 selling square feet in the United States. In Canada, we also have a smaller concept of 1,000-1,500 square feet called “PJC Clinique”. These stores are located in medical centers and offer simply a pharmacy dispensary and over-the-counter drugs. In fiscal 2006, in both Canada and the US, we will launch new store prototypes of approximately 11,000 square feet of selling space so we can offer a wider selection of products, and customers can still get in and out of the store quickly with everything they need.

Pharmacy and Professionalism

The Jean Coutu Group's focus on pharmacy and professionalism has enabled it to expand its market share in the growing North American drugstore market. This growth is being fuelled by factors such as the aging of the baby boomer generation, the increased life expectancy of North Americans, and the development of new drugs. At the same time, competition has increased, not only from other drugstore chains, but also from non-traditional distribution channels.

To ensure that our professionalism will continue to set us apart, we have always placed "pharmacy first". Pharmacy is at the heart of our drugstores, drawing customers into our stores and enabling us to develop a higher value-added customer relationship. Our professionalism also comes from our efforts to attract and retain the best people, provide best-in-class training and support, develop industry-leading technology and systems, and implement initiatives to help educate customers and respond to their health and beauty needs.

Attracting the Best People

Being an employer of choice is a key success factor in almost all businesses, but especially in a people-oriented business like ours. We strive to attract and retain the best people in all areas of our business. Attracting top-notch pharmacists is particularly important to us because of their value-added relationship with customers, and also because the demand for pharmacy graduates exceeds the supply. This situation was exacerbated several years ago when US pharmacy programs were extended from five to six years. Combined with other factors, US colleges graduate less pharmacy students today than they did 10 years ago. In Canada, competition for the best and brightest is also strong.

The Jean Coutu Group follows a multi-pronged approach to ensure that we attract and retain the top pharmacists. First, we focus on pharmacy as a career, rather than simply a job. We also endeavor to provide a high quality of life and an unequalled opportunity to practice the pharmacy profession. Our compensation and benefits plans are also reviewed regularly to ensure that we remain competitive. We also work closely with universities and colleges to help train future pharmacists, providing students with financial aid and support programs in addition to our internship programs.

Industry-leading Technology and Systems

We continue to invest in our technology and systems to ensure the accuracy of the prescriptions we fill, reduce customer wait times and, ultimately, free up pharmacists' time for more proactive patient care. Our Rx Care (US) and Rx-Pro (Canada) pharmacy systems used for filling prescriptions are considered industry-leading. For example, with thousands of different health insurers in Canada and the US, each with different conditions, our systems can verify in seconds if a prescription is covered by a patient's prescription plan, and they also prompt our pharmacists to recommend generic versus brand-name drugs, which results in a lower cost to payers and customers, in addition to higher margins for the Company.

In another example of our technological leadership, Brooks Pharmacy was the first drugstore chain in North America to execute an e-prescribe transaction. Since the acquisition, this capability has been introduced in our Eckerd drugstores. E-prescribing allows physicians to input a prescription directly into a hand-held device and send it directly to the pharmacy requested by the patient, thus reducing the time for us to fill a prescription and increasing accuracy. E-prescribing and auto-faxing can also be used by the pharmacist to request a re-fill prescription from the physician.

In recent years, the Jean Coutu Group has developed other technological tools, including an online and telephone prescription re-fill service and a complete point-of-sale business management system to more effectively manage pharmacy inventories and procurement.

To ensure we will continue to be on the leading edge in pharmacy technology and systems, we doubled the size of our Information Technology Center (Rx Center) facilities in fiscal 2005. The Rx Center is responsible for developing and implementing advanced technological solutions to improve operating efficiency. It serves as the technological and administrative hub for the Company's Canadian and American networks, as well as distribution centers on a round-the-clock basis.

Best-in-Class Training and Support

Our emphasis on professionalism extends to all areas of our business. To ensure that professionalism, we provide specialized training programs for management, pharmacists, lab technicians, cosmeticians, and customer service staff. In Canada, the Jean Coutu Academy provides professional development and support to pharmacists in our Canadian franchised outlets. Pharmacists also receive support from a medical and pharmacological information center.

The Pharmacy Jean Coutu (PJC) network has been spearheading initiatives to maximize efficiency through the reorganization of lab processes. During the year, it continued the roll out of its new Opti-Lab pharmacy departments and continued the Kaizen continuous efficiency and quality improvement program.

In the United States, we continued to improve the scope and content of our numerous Pharmacy training programs, from our student and intern programs to specialized and advanced training and development. The training and support is based on the Brooks Eckerd Pharmacy Standards of Service, which strive for excellence in personalized advice and customer service.

We also provide specialized training to our cosmeticians so they have an in-depth knowledge of our various cosmetic lines and stay on the leading edge of their specialization while building on their customer service focus.

Being of Service to our Customers

We strive to offer a complete pharmacy healthcare solution for our customers. In Canada, we educate them through the PJC Health Tip pamphlets and closed-circuit televisions in our waiting areas. We assist them through their personalized PJC Health Record, which is helpful for patients with multiple physicians or medical conditions, and in case of emergency.

In the United States, we match all competitors' coupons plus $1.00, and we support a Senior Citizen Discount Program. We accept Workers' Compensation and Medicare assignment, along with on-line claims processing. We provide extended-hour customer support through the Brooks Eckerd On Call help line, as well as the Patient Care Center. This Center helps our patients comply with key maintenance prescriptions. In select markets, we also have the largest and most extensive home delivery program in the chain drugstore industry.

In North America, pharmacists are the most accessible of all healthcare professionals. They are available in the stores, for extended hours, 7 days a week. They provide professional advice, free of charge and without an appointment. We believe that their role in the healthcare system will continue to grow, particularly with public concerns about accessibility and rising healthcare costs. According to the 2004 IMS Health Report, Intelligence.360, while the cost of pharmacotherapy is typically less than 15% of total healthcare spending on a national basis, it is also viewed as the most cost-effective form of intervention, after diet and exercise, for a very broad range of medical conditions.

The coming introduction of the Medicare Part D Drug Benefit in the United States in January 2006 gives us an excellent opportunity to strengthen our relationship with our senior clientele. We are preparing our pharmacists and other employees to be ready to help seniors and others understand what coverage option works best for their particular prescription drug needs. In addition to an extensive communications campaign, we will also provide one-on-one counselling in our stores and a community outreach program in partnership with seniors-oriented organizations to educate Americans on the benefits and options of Medicare.

Review of Operations | CANADA

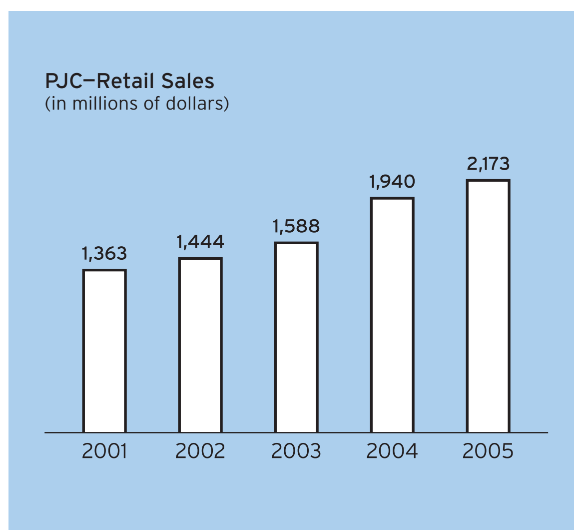
Market Position

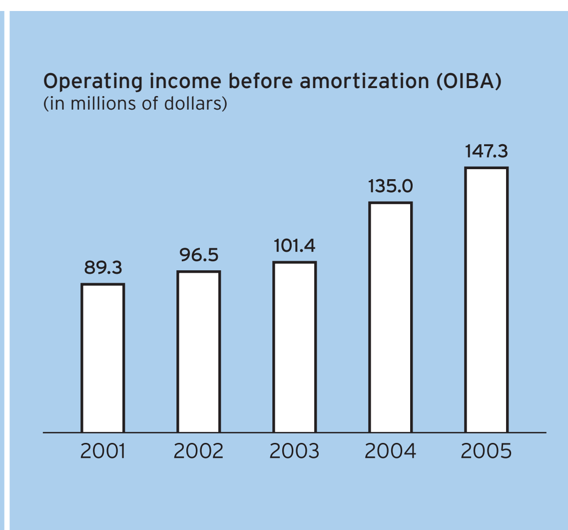
The Jean Coutu Group is the second-largest pharmacy chain in Canada and is the market leader in Québec, where it has 294 of its 321 Canadian stores. The Group is the premier provider of prescription drugs at retail in North America. The Eckerd acquisition gives us the opportunity to leverage institutional know-how and to optimize the network.

Our Canadian operations are based on a franchise model. The Company generates revenues from royalties, based on a percentage of store sales, and from the sale of merchandise to franchisees from our distribution centers. We also generate revenue from real estate properties, including many strategically located pharmacy locations. In fact, the Group either owns or has the master lease for all of its stores.

The pharmacist-owners of our franchised stores are entrepreneurial and highly motivated, giving us a strong network. Our franchisees fill approximately 47.5 million prescriptions per year in Canada, with an average per store of about 2,850 scripts per week. Our pharmacies are complemented by a first-class front-end offering, focusing on health and beauty items.

PJC also offers more than 1,800 different private label and exclusive products, which represent over 8% of our Canadian retail sales. These products help increase customer loyalty, drive store traffic and improve our gross margins.





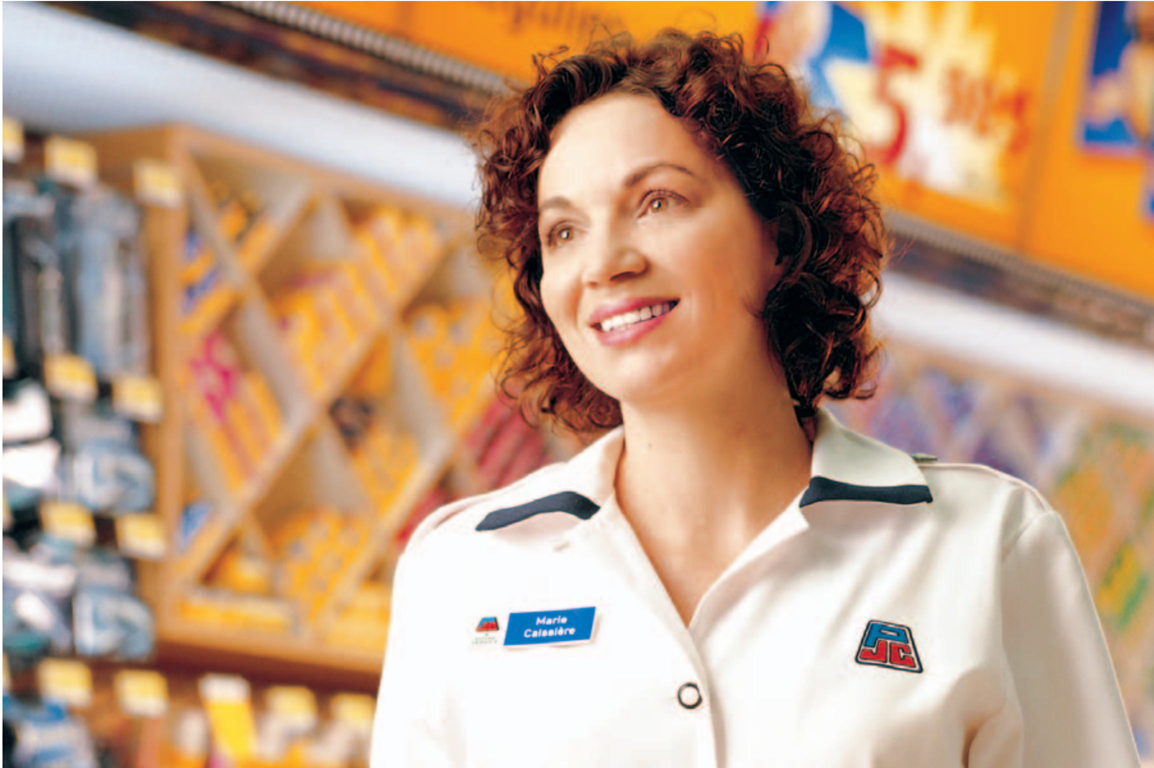
In June 2005, *Private Label Magazine* selected the Jean Coutu Group, among all other North American Drug Stores, as its 2005 Store Brand Leadership Award Winner, based on product innovation, packaging, marketing, employee involvement, and quality assurance.

2005 Performance

In fiscal 2005, our Canadian franchise network continued to out-perform the market, despite increasing competition from new entrants in the sector. Network sales increased by 5.9%. Industry sales growth was constrained by drug product withdrawals, a leaner pipeline of new molecules and the genericization of several leading brand-name drugs.

On a same-store basis, network sales were up 5.5%, pharmacy sales increased 8.0%, and front-end sales improved by 2.1%. We consider total sales per square foot to be a better indicator of our performance, given that same-stores sales exclude new stores that have been open for less than a year. Our total sales per square foot have increased in every quarter over the last two years and were over $1,246 in the fourth quarter of fiscal 2005, among the best in retail in the country. The average PJC drugstore is a leader with annual sales of close to $C 9.6 million.

Management attributes this strong performance primarily to the Company's leading market position, its strategically located stores, good customer service, strong advertising and promotion campaigns, and other strategic initiatives.



Strategic Initiatives

Private Label Program – We are continuously improving our private label program (*Personnelle*) with new products and other measures. This program has been shown to enhance margins and increase customer loyalty through its excellent value proposition and many unique products.

Imported Goods Program – During the year, we began an import program to buy an increasing amount of our seasonal merchandise and other items directly from overseas manufacturers, thereby enhancing network profitability.

Customer-focused Photo Solutions – The PJC network is a leader in pharmacy photo departments in its market. During the year, we rolled out updated digital photo outlets across the network. We now offer our customers a total of four competitive solutions for their processing needs, including analog processing, in-store digital kiosk processing and digital overnight, in addition to Web uploads with subsequent drugstore pick-up.

New Distribution Center – Construction of a new distribution center in Ontario began in fiscal 2005. This will allow us to improve network logistics by distributing cosmetics and imported goods from our own warehouse.

Network Expansion and Upgrading – In fiscal 2005, we continued to expand our network through the opening of 2 new stores, the relocation of 5 additional stores, along with 22 store renovations and expansions. Store improvements and enhancements such as these, combined with increased focus on pharmacy and front-end, have been important factors in increasing our retail sales per square foot.

Loyalty Program – Our AIR MILES[tm] program is a pharmacy exclusive in Québec and New Brunswick. This loyalty program has increased the frequency of participating Jean Coutu customers and augmented their average spending by 57%.

Brand Awareness – A highly successful television advertising campaign was launched in September 2004 with a series of four commercials, resulting in increased consumer awareness of the PJC banner.

New Initiatives in 2006

Retail is a people business, so we are inaugurating a network employee development program to attract, train and retain our best.

On the product side, we have updated the branding and packaging of our *Personnelle* private label products and will be re-launching the line with its new look during the year.

In our cosmetics department, we were the first pharmacy in Canada to offer MAKE UP FOR EVER. In fiscal 2006, we plan to increase the sales of these high-demand products and line exclusives. In addition, we will be rolling out improved and evolved Dermo cosmetics displays to over 100 of our drugstores, while expanding the network of Boutiques Passion-Beauté by 15 stores.

We also plan to step up expansion of our network by opening 7 new stores and relocating 15 others, along with numerous renovations and prototype expansions. In fact, we recently launched a new store prototype with selling square footage of about 11,000 square feet.

Another important initiative in fiscal 2006 will be the launch of innovative AIR MILES[tm] programs, which we expect will further enhance sales growth.

Finally, we plan to further enhance brand awareness and increase network sales with a follow-up to our successful television advertising campaign.

Market Outlook

We are looking forward to continued growth from our Canadian operations in fiscal 2006, based on our strong momentum in script counts, combined with solid front-end performance.

Also boding well for our future is the continued projected growth in the industry. According to IMS Health, the total market in Canada is expected to grow at a compound annual rate of 8.9% between 2004 and 2009.

Review of Operations | UNITED STATES

Market Position

On July 31, 2004, the Jean Coutu Group acquired the Eastern US stores of Eckerd Pharmacy. This acquisition represented a unique opportunity to buy a drugstore network with strong brand equity and a leading market share.

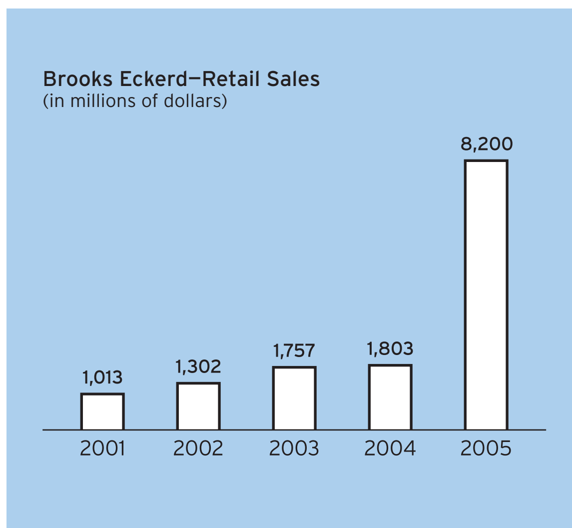
Our US network now extends across the Eastern United States under two banners: Brooks Pharmacy and Eckerd Pharmacy. In over 60% of the markets in which we operate, we are the number one or number two retail drugstore. Overall, we are the fourth-largest drugstore chain in North America and the second-largest on the East Coast.

