



## **Saskatchewan Wheat Pool Inc.**

### **2005 MANAGEMENT'S DISCUSSION AND ANALYSIS**

**October 12, 2005**

Management's Discussion and Analysis was prepared based on information available to Saskatchewan Wheat Pool Inc. (the Pool) as of October 12, 2005. Management has prepared this discussion to assist readers in interpreting the Pool's financial results for the fiscal year ended July 31, 2005, and the changes in performance relative to the previous year. Management has included information to assist readers in their understanding of the industry and the markets in which the Pool operates, as well as the trends that may impact operational and financial performance into the future. Additional information on the Pool, including the Annual Information Form is available on SEDAR under the company's name at [www.sedar.com](http://www.sedar.com).

The Pool's Management's Discussion and Analysis, Consolidated Financial Statements and Notes have been prepared in accordance with Canadian generally accepted accounting principles and are presented in Canadian dollars.

#### **COMPANY OVERVIEW**

The Pool is a vertically integrated Canadian agri-business engaged in three distinct but interrelated businesses. Founded in 1924, the company serves over 70,000 western Canadian farmers and markets commodities and food products around the world. It is the largest publicly traded agri-business in the province of Saskatchewan and the second largest in Western Canada.

The Pool's core businesses are grain handling and marketing, agri-product sales and oat processing. The Pool also participates in malt processing through an affiliated company and in other commodity-related businesses through strategic alliances and supply agreements.

The Pool's fiscal year runs from August 1<sup>st</sup> to July 31<sup>st</sup> and follows the traditional crop year. The bulk of agri-product sales in each fiscal year are in the fourth quarter, which occurs in the spring and summer when the crop is planted and is maturing. For the grain business, harvest takes place in the fall and the Pool does not typically begin receiving new crop supplies until well into the first quarter. Grain movement throughout the year is dependent upon destination customer demand, the Canadian Wheat Board's export program, and producers' marketing decisions, which are driven by commodity price expectations and cash flow requirements.

#### **Business Model**

The Pool's business model is designed to optimize its position in the agri-food pipeline by connecting producers and their commodities with destination customers around the world, generating revenue at each stage of the value-added pipeline.

The pipeline begins with the producer. The Pool provides agronomic advice to producers and works with them to deliver customized agricultural solutions to support high-quality, high-yielding crops demanded in the international marketplace. The Pool sells a wide variety of specialized grains and oilseeds, along with fertilizer, crop inputs and small agricultural equipment. Through production contracts, trucking premiums, financing options and targeted marketing programs, the Pool attracts grain into its high throughput grain handling network on the Prairies where the product is cleaned, dried and blended before it is sold to the domestic or export market. The Pool markets the grain direct to end-use customers through the Pool's commodity merchandisers or through the Canadian Wheat Board (CWB), shipping the product by truck or rail. The Pool manages the

transportation and logistics requirements to the destination and is responsible for maintaining the integrity of the product while en route and in storage. For the international marketplace, the product normally moves through one of the Pool's port terminal facilities. Once the product reaches the port, the Pool may clean the commodity again. Before being loaded onto vessels, the product is graded by Canadian Grain Commission inspectors to ensure it meets the quality specifications demanded by the international marketplace.

Pool commodities can be found in food products around the world. Whether they be in breakfast cereals and snack bars sourced from the Pool's oat processor, Can-Oat Milling, or traded through strategic alliances and supply agreements with other food processing and consumer products companies internationally, the Pool develops relationships globally to secure demand for Prairie agricultural products, completing the pipeline to the consumer.

### ***Grain Handling and Marketing***

The Pool's grain handling and marketing operations includes 43 high throughput grain handling and marketing terminals and six specialty crop cleaning and handling facilities strategically located in the prime agricultural growing regions of Western Canada. It also includes two wholly owned port terminal export facilities located in Vancouver, British Columbia, and Thunder Bay, Ontario, and an ownership interest in an export facility in Prince Rupert, British Columbia.

In fiscal 2005, the Pool created a joint venture with James Richardson International Limited (JRI). JRI operates on the Prairies and at port position under the "Pioneer" brand. The Pool and JRI combined their wholly owned port terminals in Vancouver into a single operating company. The assets remain with the parent companies but the operations are run together. Located side-by-side on the North Shore, the new venture will increase the efficiency of the Port of Vancouver, reduce overall operating costs for both companies, and increase the competitiveness of Canada's export capabilities. The joint venture, which is subject to final regulatory approvals, is operating under a temporary order from the Competition Bureau.

### ***Agri-products***

The Pool's Agri-products segment operates a network of 101 retail locations throughout Western Canada, covering over 70% of the crop growing regions of the Prairies. Each facility is involved in the specialized storage and sales of bulk fertilizer, bagged seed, crop protection products and agricultural equipment, such as storage bins. Many locations also store and sell anhydrous ammonia, a cost effective form of nitrogen fertilizer. The Pool provides educational training to producers to support the safe use of this product on-farm. All facilities provide seed, soil and moisture testing services. The Pool's retail stores are staffed by individuals with agronomic and agri-business expertise and are supported by a team of professional agronomists.

The Agri-products segment also includes a research and development center at the University of Saskatchewan, the Pool's share of jointly owned affiliate Western Co-operative Fertilizers Limited (WCFL), a fertilizer wholesaler in Calgary, Alberta, and its investment in Inter-provincial Co-operative Limited, an important manufacturer and supplier of crop protection products in Canada. Through its strategic alliances with Farm Credit Canada and John Deere Credit, the Pool offers agri-products financing to Prairie producers.

### ***Agri-food Processing***

The Pool's significant interests in agri-food processing include wholly owned Can-Oat Milling, the world's largest industrial oat miller with plants in Portage la Prairie, Manitoba and Martensville, Saskatchewan, as well as 42% owned Prairie Malt Limited, one of North America's largest single-site malting plants, located at Biggar, Saskatchewan.

Can-Oat Milling has established itself as a market leader in industrial supply and is the supplier of choice for many North American food manufacturers. Can-Oat's customers are primarily North American marquee food manufacturers and consistent brand leaders in breakfast cereals, whole grain and healthy food choices. Can-Oat controls 41% of the independent oat milling capacity in North America with technology that meets or exceeds its competition. Over 90% of its production is exported to the United States.

Prairie Malt Limited is located in the heart of Canada's vast prairie region where some of the best barley in the world is grown within a one hundred kilometer radius of the plant. Prairie Malt has an annual capacity of 220,000 metric tonnes and produces top quality malt that is shipped to customers throughout Canada, the United States, the Pacific Rim, South Africa and Latin America.