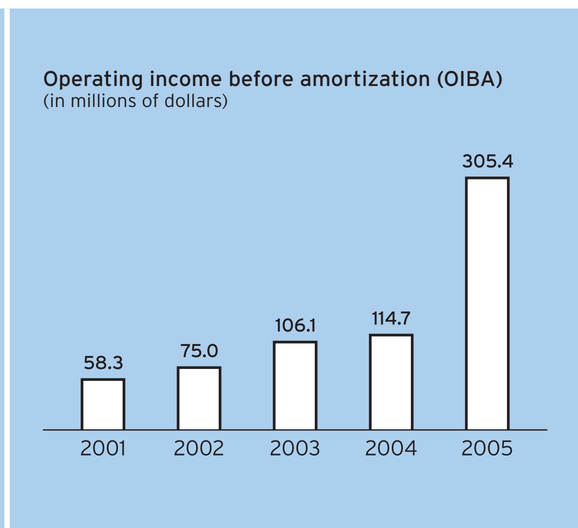
Our Brooks and Eckerd Pharmacies fill approximately 121.5 million prescriptions per year, with the average per store of approximately 1,300 scripts per week. The front-end of our stores has a health and beauty focus, including strong private label programs at Brooks Eckerd.

We began fiscal 2005 with 336 Brooks Pharmacies, adding 1,549 Eckerd drugstores during the first quarter. At year-end, our network had 1,922 stores located in 18 states.

2005 Performance

In fiscal 2005, our US network performance met expectations. Sales increased by 354.9%, primarily due to the Eckerd acquisition. In addition to our many strategic initiatives, our network also benefited from a strong flu season in fiscal 2005, while pharmacy sales growth was constrained by drug product withdrawals, a leaner pipeline of new molecules and the conversion of many brand-name drugs to a generic format in 2005.





On a same-store sales basis, excluding Eckerd, network sales were up 2.8%, while pharmacy sales increased 3.9% and front-end sales improved by 0.4%. Given that same-store sales exclude stores that have not been in operation, or part of the network, for more than a year, these figures will not include Eckerd stores until the first quarter of fiscal 2006.

We are pleased with our front-end performance. We transformed a sub-optimal component of our acquired Eckerd drugstores through the solid execution of our many initiatives.

Retail sales per square foot of the Brooks network were $636 per square foot in the fourth quarter of fiscal 2005. At this point, the average annual sales per store at Brooks is higher than at Eckerd, and simply bringing our Eckerd store to Brooks levels represents a substantial top line growth opportunity.

Brooks Eckerd Integration

Management immediately went to task to integrate the Eckerd operations with our existing network. One of the first steps was to consolidate head office functions. This involved a multi-step migration of systems, the transfer of know-how and some employees from Eckerd's head office in Florida to a combined Brooks Eckerd headquarters in Rhode Island. The final phase of this consolidation was completed in July 2005.

To streamline responsibility and accountability, we reorganized the reporting structure of our expanded network into four regions of approximately 475 stores each. A Group Vice-President was appointed to lead each of these operational regions. Each leader has many years of experience in the pharmacy and retail sectors. In addition, we de-layered the field office reporting structure and closed a distribution warehouse in Pennsylvania in order to optimize reporting, accountability and logistics, and contain expenses.

We also implemented numerous strategic initiatives to transform the Eckerd stores and drive profitable sales growth in the combined network. The roll out of these network initiatives will continue in fiscal 2006.

2005 Strategic Initiatives

"Pharmacy First" – One of the first operational changes we made at Eckerd was to instill our strong emphasis on pharmacy. This involved initiatives such as implementing our 15-minute expectation for prescription fills, improving our in-stock positions of high-demand prescription drugs, enhancing the workflow, and allocating store staff better. We also extended pharmacy hours in response to local customer demand. While we are satisfied with the progress being made in this area, Eckerd continues to have a lower average script count per store than Brooks, indicating opportunity for further improvement.

Sharper Customer Focus – To ensure a stronger customer focus at the Eckerd stores, we stabilized staffing, reallocated payroll dollars to better serve customer needs, improved store shopability by lowering shelf heights, made significant changes to the merchandising of seasonal goods, improved in-stock positions of every-day and promotional items, and expanded store hours. Early results on key elements such as seasonal merchandise sales are highly positive with sell-through improving each consecutive season.

Targeted Promotions – Once our 15-minute prescription expectation was in place in the Eckerd stores, along with other improvements, we launched a promotional campaign in an effort to invite new and former customers to have their prescriptions filled at our Brooks Eckerd drugstores. The campaign was well received, gaining tens of thousands of new Brooks Eckerd customers across many markets.

Broadcast Advertising – Broadcast advertising campaigns were launched to re-ignite the strong consumer recognition of the Brooks and Eckerd banners. The Eckerd campaign emphasized its more than 100-year heritage as well as its renewed focus on pharmacy, service, and customer care.

Innovation in the Front-End – We believe that the convenient locations and modern store base at Eckerd hold the potential for us to also increase front-end sales. To this end, we have improved Eckerd's inventory management and product categories, focusing on health and beauty and private label items. In addition, we introduced a variety of convenience items such as public photocopy and fax services, thereby enhancing front-end sales.

Private Label Initiatives – Private label products help promote customer loyalty and in general offer us higher margins. When we acquired Eckerd, its private label products 2,000 SKUs accounted for just over 7% of its front-end sales compared to about 10% for Brooks 1,200 SKUs at that time. By making Eckerd products a better value proposition, we have already seen a large increase in unit sales. Further initiatives were undertaken to enhance private label sales at Brooks Eckerd Pharmacy. The result is that, by the end of our fiscal year, we had increased Eckerd private label sales to almost 9% of front-end sales.

Supply Chain – In February 2005, we closed a distribution warehouse in Pennsylvania. In March, we renewed and expanded our five-year pharmaceutical supply agreement with McKesson Corporation, a North American leader in its field. McKesson has become the primary supplier to over 1,900 Brooks and Eckerd drugstores. We were also able to rationalize and optimize other elements of the supply chain due to our significantly increased market position.

Loss Prevention – The level of inventory shrinkage was significantly higher at Eckerd than at the Brooks network. People and processes were thus rapidly put in place to deal with this issue. We are pleased with the results to date and it is clear that our efforts should positively impact our gross margin going forward.

Store Openings and Renovations – In fiscal 2005 we continued to expand our US network with the opening of 117 new stores, 54 of which were relocations. In addition, we closed 28 stores during the year.

Store Closures – After almost a full year of operation and during the fourth quarter of fiscal 2005, the Company undertook an in-depth review of its store network on a store-by-store basis with the goal of strengthening its overall network. The result was that the Company elected to proceed with the closing of 78 Eckerd locations. These closings took place in the course of the first quarter of fiscal 2006. In most cases, prescription files were transferred to the nearest Eckerd store, along with as many pharmacy and store employees as possible.

Head Office Expansion – Our head office facilities in Rhode Island were expanded in fiscal 2005 to accommodate a combined Brooks Eckerd headquarters with about 800 employees.

New Initiatives in 2006

One of the broadest initiatives in fiscal 2006 will be the roll out of our industry-leading Rx Care system into the Eckerd network. This is expected to further improve customer care and the efficiency of its pharmacies. The Pharmacy-IT system has been developed and enhanced by us over many years, and pharmacists and customers consider it to be best-in-class.

We will also step up our initiative to have at least one 24-hour store in each strategic market by the summer of 2005. Last year, we converted 14 of our stores to 24-hour operations to bring us to a total of 34 24-hour stores at year-end. This rational 24-hour store opening strategy has proven to be a profitable way to increase our sales while containing expenses.

In addition, we will continue to grow our business through store openings and renovations. In fiscal 2006, we plan to open about 23 stores and relocate another 34 across the many states in our network.

We will also continue to optimize network supply chain and logistics in fiscal 2006.

Outlook

Over the past year, we have implemented a multitude of initiatives in the pharmacy and front-end of our stores to grow sales profitably. These initiatives are based on our tried-and-proven drugstore practices and they are already beginning to show positive results. In fact, Eckerd script count trends have reversed from negative to positive recently. Front end trends have improved in core categories, with a slight decline in overall front-end sales year-over-year.

We believe there is significant opportunity to increase network sales, considering that the average annual sales per store at Brooks is higher than that at over 1,500 Eckerd stores. There is also considerable room for us to benefit from higher operating leverage following completion of the head office consolidation in the first quarter of fiscal 2006, as well as from other initiatives.

Adding to this favorable outlook from an operational standpoint is the projected industry growth. According to IMS Health, total market sales are expected to grow at a compound annual rate of 8.2% between 2004 and 2009. Contributing to this growth will be the introduction of Medicare Part D Drug Benefit coverage, for which over 40 million Americans will be eligible as of January 2006. We are preparing for this opportunity, which will allow us to further enhance our customer relationships by helping them understand and take advantage of this new benefit.

While industry growth prospects are positive, there are still a number of uncertainties. One of these is the growth of mandatory mail-order prescription plans. As a Company focused on pharmacy and professionalism, we oppose a system without patient choice. In our view, patients should be given a choice and we have demonstrated that we can compete on price with the added benefit of our professional service, the most important part of which is the pharmacist-patient interface.

We are also well equipped to keep pace with the evolving landscape of private plans. We have thousands of plans in our North American pharmacy system and we are constantly adjusting formularies, pricing, and individual redemption rates for our patients.

Community Involvement

As part of our commitment to the communities we serve and the advancement of pharmacy, the Jean Coutu Group provides consistent support to hundreds of organizations in Canada and the United States, with a special emphasis on promoting health and education.

In fiscal 2005, the Group donated over $1 million in support of several pharmacy schools, hospitals, clinical research institutes and other worthwhile causes. Some notable examples include Brooks' support of the Rhode Island United Way Community Schools Program through a series of after-school programs in higher risk neighborhoods, helping stabilize youth and families. In addition, for Boston Celtics' home games, the Company donates up to 1,500 $10 tickets in the Brooks Family Section. Eckerd supported the Salvation Army Project Bundle-Up and St. Joseph House of Hospitality in Pittsburgh, Pennsylvania, through a $150,000 sponsorship commitment to the Eckerd Celebration of Lights. We also supported important youth initiatives such as a $200,000 sponsorship of the Eckerd Drug Quiz Show in Syracuse, New York. This show provides middle-school kids with the opportunity to have fun while gaining the knowledge, skills and self-confidence needed to make safe, healthy, real-life choices regarding the use of tobacco, alcohol and drugs.

Our in-store fundraising activities at PJC drugstores collected close to $400,000 during fiscal 2005 in support of three worthy causes: Oxfam's Tsunami Relief Fund, the Oxfam Haiti Relief Fund, and La Grande Guignolée, a Christmas basket fund. Our Brooks Eckerd network participated in similar fundraising activities, collecting over $1,000,000 for several causes, including the Genesis Fund of New England, the Children's Miracle Network and the Tsunami Disaster Relief Fund.

Our employees also give generously to their communities. At the Jean Coutu Group, we encourage our employees to give of their own time to a wide range of community causes, besides dedicating precious time to their family and friends. Through employee and Company donations, along with Company-sponsored activities, we collected over $400,000 for local Centraide and United Way campaigns in Canada and the United States.

In addition, the Marcelle and Jean Coutu Foundation supports many important organizations, including the *Université de Montréal* for the construction of new schools of pharmacy and immunology, Centraide of Greater Montréal, and *Hôpital Sainte-Justine*, a Montréal children's hospital to which the Foundation has committed to donate a total of $5 million over a five-year period. The Foundation also provides financial support to over 350 community organizations in Québec as well as supporting initiatives in several underdeveloped countries to help the fight against poverty and enhance the wellness and education of members of society.

THE SUCCESS OF THE JEAN COUTU GROUP HELPS BUILD STRONGER COMMUNITIES. IT'S ALL ABOUT PEOPLE.

Financial Information

Management's Discussion and Analysis

The discussion that follows provides an analysis of the consolidated operating results and financial position (Management's Discussion and Analysis – "MD&A") of The Jean Coutu Group (PJC) Inc. ("the Company" or the "Jean Coutu Group") for the 52-week year ended May 28, 2005.

On July 31, 2004, the Jean Coutu Group acquired 1,549 outlets of the Eckerd drugstore chain located throughout 13 states in Northeastern, mid-Atlantic and Southeastern United States, becoming the fourth largest drugstore chain in North America and the second largest in Eastern United States and Canada with a network of 2,243 stores.

Management has presented certain non Generally Accepted Accounting Principles ("GAAP") measures in this MD&A. Although operating income before amortization ("OIBA") and earnings before unrealized losses on financing activities are not performance measures defined by Canadian GAAP, management, investors and analysts use these measures to evaluate the operating and financial performance of the Company. Moreover, the Company's definition of these measures may differ from the one used by other companies. The OIBA measure is reconciled with net earnings, a performance measure defined by Canadian GAAP, in this MD&A.

Presentation of financial statements

On August 20, 2004, the Board of Directors modified the Company's reporting periods in order to conform to the National Retail Federation's 4-5-4 merchandising calendar. Effective this fiscal year, the Company is disclosing its financial results on the basis of four even quarters ending on the Saturday of the thirteenth week, respectively ending on August 28, 2004, November 27, 2004, February 26, 2005 and May 28, 2005 for the current year.

All financial information appears in US dollars, in accordance with Canadian GAAP, considering our now predominant operations in the United States and our US dollar denominated debt. The following discussion should be read in conjunction with the Consolidated Financial Statements and related notes as at May 28, 2005 as well as the Company's recent public filings.

Readers may access additional information and filings relating to the Company using the following links to the www.sedar.com (Canada) and www.sec.gov (United States) Websites.

Forward-looking statements

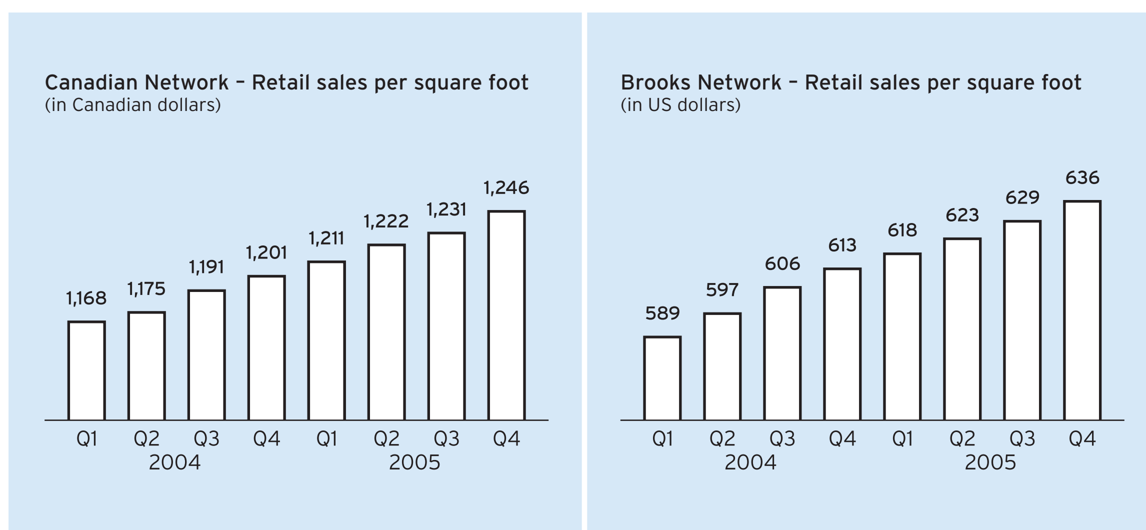
Certain statements contained in this Annual Report release may constitute "forward-looking statements" within the meaning of the US *Private Securities Litigation Reform Act* of 1995. Such forward-looking statements involve a number of known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of the Company to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. The words "looking forward," "looking ahead," "believe(s)," "should," "may," "expect(s)," "anticipate(s)," "likely," "opportunity," and similar expressions, among others, identify forward-looking statements. Such statements are not guarantees of the future performance of the Company or its segments and involve known and unknown risks and uncertainties that may cause the outlook, the actual results or performance of the Company or of its reportable segments to be materially different from any future results or performance expressed or implied by such statements. Readers are referred to the section on Risks and uncertainties contained in this MD&A section of the Annual Report as well as in other Company filings. The Company disclaims any intention or obligation to update or revise any forward-looking information contained in its communications, whether as a result of new information, future events or otherwise.

Company Profile

We exercise our activities in the North American drugstore retailing industry in two broad geographic areas, Eastern Canada and the Eastern United States, through corporate and franchised drugstores (under the banners of Brooks, Eckerd, PJC Jean Coutu, PJC Santé Beauté and PJC Clinique).

As at May 28, 2005, our Canadian network of PJC Jean Coutu franchised stores ("PJC") and American network of Brooks Eckerd drugstores was broken down as follows geographically and by type of store:

	Canada	United States	Total
Total stores	321	1,922	2,243
Freestanding stores or buildings	81	1,006	1,087
24-hour stores	—	34	34
Drive-thru pharmacies	21	870	891



Retail sales per square foot is a key performance indicator. By measuring last twelve-month total store sales divided by average square footage, the Company's management measures network performance.

In Canada, network retail sales per square foot has grown each quarter over the last two years, to $C 1,246 per square foot for the fourth quarter, which is top in our market. The average PJC drugstore is a leader with annual sales of $C 9.6 million.

In the United States, the Brooks network retail sales per square foot grew to $636 in the fourth quarter. At this point, the average annual sales per store at Brooks is higher than at Eckerd, and simply bringing our Eckerd stores to Brooks levels represents a substantial top line growth opportunity.

Canada. In Canada, franchising activities include operating a distribution center and providing services to our PJC stores. These services comprise centralised purchasing, distribution, marketing, training, human resources, management, operational consulting and information systems, as well as participation in our private label program. Our PJC franchisees own and manage their stores and are responsible for merchandising and financing their inventory. They must provision their stores from our distribution center provided that the products requested are available and priced lower than other suppliers. We supply our PJC franchisees with

approximately 72% of their products, including almost all prescription drugs. Although PJC retail sales are not included in our revenues, an increase or decrease in this regard will directly affect our performance as it impacts distribution center sales and royalties.

United States. In the US, we operate a network of 1,922 corporate stores under the Brooks and Eckerd banners, and 6 distribution centers in 18 states in the Eastern United States (336 Brooks drugstores and 1 distribution center in 6 states in 2004). The head office of The Jean Coutu Group (PJC) USA, Inc. is located in Warwick, Rhode Island, where all corporate and support functions are centralized for the Brooks and Eckerd drugstore network. These functions include finance, purchasing, distribution, marketing, human resources, information systems and support, real estate and other departments. Readers are referred to Note 20 of the Consolidated Financial Statements for a description of the Eckerd acquisition, which was completed on July 31, 2004.

At the end of fiscal 2005, the Company elected to proceed with the closing of 78 non performing Eckerd drugstores. A total of 73 stores have closed to date, with 45 transfers of script files to the nearest Eckerd store. For the remaining 33 stores, the Company has sold or plans to sell the script files and related inventories. The net addition to the provision for store closures and to the write-down of related assets, which are included in the purchase price equation at May 28, 2005 amounted to $100.5 million.

Strategies and Outlook

The Jean Coutu Group is well positioned to capitalize on the growth in the North American drugstore retailing industry, based on its strong brands, a focus on excellence in customer service in pharmacy and front-end innovation with an emphasis on health and beauty. Demographic trends in Canada and the United States are expected to contribute to growth in the consumption of prescription drugs, and to the increased use of pharmaceuticals as the primary intervention in individual healthcare. Management believes that these trends will continue and that the Company will achieve sales growth through quality of offering and service levels in its drugstore network.

The Company operates its Canadian and US network with a focus on sales growth, network renovation, relocation and expansion projects and operating efficiency. The Company has substantially completed the Brooks Eckerd integration, which was focused on three principal areas:

– ***Reduction of support functions and other initiatives***
  Head and field office head count reductions are substantially complete, with net reductions of approximately 1,273 positions. As a result, accountability and productivity have been enhanced with the streamlining of operations. The Company will continue to move toward the right-sized support structure as it reduces dual infrastructures during the first quarter of fiscal 2006. The Company will continue to optimize logistics and supply chain efficiency over the next fiscal year.

– ***Operational improvements***
  The Company has recently right-sized its Eckerd network and will continue to open new stores in fiscal 2006, with a focus on growing network sales profitably. It has also implemented plans, processes and deployed people to reduce inventory shrink and expects to record early financial results from this initiative in fiscal 2006.

– ***Growth initiatives***
  Customer focused initiatives have been taken and will continue to be implemented to drive sales growth profitably. The goal is to differentiate the network through quality of offering and customer service levels.

The Brooks Eckerd drugstore network is making good progress. The Company has now begun to capture the integration cost savings while it continues to profitably grow the sales of its US drugstore network. At the same time it will continue to build on the strong base of its Canadian network.

Financial data

The following table presents selected data and operating results for the 52-week year ended May 28, 2005 and the year ended May 31, 2004.

(in thousands of US dollars, except per share amounts)	2005 Canada	2005 United States	2005 Consolidated	2004 Canada	2004 United States	2004 Consolidated
Sales	1,247,898	8,200,445	9,448,343	1,090,503	1,802,585	2,893,088
Cost of goods sold	1,129,999	6,159,873	7,289,872	985,432	1,358,566	2,343,998
Gross profit	117,899	2,040,572	2,158,471	105,071	444,019	549,090
As a % of sales	9.4%	24.9%	22.8%	9.6%	24.6%	19.0%
Other revenues[1]	161,786	10,779	172,565	148,291	4,625	152,916
General and operating expenses	132,343	1,745,953	1,878,296	118,366	333,918	452,284
Operating income before amortization	147,342	305,398	452,740	134,996	114,726	249,722
Amortization[1]	14,013	184,840	198,853	10,029	31,404	41,433
Operating income	133,329	120,558	253,887	124,967	83,322	208,289
Financial expenses			162,092			14,535
Earnings before income taxes			91,795			193,754
Income taxes (recovery)			(12,583)			61,071
Net earnings			104,378			132,683
Net earnings per share			0.41			0.58
Earnings per share before unrealized losses on financing activities			0.44			0.58

(1) Amortization of incentives paid to franchisees is grouped with other revenues in the GAAP financial statements.

(in thousands of US dollars, except for sales growth figures)	2005 $	2004 $
Network performance – Retail sales		
Canada[2]	2,173,428	1,939,637
United States	8,200,445	1,802,585
	10,373,873	3,742,222
Retail sales growth – same store[3]		
Canada[2]		
Total	5.5%	6.8%
Front-end	2.1%	2.3%
Pharmacy	8.0%	10.3%
United States[4]		
Total	2.8%	4.3%
Front-end	0.4%	2.1%
Pharmacy	3.9%	5.3%
Other operating data		
Total assets	5,694,926	1,343,754
Long-term debt (including current portion)	2,561,432	192,175
Reconciliation of OIBA with net earnings		
Net earnings	104,378	132,683
Interest on long-term debt	152,731	11,752
Unrealized foreign exchange loss on monetary items	7,767	—
Other financing expenses, net	1,594	2,783
Income taxes (recovery)	(12,583)	61,071
Operating income	253,887	208,289
Amortization per GAAP financial statements	195,308	38,396
Amortization of incentives[1]	3,545	3,037
Operating income before amortization	452,740	249,722

(1) Amortization of incentives paid to franchisees is grouped with other revenues in the GAAP financial statements.
(2) Franchised outlets' retail sales are not included in the Company's consolidated financial statements.
(3) Growth is calculated in local currency and is based on comparable periods.
(4) This measure does not include same-store sales for the acquired Eckerd corporate outlets, which will be included in same-store sales beginning in August 2005.

Definition of financial data

Revenues

Revenues consist of Canadian and US sales plus other revenues derived from franchising and retail sales.

Canada. Merchandise sales by our distribution center to PJC franchisees account for most of our sales in Canada. PJC retail store sales are not included in our revenues. However, changes in their retail sales directly affect our revenues since PJC franchisees purchase most of their inventory from our distribution center. Other revenues consist of royalties from our franchisees based on a percentage of sales, rental revenues and charge-backs to our franchisees in exchange for certain services.

United States. US sales consist of retail sales generated by corporate stores operating under the Eckerd and Brooks banners. Other revenues include rental revenues from our properties leased to third parties.

Gross profit

Gross profit is calculated as follows: sales minus the cost of goods sold from our distribution center for our Canadian operations, and the cost of goods sold (which includes distribution costs and estimated inventory losses) in our stores for the US network.

General and operating expenses

General and operating expenses comprise costs associated with salaries and benefits, rent, advertising, repairs and maintenance, insurance and professional fees.

Operating income before amortization ("OIBA")

OIBA is not a measure of performance under Canadian GAAP; however management uses this performance measure in assessing the operating and financial performance of its reportable segments. Besides, we believe that OIBA is an additional measure used by investors to evaluate operating performance and capacity of a company to meet its financial obligations. However, OIBA is not and must not be used as an alternative to net earnings or cash flow generated by operating activities as defined by Canadian GAAP. OIBA is not necessarily an indication that cash flow will be sufficient to meet our financial obligations. Furthermore, our definition of OIBA may not be necessarily comparative to similar measures reported by other companies.

Exchange rate data

The Company's US dollar reporting currency provides shareholders with more relevant information considering the predominant operations in the United States and US dollar denominated debt. The following table shows exchange rates based on the Federal Reserve Bank of New York closing rate expressed as US dollars per Canadian dollar.

	May 28, 2005	May 31, 2004	May 31, 2003
Average rate[(1)]	0.7937	0.7446	0.6557
Closing rate	0.7946	0.7317	0.7293

(1) Calculated using the average noon buying rates for each day in the relevant period.

Selected Annual Financial Information

(in thousands of US dollars except for per share amounts)	52 weeks ended May 28, 2005 $	Year ended May 31, 2004 $	Year ended May 31, 2003 $
Revenues	9,617,363	3,042,967	2,646,669
OIBA	452,740	249,722	207,475
Net earnings	104,378	132,683	104,784
Net earnings per share	0.41	0.58	0.46
Earnings per share before unrealized losses on financing activities	0.44	0.58	0.46
Cash dividend per share ($C)	0.12	0.12	0.12

Comparison of the 52-week year ended May 28, 2005 and the year ended May 31, 2004

Net earnings

For the 52-week year ended May 28, 2005, net earnings were $104.4 million ($0.41 per share) compared with net earnings of $132.7 million ($0.58 per share) for the year ended May 31, 2004. Earnings before unrealized losses on financing activities were $112.2 million ($0.44 per share) compared to $132.7 million ($0.58 per share) for the corresponding fiscal year. There was an unrealized foreign exchange loss on monetary items of $7.8 million ($0.03 per share) recorded during fiscal 2005. During the fiscal year, the Company reviewed its arrangements and documentation in order to ensure that all significant monetary items are properly hedged against future foreign exchange risk. The Company completed most aspects of the Brooks Eckerd integration during the current fiscal year, and had to bear the costs of operating several head office infrastructures during this period.

Revenues

Total revenues, which include sales and other income, rose $6.574 billion or 216.1% to $9.617 billion for the 52-week year ended May 28, 2005 compared with $3.043 billion for the year ended May 31, 2004.

Pharmacy sales are negatively impacted by the conversion of brand name drugs to generics, which generally have a lower selling price, but higher gross profits to the drugstore retailer. Over the past two fiscal years, the decrease in same-store pharmacy volume was partially due to the conversion of Claritin and Prilosec from prescription to over-the-counter status and continued health concerns over women's hormone replacement therapy drugs. The Company made very good progress with Eckerd during the year. Generics as a percentage of total Eckerd pharmacy sales increased from 49% at the time of purchase to 53% by year-end with the generic substitution rate increasing from 84% to 92%. Eckerd sales trends have improved significantly in both the pharmacy and front-end. Script count trends have reversed from negative in early fiscal 2005 to positive recently. Front-end trends have improved, with strong growth in core health and beauty categories and private label products, with a slight decline in overall front-end sales year-over-year.

Canada. Revenues from Canadian operations showed double digit growth during the year, reaching $1.406 billion, an increase of $170.4 million or 13.8% from revenues of $1.236 billion in fiscal 2004. Canadian revenues increased by 6.6%, excluding the impact of currency exchange rate fluctuations. During the 52-week year there were 7 openings including 5 relocations of PJC franchised stores compared with 13 openings, 4 relocations and 1 closure in fiscal 2004. In addition, 7 stores were significantly renovated and 6 were expanded during fiscal 2005. Sales increases reflect growth resulting from previous period openings, renovations or moves of network stores and growth in PJC same store retail sales. For the 52-week year ended May 28, 2005 compared with the year ended May 31, 2004, on a same-store basis and in local currency, total PJC retail sales advanced 5.5%, pharmacy sales gained 8.0% and front-end sales picked up 2.1% year-over-year.

United States. Revenues from US operations increased substantially to $8.211 billion for the 52-week year ended May 28, 2005, up $6.404 billion or 354.4% from revenues of $1.807 billion in fiscal 2004. The increase is principally due to the additional revenue from the acquired Eckerd drugstores as of July 31, 2004. Third party health plans covered approximately 95% of pharmacy sales in fiscal 2005 and 2004. In the front-end, we continued our shift towards health and beauty and confectionery categories with a positive effect on gross margin, while we saw a decline in overall photography department sales due to the shift to digital photography. On a same-store basis, total retail sales advanced 2.8%, pharmacy sales gained 3.9% and front-end sales increased 0.4% year-over-year. This measure does not include same-store sales for the acquired Eckerd drugstores, which will be included in same-store sales beginning in the first quarter of fiscal 2006, after one year of ownership by the Company. During fiscal 2005, in addition to the acquisition of 1,551 drugstores, there were 117 new store openings including 54 relocations and 28 store closures, bringing our US network to 1,922 Brooks and Eckerd stores at May 28, 2005. During fiscal 2004, there were 4 net openings of Brooks drugstores and our US network had 336 Brooks drugstores at May 31, 2004.

Gross profit

Canada. Total Canadian gross profit improved to $117.9 million for the 52-week year ended May 28, 2005 compared with $105.1 million for the previous fiscal year. Gross margin decreased slightly to 9.4% in fiscal 2005 compared with 9.6% for the corresponding fiscal year.

United States. United States gross profit amounted to $2.041 billion for the 52-week year ended May 28, 2005 compared with $444.0 million for the corresponding fiscal year. The increase is attributable to the addition of the Eckerd business during our current fiscal year. The gross margin percentage of our US operations improved to 24.9% during the current fiscal year compared with 24.6% in fiscal 2004. The improvement is due to management's focus on optimal merchandising, mix and pricing in the front-end. In addition, since pharmacy sales have lower gross profit than front-end sales, as the acquired Eckerd stores increase their front-end sales, this has a positive effect on gross profit. Also, our gross profit benefited from reduced inventory losses as a result of loss prevention programs implemented across the US network. The Company's management believes that these programs will provide operational benefits and expects future financial improvement in fiscal 2006.

Other revenues

Other revenues, which are included in total revenue in the Company's GAAP financial statements, increased to $169.0 million in fiscal 2005 from $149.9 million the previous year due principally to increased franchise fees, rental and other income.

General and operating expenses

General and operating expenses for the 52-week year ended May 28, 2005 were $1.878 billion, up from $452.3 million from previous fiscal year. This increase is essentially attributable to the US operations and operation of the acquired Eckerd drugstores. General and operating expenses performance represented 9.4% of revenues in Canada in fiscal 2005 versus 9.6% in fiscal 2004 and 21.3% versus 18.5% of revenues a year earlier in the US. The Company incurred certain non-recurring acquisition and integration expenses during the 2005 fiscal year. Also, since the acquired Eckerd drugstores had lower average sales per store than the then existing US network, general and operating expenses increased during the current fiscal year while we integrated and optimized headquarter and field staff and structure. In addition, the networks are undertaking several store openings and other measures, which increase general and operating expenses while store sales are being built.

OIBA

OIBA increased during fiscal 2005, advancing 81.3% to $452.7 million from $249.7 million in the corresponding 2004 fiscal year. OIBA as a percentage of revenues ended the year at 4.7% compared with 8.2% for the previous fiscal year. The decrease in OIBA margin for the 52-week year ended May 28, 2005 was affected by lower margins in the acquired Eckerd drugstores along with network integration and enhancement efforts during the fiscal year. This was partially offset by the continuing strong performance of existing Canadian operations.

Amortization

Amortization charges increased to $195.3 million during fiscal 2005, up $156.9 million from fiscal 2004, from $38.4 million. The increase in the charges during fiscal 2005 is reflective of the Eckerd drugstore acquisition.

Financial expenses

Financial expenses were $162.1 million during fiscal 2005 (including the $7.8 million unrealized foreign exchange loss on monetary items), an increase of $147.6 million over the year-earlier amount of $14.5 million. During the year, average long-term debt (including current portion of long-term debt) increased from $202.6 million for fiscal 2004 to $2.181 billion for fiscal 2005. The weighted average interest rate on the Company's long term debt was 6.3% during the current fiscal year compared with 4.3% for fiscal 2004. The additional credit facilities and issuance of notes were used to provide the funds required for the Eckerd drugstore acquisition. During the year, there was a $7.8 million unrealized foreign exchange loss on monetary items related to the Eckerd acquisition, reflecting the loss until the Company reviewed its arrangements and documentation in order to ensure that all significant monetary items were properly hedged against future foreign exchange risk.

Income taxes

There was an income tax recovery of $12.6 million in fiscal 2005 compared with an expense of $61.1 million for fiscal 2004. The low effective tax rate of the current fiscal year is a result of the financing structure established as part of the Eckerd acquisition.

Comparison of the years ended May 31, 2004 and May 31, 2003

Net earnings

For the year ended May 31, 2004, net earnings were $132.7 million ($0.58 per share) compared with net earnings of $104.8 million ($0.46 per share) for the year ended May 31, 2003.

Revenues

Total revenues, which include sales and other income, increased by $396.3 million, or 15.0%, to $3.043 billion for the year ended May 31, 2004 from $2.647 billion for the year ended May 31, 2003.

Canada. Canadian revenues increased by $350.9 million, or 39.7%, to $1.236 billion for the year ended May 31, 2004 from $884.9 million for the year ended May 31, 2003. Canadian revenues increased by 23.2% excluding the impact of currency exchange rate fluctuations. The strong growth reflects the fact that there was no work stoppage in the 2004 fiscal year while there was a 58-day labor strike at our Canadian warehouse and distribution center during fiscal 2003. Canadian revenues were also impacted during the period by 8 net openings of PJC franchised stores and the renovation or relocation of 17 existing stores, as well as internal sales growth in PJC sales. For the year ended May 31, 2004, on a comparable store basis and in local currency, total PJC retail sales increased by 6.8%, pharmacy sales increased 10.3% and front-end sales increased 2.3%, each as compared to the year ended May 31, 2003 figures.

United States. United States revenues increased by $45.4 million, or 2.6%, to $1.807 billion for the year ended May 31, 2004 from $1.762 billion for the year ended May 31, 2003. In our US stores, total sales increased by 2.6%, pharmacy sales increased by 3.4% and front-end sales increased by 0.8% during fiscal 2004 as compared with fiscal 2003. This slight increase resulted from a 53-week period for fiscal 2003 for our US operations compared with a 52-week period in fiscal 2004. In addition, sales were impacted by an early and harsh winter season in December 2003. On a comparable store and comparable week basis, total sales increased by 4.3%, pharmacy sales increased by 5.3% and front-end sales increased by 2.1% for the year ended May 31, 2004 as compared to fiscal 2003.

Gross profit

Total gross profit increased by $43.2 million, or 8.6%, to $549.1 million for the year ended May 31, 2004 from $505.9 million for the year ended May 31, 2003.

Canada. Canadian gross profit increased by $30.3 million, or 40.5%, to $105.1 million for the year ended May 31, 2004 from $74.8 million for the year ended May 31, 2003. This strong growth reflects sales growth in our PJC franchised stores during fiscal 2004 and the fact that there was no work stoppage in fiscal 2004 while there was a 58-day strike at our Canadian warehouse and distribution center in fiscal 2003. Our Canadian gross margin percentage deteriorated slightly to 9.6% for the year ended May 31, 2004 from 9.8% for the year ended May 31, 2003.

United States. United States gross profit increased by $12.9 million, or 3.0%, to $444.0 million for the year ended May 31, 2004 from $431.1 million for the year ended May 31, 2003. Even though there was a regular 52-week period in fiscal 2004, there was an increase in total gross profit as compared to the figures for the 53-week period in fiscal 2003. Our US gross margin percentage increased slightly for the year ended May 31, 2004 to 24.6% compared with 24.5% in the year ended May 31, 2003.