### ***Discontinued Operations***

The Pool exited the hog production, feed processing and aquaculture industries in fiscal 2004. The results from these operations have been classified as discontinued operations on the Consolidated Statements of Earnings and Retained Earnings (Deficit). Readers may refer to Note 19 in the Notes to the Consolidated Financial Statements for additional information.

### **MARKET ENVIRONMENT**

#### ***Grains and Oilseeds***

Western Canada produces, on average, 53 million metric tonnes (mmt) of grains and oilseeds annually (based on the 1997-2001 average of the six major grains and oilseeds), of which 63%, or 33 mmt is available to Prairie grain handling companies to market to end-use customers or through the Canadian Wheat Board (CWB). The rest remains in Canada and is consumed domestically by food processors and feedlots.

#### **Six Major Grains: % of Average Crop**

Wheat	46%
Barley	24%
Canola	15%
Oats	7%
Peas	6%
Flax	2%

Source: Statistics Canada Production – weighted three-year average from 2003-04 to 2005-06

#### **Western Canadian Production (in millions of metric tonnes)**

<u>F1997</u>	<u>F1998</u>	<u>F1999</u>	<u>F2000</u>	<u>F2001</u>	<b>1997-01 Five Yr Avg</b>	<u>F2002</u>	<u>F2003</u>	<u>F2004</u>	<u>F2005</u>	<b>F2006* Estimate</b>
55.7	49.1	50.3	54.6	52.9	52.5	40.4	30.9	46.6	53.0	52.5
% of Avg						77%	58%	89%	101%	

Source: 1997 – 2005 data – Statistics Canada

\* October 5, 2005, Statistics Canada Estimate

Prairie production available for the 2005 fiscal year returned to pre-drought levels, after three years of dry weather hampered grain and oilseeds production across Western Canada. Fiscal 2005 crop production (harvested in the fall of 2004) totaled 53 million tonnes, in line with the five-year average in Western Canada. Heavy rain in the spring seeding period restored much needed moisture to

the land but delayed planting by as much as six weeks in some areas. As a result, when an unprecedented early frost hit in late summer, the immature plants sustained significant damage. This was followed by heavy rains, which halted harvest and caused further deterioration. The result was a poor quality crop and a shortened export period for fiscal 2005. These factors impacted fiscal 2005 results and were the primary reasons for the year-over-year earnings variance in Grain Handling and Marketing.

Seeding conditions for the 2006 crop (harvested in 2005) were ideal in Alberta and Saskatchewan with ample rains and sunshine, particularly in Saskatchewan, setting the stage for an above average crop. Manitoba farmers were not as fortunate experiencing cold, wet weather and significant flooding in some areas. For most of the summer months, crop development was normal across the Prairies and based on the October 5, 2005 Statistics Canada estimate, the 2006 crop in Western Canada will be average at 52.5 million tonnes. A larger than average crop in Saskatchewan is expected to offset the significant decline in Manitoba production, which is down 40% from the five-year average.

<b>Production Volumes: (MMT)</b>	<b>Estimate Fiscal 2006</b>	<b>Fiscal 2005</b>	<b>1997-2001 Five-Year Average</b>
Saskatchewan	29.0	26.1	26.7
Alberta	18.2	18.4	17.2
Manitoba	5.0	8.3	8.4
B.C.	0.3	0.2	0.2
Western Canada	52.5	53.0	52.5

Source: Statistics Canada October 5, 2005 Estimate

Farmers have held approximately 7.7 million tonnes of lower quality grains (average annual carry-over is approximately 5 million tonnes for the six major grains) on farm from fiscal 2005 (harvested in 2004). Given historically low prices, the Pool expects a similar carry-over level at the end of fiscal 2006.

Based on October 11, 2005 reports, harvest in Western Canada was 70 to 75% complete, with Saskatchewan at approximately 80%, Manitoba at 95% and Alberta at 60 to 70%. Wetter, cooler weather in the northern grain belt has left those regions lagging behind the southerly regions. In addition, crop quality, primarily for cereal grains being harvested in the northern areas, will experience some deterioration due to the wet weather, the extent of which won't be determined until harvest is complete. Crop quality in fiscal 2006 is still expected to be better than the previous year and based on current views, a reasonable mix of crops will be available for fiscal 2006. However, the feed grain component will be a larger portion than average as a result of weather.

Grain handling and marketing is seasonal with the strongest movement typically occurring in the August to October and May to July periods, the first and fourth quarters for the Pool.

The Canadian Wheat Board is the sole exporter of western Canadian wheat and barley (Board grains). The Pool also buys and markets for its own account, non-Board grains such as canola, oats, peas and mustard. About 60% of the Pool's total shipments are Board grains (five-year average) and this can fluctuate by as much as 10% depending on wheat and barley production and the Board's export program in any given year. Grain is classified, graded and inspected by the Canadian Grain Commission.

Grain handling companies market non-Board grains and oilseeds directly to end-use customers domestically and into the international marketplace. A significant portion of the Pool's international demand is secured through strategic alliances and supply agreements with international food processors and commodity trading firms.

**Canadian Exports (in millions of metric tonnes)  
Six Major Grains**

	<u>1997</u>	<u>1998</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>1997-2001 Five-year Average</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006 Estimate</u>
Board grains	22.6	21.9	15.6	19.8	18.4	19.7	16.5	8.9	16.7	14.8	18.0
Non-Board grains & oilseeds	4.3	4.4	5.6	5.5	6.4	5.2	4.9	3.8	6.2	5.8	7.2
	26.9	26.3	21.2	25.3	24.8	24.9	21.4	12.7	22.9	20.6	25.2

Sources: *2005 Agriculture & Agri-Food Canada September 20, 2005 Grains & Oilseeds Outlook and Pulse and Special Crops Outlook (with product exports subtracted)*

*Canadian Grain Commission, "Exports of Canadian Grain" (includes Eastern Canadian wheat exports of about 0.4 mmt)*

Exports in 2005 were approximately 83% of the five-year average despite a 12% increase in non-Board grain and oilseed exports. The CWB, which originally targeted exports at 16.3 million tonnes for fiscal 2005, was challenged with an abundance of low quality commodities and poor grain prices and achieved only 14.8 million tonnes of exports in 2005.

Exports for 2006 are currently expected to rebound with the CWB targeting a 22% year-over-year increase. Their ability to meet this target is dependent on the quality of harvested crops as the majority of their customers seek higher quality commodities. The quality of wheat and barley that is yet to be harvested is unknown but some quality deterioration is expected as a result of recent rains. Oilseeds and pulse crop quality is good to excellent and non-Board exports are expected to increase by 24% given the abundance of canola available for shipment this year.

Transportation is a significant factor in the agricultural industry because of competing demands for railcars and equipment to support Canada's exports. Over the past three years, the amount of rail capacity dedicated to grain movement has declined because of the drought-reduced crop size, together with increased demand from China and other importing nations for commodities like potash. Canadian National Railway Company and Canada Pacific Railway Limited are the primary transportation providers for Prairie farmers. With a return to normal crop production levels on the Prairies, and a larger than average crop in Saskatchewan, the agricultural industry is encouraging additional rail capacity in order to meet its export objectives in 2006.

The CWB also plays a significant role in the transportation of wheat and barley. The CWB allocates 80% of the railcars based on a formula that calculates each grain company's previous 18-week producer deliveries. The remaining 20% of the CWB sales program is put to tender where grain companies can bid on the railcars. The winning bidder has the ability to spot those cars at any location and work with area producers to source the grain just in time to maximize efficiency. In fiscal 2005, the CWB executed tenders for approximately 17% of their shipments in an attempt to capitalize on the efficiencies and cost savings available through high throughput elevators to offset overall declines in grain prices. The Pool expects tenders to return to the 20% target for the CWB export program in 2006.

**Agri-products Market**

The Agri-products industry in Western Canada is a mature market. It is made up of about 240 competitors servicing 900 locations throughout Western Canada (750 retail operations in the Pool's market area). Independent retailers, who hold about 30% of the market, together with a host of major grain handlers, sell seed, fertilizer, crop protection products and small agricultural equipment. The total market is approximately \$3.3 billion in sales, geographically distributed as follows:

(Source: Statistics Canada, May 2005 Farm Expense Report)

Saskatchewan \$1.5 billion  
 Alberta \$1.1 billion  
 Manitoba \$0.8 billion

The Pool competes in 16 market centres with effective market coverage of about \$2.2 billion. It does not operate retail stores in all areas of Manitoba and Alberta and therefore does not have access to their entire markets. Low crop prices and poor growing conditions can put pressure on volumes and margins from time to time, but in general, the industry has historically supported retail gross margins in the 15% range.

Total market acreage of about 62 million has remained essentially the same for the past five years with some growth in seed sales as a result of producers shifting from cereal grains to canola and special crops.

**Seeded Acreage – Western Canada (in millions of acres)**

	<u>All Wheat</u>	<u>Coarse Grains</u>	<u>Oilseeds</u>	<u>Special Crops</u>	<u>Total</u>
Five year average	25.5	16.5	12.9	6.7	61.6
2001	26.4	16.3	13.6	6.5	62.9
2002	26.2	15.4	11.1	7.1	59.8
2003	25.5	17.6	11.3	6.7	61.0
2004	25.0	17.4	13.5	6.2	62.1
2005	24.5	15.8	14.9	7.1	62.3
2006 estimate	23.8	14.9	15.3	6.8	60.8

Five year average 2000 to 2004

Source: Statistics Canada

Fertilizer prices can also alter buying behaviour and sales. Pricing is highly dependent upon natural gas prices. If producers believe that fertilizer (and/or natural gas) prices are on the rise they will pre-buy product in an attempt to reduce overall input costs.

While seeded acreage has been relatively stable historically, there has been growth in input usage driven by new seed technologies and varieties, new fungicides and by a shift from cereal grains to oilseeds and special crops. This growth is expected to taper off and general agri-products growth will more closely track inflation in the future.

**Western Canada Agri-Products Sales (excluding equipment)**

(\$ 000s)

	1999	2000	2001	2002	2003	2004
Saskatchewan	1,161,078	1,292,284	1,397,007	1,289,372	1,520,181	1,482,564
Alberta	923,244	965,383	1,003,613	986,383	1,047,811	1,080,632
Manitoba	591,922	617,128	676,489	689,891	759,878	764,663
Total	2,676,244	2,874,795	3,077,109	2,965,646	3,327,870	3,327,859

Source: Statistics Canada – Farm Expenses and Depreciation Charges, Agriculture Economic Statistics

The industry is highly seasonal with approximately 75% of seed, fertilizer and crop protection products sold and delivered from mid-April to the end of June in a typical year. The fall season from August to November represents about 15% of the business. The post-harvest buying period is

dependent on the weather as freezing temperatures and snowfall can bring the season to a halt and push sales into the spring. A strong fall application period can relieve some of the spring logistical requirements because fertilizer will not be reapplied in the spring, while other products such as herbicides are not affected by fall application conditions and will be applied in the spring.

### ***Oat Processing***

Canada is the third largest oat producer and the largest oat and oat product exporter in the world, representing 56% of the world's oat export trade. Total world production stands at 25 million tonnes of oats, which includes oats for feed and human consumption. Canada's oat production has remained relatively stable over the past 15 years and represents about 14% of the world's total. Over 85% of Canada's oats are produced in Western Canada, with the majority, about 65%, grown in Saskatchewan and Manitoba.

### ***World Oat Exports***

<i>Canada 56%</i>	<i>Finland 11%</i>	<i>Sweden 10%</i>
<i>Australia 9%</i>	<i>Other EU Countries 5% Other 9%</i>	

Source: Statcom Inc.

The industry has seen strong growth in North American milling demand. As a result, the percentage of total oat production that is utilized for food and industrial purposes has increased. Approximately 25% to 30% of the annual crop is milling quality, while the rest is utilized as feed. Canada consumes less than 50% of its production and exports the remainder primarily to the United States. Canada exported 1.2 mmt to the United States last year, representing approximately 78% of that country's total oat imports.

Oat milling is an attractive segment of the food ingredients market and holds a strong position in the economy. Oats are non-GMO (genetically modified organism) and are a wholesome and natural whole grain, grown and processed with very little chemical application. Oat ingredients are functionally suitable for the rapidly growing "convenience food" product categories, which is another important growth driver for the food industry. Oat demand is stable and particularly resistant to industry downturn as a result of being a very economical food source. Demand for oat ingredients has risen in 2005 reflecting consumers' switch from protein-based diets to whole grain alternatives. The Food and Drug Administration in the United States approved a health claim for oat-based products stating that the soluble fibre from oatmeal, as part of a low-saturated fat, low-cholesterol diet, may reduce the risk of heart disease. This official acceptance toward whole grain consumption has heightened consumer interest in oat-based foods. Many cereal and snack bar makers are now altering their product lines to include whole grains, a positive development for the oats industry over the long-term.

Prices for Can-Oat's human consumption sales are determined in the United States. Foreign exchange exposure is an issue that must be managed by Canadian oat millers. Can-Oat has hedging strategies in place to manage their exposure and to ensure their products remain competitively priced in the US market.