General and operating expenses

General and operating expenses increased by $28.1 million, or 6.6%, to $452.3 million for the year ended May 31, 2004 from $424.2 million for the year ended May 31, 2003. General and operating expenses as a percentage of total revenues decreased to 14.9% for the year ended May 31, 2004 from 16.0% for fiscal 2003. General and operating expenses improved in Canada, representing 9.6% of revenues versus 10.7% in fiscal 2003. This decrease is primarily the result of reduced labor costs resulting from the impact of a 58-day labor strike at our Canadian warehouse and distribution center in fiscal 2003. General and operating expenses decreased slightly in the US (18.5% of revenues versus 18.7% in 2003).

OIBA

OIBA increased during fiscal 2004, advancing 20.4% to $249.7 million from $207.5 million in the corresponding 2003 fiscal year. OIBA as a percentage of revenues was 8.2% in fiscal 2004 compared with 7.8% for the previous fiscal year.

Amortization

Amortization charges increased by $2.7 million, or 7.5%, to $38.4 million for the year ended May 31, 2004 from $35.7 million for the year ended May 31, 2003.

Financial expenses

Financial expenses decreased by $3.4 million to $14.5 million for the year ended May 31, 2004 from $17.9 million for the year ended May 31, 2003. This decrease was a result of the use of short term bank loans in fiscal 2003 with respect to our Canadian operations to fund the temporary deferral of sales tax credits from October 2002 to May 2003.

Income taxes

Income tax expense increased by $15.0 million to $61.1 million for the year ended May 31, 2004 from $46.1 million for the year ended May 31, 2003. Our effective tax rate increased to 31.5% for the year ended May 31, 2004 from 30.6% for the year ended May 31, 2003.

Fourth quarter ended May 28, 2005 compared with the fourth quarter ended May 31, 2004

Selected Unaudited Quarterly Financial Information

(in thousands of US dollars, except per share amounts)	52 weeks ended May 28, 2005 $	Q4 2005 $	Q3 2005 $	Q2 2005 $	Q1 2005 $
Sales	9,448,343	2,725,566	2,771,230	2,653,312	1,298,235
Cost of goods sold	7,289,872	2,078,107	2,129,709	2,053,990	1,028,066
Gross profit	2,158,471	647,459	641,521	599,322	270,169
As a % of sales	22.8%	23.8%	23.1%	22.6%	20.8%
Other revenues[1]	172,565	43,751	45,091	44,469	39,254
General and operating expenses	1,878,296	542,822	561,247	526,731	247,496
Operating income before amortization	452,740	148,388	125,365	117,060	61,927
Amortization[1]	198,853	57,909	58,332	56,494	26,118
Operating income	253,887	90,479	67,033	60,566	35,809
Financial expenses	162,092	47,494	32,845	64,045	17,708
Earnings before income taxes	91,795	42,985	34,188	(3,479)	18,101
Income taxes (recovery)	(12,583)	(3,231)	(5,666)	515	(4,201)
Net earnings	104,378	46,216	39,854	(3,994)	22,302
Net earnings per share	0.41	0.18	0.15	(0.02)	0.09
Earnings per share before unrealized losses on financing activities	0.44	0.18	0.10	0.06	0.09

[1] Amortization of incentives paid to franchisees is grouped with amortization instead of other revenues as in the GAAP financial statements.

Selected Unaudited Quarterly Financial Information (continued)

(in thousands of US dollars, except per share amounts)	Year ended May 31, 2004 $	Q4 2004 $	Q3 2004 $	Q2 2004 $	Q1 2004 $
Sales	2,893,088	744,932	747,103	721,257	679,796
Cost of goods sold	2,343,998	603,334	604,001	587,032	549,631
Gross profit	549,090	141,598	143,102	134,225	130,165
As a % of sales	19.0%	19.0%	19.2%	18.6%	19.1%
Other revenues[1]	152,916	36,792	40,067	37,198	38,859
General and operating expenses	452,284	116,100	116,488	110,744	108,952
Operating income before amortization	249,722	62,290	66,681	60,679	60,072
Amortization[1]	41,433	10,941	10,462	10,143	9,887
Operating income	208,289	51,349	56,219	50,536	50,185
Financial expenses	14,535	3,351	3,755	3,322	4,107
Earnings before income taxes	193,754	47,998	52,464	47,214	46,078
Income taxes	61,071	15,394	16,429	14,708	14,540
Net earnings	132,683	32,604	36,035	32,506	31,538
Net earnings per share	0.58	0.14	0.16	0.14	0.14
Earnings per share before unrealized losses on financing activities	0.58	0.14	0.16	0.14	0.14

(1) Amortization of incentives paid to franchisees is grouped with amortization instead of other revenues as in the GAAP financial statements.

Net earnings

For the 13 weeks and fourth quarter ended May 28, 2005, net earnings were $46.2 million ($0.18 per share) compared with net earnings of $32.6 million ($0.14 per share) for the fourth quarter of the previous fiscal year. For the fourth quarter and in fiscal 2005, the Company had to bear the costs of operating dual head office infrastructures in the United States. The Company has substantially completed the Brooks Eckerd information technology integration during the first quarter of fiscal 2006.

Revenues

Total revenues, including sales and other income, rose $1.987 billion or 254.4% to $2.768 billion for the 13-week period ended May 28, 2005 compared with $781.1 million for the corresponding period in fiscal 2004.

Canada. Revenues from Canadian operations showed significant growth, reaching $368.5 million, an increase of $43.7 million or 13.5%. Canadian revenues increased by 3.7% excluding the impact of currency exchange rate fluctuations. During the 13-week period there were no openings of PJC franchised stores, but sales increases reflect growth resulting from previous period openings, renovations or relocations of network stores and growth in PJC same store retail sales. For the fourth quarter ended May 28, 2005, on a same-store basis and in local currency, total PJC retail sales advanced 4.3%, pharmacy sales gained 5.5% and front-end sales picked up 2.6% year-over-year.

United States. Revenues from US operations increased substantially to $2.400 billion for the 13-week period ended May 28, 2005, up $1.944 billion or 425.9% from last year. The increase is principally due to the additional revenue from the acquired Eckerd drugstores for the fourth quarter of fiscal 2005. On a same-store basis, total retail sales advanced 3.1%; pharmacy sales gained 3.8% and front-end sales increased 1.6% year-over-year. This measure does not include same-store sales for the acquired Eckerd drugstores, which will be included in same-store sales beginning in the first quarter of fiscal 2006, after one year of ownership by the Company. During the fourth quarter of fiscal 2005, there were 40 new store openings including 14 relocations, 2 acquisitions and 16 store closures.

Gross profit

Canada. Gross profit from Canadian operations was $31.9 million for the fourth quarter compared to $28.4 million for the corresponding period the previous year. Gross margin decreased to 9.7% for the 13-week period ended May 28, 2005 compared with 9.9% for the corresponding period in fiscal 2004.

United States. Gross profit from US operations amounted to $615.5 million for the 13-week period ended May 28, 2005 compared with $113.2 million for the corresponding period the previous year. The increase is attributable to the addition of the Eckerd business during the quarter.

Other revenues

Other revenues, which are included in total revenue in the GAAP financials, increased to $42.9 million in the fourth quarter of fiscal 2005 from $36.2 million for the same period the previous year. This is due to additional franchise fee and rental income in Canada and other income in both Canada and the United States during the current quarter.

General and operating expenses

General and operating expenses for the 13-week period ended May 28, 2005 were $542.8 million, up from $116.1 million from the same period in fiscal 2004. This increase is essentially attributable to the US operations and the acquired Eckerd drugstores. General and operating expenses performance was mixed, representing 8.8% of revenues in Canada versus 10.0% last year and 21.3% versus 18.3% a year earlier in the US. The Company incurred certain non-recurring acquisition and integration expenses at Brooks Eckerd during fiscal 2005. In addition, the networks are undertaking several store openings and other measures, which increase general and operating expenses while store sales are being built.

OIBA

OIBA increased in the fourth quarter of fiscal 2005, advancing 138.2% to $148.4 million from $62.3 million in the corresponding fiscal 2004 period. OIBA as a percentage of revenues ended the quarter at 5.4% compared with 8.0% for the same period in 2004. The decrease in OIBA margin for the 13-week period ended May 28, 2005 was affected by the lower margin in the acquired Eckerd drugstores along with network integration and enhancement efforts. This was partially offset by the performance of existing Canadian operations.

Fourth quarter results were positively impacted by changes in estimates for some Eckerd network operating expenses and revenues on the basis of new information obtained in the quarter. These items are related to the estimate of workers' compensation and general liability expense, the accrual for vendors allowances and finally a distribution center inventory adjustment. Of these favorable changes in estimates, approximately $12 million impacted the cost of goods sold and $9 million the general and operating expenses. These changes in estimates were accounted for on a prospective basis.

Amortization

Amortization charges increased to $57.0 million during the fourth quarter of fiscal 2005, up $46.7 million from the corresponding period in 2004. The increase in the charges for both periods is due to the amortization of assets related to the acquired Eckerd drugstores.

Financial expenses

Financial expenses were $47.5 million during the fourth quarter of fiscal 2005, an increase of $44.1 million over the year-earlier period. During the quarter, average long-term debt (including current portion of long-term debt) increased from $192.2 million during the fourth quarter of fiscal 2004 to $2.564 billion for the fourth quarter of the current fiscal year. The weighted average interest rate on the Company's long term debt was 6.6% during the fourth quarter of the current fiscal year compared with 4.3% for the corresponding period of fiscal 2004. The additional credit facilities and issuance of notes were used to provide the funds required for the Eckerd drugstore acquisition.

Income taxes

There was an income tax recovery of $3.2 million for the fourth quarter of fiscal 2005 compared with an expense of $15.4 million for the corresponding period in fiscal 2004. The low effective tax rate of the current fiscal year is a result of the financing structure established as part of the Eckerd aquisition.

Other initiatives

As of the end of the fiscal year ended May 28, 2005, the Company elected to proceed with the closing of 78 non performing Eckerd drugstores. A total of 73 stores have closed to date, with 45 transfers of script files to the nearest Eckerd store. For the remaining 33 stores, the Company has sold or plans to sell the script files and related inventories. The net addition to the provision for store closures and to the write-down of related assets, which are included in the purchase price equation at May 28, 2005, amounted to $100.5 million.

In June 2005, the Company received a cash payment of $24.0 million from J.C. Penney related to the final settlement of the Eckerd purchase price adjustment for working capital valuation on the closing of the acquisition.

Financial position

The company used a combination of debt and equity financing for the Eckerd acquisition. Readers are also referred to the Notes of the Consolidated Financial Statements and to publicly available credit and debt agreements. The following table provides a summary of information of certain measures with respect to the Company's financial position at the end of the financial years indicated.

	As at May 28, 2005	As at May 31, 2004
Net debt/Book capitalization	62.5%	18.4%
Net debt/LTM OIBA(1)	4.8	0.8
LTM OIBA/Interest(1)	2.6	17.2

(1) Pro forma in fiscal 2005, Eckerd and related financing on a 52-week basis.

The Company's target is to reduce leverage (net debt/OIBA) to less than 3.5 times within 24 months after the closing of the Eckerd acquisition (July 31, 2004).

Liquidity and capital resources

The Company's cash flows are generated by: i) the sale of prescription drugs and other products by corporate-owned stores, ii) merchandise sales to and rent received from PJC franchised stores, iii) the collection of royalties from PJC franchisees, and iv) rent from properties leased to tenants other than franchisees. These cash flows are used: i) to purchase products and services for resale, ii) to finance operating expenses, iii) for debt service, iv) for real estate investments, and v) to finance capital expenditures incurred to renovate and open stores and replace equipment. We have typically financed capital expenditures and working capital requirements through cash flow from operating activities. Our larger acquisitions have been financed through long-term debt and equity.

Cash flow from operating activities

Cash provided by operating activities was $222.1 million for the 52-week year ended May 28, 2005, compared with $185.9 million in fiscal 2004. This increase results primarily from the cash generated from net cash earnings, net of changes in non-cash items resulting from the Company's larger drugstore network in fiscal 2005. Company management focused on the efficient use of cash and working capital throughout the year.

Cash flow from investing activities

Cash used in investing activities was at $2.835 billion for the 52-week year ended May 28, 2005 compared with $91.8 million for fiscal 2004. During fiscal 2005, $2.492 billion was used to acquire 1,549 Eckerd drugstores and related operations. In June 2005, the Company received a cash payment of $24.0 million from J.C. Penney related to the final settlement of the Eckerd purchase price adjustment for working capital valuation on the closing of the acquisition. A total of $75.1 million was used for investments and temporary investments in fiscal 2005 compared with $5.7 million in fiscal 2004. The temporary investments held as of May 28, 2005 are comprised of highly liquid investment grade commercial paper with terms of less than one year. $195.3 million was used for capital assets in fiscal 2005 compared with $74.0 million for fiscal 2004. During fiscal 2005, 124 new drugstores were opened, of which 59 were relocations. 28 drugstores were closed and several others were expanded or renovated. During the fiscal year, the Company closed a distribution center in Pennsylvania.

As of the end of the fiscal year ended May 28, 2005, the Company elected to proceed with the closing of 78 non performing Eckerd drugstores. A total of 73 stores have closed to date, with 45 transfers of script files to the nearest Eckerd store. For the remaining 33 stores, the Company has sold or plans to sell the script files and related inventories. The net addition to the provision for store closures and to the write-down of related assets, which are included in the purchase price equation at May 28, 2005, amounted to $100.5 million. The Company will continue to relocate and open new stores in convenient and profitable mostly freestanding locations. In fiscal 2006, we plan to open approximately 30 new stores, relocate another 49 stores combined with renovating and remodelling a significant amount of stores. We expect net capital expenditures in fiscal 2006 to be approximately $225 million, primarily for existing store renovations and improvements, new store investments, logistics, technology and supply chain improvements. In addition, in the ordinary course of business, the Company may acquire stores and related assets including pharmacy customer lists or other complementary businesses.

Cash flow from financing activities

During the 52-week year ended May 28, 2005, $2.719 billion was provided by financing activities compared to cash used of $72.0 million for fiscal 2004. During fiscal 2005, the Company established credit facilities and issued notes to fund the Eckerd acquisition; this resulted in a $2.333 billion net increase in long-term debt year-over-year compared with a $21.3 million repayment of long-term debt in fiscal 2004. During fiscal 2005, the Company received net proceeds of $426.5 million from the issuance of capital stock compared with proceeds of $1.9 million in fiscal 2004. The Company paid dividends of $25.3 million in fiscal 2005, up from $20.3 million in fiscal 2004, due to the increase in the number of shares issued during the year.

Planned capital expenditures in fiscal 2006 will be funded entirely from internally generated cash flow. Remaining free cash flow will be used for the quarterly payment of dividends with the balance directed largely towards the repayment of debt.

Conclusion on liquidity position

The Company had $210.7 million of cash, cash equivalents and temporary investments, made up of $132.2 million cash and cash equivalents and $78.5 million of temporary investments, as of May 28, 2005 compared with cash of $14.6 million at May 31, 2004. In addition, it had access to up to an unused $282.1 million (net of $67.9 million of outstanding letters of credit) five-year revolving facility which was put in place during the Eckerd transaction. The Company has operating liquidities and access to credit facilities to finance its operating activities.

Current ratings for the Company's credit facilities as confirmed by Standard & Poor's Corporation (S&P) and Moody's Investors Service (Moody's) are as follows:

	S&P	Moody's
Secured credit facilities	BB	B1
Senior notes		
Unsecured	B	B2
Unsecured subordinated	B	B3

In assessing the Company's financial strength, management believes that both S&P and Moody's considered the Company's strategies, results, capital structure, financial policies as well as the consolidated balance sheet and the Eckerd acquisition. The Company's debt ratings have a direct impact on future borrowing costs, access to capital markets and new store operating leases.

Capital stock

During fiscal 2005, 33,350,000 Class A subordinate voting shares were issued at a price of C$17.45 per share for net proceeds of C$564.4 million or US$424.4 million. During the same fiscal year, 865,000 Class B shares were exchanged for an equivalent number of Class A subordinate voting shares. In addition, 1,363,590 new Class A subordinate voting shares were issued during the year due to the exercise of stock options.

These transactions brought the total number of Class A subordinate voting shares (TSX: PJC.SV.A) issued to 142,252,100 (2004 – 106,673,510 shares) and the number of Class B shares to 119,385,000 as at May 28, 2005 (2004 – 120,250,000). The Company has a total of 261,637,100 shares outstanding as at May 28, 2005 (2004 – 226,923,510).

Contractual obligations and commercial commitments

Set out below is a summary of our material contractual cash obligations as of May 28, 2005 for the periods indicated under our long-term debt, long-term leases, inventories, services and capital assets commitments:

Payments due in fiscal years

(in thousands of US dollars)	2006 $	2007- 2008 $	2009- 2010 $	2011 and thereafter $	Total $
Long-term debt	57,726	151,353	107,624	2,227,659	2,544,362
Capital lease obligations	8,570	8,431	1,351	—	18,352
Operating lease obligations	381,192	711,335	637,575	2,615,568	4,345,670
Purchase commitments	75,083	1,344	—	—	76,427
Total	522,571	872,463	746,550	4,843,227	6,984,811

Long-term debt

On July 31, 2004, the Company completed the Eckerd acquisition. This acquisition was funded by a combination of long-term credit facilities, notes and issuance of subordinate voting shares. As a result, the Company's long-term debt, including current portion, increased to $2.561 billion at May 28, 2005 from $192.2 million at May 31, 2004.

Capital lease obligations

The Company has generally not used capital leases as a means of financing. The Company has capital leases for certain store and operating equipment. The information listed in the above table includes interest obligations under such capital lease obligations and obligations in connection with these contracts and related assets are also included in our consolidated balance sheet.

Operating lease obligations

The Company leases a substantial portion of its real estate using conventional operating leases. Generally, the Company's real estate leases in Canada are for primary terms of 10 years and in the United States for primary terms of 10 to 20 years, in both cases, with options to renew.