### ***The Malt Industry***

Malt, a processed form of top quality barley, is the basic ingredient used in the production of beer. Malt provides most of the complex carbohydrates and sugars, which are necessary to give beer its distinctive flavour and alcohol content. For the same reasons, malt is used in making whiskey and other distilled spirits. It is also gaining considerable popularity in the food industry as a flavouring

component and a source of nutrition. Quality, therefore, is essential. The main raw material used in the production of malt is malting quality barley.

Total world production of malt is approximately 18 million tonnes.

### **Global Malt Production**

EU	48%
China	17%
USA	11%
Canada	6%
Australia	4%
Other	14%

Source: Rabobank estimates, 2005

Global beer demand continues to grow with annual growth rates estimated at 2% per year. The main source of increased demand comes from emerging markets. This growth is attributable to increasing demand from China and Latin America, which is expected to gradually offset decreasing trade with Russia.

The CWB holds a monopoly on Canadian malting barley sales to domestic and international customers. Sales are made directly by the CWB or by Accredited Exporters of the CWB. Canadian maltsters purchase all of their malting barley from the CWB, with prices for malting barley based on North American and international market prices.

The malting industry is the largest value-added exporter of grain in Canada and the largest barley customer of the CWB purchasing over 50% of available CWB stocks annually. Between 1985 and 2001, the industry virtually tripled its malt exports to approximately 550,000 tonnes and Canada became the second largest malt exporter in the world. (source: Malting Industry Association of Canada, Third Canadian Barley Symposium)

### **KEY BUSINESS DRIVERS FOR THE POOL**

The Pool's ability to achieve success in the western Canadian agricultural industry is dependent upon key drivers.

In the grain business, volume, quality and throughput are the key profitability drivers. Volume is important because of the high fixed cost nature of the business. The more grain that flows through the Pool's pipeline, the lower the cost per tonne resulting in higher profitability. A significant portion of earnings is generated in the fourth quarter.

### **Fiscal 2005 – Quarter Ending**

	<b>October 31</b>	<b>January 31</b>	<b>April 30</b>	<b>July 31</b>
Primary shipments (mmt)	1.5	1.8	1.6	1.9
EBITDA <sup>1</sup> (\$M)	0.8	7.1	10.4	14.3
EBITDA/tonne	\$0.53 <sup>2</sup>	\$3.94	\$6.47	\$7.45

<sup>1</sup> before one-time items

<sup>2</sup> EBITDA (Earnings before interest, taxes, depreciation and amortization, provision recoveries and discontinued operations) in the first quarter of 2005 was unusually low because of the late harvest, which limited supplies required to meet sales commitments and resulted in increased premium payments and first quarter costs.

With the dominant market share in Saskatchewan, where typically over 50% of western Canadian grains and oilseeds are grown, the Pool has access to sufficient supplies to maximize both its primary capacity on the Prairies and its port terminal capacity at export. In a normal year, every 5% change in western Canadian production has approximately a \$6 million EBITDA impact to the Pool.

Quality is also an important factor that drives profitability and impacts margins in two ways. First, the higher quality the commodity, the higher the margin the Pool extracts for services it provides to move the farmer's grain to market. In addition to elevation and storage fees, the Pool charges for cleaning and drying, and for processing at port position to ensure the commodity is export ready. The Pool can also generate additional revenue from blending provided there are sufficient quantities of varying grades.

Quality can also impact volumes and shipments. For instance, the CWB has ample international demand for milling quality wheat in the top three grades and for quality malt barley for brewing. However, international demand for feed grain is limited. CWB exports depend, to some extent, on the total quality and mix of the Canadian crop, and their exports directly impact western Canadian grain handling shipments for all industry players.

The average pipeline margin per tonne (gross margin per tonne excluding other revenue and one-time items) available to the Pool assuming a normal quality mix, average production levels and regular export program is between \$20 and \$22 per tonne. A \$1 swing in margin translates into approximately \$8 million in EBITDA for the Pool.

	<u>F2003</u>	<u>F2004</u>	<u>F2005</u>
Average Annual Pipeline Margin per tonne	\$15.50	\$21.00	\$17.72

The Pool believes that its margin per tonne will improve in fiscal 2006 due to the larger Saskatchewan crop. However, the extent of that improvement will also be dependent upon the crop mix and the amount of feed grain that moves through the system in 2006.

Velocity is important in the Pool's grain handling system - that is the ability to move volume through our primary grain handling network quickly and efficiently while maintaining quality specifications. The Pool has 38% of the 100-car loading capacity, which is well ahead of the 21% held by its closest competitor. This is important because rail companies, which are responsible for moving the grain to export position, offer grain handling companies incentives for loading product onto multi-car unit trains. The Pool shares these incentives with producers to lower their costs, and to attract grain into its system in an effort to increase profitable market share.

In fiscal 2005, the Pool shipped 91% of its grain and oilseeds in 25, 50 and 100 carloads, with 74% of the grain being shipped in 50's and 100's. The key to managing the pipeline and maximizing future earnings is to target opportunities for large multi-car shipments. Rail incentives on 25 cars can be as low as \$0 per tonne, rising to \$7.00 per tonne for 100-car trains (railcars can hold about 90 tonnes of grains or oilseeds, depending on the commodity).

The Pool's western Canadian market share is 23%, up from 21% in fiscal 2004. Assuming normal industry conditions, every 1% change in market share translates into approximately \$5 million of EBITDA for the Grain Handling and Marketing segment.

In the Pool's Agri-products segment, seeded acreage is a key driver of profitability. Crop mix drives agri-product sales because commodities like wheat and barley require substantially fewer inputs than special crops and canola. The type of crops seeded each year varies depending upon commodity price forecasts and input costs. Each crop requires a different type and level of agri-products inputs and as a result margin opportunities vary.

Average input costs:

Wheat	\$40-\$60/acre
Barley	\$20-\$50/acre
Canola	\$60-\$80/acre

Canola and special crop growers typically purchase seed each year. For wheat, seed purchases are made for special varieties but farmers can re-seed regular varieties using seed from the previous harvest.

Fertilizer pricing is also a business driver for agri-products suppliers. Natural gas is a primary component of nitrogen fertilizer and as its price fluctuates so do fertilizer prices. Producers' buying behaviour, both in terms of timing and quantity, will change depending on pricing. As a result, companies must monitor pricing to secure fertilizer at the right time and be flexible with supply to ensure the demand will be there during the application periods. Weather also influences the timing and quantity of sales in this business. Farmers regularly purchase crop protection products and fertilizer in the fall and spring periods. Extremely wet or dry conditions will alter the type and quality of input purchases depending on the level of plant disease and insect infestations for crop protection products and the amount of soil moisture for fertilizer. Each 1% change in agri-products retail sales revenue results in approximately \$0.5 million in EBITDA. A 1% change in retail gross margin translates into approximately \$3 million in EBITDA.