Operating lease obligations until 2035 amount to $4.346 billion and are mostly in connection with properties that are leased in Canadian and US operations. The Company has also signed lease and sublease agreements under which it will receive minimum payments totalling $286.8 million until 2035, which are not included in the table of contractual commitments above.

Financial instruments and off-balance sheet arrangements

Other than the two interest rate swap contracts mentioned below, the Company does not make use of any off-balance sheet arrangements that currently have or that we expect are reasonably likely to have a material effect on financial condition, results of operations or cash flow. The Company uses operating leases for many of its US store locations, and from time to time, engages in sale-leaseback transactions for financing purposes. The Company does not use special purpose entities in any of its leasing arrangements.

We are exposed to market risk relating to changes in interest rates with regard to our variable rate debt. We have a significant amount of debt, $1.3 billion of which bears interest at floating rates.

The Company had a fixed interest rate swap contract that matured in January 2005 to hedge interest rate fluctuations on a term loan which was repaid as part of the Eckerd acquisition financing, which amounted to $180 million as at July 31, 2004. After July 31, 2004, the Company recorded a $2.1 million pre-tax charge to results related to this contract.

During fiscal 2005, the Company entered into two interest rate swap transactions to fix the interest rate on $200 million of the Company's term loan facilities. These transactions qualified for hedge accounting.

Other than the transactions mentioned herein, the Company has not taken any other specific actions to cover its exposure to interest rate risk. Depending on the interest rate environment and subject to approval by the Board of Directors, the Company may make use of other derivative financial instruments or other interest rate management vehicles in the future. A 10% change in interest rate (45 basis points on the Company's floating rate debt for fiscal 2005) would have a $4.6 million pre-tax effect on results and cash flows for the 52-week year ended May 28, 2005.

Guarantees and buyback agreements

The Company has guaranteed reimbursement of certain bank loans contracted by franchisees to a maximum amount of $6.0 million (2004 – $8.8 million). The Company is also committed to financial institutions to purchase the equipment and inventories of some of its franchisees. As of May 28, 2005, the maximum value of the equipment and inventories buyback agreements was approximately $23.1 million and $46.1 million respectively ($21.0 million and $54.2 million in 2004).

On July 31, 2004, the Company acquired the shares of three subsidiaries of TDI Consolidated Corporation to complete the acquisition of the Eckerd drugstore properties. The Company has entered into an indemnification agreement that is described in Note 17 of the Consolidated Financial Statements.

Foreign exchange risk management

Even though the Company's reporting currency is US dollars, non-Consolidated Financial Statements of the parent company and its subsidiaries are prepared based on their respective functional currencies, which is the US dollar for US operations and the Canadian dollar for Canadian operations and corporate activities.

Transactions denominated in currencies other than an entity's functional currency are translated according to the temporal method. Under this method, monetary assets and liabilities are translated at the exchange rate in effect at the balance sheet date, non-monetary assets and liabilities at their historical rates and statement of earnings items at the average monthly exchange rates. All exchange gains and losses are current in nature and are included in the consolidated statement of earnings.

The significant variation of the Canadian dollar against the US dollar during fiscal 2005 resulted in the Company recording an unrealized foreign exchange loss on monetary items. This loss is attributable to US dollar net monetary assets held by the parent company for the benefit of its US subsidiaries. In order to avoid the impact of these foreign currency fluctuations in the future, in February 2005, the Company reviewed its arrangements and related documentation in order to ensure that all significant monetary items are properly hedged against foreign exchange risk. The fiscal 2005 unrealized foreign exchange loss on monetary items amounted to $7.8 million, reflecting the loss until such arrangements and documentation became effective.

Related party transactions

Our operations include transactions with enterprises controlled by shareholders and executives with significant influence on the Company. Mr. Jean Coutu, Founder and Chairman of the Board, owned a PJC franchise as at May 31, 2004. Mr. François J. Coutu, the Company's President and CEO, owned four PJC franchises as at May 31, 2004 and one as at May 28, 2005.

The transactions between the Company and these enterprises are executed in the normal course of business and measured at the exchange amount. Details are included in Note 21 of the Consolidated Financial Statements.

Critical accounting policies and estimates

Estimates

This MD&A is based on the Company's Consolidated Financial Statements, which have been prepared in accordance with Canadian GAAP. The preparation of these Consolidated Financial Statements and related notes requires the Company's management to make estimates and assumptions that affect the reported amounts. These estimates are based on historical experience and various other assumptions that management believes to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources.

Inventory

Our inventory consists primarily of products acquired for resale, including prescription drugs and over-the-counter medications, as well as household, cosmetic and photography products. Inventory is valued at the lower of cost and net realizable value, the cost being determined using the first in, first out method and retail selling price less a normal gross profit method. Determining gross profit margins requires that management make judgments and estimates that could affect inventory valuation at the end of the year and related annual operating results.

Intangible assets

Intangible assets with a finite life are accounted for at cost and are made up of customer prescription files, non-compete agreements and favorable leases. Prescription files are amortized over a period of five to ten years, non-compete agreements over the terms of the agreements and favorable leases are amortized on a straight-line basis over the term of the leases. The use of different assumptions with regards to the duration of useful life could give rise to different book values for intangible assets.

Goodwill and trade name

Goodwill represents the excess of the acquisition cost of companies over the fair value of the identifiable net assets acquired. Trade name is an intangible asset with an indefinite life, not subject to amortization. Goodwill and trade name are tested for impairment annually or more frequently when changes in circumstances indicate a potential impairment. An impairment test may be necessary if a return is clearly insufficient in relation to historical or projected operating results, material changes in the use of acquired assets or in the Company's broad strategy, and significant negative economic or segmented trends. For the purposes of our analysis on impairment, the Company uses estimates and assumptions to establish the fair value of its reporting units. If these assumptions are incorrect, the carrying values of goodwill and trade name may have been overstated.

Other long-term assets

Other long-term assets are principally deferred costs related to financing fees and incentives paid to franchisees. Financing fees are amortized over a 5- to 10-year period and incentives paid to the franchisees are amortized over a 10-year period. The use of various assumptions with regards to useful life or term could give rise to different book values for these items that are included in long-term assets.

Impairment of long-lived assets

The Company determines the book value of long-lived assets on an ongoing basis. To determine the possibility of impairment, the Company examines the estimated undiscounted cash flows expected to be generated by these assets as well as other indicators. Any permanent impairment in the carrying value of the assets is charged against earnings in the period the impairment is determined.

Defined benefit pension plans

The cost of pensions and other retirement benefits earned by employees is actuarially determined using the projected benefit method prorated on service and management's best estimate of expected plan investment performance, salary escalation and retirement age of employees. The use of different assumptions could result in different book values.

Changes in accounting policies and recent pronouncements

Readers are referred to Note 2 of the Consolidated Financial Statements for a full description of changes in accounting policies and recent pronouncements.

Lease accounting

During fiscal 2005, like several retail companies, the Company completed a review of its methods of amortization of leasehold improvements and related lease incentives following the views expressed by the Office of the Chief Accountant of the US Securities and Exchange Commission (SEC) on certain operating lease matters. The results of this review had no material impact on the Company's Consolidated Financial Statements.

Risks and uncertainties

The Company is well positioned to capitalize on the growth in the North American drugstore retailing industry, based on its strong brands, a focus on excellence in customer service in pharmacy and front-end innovation with an emphasis on health and beauty. Demographic trends in Canada and the United States are expected to contribute to growth in the consumption of prescription drugs, and to the increased use of pharmaceuticals as the primary intervention in individual healthcare. Management believes that these trends will continue and that the Company will achieve sales growth through quality of offering and service levels in its drugstore network.

Eckerd acquisition

The Eckerd integration is the Company's largest to date. The Company could run into difficulties in realizing synergies and improving outlet performance in accordance with plan.

The market for prescription drugs

The Company is reliant on prescription drug sales for a significant and growing portion of its revenues and earnings. Prescription drug sales are subject to numerous federal, state, provincial and local laws and regulations governing many aspects of the sale and dispensing of prescription drugs, as well as the approval of new drugs. In addition, the conversion of prescription drugs to over-the-counter medication often creates a source of confusion for the customer that could result in a decrease in retail sales.

The continued efforts of health maintenance organizations, managed care organizations, pharmacy benefit management companies, governmental entities and organizations and other third party payers to reduce prescription drug costs and pharmacy reimbursement rates could have an effect on revenue growth. The Company is therefore deploying the resources necessary to ensure that all stakeholders are aware of the issues at play in the pharmacy field.

Mail order pharmacy (United States only)

The growth of mail order pharmacies and changes to pharmacy benefit plans requiring maintenance medications to be filled through a mandatory mail channel could constrain the Company's revenue growth.

Competition

The Company faces competition from all sides: local, regional, national and international companies, other drugstore chains and banners, independent pharmacies, supermarkets, discount retailers and Internet companies. This increased competition could lead to greater pricing pressure, a situation that would force us to increase sales volume and sell products and services at a lower price in order to remain competitive.

Pharmacists and personnel

The Company is known for its diversified approach which enables it to attract, hire and retain suitable pharmacists and management personnel. Over the past few years, the Company has successfully implemented pharmacist and management recruitment and retention programs.

Pharmaceutical products supply chain

Eckerd and Brooks drugstores obtain a majority of their pharmaceutical products from a single supplier, McKesson Corporation, with whom the Company has a long-term supply contract that is scheduled to expire in fiscal 2010. Any significant disruption in the Company's relationship with McKesson and related issues could have a material adverse effect on the Company. Failure to renew this contract with McKesson or another supplier under similar terms and conditions, or to move to a self-distribution model could significantly disrupt operations and adversely affect the sales and profitability of US operations.

Marketing programs

The Company's ability to effectively establish effective marketing programs (including pricing strategies and price reduction programs implemented in response to competitive pressures and /or to stimulate demand).

Variable rate debt

Our credit facilities are subject to variable interest rates, thus exposing us to interest rate risk. Should interest rates rise, our variable-rate debt service obligations would increase even if the amount borrowed remained the same.

Currency fluctuation

Our revenues are earned in US and Canadian dollars whereas our credit facilities are denominated in US dollars only. Fluctuations in US and Canadian exchange rates could therefore expose the Company to currency risks.

Seasonal nature of the business

The weather has an effect on the general population's health and by extension the Company's retail sales and those of our franchised outlets. For example, in winter, the Company sells more cold and flu medecine, while in the summer, allergy and sun protection products are in greater demand. Corporate and franchised outlet sales are affected by holidays such as Christmas, Easter, Thanksgiving, Valentine's Day, Mother's Day and Father's Day. The peak sales period is generally the Company's third quarter of its fiscal year, which includes Christmas.

Company filing under *Sarbanes-Oxley Act*

As required by the *Sarbanes-Oxley Act* enacted by the US Congress in July 2002 and the rules promulgated by the US Securities and Exchange Commission (SEC) thereunder, we have filed with the SEC certificates relating to, among others, the accuracy of the financial information contained in our 2005 Annual Report including our MD&A and annual Consolidated Financial Statements and notes thereto, and the adequacy of our procedures and controls relating to disclosure and financial reporting.

As disclosed thereunder, there were no changes in the Company's internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting, for the 52-week year ended May 28, 2005, except for the changes described below.

On July 31, 2004, the Company consummated its acquisition of 1,549 Eckerd drugstores and support facilities. The Company considers this acquisition to be material to the results of its operations, financial position and cash flows from the date of the acquisition through year-end and believes that Eckerd's internal control over financial reporting is reasonably likely to materially affect the Company's internal control over financial reporting.

The Company is reviewing its existing internal control over financial reporting in preparation for the reporting and certification requirements of Section 404 of the *Sarbanes-Oxley Act* of 2002 becoming effective. In connection with such review, modifications will, as appropriate, be made to the Company's disclosure controls and procedures or internal control over financial reporting in the future.

August 2, 2005

Management's report with respect to the financial statements

The consolidated financial statements of The Jean Coutu Group (PJC) Inc. contained in this report are the responsibility of management, and have been prepared in accordance with Canadian generally accepted accounting principles. Where necessary, management has made judgments and estimates of the outcome of events and transactions, with due consideration given to materiality. Management is also responsible for all other information in the Annual Report and for ensuring that this information is consistent, where appropriate, with the information and data included in the consolidated financial statements.

To discharge its responsibility, management maintains a system of internal controls to provide reasonable assurance as to the reliability of financial information and the safeguarding of assets.

The Board of Directors carries out its responsibility relative to the consolidated financial statements principally through its Audit Committee, consisting solely of independent directors, which reviews the consolidated financial statements and reports thereon to the Board. The Committee meets periodically with the external auditors, internal auditors and management to review their respective activities and the discharge by each of their responsibilities. Both the external auditors and the internal auditors have free access to the Committee, with or without the presence of management, to discuss the scope of their audits, the adequacy of the system of internal controls and the adequacy of financial reporting.

The consolidated financial statements have been reviewed by the Audit Committee and approved by the Board of Directors. In addition, the Company's external auditors, Deloitte & Touche, LLP, are responsible for auditing the consolidated financial statements and providing an opinion thereon. Their report is provided hereafter.

François J. Coutu
President and Chief Executive Officer

André Belzile
Senior Vice-President, Finance and Corporate Affairs

Auditors' report

To the Shareholders of The Jean Coutu Group (PJC) Inc.

We have audited the consolidated balance sheets of The Jean Coutu Group (PJC) Inc. as at May 28, 2005 and May 31, 2004 and the consolidated statements of earnings, retained earnings and cash flows 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 Canadian 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 May 28, 2005 and May 31, 2004 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Chartered Accountants
Montréal, Canada
August 2, 2005

Consolidated statements of earnings

For the years ended May 28, 2005 and May 31, 2004 (in thousands of US dollars except for per share amounts)	2005 $	2004 $ (restated)
Sales	9,448,343	2,893,088
Other revenues (Note 3)	169,020	149,879
	9,617,363	3,042,967
Operating expenses		
Cost of goods sold	7,289,872	2,343,998
General and operating expenses	1,878,296	452,284
Amortization (Note 4)	195,308	38,396
	9,363,476	2,834,678
Operating income	253,887	208,289
Financing expenses		
Interest on long-term debt	152,731	11,752
Unrealized foreign exchange loss on monetary items	7,767	—
Other financing expenses, net	1,594	2,783
	162,092	14,535
Earnings before income taxes	91,795	193,754
Income taxes (recovery) (Note 5)	(12,583)	61,071
Net earnings	104,378	132,683
Net earnings per share (Note 6)		
Basic	0.41	0.58
Diluted	0.41	0.58

The segmented information and the accompanying notes are an integral part of these consolidated financial statements.

Consolidated statements of retained earnings

For the years ended May 28, 2005 and May 31, 2004 (in thousands of US dollars)	2005 $	2004 $ (restated)
Balance, beginning of year		
As previously reported	709,419	597,601
Restatement related to a change in accounting policy (Note 2a)	(867)	(1,453)
Restated balance	708,552	596,148
Net earnings	104,378	132,683
	812,930	728,831
Dividends	25,291	20,279
Balance, end of year	787,639	708,552

The segmented information and the accompanying notes are an integral part of these consolidated financial statements.

Consolidated balance sheets

As at May 28, 2005 and May 31, 2004 (in thousands of US dollars)	May 28, 2005 $	May 31, 2004 $ (restated)
Assets		
Current assets		
Cash and cash equivalents	132,175	14,554
Temporary investments	78,489	—
Accounts receivable	544,810	199,516
Inventories	1,678,245	391,916
Prepaid expenses	40,981	12,235
Income taxes receivable	6,822	—
Future income taxes (Note 5)	—	10,220
	2,481,522	628,441
Investments (Note 7)	18,819	21,298
Capital assets (Note 8)	1,492,499	544,174
Intangible assets (Note 9)	729,639	19,277
Goodwill (Note 10)	866,451	95,330
Other long-term assets (Note 11)	105,996	35,234
	5,694,926	1,343,754
Liabilities		
Current liabilities		
Bank loans (Note 12)	—	15,000
Accounts payable and accrued liabilities	1,109,902	231,306
Income taxes payable	32,870	42,004
Future income taxes (Note 5)	97,809	—
Current portion of long-term debt (Note 13)	65,631	22,566
	1,306,212	310,876
Long-term debt (Note 13)	2,495,801	169,609
Other long-term liabilities (Note 14)	480,810	9,826
	4,282,823	490,311
Shareholders' equity		
Capital stock (Note 15)	577,463	144,996
Contributed surplus	764	188
Retained earnings	787,639	708,552
Foreign currency translation adjustments	46,237	(293)
	1,412,103	853,443
	5,694,926	1,343,754

Guarantees, contingencies and commitments (Notes 17 and 18).
The segmented information and the accompanying notes are an integral part of these consolidated financial statements.

Approved by the Board

François J. Coutu
Director

L. Denis Desautels
Director

Consolidated statements of cash flows

For the years ended May 28, 2005 and May 31, 2004 (in thousands of US dollars)	2005 $	2004 $ (restated)
Operating activities		
Net earnings	104,378	132,683
Items not affecting cash		
Amortization	195,308	38,396
Amortization of incentives paid to franchisees	3,545	3,037
Amortization of deferred financing fees	10,324	1,161
Unrealized foreign exchange loss on monetary items	7,767	—
Future income taxes	(53,826)	(13,616)
Other	2,181	185
	269,677	161,846
Net changes in non-cash asset and liability items	(47,607)	24,096
Cash flow provided by operating activities	222,070	185,942
Investing activities		
Business acquisitions (Note 20)	(2,491,813)	(3,910)
Investments and temporary investments	(75,100)	(5,669)
Purchase of capital assets	(195,278)	(74,040)
Proceeds from the disposal of capital assets	15,143	1,651
Intangible assets	(5,128)	(4,235)
Other long-term assets	(82,450)	(5,571)
Cash flow used in investing activities	(2,834,626)	(91,774)
Financing activities		
Changes in bank loans	(15,000)	(32,397)
Issuance of long-term debt	2,550,000	—
Repayment of long-term debt	(217,289)	(21,288)
Issuance of capital stock	426,456	1,932
Dividends	(25,291)	(20,279)
Cash flow provided by (used in) financing activities	2,718,876	(72,032)
Foreign currency translation adjustments	11,301	691
Increase in cash and cash equivalents	117,621	22,827
Cash and cash equivalents (bank overdraft), beginning of year	14,554	(8,273)
Cash and cash equivalents, end of year	132,175	14,554

See complementary cash flow information in Note 23.
The segmented information and the accompanying notes are an integral part of these consolidated financial statements.

Consolidated segmented information

The Company applied on a retroactive basis changes in its reportable segments determination. The impact of these changes is the aggregation of the franchising and real estate segments. The Company has now two reportable segments: franchising and retail sales. Within the segment of franchising, the Company carries on the franchising activity of the "PJC Jean Coutu" banner, operates a distribution center and coordinates several other services for the benefit of its franchisees. The Company operates retail sales outlets selling pharmaceutical and other products under the "Brooks" and "Eckerd" banners.

The Company analyzes the performance of its operating segments based on their operating income before amortization, which is not a measure of performance under Canadian generally accepted accounting principles ("GAAP"); however, management uses this performance measure for assessing the operating performance of its reportable segments.

Segmented information is summarized as follows:

For the years ended May 28, 2005 and May 31, 2004 (in thousands of US dollars)	2005 $	2004 $ (restated)
Revenues[1]		
Franchising	1,406,139	1,235,757
Retail sales	8,211,224	1,807,210
	9,617,363	3,042,967
Operating income before amortization		
Franchising	147,342	134,996
Retail sales	305,398	114,726
	452,740	249,722
Amortization		
Franchising[2]	14,013	10,029
Retail sales	184,840	31,404
	198,853	41,433
Operating income		
Franchising	133,329	124,967
Retail sales	120,558	83,322
	253,887	208,289

[1] Revenues include sales and other revenues.
[2] Including amortization of incentives paid to franchisees.

For the years ended May 28, 2005 and May 31, 2004 (in thousands of US dollars)	2005 $	2004 $
Acquisition of capital assets and intangible assets[3]		
Franchising	33,006	31,164
Retail sales	167,400	47,111
	200,406	78,275

	May 28, 2005 $	May 31, 2004 $ (restated)
Total assets		
Franchising	737,213	464,758
Retail sales	4,957,713	878,996
	5,694,926	1,343,754

The Company's revenues, capital assets, intangible assets and goodwill attributed to Canada and the United States are as follows:

For the years ended May 28, 2005 and May 31, 2004 (in thousands of US dollars)	2005 $	2004 $ (restated)
Revenues[1]		
Canada	1,406,139	1,235,757
United States	8,211,224	1,807,210
	9,617,363	3,042,967

	May 28, 2005 $	May 31, 2004 $
Capital assets, intangible assets and goodwill		
Canada	300,212	254,661
United States	2,788,377	404,120
	3,088,589	658,781

(1) Revenues include sales and other revenues.
(2) Including amortization of incentives paid to franchisees.
(3) Excluding business acquisitions.

Notes to the Consolidated Financial Statements

For the years ended May 28, 2005 and May 31, 2004

(Tabular amounts are in thousands of US dollars except for shares and options data)

1. Description of business and significant accounting policies

a) Description of business

The Company is incorporated under the *Companies Act of Québec*. It has two reportable segments. In Canada, the Company operates a franchisee network. Its franchising operations involve coordinating various services for its franchised network of 321 outlets as of May 28, 2005 (May 31, 2004 – 319), and operating a distribution center. Its franchised network retails pharmaceutical and parapharmaceutical products. The Company also manages all properties that house franchisee outlets. In the United States, the Company operates a network comprising 1,922 corporate establishments as of May 28, 2005 (May 31, 2004 – 336) that retail pharmaceutical and parapharmaceutical products, located in 18 states of the Northeast, mid-Atlantic and Southeast.

b) Financial statements presentation

The consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). The Company has historically prepared its consolidated financial statements in Canadian dollars. Effective June 1, 2004, the Company changed its reporting currency to US dollars to provide shareholders with more relevant information considering the predominant operations in the United States and the US dollar denominated debt.

Effective June 1, 2004, the Company changed its reporting periods to comply with the US National Retail Federation 4-5-4 merchandising calendar. Accordingly, the year-end date was May 28, 2005.

c) Consolidation

The consolidated financial statements include the accounts of the parent company and all its subsidiaries. All intercompany transactions and balances have been eliminated on consolidation.

d) Use of estimates

The preparation of the consolidated financial statements in conformity with Canadian GAAP requires management to make certain estimates and assumptions. These may affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements. They may also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The most significant areas requiring the use of management estimates relate to: inventory valuation, valuation of long-term assets, and reserves and allowances, specifically those related to store closures, workers' compensation and general liabilitiy, and income taxes.

e) Revenue recognition

Sales to franchisees are recognized when merchandise is shipped. Revenues from retail sales are recognized at the time of the sale to the consumer. The Company recognizes its revenues net of returns and reports all direct merchandise shipment transactions on a net basis when acting as an agent between suppliers and franchisees.

Royalties, based on the franchisees' retail sales, are recorded as income as they are earned.

Services to franchisees and rental income are recognized when services are rendered. When a lease contains a predetermined fixed escalation of the minimum rent, the Company recognizes the related rent income on a straight-line basis.

Revenues are recognized when reasonable assurance exists regarding collectibility.

1. Description of business and significant accounting policies (continued)

f) Vendor allowance

Cash considerations received from vendors are a reduction of the prices of the vendors' products or services and are accounted for as a reduction of cost of goods sold and related inventory when recognized in the Company's consolidated statement of earnings and balance sheet. Certain exceptions apply when the cash considerations received are either a reimbursement of incremental selling costs incurred by the Company, or is a payment for assets or services delivered to the vendors.

g) Foreign currency translation

The non-consolidated financial statements of the parent company and its subsidiaries are prepared based on their respective functional currencies, which is US dollar for US operations and Canadian dollar for Canadian operations and corporate activities.

The financial statements of entities whose functional currency is not the US dollar are translated into the reporting currency according to the current rate method. Under this method, statement of earnings and statement of cash flow items of each year are translated to the reporting currency at the average monthly exchange rates and asset and liability items are translated at the exchange rate in effect at the balance sheet date. Translation adjustments resulting from exchange rate fluctuations are recorded in foreign currency translation adjustments in shareholders' equity.

Transactions denominated in currencies other than an entity's functional currency are translated according to the temporal method. Under this method, monetary assets and liabilities are translated at the exchange rate in effect at the balance sheet date, non-monetary assets and liabilities at their historical rates and statement of earnings items at the average monthly exchange rates. All exchange gains and losses are current in nature and are included in the consolidated statement of earnings.

h) Inventories

Inventories are valued at the lower of cost and net realizable value, the cost being determined using the first in, first out basis and retail selling price less a normal gross profit.

i) Investments

Investments in companies subject to significant influence are accounted for using the equity method. Other investments are accounted for using the cost method. Periodically, management analyzes each loan, advance and long-term receivable from franchisees and when a serious doubt as to their recovery is identified, a provision is applied to reduce their book value to the estimated realizable value.

j) Capital assets

Capital assets are accounted for at cost.

Amortization of buildings held for leasing was based on their estimated useful lives using the compound interest method until June 1, 2004. Since this date, the Company uses the straight-line method (Note 2b). Constructions in progress are not amortized until the asset is ready for its intended use. Amortization of other capital assets is based on their estimated useful lives using the straight-line and the diminishing balance methods at the following rates:

Buildings	3% to 5%
Buildings held for leasing	2 1/2% and 10%
Furniture and equipment	10% to 33 1/3%
Computer equipment and software	20% to 33 1/3%
Leasehold improvements	Term of the lease or useful life, whichever is shorter
Vehicles	14% to 30%

1. Description of business and significant accounting policies (continued)

k) Intangible assets

Intangible assets with a finite service life are accounted for at cost. They consist mainly of the customer prescription files, non-compete agreements and favorable leases. The prescription files are amortized over a five to ten-year period. Non-compete agreements are amortized over the terms of the agreements. Favorable leases represent the value attributed to leases resulting from a business acquisition. The value of favorable leases is amortized on a straight-line basis over the term of the leases.

Intangible assets with indefinite service life representing trade name are accounted for at cost and are not amortized. Trade name is tested for impairment annually or more frequently if changes in circumstances indicate a potential impairment. As at May 28, 2005, the Company has performed an impairment test and no write-down was necessary.

l) Goodwill

Goodwill represents the excess of the acquisition cost of companies over the fair value of the identifiable net assets acquired and is not amortized. Goodwill is tested for impairment annually or more frequently if changes in circumstances indicate a potential impairment. As at May 28, 2005, the Company has performed an impairment test and no write-down was necessary.

m) Other long-term assets

Other assets are mainly the incentives paid to franchisees and deferred costs. Incentives paid to franchisees are amortized over a ten-year period and amortization is applied against royalties, included in other revenues. Deferred costs are accounted for at cost and are mainly financing fees. Amortization is calculated using the straight-line method over the term of the long-term loan and is recorded in interest on long-term debt.

n) Future income taxes

The Company uses the tax asset and liability method to account for income taxes. Under this method, future tax assets and liabilities are determined according to differences between the carrying amounts and tax bases of assets and liabilities. They are measured by applying enacted or substantively enacted tax rates and laws at the date of the financial statements for the years in which the temporary differences are expected to reverse. It is more likely than not that all of the future income tax assets will be realized.

o) Other long-term liabilities

Except for the future income taxes, other long-term liabilities consist mainly of the deferred revenues, deferred lease obligations, unfavorable leases, workers' compensation and general liability and liabilities for store closures.

Deferred revenues: The Company receives allowances from its vendors as consideration for exclusivity agreements. The revenues related to these agreements are deferred when received and recognized as purchases are made, as stipulated by the agreement.

Deferred lease obligations: The Company conducts a part of its operations in leased premises and recognizes minimum rent starting when possession of the property is taken from the landlord, which normally includes a pre-opening period. When a lease contains a predetermined fixed escalation of the minimum rent, the Company recognizes the related rent expense on a straight-line basis and consequently, records the difference between the recognized rental expense and the amounts payable under the lease as deferred lease obligations. The Company also receives tenant allowances which are amortized on a straight-line basis.

1. Description of business and significant accounting policies (continued)

Lease payments that depend on factors that are not measurable at the inception of the lease, such as future sales volume, are contingent rentals in their entirety and are excluded from minimum lease payments and included in the determination of total rental expense when it is probable that the expense has been incurred and the amount is reasonably estimable.

Unfavorable leases: The value attributed to unfavorable leases resulting from a business acquisition is amortized on a straight-line basis over the term of the leases.

Workers' compensation and general liability: Workers' compensation and general liability reserves are based on actuarially determined estimates of reported and incurred but not reported claims resulting from historical experience and current data.

Liabilities for store closures: Store closure reserves are established at the present value of lease obligations, net of estimated sublease rental income and other exit costs.

p) Defined benefit pension plans

The Company maintains defined benefit pension plans for some of its senior officers, which include a registered pension plan as well as a non-registered supplemental pension plan. The registered pension plan is funded as required by the applicable law and the supplemental plan is partly funded through retirement compensation arrangements (RCA). Under the terms of the RCA, 50% of all contributions are required to be deposited with the Canada Revenue Agency.

The amount of contributions required for funding purposes is determined by actuarial valuations performed triennially. The most recent actuarial valuation was performed as at December 31, 2002 and the effective date of the next required actuarial valuation is December 31, 2005.

The Company accrues its obligations under employee benefit plans and the related costs, net of plan assets. The cost of pensions and other retirement benefits earned by employees is actuarially determined using the projected benefit method prorated on service and management's best estimate of expected plans' investment performance, salary escalation and retirement age of employees. For the purpose of calculating the expected return on plan assets, those assets are valued at fair value. The fair value is market value.

Past service costs are amortized on a straight-line basis over the average remaining service period of active employees, which was eight years as of May 28, 2005 (nine as at May 31, 2004).

The excess of the net actuarial gain or loss over 10% of the greater of the benefit obligation and the fair value of plan assets is amortized over the average remaining service period of active employees.

q) Defined contribution pension plan

For the defined contribution plan, the pension expense is equal to the contributions paid by the Company.

r) Stock-based compensation plan

The Company has a fixed stock option plan, which is described in Note 16. Since June 1, 2003, stock-based compensation is recorded under the fair value method. According to that method, awards of stock options are measured on their date of grant using the fair value based method. They are expensed and credited to contributed surplus over their vesting period. This credit is reclassified to capital stock when stock options are exercised.

1. Description of business and significant accounting policies (continued)

s) Derivative financial instruments
The Company uses various derivative financial instruments to manage interest rate risk and foreign exchange rate risk. The Company does not use derivative financial instruments for speculative or trading purposes.

The Company formally documents all relationships between derivatives and the items it hedges, and its risk management objective and strategy for using various hedges. Derivatives that are economic hedges, but do not qualify for hedge accounting, are recognized at fair value with the changes in fair value recorded in earnings.

The Company uses interest rate swap agreements to help manage the fixed and floating interest rate mix of its total debt portfolio. These agreements involve exchanging interest payments without exchanging the notional principal amount that the payments are based on. The Company records the exchange of payments as an adjustment of interest expense on the hedged debt. The Company includes the related amount receivable or payable from counterparties in accounts receivable or in accounts payable and accrued liabilities.

The Company uses a portion of its US dollar liabilities as a foreign exchange hedge of its net investments in its US subsidiaries. Accordingly, corresponding foreign exchange gains and losses are recorded in foreign currency translation adjustments in the shareholders' equity to offset the foreign currency translation adjustments on the investments.

t) Cash and cash equivalents
Cash and cash equivalents are defined as cash and highly liquid investments that have maturities of less than three months at the date of acquisition.

u) Temporary investments
Temporary investments are comprised of commercial paper that have maturities of more than three months and are valued at cost.

2. Accounting policies

Changes in accounting policies

2005

a) Recording of certain consideration received by a vendor
In January 2004, the Emerging Issues Committee of the Canadian Institute of Chartered Accountants (CICA) released Abstract 144 (EIC-144), "Accounting by a Customer (Including a Reseller) for Certain Consideration Received from a Vendor." EIC-144 specifies the accounting methods to be applied to certain consideration received from a vendor. EIC-144 should be applied retroactively to all financial statements for annual and interim periods ending after August 15, 2004.

EIC-144 stipulates that cash consideration received by a company from a vendor is presumed to be a reduction of the prices of the vendor's products or services and should, therefore, be accounted for as a reduction of cost of goods sold and related inventory when recognized in the company's statement of earnings and balance sheet. Certain exceptions apply when the cash consideration received is either a reimbursement of incremental selling costs incurred by the reseller, or is a payment for assets or services delivered to the vendor.

2. Accounting policies (continued)

The Company applied this new recommendation on June 1, 2004. The impact of this new recommendation for the years ended May 28, 2005 and May 31, 2004 was as follows:

	2005		2004	
	Increase $	Decrease $	Increase $	Decrease $
Sales	5,036	—	4,918	—
Other revenues	—	12,369	—	14,547
Cost of goods sold	—	47,474	—	47,677
General and operating expenses	40,120	—	37,115	—
Income taxes	26	—	347	—
Net earnings	—	5	586	—
Retained earnings at beginning of year	—	867	—	1,453

The impact of that change on the consolidated balance sheet as of May 28, 2005 and as of May 31, 2004 is to decrease inventories by approximately $1,454,000 and $1,359,000 respectively and to increase income taxes by approximately $451,000 and $440,000 respectively.

b) Generally accepted accounting principles
In July 2003, the CICA issued Handbook Section 1100, "Generally Accepted Accounting Principles." This Section establishes standards for financial reporting in accordance with Canadian GAAP, and provides guidance on sources to consult when selecting accounting policies and determining appropriate disclosures when a matter is not dealt with explicitely in the primary sources of Canadian GAAP. The Company implemented the new section prospectively on June 1, 2004.

Effective June 1, 2004, the compounded interest method of amortization previously used for buildings held for leasing is no longer used. Accordingly, effective June 1, 2004, the Company amortizes the building costs of its buildings held for leasing on a straight-line basis over their useful lives. Building amortization is higher than it would have been reported under the prior policy by approximately $2,500,000 for the period ended May 28, 2005.

c) Hedging relationships
On June 1, 2004, the Company adopted the provisions of Accounting Guideline 13 (AcG-13), "Hedging Relationships," that deals with the identification, designation, documentation and measurement of effectiveness of hedging relationships for the purposes of applying hedge accounting and EIC-128, "Accounting for Trading Speculative, or Non-Hedging Derivative Financial Instruments" issued in December 2001. Under EIC-128, derivative instruments that do not qualify as a hedge under AcG-13, are recorded in the balance sheet at fair value with changes in fair value recognized in net earnings. The effect of adopting the new recommendations had no material impact on the Company's consolidated financial statements.

2. Accounting policies (continued)

d) Consolidation of variable interest entities
In June 2003, the CICA issued Accounting Guideline 15 (AcG-15), "Consolidation of Variable Interest Entities." This Guideline addresses consolidation of variable interest entities (VIEs) to which the usual condition for consolidation does not apply because the VIEs have no voting interests or are otherwise not subject to control through ownership of voting interests. It requires existing unconsolidated VIEs to be consolidated by the primary beneficiary. This Guideline is required for annual and interim periods beginning on or after November 1, 2004. The adoption of AcG-15 had no material impact on the Company's consolidated financial statements.

e) Asset retirement obligations
In March 2003, the CICA issued Handbook Section 3110, "Asset Retirement Obligations," which is effective for fiscal years beginning on or after January 1, 2004 with retroactive restatement. The new standard provides guidance for the recognition, measurement and disclosure of liabilities for asset retirement obligations and the associated retirement costs. It applies to legal obligations pertaining to the retirement of tangible long-lived assets from acquisition, contruction, development or normal operations. The standard requires the recognition of the fair value of a liability for an asset retirement obligation in the year in which it is incurred and when a reasonable estimate of fair value can be made. The adoption of CICA Handbook Section 3110 had no material impact on the Company's consolidated financial statements.