For the oat milling business, yield is a significant factor in profitability. In an average year, it takes 1.6 tonnes of raw oats to produce one tonne of oat ingredients. The quality of raw oats has the most significant impact on yield. Yields typically range from 1.6 tonnes to 1.7 tonnes. Oat varieties, soil conditions and farm practices can have a significant impact on quality and on a number of characteristics which are required to meet specifications defined by select customers. Every new crop has its own characteristics and milling adjustments are typically required to attain the best yield.

Oats are priced in US dollars and are predominantly driven by the world feed grain market. The price of finished goods moves up and down with the price of oats. A strong Canadian dollar can create foreign exchange challenges and hedging practices are important to protect margins and ensure that Canadian product remains competitive with American millers.

In the malt business, reliable quality is a key factor in maintaining sales with international customers. Only high quality malt barley is selected for the malting process so crop quality issues can affect supply and increase production costs. Based on initial views of the trade as of September 30, 2005, the amount of malt barley that may be selected for malting purposes in 2006 is in the range of 70% to 80% of average. These estimates could improve or decline by the end of harvest depending on quality tests on the remaining malt barley that is still in the fields.

Energy consumption, labour, and yield maximization (the amount of malt produced from a tonne of barley) are also key production drivers for Prairie Malt. Natural gas is an important element and rising prices can significantly impact margins. In addition, because sales are priced in US dollars, a strengthening Canadian dollar can affect earnings. Prairie Malt reduces the impact of foreign currency fluctuations by engaging in hedging activities.

### ***STRATEGIC FOCUS***

Fiscal 2005 was an important year for the Pool. The Pool implemented a Recapitalization that allowed the company to change its corporate structure, redesign its share structure, reduce debt and enhance corporate governance. In February of 2005, the Pool announced a multi-step approach that resulted in:

- The Pool continuing as a Canada Business Corporation effective March 31, 2005.
- Issuing a single class of common voting shares to Class A shareholders (The Pool's farm members under the previous co-operative structure), to Class B shareholders and to holders of the Pool's Convertible Subordinated Notes.
- At the same time, the Pool changed its governance structure to more closely align Board representation with the economic interest of its entire shareholder base. The Board of Directors is made up of:
  - five farmer-directors (previously eight) all of whom have previous board experience with the Pool and bring valuable agricultural expertise and customer intelligence to the Board;
  - six directors (previously four) from the business community with expertise in the areas of finance, accounting, law and corporate governance; and
  - the Chief Executive Officer (not previously on the Board).

Following the Recapitalization:

- the Pool completed a \$150 million rights offering;
- the rights offering was substantially oversubscribed; and
- after costs associated with the rights offering, the Pool raised \$142 million in net proceeds. The Pool repaid its \$100 million term loan and used the remaining proceeds to support working capital.

With renewed balance sheet strength, the Pool has sufficient funds available and financial flexibility to maximize operational opportunities, a factor that has restored customer confidence and allowed the Pool to increase sales and market share in 2005. The Pool is now in a position to more adequately absorb the impact of adverse weather-related issues.

As the Pool looks to the future, management recognizes that with normal crops, the Pool can produce healthy cash flow. The Board of Directors and the management team are assessing the appropriate use of cash with a view to shareholder value, managed growth and risk mitigation.

The Pool believes there are opportunities to grow its core business organically through customer expansion strategies, regional acquisitions, joint ventures and alliances. The Pool's joint venture with James Richardson International at the Vancouver port is an example of how alliances and partnerships can create additional industry efficiencies, improve competitiveness and productivity without adding additional capacity.

The Pool also believes in Can-Oat's potential and is currently assessing strategies to expand their product offerings, customer base and capacity utilization. Can-Oat's reputation for quality and service, together with its consistent bottom line performance, illustrates how value-added processing, managed strategically, can succeed on the Prairies.

With excess capacity still present across Western Canada in the primary grain handling system and in the agri-products industry, consolidation is key if the industry is to be healthy for the long-term. The Pool will continue to encourage consolidation. This will be accomplished by working with industry players, governments and regulatory bodies to implement economic and regulatory policies that encourage efficiency, support de-regulation and provide a fair and equitable marketplace for all participants. Farmers will benefit from the increased efficiency and lower cost industry structure thereby improving their on-farm profitability.

The Pool will also focus on its farming customers by developing customized solutions, program bundles and marketing packages that improve their on-farm efficiency and cash flow. Through the newly established Western Farm Leadership Co-operative Ltd., which is in the process of being incorporated, the Pool will team with select farm leaders throughout Western Canada to provide training and growth opportunities that not only support their individual operations, but also the rural communities in which the Pool operates.

Quality and food safety continues to be a strong focus for the Pool. In fiscal 2005, the Pool successfully certified 41 of its grain handling facilities on the Prairies and two port terminal operations to internationally recognized food handling and safety standards, known as ISO 9001:2000 (International Organization for Standardization). Virtually all Pool grain facilities are now certified and the Pool employs HACCP (Hazard Analysis Critical Control Point) policies and procedures to illustrate its ongoing commitment to food safety and security.

Can-Oat elevated its quality measurements in 2005 through the American Institute of Baking (AIB), which audits sanitation and food safety practices in the milling industry. Can-Oat requested that the AIB conduct an unannounced audit. Can-Oat received a superior rating and is the first company within their industry to participate in an unplanned audit process. This commitment to quality is at the heart of the Pool and its affiliates and will continue to be a focus for the company into the future.

The Pool expects that demand for identity preservation of the crop from farm-gate through the pipeline and the ability to trace commodities throughout the cycle will become more and more important to domestic and international customers. Its high throughput grain handling terminals already have the ability to segregate products within the system. The Pool has developed information systems that track the needed intelligence on cropping patterns, chemical use, yields and quality to support future traceability programs. The Pool's ability to anticipate future consumer trends, food choices and information needs and develop required solutions in advance is a key thrust and the foundation for its strategic growth going forward.

Finally, the Pool, over the coming months, will look at options to reduce its overall cost of borrowing and further improve financial flexibility and balance sheet strength. The Pool has \$150 million of Senior Subordinated Notes outstanding that currently pay 12% interest annually. The Pool is exploring various options to reduce its overall interest costs in 2006, including options with respect to these outstanding Notes.