2004

f) Incentives paid to franchisees
During the fourth quarter of the year ended May 31, 2004, the Company changed its basis of accounting for banner development costs. Banner development costs were previously considered indefinite life intangible assets and therefore not subject to amortization. Banner development costs are now considered deferred costs representing incentives paid to franchisees. These costs are amortized over a ten-year period and are applied against royalties included in other revenues.

g) Stock-based compensation
On June 1, 2002, the Company adopted the recommendations of Section 3870 of the CICA Handbook related to stock-based compensation and other stock-based payments. Subsequently, on June 1, 2003, the Company prospectively adopted the new recommendations of Section 3870 of the CICA Handbook. Under these new recommendations, stock-based compensations are to be recorded under the fair value method. According to that method, awards of stock options are measured on their date of grant using the fair value based method. They are expensed and credited to contributed surplus over their vesting period. This credit is reclassified to capital stock when stock options are exercised. The impact of these recommendations as at May 28, 2005 was to decrease the net earnings by $623,000 (2004 – $188,000) to increase contributed surplus by $576,000 (2004 – $188,000) and to increase capital stock by $47,000 (2004 – nil).

Prior to June 1, 2003, the Company accounted for stock-based compensation by measuring compensation cost for employee stock options as the excess, if any, of the quoted market price of the Class A subordinate voting shares at the date of grant over the amount an employee must pay to acquire these shares. Besides, for the options granted during the year ended May 31, 2003, the Company includes in the notes to the consolidated financial statements pro forma disclosures of net earnings and net earnings per share as if the fair value method of accounting had been applied (Note 16). Any consideration paid on exercise of stock options or purchase of stock is credited to capital stock.

Recent pronouncements

h) Financial Instruments – Disclosure and Presentation
In November 2003, the Accounting Standards Board approved a revision to CICA Handbook Section 3860, "Financial Instruments – Disclosure and Presentation." These revisions change the accounting for certain financial instruments that have liability and equity characteristics. It requires instruments that meet

2. Accounting policies (continued)

specific criteria to be classified as liabilities on the balance sheet. Some of these financial instruments were previously classified as equities. These revisions are effective for fiscal years beginning on or after November 1, 2004. Because the Company does not have any instruments with these characteristics, adopting these revisions on June 1, 2005 will not affect its consolidated financial statements.

i) Comprehensive Income

In April 2005, the CICA issued Handbook Section 1530, "Comprehensive Income." This Section is effective for fiscal years beginning on or after October 1, 2006. It describes how to report and disclose comprehensive income and its components. Comprehensive income is the change in a company's net assets that results from transactions, events and circumstances from sources other than the company's shareholders. It includes items that would not normally be included in net earnings, such as:

- changes in the currency translation adjustment relating to self-sustaining foreign operations;
- unrealized gains or losses on available-for-sale investments.

In April 2005, the CICA also made changes to Handbook Section 3250, "Surplus," and reissued it as Section 3251, "Equity." This Section is also effective for fiscal years beginning on or after October 1, 2006. The changes in how to report and disclose equity and changes in equity are consistent with the new requirements of Section 1530, "Comprehensive Income."

Adopting these Sections on June 1, 2007 will require the Company to start reporting the following items in the consolidated financial statements:

- comprehensive income and its components;
- accumulated other comprehensive income and its components.

j) Financial Instruments – Recognition and Measurement

In April 2005, the CICA issued Handbook Section 3855, "Financial Instruments – Recognition and Measurement." This Section is effective for fiscal years beginning on or after October 1, 2006. It describes the standards for recognizing and measuring financial assets, financial liabilities and non-financial derivatives.

This Section requires that:

- all financial assets be measured at fair value, with some exceptions like loans and investments that are classified as held-to-maturity;
- all financial liabilities be measured at fair value if they are derivatives or classified as held for trading purposes. Other financial liabilities are measured at their carrying value;
- all derivative financial instruments be measured at fair value, even when they are part of a hedging relationship.

The Company is currently evaluating the impact on its consolidated financial statements of adopting this Section on June 1, 2007.

k) Hedges

In April 2005, the CICA issued Handbook Section 3865, "Hedges." This Section is effective for fiscal years beginning on or after October 1, 2006, and describes when and how hedge accounting can be used. Hedging is an activity used by a company to change an exposure to one or more risks by creating an offset between:

- changes in the fair value of a hedged item and a hedging item;
- changes in the cash flows attributable to a hedged item and a hedging item; or
- changes resulting from a risk exposure relating to a hedged item and a hedging item.

Hedge accounting makes sure that all gains, losses, revenues and expenses from the derivative and the item it hedges are recorded in the statement of earnings in the same period.

The Company is currently evaluating the impact on its consolidated financial statements of adopting this Section on June 1, 2007.

3. Other revenues

	2005 $	2004 $ (restated)
Royalties[1]	75,104	67,544
Rent	54,303	46,531
Sundry	39,613	35,804
	169,020	149,879

[1] The amortization of incentives paid to franchisees of $3,545,000 is applied against royalties (2004 – $3,037,000).

4. Amortization

	2005 $	2004 $
Capital assets	150,533	30,848
Intangible assets	44,412	6,763
Deferred costs	363	785
	195,308	38,396

5. Income taxes

Provision for income taxes (recovery) is as follows:

	2005 $	2004 $ (restated)
Current	41,243	74,687
Future	(53,826)	(13,616)
	(12,583)	61,071

5. Income taxes (continued)

The Company's effective tax rate differs from the combined statutory rate. The difference is attributable to the following items:

	2005 %	2004 %
Canadian combined statutory tax rate	31.0	32.2
Effect of tax rates of American subsidiaries	9.5	2.6
Global tax rate	40.5	34.8
Tax rate increase (decrease) resulting from:		
Benefit arising from investment in subsidiaries	(58.0)	(3.9)
Other	3.8	0.6
	(13.7)	31.5

Future income tax assets and liabilities are as follows:

	May 28, 2005 $	May 31, 2004 $ (restated)
Future income tax assets:		
Accounts receivable	17,289	2,084
Capital assets	108	11,289
Intangible assets, goodwill and incentives paid to franchisees	4,566	5,621
Current liabilities	77,383	4,611
Other long-term liabilities	100,778	1,188
Capital stock issuance expenses	5,057	288
Other	1,046	4,256
	206,227	29,337
Future income tax liabilities:		
Inventories	192,858	—
Capital assets	237,054	6,787
Intangible assets and goodwill	116,799	859
Other	3,799	132
	550,510	7,778
Future income tax assets (liabilities), net	(344,283)	21,559

5. Income taxes (continued)

	May 28, 2005 $	May 31, 2004 $ (restated)
Allocated as follows:		
Short-term future income tax asset	—	10,220
Long-term future income tax asset	37	14,382
Short-term future income tax liability	(97,809)	—
Long-term future income tax liability	(246,511)	(3,043)
	(344,283)	21,559

6. Net earnings per share

The reconciliation of the numbers of shares used to calculate the diluted net earnings per share is established as follows:

	2005	2004
Weighted average number of shares used to compute basic net earnings per share	255,659,552	226,812,864
Dilution effect	790,386	1,204,894
Weighted average number of shares used to compute diluted net earnings per share	256,449,938	228,017,758

The Company uses the treasury stock method for the calculation of the diluted net earnings per share and excludes anti-dilutive options.

7. Investments

	May 28, 2005 $	May 31, 2004 $
Loans, advances and long-term operating receivables from franchisees, variable interest, some of which carry repayment terms until 2012 and are renewable (net of a provision for losses of $1,760,000 as at May 28, 2005; May 31, 2004 – $1,153,000)	19,085	24,380
Other	2,132	2,920
	21,217	27,300
Current portion (included in accounts receivable)	2,398	6,002
	18,819	21,298

During the year, a $668,000 bad debt expense has been accounted for in respect of these receivables (2004 – $447,000).

8. Capital assets

			May 28, 2005
	Cost $	Accumulated amortization $	Net book value $
Land	174,668	—	174,668
Land held for leasing	68,822	—	68,822
Buildings	340,058	41,471	298,587
Buildings held for leasing	191,188	22,968	168,220
Furniture and equipment	480,148	80,450	399,698
Computer equipment and software	117,328	74,236	43,092
Leasehold improvements	355,625	83,020	272,605
Vehicles	14,112	3,563	10,549
Computer equipment and software under capital leases	41,043	16,850	24,193
Construction in progress	32,065	—	32,065
	1,815,057	322,558	1,492,499

8. Capital assets (continued)

			May 31, 2004
	Cost $	Accumulated amortization $	Net book value $
Land	67,532	—	67,532
Land held for leasing	62,445	—	62,445
Buildings	170,013	28,117	141,896
Buildings held for leasing	164,796	19,808	144,988
Furniture and equipment	66,086	36,977	29,109
Computer equipment and software	50,855	37,622	13,233
Leasehold improvements	121,032	44,727	76,305
Vehicles	2,960	1,954	1,006
Computer equipment and software under capital leases	2,888	1,921	967
Construction in progress	6,693	—	6,693
	715,300	171,126	544,174

9. Intangible assets

Intangible assets are detailed as follows:

			May 28, 2005
	Cost $	Accumulated amortization $	Net book value $
Prescription files	332,595	54,667	277,928
Non-compete agreements	5,891	4,365	1,526
Favorable leases	113,216	16,031	97,185
Trade name[1]	353,000	—	353,000
	804,702	75,063	729,639

[1] Non-amortized indefinite service life intangible asset.

			May 31, 2004
	Cost $	Accumulated amortization $	Net book value $
Prescription files	42,087	26,186	15,901
Non-compete agreements	5,231	3,820	1,411
Favorable leases	4,751	2,786	1,965
	52,069	32,792	19,277

The Company acquired intangible assets for an amount of $752,328,000 (2004 – $6,746,000) of which $747,200,000 is related to the Eckerd acquisition as described in Note 20.

10. Goodwill

The changes in the book value of goodwill are as follows:

			May 28, 2005
	Franchising $	Retail sales $	Total $
Balance, beginning of year	15,837	79,493	95,330
Acquisition (Note 20)	—	769,763	769,763
Foreign currency translation adjustments	1,358	—	1,358
Balance, end of year	17,195	849,256	866,451

			May 31, 2004
	Franchising $	Retail sales $	Total $
Balance, beginning of year	14,605	79,493	94,098
Acquisition (Note 20)	1,165	—	1,165
Foreign currency translation adjustments	67	—	67
Balance, end of year	15,837	79,493	95,330

11. Other long-term assets

	May 28, 2005 $	May 31, 2004 $
Incentives paid to franchisees, net	18,333	18,002
Deferred costs, net	75,740	2,616
Future income taxes (Note 5)	37	14,382
Other	11,886	234
	105,996	35,234

12. Bank loans

Bank loans reflect the used portion of the revolving credit facilities available to the Company.

As at May 31, 2004, the Company had an annually renewable credit facility in the amounts of $C75,000,000 and $60,000,000, also available as letters of credit not exceeding $15,000,000. As of that date, the Company had an outstanding $15,000,000 bank loan bearing interest at LIBOR rate plus a margin of 0.75% and $7,091,000 of letters of credit.

12. Bank loans (continued)

Credit agreement

On July 30, 2004, the Company entered into a new credit agreement, which included credit facilities and two term loans described in Note 13. Under the terms of the credit agreement, the Company must satisfy certain restrictive covenants as to minimum financial ratios and must satisfy certain conditions. The credit agreement is secured by a first ranking security interest in substantially all of the Company's assets and a first ranking pledge of the capital stock of the Company's subsidiaries.

Consequently, maturing on July 30, 2009, an amount of $350,000,000 is available as a revolver loan or as letters of credit for an amount not exceeding $180,000,000. Revolver borrowings under the credit agreement bear interest at the Canadian or US prime rate plus a variable margin or at LIBOR rate plus a variable margin (varying from 0.50% to 2.50%). Margins depend on whether certain financial ratios are achieved. Available credit facilities were unused as at May 28, 2005, with the exception of an amount of $67,927,000 for letters of credit.

13. Long-term debt

	May 28, 2005 $	May 31, 2004 $
Term loan facility maturing on July 30, 2009, secured first rank, bearing interest at LIBOR rate plus a variable margin (totalling 5.75% as of May 28, 2005), repayable by quarterly instalments based on yearly tranches from 5% to 25% of the original loan balance, according to the credit agreement described in Note 12.	243,750	—
Term loan facility maturing July 30, 2011, secured first rank, bearing interest at LIBOR rate plus a variable margin (totalling 5.50% as of May 28, 2005), repayable by quarterly instalments based on yearly tranches of 1% of the original loan balance over the first six years and the balance owing in 2011, according to the credit agreement described in Note 12.	1,094,500	—
Unsecured senior notes, bearing interest at 7.625% and maturing on August 1, 2012, redeemable after August 1, 2008.	350,000	—
Unsecured senior subordinated notes, bearing interest at 8.50% and maturing on August 1, 2014, redeemable after August 1, 2009.	850,000	—
Computer equipment and software capital leases bearing interest calculated at rates varying from 4.55% to 10.75% (4.55% to 6.55% as at May 31, 2004).	17,070	1,109
Term loan bearing interest at LIBOR rate plus a variable margin (totalling 2.125% as of May 31, 2004). This loan was refinanced on July 30, 2004.	—	185,000
Other	6,112	6,066
	2,561,432	192,175
Current portion	65,631	22,566
	2,495,801	169,609

13. Long-term debt (continued)

Minimum repayments
Minimum repayments to be made during the following years are as follows:

	Long-term debt	Capital leases	
	Principal $	Principal $	Interest $
2006	57,726	7,905	665
2007	76,737	4,949	371
2008	74,616	2,939	172
2009	55,180	1,249	72
2010	52,444	28	2

Additional repayments in excess of the minimum amounts mentioned above may be made by the Company based on cash flow provided during the year.

14. Other long-term liabilities

	May 28, 2005 $	May 31, 2004 $
Deferred revenues	9,836	1,242
Deferred lease obligations	17,781	1,418
Unfavorable leases	32,349	4,123
Workers' compensation and general liability	68,794	—
Liabilities for store closures	96,587	—
Future income taxes (Note 5)	246,511	3,043
Other	8,952	—
	480,810	9,826

15. Capital stock

Authorized, unlimited number:
Class A subordinate voting shares, participating, one vote per share, exchangeable, at the option of the holder, for the same number of Class B shares in the event of a take-over bid being made in respect to Class B shares, without par value, dividend declared in Canadian dollars.

Class B shares, participating, ten votes per share, exchangeable for Class A subordinate voting shares on the basis of one Class A subordinate voting share for one Class B share, without par value, dividend declared in Canadian dollars.

Class C shares, to be issued in one or more series subject to rights, privileges, conditions and restrictions to be determined, non-participating, non voting, without par value.

15. Capital stock (continued)

Changes that occurred on Class A subordinate voting shares are presented as follows:

	2005		2004	
	Shares	$	Shares	$
Outstanding shares, beginning of year	106,673,510	144,994	102,569,550	143,062
Issuance in cash consideration[1]	33,350,000	424,383	—	—
Class B shares converted into Class A subordinate voting shares	865,000	1	3,750,000	—
Options exercised	1,363,590	8,084	353,960	1,932
Outstanding shares, end of year	142,252,100	577,462	106,673,510	144,994

[1]Net of share issuance fees of $19.3 million less related income taxes of $6.0 million.

Changes that occurred on Class B shares are presented as follows:

	2005		2004	
	Shares	$	Shares	$
Outstanding shares, beginning of year	120,250,000	2	124,000,000	2
Class B shares converted into Class A subordinate voting shares	(865,000)	(1)	(3,750,000)	—
Outstanding shares, end of year	119,385,000	1	120,250,000	2

16. Stock-based compensation plan

The Company has a fixed stock option plan. Under the 1995 executive officers Stock Option Plan, the Company may grant options to those employees totalling up to 8 million Class A subordinate voting shares. Under the plan, the exercise price of each option equals the closing market price of the Company's stock at the Toronto Stock Exchange on the date of grant, and an option's maximum term is 10 years. Granted options vest annually by increments of 20%.

Changes that occurred in the number of options are presented as follows:

	2005		2004	
	Number of options	Weighted average exercise price $C	Number of options	Weighted average exercise price $C
Options outstanding, beginning of year	2,907,090	10.15	2,956,790	9.10
Options granted	492,780	15.76	331,600	17.02
Options exercised	(1,363,590)	7.53	(353,960)	7.46
Options cancelled	(163,720)	15.98	(27,340)	14.75
Options outstanding, end of year	1,872,560	13.05	2,907,090	10.15
Options exercisable, end of year	1,213,676	11.34	2,171,258	8.75

16. Stock-based compensation plan (continued)

The following table summarizes information about the fixed stock options outstanding at May 28, 2005:

	Options outstanding		Options exercisable
Exercise price $C	Number of options	Weighted average remaining contractual life (years)	Number of options
4.24	5,000	2.4	5,000
7.01	130,040	4.4	130,040
8.85-9.38	566,840	5.3-5.4	566,840
13.00	250,600	6.4	200,480
15.65-18.95	920,080	7.4-10	311,316
	1,872,560		1,213,676

Had compensation cost been determined using the fair value based method at the date of grant for awards granted during the year ended May 31, 2003, the Company's net earnings for the year ended May 28, 2005 would have been reduced by $300,000 (2004 – $281,000). Basic net earnings per share and diluted net earnings per share would have been unchanged for the years ended May 28, 2005 and May 31, 2004.

The following data represents the weighted average assumptions used in the stock option valuation in accordance with the Black-Scholes model:

	2005 %	2004 %
Dividend yield	0.70	0.73
Expected volatility	27.10	28.20
Risk-free interest rate	4.01	4.19
Expected life (years)	6	6

During the year ended May 28, 2005, the Company granted 492,780 stock options (2004 – 331,600). The weighted average fair value of those options is $C5.07 as at May 28, 2005 (2004 – $C5.61). Therefore, an amount of $623,000 for the year ended May 28, 2005 was expensed for the stock option plan (2004 – $188,000).