## **SELECTED CONSOLIDATED FINANCIAL INFORMATION**

### **ANNUAL:**

#### **Income Statement Data**

(in millions) <sup>1</sup>	<u>Year Ended July 31, 2005</u>	<u>Year Ended July 31, 2004<sup>3</sup></u>	<u>Six Months Ended July, 31 2003<sup>3</sup> (restated) Post- reorganization</u>	<u>Six Months Ended January, 2003<sup>3,5</sup> (restated) Pre- reorganization</u>
Sales and Other Operating Revenues	\$1,385.7	\$1,407.3	\$653.0	\$687.5
Net income (loss) from continuing operations	7.0	17.9	(9.1)	(30.6)
Net recovery (loss) from discontinued operations	5.1	(12.9)	(6.8)	(3.9)
Net income (loss)	<u>12.1</u>	<u>5.0</u>	<u>(15.9)</u>	<u>(34.5)</u>
Earnings (loss) per common share (EPS):				
From continuing operations, prior to accretion and inducement premium	0.25	1.74	(1.83)	(16.34)
From discontinued operations	0.18	(1.25)	(1.36)	(2.06)
From continuing operations, after accretion and inducement premium				
- Basic and diluted <sup>2</sup>	<u>(1.44)<sup>4</sup></u>	<u>(0.18)</u>	<u>(4.12)</u>	<u>(16.34)</u>
Total EPS – earnings (loss)				
- Basic and diluted <sup>2</sup>	<u>(1.26)</u>	<u>(1.43)</u>	<u>(5.48)</u>	<u>(18.40)</u>

- 1 In millions except earnings per share data.
- 2 There is no dilutive effect from the exercise of options related to stock option plans or the Convertible Subordinated Notes because it would be anti-dilutive.
- 3 Periods ending prior to March 31, 2005, are restated to reflect the one for 20 share consolidation that was part of the March 31, 2005 Recapitalization (further information is provided in the July 31, 2005 Notes to the Consolidated Financial Statements – Note 16).
- 4 The net loss per share for fiscal 2005 reflects non-cash charges to retained earnings of \$13.7 million for the accretion of the equity component of the Convertible Subordinated Notes and a share capital inducement premium of \$33.8 million for Convertible Subordinated Noteholders as part of the Pool's Recapitalization initiative. Holders of the Convertible Subordinated Notes received a premium on their conversion rate (3.5 million of additional shares valued at \$33.8 million) as an inducement to convert their Notes on March 31, 2005.
- 5 The selected income statement data for the six months ended January 31, 2003 does not reflect the effects of the financial reorganization that became effective on January 31, 2003 or the application of fresh start accounting and as a result are not comparable to the income statement data for the subsequent financial periods shown.

Sales and operating revenues reflect the contributions of the Pool's three core businesses along with sales from the Pool's subsidiaries and joint ventures, proportionately consolidated based on the Pool's ownership position. Non-Board grain and oilseed prices have been trending downward since 2003, contributing to lower sales prices in each of the past three years. Grain shipments and agri-product sales, on the other hand, have improved each year as crop production and growing conditions normalized after three years of drought that began in late 2001. For Agri-food Processing, sales dipped in fiscal 2004 relative to 2003 because of lower commodity prices and a temporary reduction in demand due to the low carbohydrate trend in that year. Demand and sales from this segment strengthened in 2005 as consumer products companies began marketing the benefits of whole grain oat products.

The net income (loss) from continuing operations recovered in 2004 after a difficult 2003 fiscal year when production levels were nearly cut in half and crop quality was poor because of drought conditions. The 2004 production (harvested in the fall of 2003) was approximately 88.8% of the five-year, pre-drought average and the quality was good allowing exports to increase by 80.3% year-over-year and pipeline margins per tonne (gross margin excluding other revenue and one-time items) of grain to increase from \$15.50 to \$21.00 on average. In 2005, production (harvested in the fall of 2004) normalized to the five-year pre-drought average allowing for additional shipments. However, wet cold weather and an unprecedented early frost impacted crop quality and reduced exports for the year. Grain margins for fiscal 2005 averaged \$17.72 as a result.

With respect to discontinued operations, the Pool exited these businesses and divested of the assets in 2004 after several difficult years and mounting losses from its investments in hog production, feed processing and aquaculture businesses. In 2004, the Pool recorded a net loss from discontinued operations of \$12.9 million. This after-tax loss consisted of a \$9.0 million loss on divestiture and \$3.9 million in operating losses. The 2005 after-tax recovery from discontinued operations was \$5.1 million, including a \$3.8 million recovery related to filings under the Canadian Agricultural Income Stabilization Program (a federal provincial risk management program also known as CAIS), as well as a partial recovery of \$0.9 million from the loss on divestiture booked in 2004. The recovery on CAIS represents a portion of the operating losses incurred by discontinued operations in prior years.

The earnings per share calculations over the last three years reflect a number of events:

- The number of shares outstanding grew from 111.7 million shares at July 31, 2003 to 232.2 million shares at the end of July 2004, as holders of the Pool's Convertible Subordinated Notes chose to convert their notes into Class B non-voting shares.
- The per share amounts in 2003, 2004 and up to March 31, 2005, also include accretion that was charged against retained earnings. When the Convertible Subordinated Notes were first issued they were recorded on the balance sheet at their market value at the time, as required by accounting rules. Each quarter, the Pool would accrete a portion of the difference between the market value and face value of notes against retained earnings.

- On March 31, 2005, the Pool exchanged all outstanding Class B non-voting shares with common shares at a rate of one for 20. Convertible noteholders were asked to convert early and received a premium of 3.5 million additional shares to do so. The number of shares outstanding as a result of the Recapitalization was 35.1 million.
- In May 2005, the Pool issued a rights offering raising gross proceeds of \$150.1 million. An additional 46.8 million shares were issued. The total number of shares outstanding as at July 31, 2005 was 81.8 million.

### **Balance Sheet Data**

(in millions)	As at July 31, 2005	As at July 31, 2004	As at July 31, 2003
Total assets	\$721.9	\$683.4	\$787.8
Total long-term liabilities	\$189.9	\$298.9	\$322.0
Dividends paid per share	\$ -	\$ -	\$ -

The Pool's total long-term liabilities declined substantially as at July 31, 2005, as a result of the Recapitalization and rights offering that raised \$142.3 million in net proceeds. The Pool used \$100.0 million to retire long-term debt and the remaining proceeds were used to support ongoing working capital requirements.

The Pool did not pay dividends in the years listed above. Under the terms of its credit facility, the Pool cannot pay dividends on its shares without prior approval from its principal lenders.

### **SELECTED QUARTERLY FINANCIAL INFORMATION:**

#### **QUARTERLY:**

<b>Fiscal 2005</b> (in millions except for per share data)	<b>October 31</b>	<b>January 31</b>	<b>April 30</b>	<b>July 31</b>	<b>Total</b>
Sales and Other Operating Revenues	\$ 229	\$ 322	\$ 288	\$ 547	\$ 1,386
Net income (loss) from continuing operations	(15.6)	(0.9)	(2.1)	25.6	7.0
Net income (loss) from discontinued operations	-	-	1.2	3.9	5.1
Net income (loss)	\$ (15.6)	\$ (0.9)	\$ (0.9)	\$ 29.5	\$ 12.1
Earnings (loss) per common share:					
Prior to accretion from continuing operations	\$ (1.30)	\$ (0.07)	\$ (0.11)	\$ 0.38	\$ 0.25
After accretion					
From continuing operations	\$ (1.72)	\$ (0.50)	\$ (1.98)	\$ 0.38	\$ (1.44)
From discontinued operations	-	-	\$ 0.06	\$ 0.06	\$ 0.18
Earnings (loss) per common share	\$ (1.72)	\$ (0.50)	\$ (1.92)	\$ 0.44	\$ (1.26)
Diluted earnings (loss) per common share	\$ (1.72)	\$ (0.50)	\$ (1.92)	\$ 0.44	\$ (1.26)

<b>Fiscal 2004</b> (in millions except for per share data)	<b>October 31</b>	<b>January 31</b>	<b>April 30</b>	<b>July 31</b>	<b>Total</b>
Sales and Other Operating Revenues	\$ 284	\$ 326	\$ 255	\$ 542	\$ 1,407
Net income (loss) from continuing operations	\$ (7.1)	\$ 9.5	\$ (4.8)	\$ 20.3	\$ 17.9
Net income (loss) from discontinued operations	\$ (2.7)	\$ (14.3)	\$ (4.3)	\$ 8.4	\$ (12.9)
Net income (loss)	\$ (9.8)	\$ (4.8)	\$ (9.1)	\$ 28.7	\$ 5.0
Earnings (loss) per common share (restated (a)):					
Prior to accretion from continuing operations	\$ (0.80)	\$ 0.97	\$ (0.43)	\$ 1.76	\$ 1.74
After accretion					

From continuing operations	\$ (1.37)	\$ 0.45	\$ (0.87)	\$ 1.34	\$ (0.18)
From discontinued operations	\$ (0.30)	\$ (1.45)	\$ (0.39)	\$ 0.73	\$ (1.25)
Earnings (loss) per common share	\$ (1.67)	\$ (1.00)	\$ (1.26)	\$ 2.07	\$ (1.43)
Diluted earnings (loss) per common share	\$ (1.67)	\$ (1.00)	\$ (1.26)	\$ 0.92	\$ (1.43)

(a) For periods prior to April 30, 2005, earnings per share has been restated to reflect the one for 20 share consolidation that was part of the March 31, 2005 conversion process.

The Pool's sales and other operating revenues are seasonal, with the largest percentage of sales occurring in the fourth quarter (May to July period), when the majority of the Pool's agri-products are sold and producers ship grain to free up on-farm storage for the following harvest. In general, the primary variances between the quarterly sales in 2005 versus 2004 are the result of:

- higher grain shipments in 2005 reflecting normal production levels and an increase in the Pool's western Canadian market share from 21% in fiscal 2004 to 23%,
- lower non-Board grain prices in 2005 versus 2004,
- higher agri-products sales in 2005 reflecting strong producer demand for crop inputs, particularly fertilizer, and
- higher sales from the Agri-food Processing segment resulting from increased sales of finished whole oat products through Can-Oat Milling.

Earnings from continuing operations primarily reflect lower grain margins this year in the Grain Handling and Marketing segment resulting from poor quality crops that limited Canadian Wheat Board shipments and higher costs resulting from premiums paid in the first half of 2005 because of the late harvest, which limited supplies required to meet sales commitments.

### **SUMMARY OF CONSOLIDATED RESULTS**

Readers should refer to the following chart that summarizes one-time items included in fiscal 2005 and 2004 when comparing the operating results in both years.

<b>Saskatchewan Wheat Pool Inc.</b>					
<b>One-time Items – Summary</b>					
<b>Fiscal 2005</b> (in millions of \$)	<b>October 31</b>	<b>January 31</b>	<b>April 30</b>	<b>July 31</b>	<b>Total</b>
Grain	0.7	0.9	0.0	2.9	4.5
Corporate	0.0	0.0	0.0	0.0	0.0
Total one-time items in EBITDA	0.7	0.9	0.0	2.9	4.5
Total one-time items in EBIT	0.7	0.9	0.0	2.9	4.5
Tax recoveries	0.7	0.7	0.0	0.0	1.4
Tax impact of one-time items	(0.1)	(0.1)	0.0	(0.3)	(0.5)
Total tax impact	0.6	0.6	0.0	(0.3)	0.9
Total one-time items in earnings (loss) from continuing operations	1.3	1.5	0.0	2.6	5.4
	(a)	(b)		(c)	
<b>Fiscal 2004</b> (in millions of \$)	<b>October 31</b>	<b>January 31</b>	<b>Apr 30</b>	<b>July 31</b>	<b>Total</b>
Grain	0.0	6.5	0.0	3.5	10.0
Corporate	0.0	0.6	1.6	(0.6)	1.6
Total one-time items in EBITDA	0.0	7.1	1.6	2.9	11.6
Provisions	0.0	0.0	0.0	6.2	6.2
Total one-time items in EBIT	0.0	7.1	1.6	9.1	17.8
Tax recoveries	0.0	2.6	0.0	0.0	2.6
Tax impact of one-time items	0.0	(2.6)	(3.2)	(1.2)	(7.0)
Total tax impact	0.0	0.0	(3.2)	(1.2)	(4.4)
Total one-time items in earnings (loss) from continuing operations	0.0	7.1	(1.6)	7.9	13.4
		(d)	(e)	(f)	

One-time items primarily include:

- (a) Ontario capital tax refund
- (b) Settlement of a property tax dispute and receipt of a research and development investment tax credit
- (c) Interest income on corporate income tax refunds
- (d) Property taxes rebate and interest income on corporate income tax refund
- (e) Capital refund net of income taxes
- (f) Recovery from sale of interest in Mexican terminal

Fiscal 2005 consolidated sales and other operating revenues were \$1.39 billion, down \$21.6 million from the \$1.41 billion generated in the previous year. Sales through the Agri-products segment were up 11.8% year-over-year. Agri-food Processing sales grew 7.1% and Grain Handling and Marketing increased shipments by 7.2%. The year-over-year variance reflects lower commodity prices for non-Board grains and oilseeds, which were down on average 19.0% compared to 2004 levels. This impacted the value of consolidated sales for the Grain Handling and Marketing segment. However, it is important to note that the key earnings drivers in that business are volume, exports and crop quality as opposed to commodity prices.