17. Guarantees and contingencies

Guarantees

On July 31, 2004, the Company acquired the shares of three subsidiaries of TDI Consolidated Corporation (Note 20). Pursuant to the stock purchase agreement, the Company agreed to enter into certain customary indemnification obligations in favor of the Seller. The Company has agreed to indemnify the Seller for taxes, damages and certain liabilities related to the business acquired. Certain portions of the Company's indemnification obligations are capped at $350 million while other provisions are not subject to such a limit. Certain of the indemnification obligations survive the closing date of the acquisition until 2006 and still others will survive until the expiration of the applicable statute of limitations. The maximum amount of future payments cannot be estimated as it results from future events that cannot be predicted.

Certain debt agreements require the Company to indemnify the parties in the event of changes in elements such as withholding tax regulations. The nature and scope of such indemnifications is contingent on future events, none of which can be foreseen as at May 28, 2005. Also, the structure of such transactions makes these events unlikely. Consequently, no provisions have been recorded in the consolidated financial statements.

The Company has guaranteed the reimbursement of certain bank loans contracted by franchisees for a maximum amount of $5,981,000 as at May 28, 2005 (May 31, 2004 – $8,775,000). Most of those guarantees apply to loans with a maximum maturity of eight years. Those loans are also personally guaranteed by the franchisees.

Buyback agreements

Under buyback agreements, the Company is committed to financial institutions to purchase the inventories of some of its franchisees up to the amount of advances made by those financial institutions to the franchisees. As of May 28, 2005, financing related to these inventories amounted to approximately $46,122,000 (May 31, 2004 – $54,242,000). However, under these agreements, the Company is not committed to cover any deficit that may arise should the value of these inventories be less than the amount of the advances.

Under buyback agreements, the Company is committed to financial institutions to purchase equipment held by franchisees and financed by capital leases not exceeding five years and loans not exceeding eight years. For capital leases, the buyback value is linked to the net balance of the lease at the date of the buyback. For equipment financed by bank loans, the minimum buyback value is set by contract with the financial institutions. As at May 28, 2005, financing related to the equipment amounts to approximately $23,132,000 (May 31, 2004 – $20,998,000). However, it is the opinion of management that the realizable value of the assets cannot be lower than the eventual amount of the buyback.

Historically, the Company has not made any indemnification payments under such agreements and no amount has been accrued with respect to these guarantees in its consolidated financial statements for May 28, 2005 and May 31, 2004.

Contingencies

Various claims and legal proceedings have been initiated against the Company in the normal course of its operating activities. Although the outcome of these proceedings cannot be determined with certainty, management estimates that any payments resulting from their outcome are not likely to have a substantial negative impact on the Company's consolidated financial statements.

18. Commitments

The balance of the commitments under the terms of building and vehicle operating leases maturing in 2035 totals $4,345,670,000. The Company also has commitments for the construction of buildings with contractors totalling $65,938,000 and agreements with suppliers to purchase inventory and services totalling $10,489,000. Minimum payments payable over the next five years are as follows:

	Operating leases $	Other commercial commitments $
2006	381,192	75,083
2007	364,394	1,062
2008	346,941	282
2009	329,634	—
2010	307,941	—

Under the terms of building leases and subleases, the Company will receive, up to the year 2035, minimum payments totalling $286,846,000. This amount takes into account the renewal of subleases at the same terms and conditions as the lease agreements.

19. Pension plans

The Company offers defined benefit and defined contribution pension plans providing pension benefits to its employees. The measurement date used for financial reporting purposes of the plan assets and benefit obligations is May 28, 2005 (May 31 in 2004).

The defined benefit and defined contribution plans expenses are as follows:

	2005 $	2004 $
Defined contribution plan	18,212	2,541
Defined benefit plans		
Current service costs	482	439
Interest expense	412	540
Actual return on plan assets	(115)	(87)
Amortization of past service cost	926	1,456
Actuarial gains	(226)	(227)
Benefit plans expense	1,479	2,121

19. Pension plans (continued)

Information about the Company's defined benefit plans is as follows:

	May 28, 2005 $	May 31, 2004 $
Accrued benefit obligations		
Balance, beginning of year	6,659	8,396
Current service cost	482	439
Interest expense	412	540
Benefits paid	(135)	(74)
Settlements	(673)	(2,476)
Actuarial gains	(226)	(227)
Foreign currency translation adjustment	571	61
Balance, end of year	7,090	6,659

	May 28, 2005 $	May 31, 2004 $
Plan assets		
Fair value, beginning of year	3,084	2,297
Actual return on plan assets	115	87
Employer contributions	683	3,256
Benefits paid	(135)	(74)
Settlements	(673)	(2,476)
Foreign currency translation adjustment	265	(6)
Fair value, end of year	3,339	3,084
Accrued benefit obligations	7,090	6,659
Plan assets	(3,339)	(3,084)
	3,751	3,575
Unamortized balances	1,950	2,650
Accrued benefit liability (included in accounts payable and accrued liabilities)	1,801	925

19. Pension plans (continued)

As at May 28, 2005, 36% (2004 – 28%) of the plan assets at fair value was deposited as refundable tax and 64% (2004 – 72%) was invested. The balance invested consists of the following allocations:

	May 28, 2005 %	May 31, 2004 %
Balanced funds	57	48
Equity income and insured annuity	34	35
Equity funds	7	6
Other	2	11

No plan assets are directly invested in the parent company and its subsidiaries securities.

The main actuarial assumptions adopted in measuring the Company's accrued benefit obligations and the benefits costs are as follows:

	2005 %	2004 %
Discount rate	6.00	6.00
Expected long-term rate of return on plan assets	6.75	6.75
Rate of compensation increase	4.00	4.00

20. Business acquisitions

Eckerd

On July 31, 2004, the Company acquired the shares of three subsidiaries of TDI Consolidated Corporation, a wholly-owned subsidiary of J.C. Penney Corporation, Inc., that own 1,549 outlets of the Eckerd drugstore chain located throughout 13 states in Northeastern, mid-Atlantic and Southeastern United States. The acquisition has been accounted for under the purchase method and the results of operations have been included in the consolidated financial statements since the acquisition date.

The Company completed its allocation of the purchase price based on information available, and on the basis of evaluations. The acquired goodwill is not deductible for income tax purposes. This allocation is subject to changes related to the final determination of the future income taxes.

20. Business acquisitions (continued)

Purchase price allocation:

	Millions of dollars (revised)	Millions of dollars (initial)
Net assets acquired		
Non-cash working capital	751.9	780.3
Capital assets[1]	898.1	858.0
Intangible assets:		
Trade name (not subject to amortization)	353.0	322.4
Prescription files (amortized over a 10-year period)	286.4	438.3
Favorable leases (amortized over the term of the leases)[2]	75.9	6.9
Goodwill	769.8	621.1
Future income tax liabilities	(425.8)	(372.0)
Liabilities for store closures[3]	(111.5)	(29.7)
Other long-term liabilities	(106.0)	(110.8)
Non-cash net assets acquired	2,491.8	2,514.5
Cash	4.3	4.2
Net assets acquired	2,496.1	2,518.7
Cash consideration and acquisition costs	2,496.1	2,518.7

(1) Include $42.6 million of assets held for sale.
(2) Net of $31.9 million of unfavorable leases.
(3) Long-term portion.

Pharmasave

During the second quarter of fiscal 2004, the Company purchased the shares of three drugstores operating in Ontario under the "Pharmasave" banner. The acquisition has been accounted for under the purchase method and the results of operations have been included in the consolidated financial statements since the acquisition date.

Purchase price allocation:

	2004 $
Net assets acquired:	
Non-cash working capital	850
Capital assets	287
Intangible assets:	
Prescription files	1,934
Non-compete agreements	577
Goodwill	1,165
Future income tax liabilities	(903)
Non-cash net assets acquired	3,910
Cash	117
Net assets acquired	4,027
Cash consideration	4,027

21. Related party transactions

The Company entered into the following transactions with enterprises controlled by shareholders or executives having a significant influence over the Company:

	2005 $	2004 $
Revenues		
Sales	6,124	15,719
Royalties	334	672
Rent	350	1,294
Sundry	147	298
	6,955	17,983

As at May 28, 2005, accounts receivable include an amount of $598,000 (May 31, 2004 – $807,000) resulting from these transactions. This amount is presented in the Company's accounts receivable. These transactions are carried out in the ordinary course of business and are measured at the exchange amount.

22. Financial instruments

Fair value

The fair value of cash and cash equivalents, temporary investments, accounts receivable, bank loans and accounts payable and accrued liabilities approximates their book value because of their forthcoming maturity.

The fair value of loans, advances and long-term receivables from franchisees was not determined, since these balances result from transactions carried out in the context of privileged commercial relationships and under terms and conditions that may differ from those that could be negotiated with non-franchisees.

The estimated fair value of other financial instruments subject to fair value disclosure is determined based on quoted market prices or interest rates for the same or similar instruments. Estimated fair value and carrying amount of those instruments are as follows:

	May 28, 2005		May 31, 2004	
	Fair value $	Carrying amount $	Fair value $	Carrying amount $
Long-term debt	2,540,307	2,561,432	192,175	192,175
Derivative financial instruments, net assets (liability) position:				
Interest rate swap agreements	945	—	(3,685)	—

22. Financial instruments (continued)

Interest rate risk

Interest rate swap agreements
The Company enters into interest rate swap agreements in order to reduce the impact of fluctuating interest rates on a portion of its long-term debt. These swaps require the periodic exchange of payments without the exchange of the notional principal amount on which the payments are based. The Company designates these interest rate swap agreements as hedges of the underlying debt. Interest expense on the debt is adjusted to include the payments made or received under the interest rate swaps designated as hedges.

These agreements are detailed as follows:

	May 28, 2005		May 31, 2004	
	$	Interest rate %	$	Interest rate %
Agreement maturing in July 2011	200,000	4.11	—	—
Agreement maturing in January 2005	—	—	185,000	4.34

Credit risk
The Company's exposure to concentrations of credit risk is limited. The non-collection risk is reduced by the fact that accounts receivable are generated by numerous customers.

Foreign currency risk
Even though the Company's reporting currency is US dollars, non-consolidated financial statements of the parent company and its subsidiaries are prepared based on their respective functional currencies, which is US dollar for US operations and Canadian dollar for Canadian operations and corporate activities.

Transactions denominated in currencies other than an entity's functional currency are translated according to the temporal method. Under this method, monetary assets and liabilities are translated at the exchange rate in effect at the balance sheet date, non-monetary assets and liabilities at their historical rates and statement of earnings items at the average monthly exchange rates. All exchange gains and losses are current in nature and are included in the consolidated statement of earnings.

For the purpose of minimizing volatility of earnings resulting from the translation of its parent company and subsidiaries monetary items denominated in currencies other than the entity's functional currency, the Company designates, since February 2005, a significant portion of its US dollar liabilities as a foreign exchange hedge of its net investment in its US subsidiaries. Accordingly, since the designation date, unrealized foreign exchange gains and losses generated by the translation of those monetary items are recorded in foreign currency translation adjustments in shareholders' equity.

Concentration
During fiscal 2005, the Company purchased approximately 87% of its branded prescription drugs for its US network from a single supplier, McKesson Corporation, with whom the Company has a long-term supply contract.

23. Supplemental cash flow information

Net changes in non-cash asset and liability items

The net changes in non-cash asset and liability items are detailed as follows:

	2005 $	2004 $ (restated)
Accounts receivable, prepaid expenses and income taxes receivable	(17,563)	4,851
Inventories	(74,429)	(35,718)
Accounts payable, accrued liabilities and income taxes payable	57,461	55,088
Other long-term assets	(8,010)	—
Other long-term liabilities	(4,738)	(1,327)
Other items	(328)	1,202
Net changes in non-cash asset and liability items	(47,607)	24,096

	2005 $	2004 $
Other information		
Interest paid	104,079	14,138
Income taxes paid	48,660	38,124

24. Comparative figures

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

25. Reconciliation of Canadian GAAP to United States GAAP

These consolidated financial statements are prepared in accordance with Canadian GAAP, which differ, in certain material respects, from generally accepted accounting principles in the United States ("US GAAP"). While the information presented below is not a comprehensive summary of all differences between Canadian GAAP and US GAAP, other differences are considered unlikely to have a significant impact on the consolidated results and shareholders' equity of the Company.

25. Reconciliation of Canadian GAAP to United States GAAP (continued)

All material differences between Canadian GAAP and US GAAP and the effect on net earnings and shareholders' equity are presented in the following tables with an explanation of the adjustments.

	2005 $	2004 $
Reconciliation of net earnings		
Net earnings – Canadian GAAP	104,378	132,683
Adjustment in respect of amortization (a)	346	(2,129)
Tax effect of above adjustment	(107)	689
Net earnings – US GAAP	104,617	131,243
Net earnings per share – US GAAP		
Basic	0.41	0.58
Diluted	0.41	0.58
Other comprehensive income items		
Cumulative translation adjustments, net of tax (c)	46,530	841
Cumulative translation adjustments on amortization, net of tax (c)	(800)	(2)
Changes in fair value of derivatives, net of tax (b)	(1,118)	(6)
Reclassification of realized gain on derivatives to the earnings (b)	2,715	4,014
Other comprehensive income items	47,327	4,847

	May 28, 2005 $	May 31, 2004 $
Statement of accumulated other comprehensive income items		
Accumulated other comprehensive income items:		
Cumulative translation adjustments, net of tax (c)	46,237	(293)
Cumulative translation adjustments on amortization, net of tax (c)	(1,441)	(641)
Cumulative changes in fair value of derivatives net of reclassification of realized gain (loss) to the earnings and net of tax (b)	(798)	(2,395)
Accumulated other comprehensive income items	43,998	(3,329)
Reconciliation of total shareholders' equity		
Shareholders' equity – Canadian GAAP	1,412,103	853,443
Adjustments in respect of:		
Amortization (a)	(12,962)	(13,308)
Tax effect of above adjustment	4,515	4,622
Cumulative translation adjustments, net of tax (c)	(46,237)	293
Accumulated other comprehensive income items (b) and (c)	43,998	(3,329)
Shareholders' equity – US GAAP	1,401,417	841,721

25. Reconciliation of Canadian GAAP to United States GAAP (continued)

The impact of differences between Canadian GAAP and US GAAP on consolidated balance sheet items is as follows:

	May 28, 2005		May 31, 2004	
	Canadian GAAP $	US GAAP $	Canadian GAAP $	US GAAP $
Consolidated balance sheets items				
Assets				
Capital assets (a)	1,492,499	1,477,334	544,174	529,888
Other long-term assets (a) and (b)	105,996	111,629	35,234	41,483
Liabilities				
Other long-term liabilities (b)	480,810	481,964	9,826	13,511
Shareholders' equity	1,412,103	1,401,417	853,443	841,721

a) Amortization

Under Canadian GAAP, the Company has used the compounded interest method to depreciate its buildings held for leasing until May 31, 2004 (Note 2b). This method is not acceptable under US GAAP. The Company records depreciation under US GAAP for its buildings held for leasing using the straight-line method at a rate of 2.5%.

b) Derivative financial instruments and hedging

On June 1, 2001, the Company adopted the provisions of SFAS 133, "Accounting for Derivative Instruments and Hedging Activities," as amended by SFAS 138, "Accounting for Certain Derivative Instruments and Certain Hedging Activities." This statement requires companies to record derivatives on the balance sheet as assets or liabilities measured at their fair value. Gains and losses resulting from changes in the values of those derivatives are accounted for depending on the use of the derivative and whether it qualifies for hedge accounting. The adoption of SFAS 133 was not material to the Company's consolidated financial statements.

The Company enters into interest swaps in order to fix the interest rate on a portion of its variable interest debt. These interest rate swaps are designated as cash flow hedges with changes in the fair value of those contracts recorded as a component of other comprehensive income items and subsequently recognized as interest on long-term debt in the period in which the hedged exposure takes place. Under Canadian GAAP, changes in fair value of those contracts are not recognized (Note 2c).

c) Foreign currency translation adjustment

Under Canadian GAAP, the Company gains and losses arising from the translation of the financial statements of the foreign currency operations are deferred in a "foreign currency translation adjustments" in shareholders' equity. Under US GAAP, foreign currency translation adjustments are presented as a component of other comprehensive income items under shareholders' equity.

25. Reconciliation of Canadian GAAP to United States GAAP (continued)

d) Changes to US accounting policies

2005

Consolidation of Variable Interest Entities
In January 2003, the Financial Accounting Standards Board ("FASB") issued Interpretation No. 46, "Consolidation of Variable Interest Entities – an Interpretation of ARB No. 51." The Interpretation addresses consolidation of variable interest entities ("VIEs") to which the usual condition for consolidation does not apply because the VIEs have no voting interests or otherwise are not subject to control through ownership of voting interests. It requires existing unconsolidated VIEs to be consolidated by their primary beneficiaries if the entities do not effectively disperse risks among parties involved. In December 2003, the FASB revised FIN 46 ("FIN 46R"), which delayed the required implementation date for periods ending after March 15, 2004. The Company was required to apply the provisions of FIN 46R effective June 1, 2004. The adoption of this interpretation had no material impact on the Company's consolidated financial statements.

2004

Derivative Instruments and Hedging Activities
In April 2003, the FASB issued SFAS No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities." The Statement amends and clarifies accounting for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities under SFAS No. 133. SFAS No. 149 is effective for contracts entered into or modified after June 30, 2003, for hedging relationships designated after June 30, 2003, and to certain preexisting contracts. The Company adopted SFAS No. 149 on July 1, 2003 on a prospective basis in accordance with the new statement. The adoption of SFAS No. 149 had no material impact on the Company's consolidated financial statements.

Accounting for Certain Financial Instruments with characteristics of both Liabilities and Equity
In May 2003, the FASB issued SFAS No. 150, "Accounting for Certain Financial Instruments with characteristics of both Liabilities and Equity." This Statement establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. SFAS No. 150 requires that an issuer classify a financial instrument that is within its scope as a liability or, in some circumstances, as an asset, with many such financial instruments having been previously classified as equity. The Company adopted SFAS No. 150 on September 1, 2003. The adoption of SFAS No. 150 had no material impact on the Company's consolidated financial statements.

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