Selling and administrative expenses for fiscal 2005 were \$54.7 million, which compares to \$52.4 million in fiscal 2004. The primary reason for the variance is related to \$2.4 million in capital taxes that the Pool is now required to pay as a result of becoming a Canada Business Corporation in 2005.

The Pool generated \$70.5 million in EBITDA for 2005, which compares to \$87.3 million in fiscal 2004. The decline was the direct result of crop quality issues and a late harvest that limited supplies of quality commodities in the first quarter of fiscal 2005. Crop production available for fiscal 2005 was average in size but quality was well below average because of an early frost that hit at a critical time in the growing cycle followed by substantial rains during the harvest period that further reduced the value of the crop. As a result of these two events, a significant portion of the grain that was available to handlers was feed quality. Typically, approximately 10% of the wheat grown in Western Canada is feed. Over 45% of Saskatchewan's wheat crop graded as feed in fiscal 2005. Margins are lower on feed wheat because it is not cleaned, dried or blended and is typically consumed domestically as opposed to moving into the export market. Limited export opportunities for feed grains challenged the Canadian Wheat Board in fiscal 2005 and, as a result, the Board was only able to secure 14.8 million tonnes of export sales on a target of 16.3 million tonnes for the year.

Despite the challenges in the Grain Handling and Marketing segment, the Pool's Agri-products and Agri-food Processing segments had strong results, generating EBITDA of \$39.3 million and \$16.4 million respectively. For the Agri-products segment, this represented a 22.6% increase over fiscal 2004 results and for Agri-food Processing, a 15.2% increase. Grain Handling and Marketing EBITDA, excluding one-time items, was down approximately \$17.0 million on a full year basis as a result of the quality factors previously mentioned.

Amortization for the twelve months was \$26.5 million compared to \$24.6 million for property, plant and equipment and certain other long-term assets. Increased amortization year-over-year is reflective of ongoing investment in property, plant and equipment.

Corporate costs for fiscal 2005 were \$22.3 million, which compares to \$18.6 million in the prior year. The primary reason for the increase is related to \$2.4 million in Saskatchewan capital taxes that the Pool is now required to pay as a result of becoming a Canadian Business Corporation in 2005. In addition, in 2004, the Pool received a \$1.6 million one-time capital refund related to one of its investments that reduced corporate costs in that year.

Interest expense for the year totaled \$37.1 million down from \$39.1 million in 2004. Cash interest expense was \$21.7 million in 2005, which is down \$6.9 million or 24.1% from 2004. The lower cash costs primarily reflect a reduction in short-term borrowings because of lower grain commodity prices year-over-year, in conjunction with the repayment of \$100.0 million of term debt in June of 2005. The \$15.4 million non-cash component included:

- seven months of accretion related to the debt component of Convertible Subordinated Notes that were retired effective March 31, 2005;
- \$3.9 million of financing costs that were incurred during the year and written off in the fourth quarter when the Pool repaid its \$100.0 million term loan;
- a full year of accretion related to the company's Senior Subordinated Notes; and
- approximately \$1.0 million related to the amortization of deferred financing costs. The un-amortized balance of \$4.1 million at July 31, 2005, will be recognized as a charge to interest expense over the remaining life of the Pool's operating lines, which mature March 2008.

Last year, the Pool's non-cash interest expense was \$10.5 million.

The Pool recorded earnings before interest and taxes (EBIT) of \$44.1 million in fiscal 2005 and \$69.0 million in 2004. Excluding one-time items in both years, EBIT was \$39.6 million this year compared to \$51.1 million in 2004.

Earnings from continuing operations for the twelve-month period ended July 31, 2005 was \$7.0 million compared to \$17.9 million in 2004. The Pool recovered approximately \$5.1 million from discontinued operations in 2005. In 2004, the Pool recorded a \$12.9 million loss from discontinued operations associated with its investments in hog production, aquaculture and feed mill operations.

On a net income basis, Saskatchewan Wheat Pool earned \$12.1 million in fiscal 2005 up from \$5.0 million a year earlier. Earnings per share information is summarized below:

### ***Earnings Per Share***

	Year ended July 31, 2005	Year ended July 31, 2004
Weighted average shares outstanding (M)	28,103	10,333
Diluted weighted average shares outstanding (M)	28,103	10,333
EPS from continuing operations prior to accretion and inducement premium	0.25	1.74
EPS from discontinued operations after accretion	0.18	(1.25)
EPS from continuing operations after accretion and inducement premium		
- Basic	(1.44)	(0.18)
- Diluted	(1.44)	(0.18)
Total EPS – earnings (loss)		
- Basic	(1.26) <sup>1</sup>	(1.43)
- Diluted	(1.26)	(1.43)

- 1 The net loss per share for 2005 reflects non-cash charges to retained earnings of \$13.7 million for the accretion of the equity component of the Convertible Subordinated Notes and a share capital inducement premium of \$33.8 million for Convertible Subordinated Noteholders as part of the Pool's Recapitalization initiative. Noteholders received a premium on their conversion rate (3.5 million of additional shares valued at \$33.8 million) as an inducement to convert their Notes on March 31, 2005.

### ***Grain Handling and Marketing Segment***

The Pool shipped 6.9 million tonnes of grains and oilseed in fiscal 2005, up 7.2% over 2004. A larger crop in Saskatchewan coupled with strong producer deliveries more than offset an 11.4% decrease in Canadian Wheat Board exports year-over-year. Approximately 63.7% of Pool shipments for the twelve months were Board grains, which was on par with fiscal 2004. However, CWB shipments dropped off in the final quarter of the year (62.0% in f2005's Q4 versus 69.5% in f2004's Q4) reflecting the significant marketing challenges the CWB faced in securing feed grain sales into the international marketplace.

Port terminal volumes improved by approximately 8.4% year-over-year despite these export challenges. Market share gains across the Prairies supported port terminal volumes as producer

confidence grew and deliveries into the primary system increased. The Pool's fiscal 2005 western Canadian market share grew to 23% for the year, a 9.9% or two point increase year-over-year. The Pool realized market share gains in all three Prairie provinces, with the largest gain being recorded in Saskatchewan.

#### **Twelve-Month Volumes (000's)**

	<b>F2005</b>	<b>F2004</b>	<b>Increase</b>
Primary Elevator Receipts	<b>6,813</b>	<b>6,170</b>	<b>10%</b>
Primary Elevator Shipments			
Board grains	4,363	4,101	6%
Non-Board grains & oilseeds	2,490	2,290	9%
<b>Total Primary Elevator Shipments</b>	<b>6,853</b>	<b>6,391</b>	<b>7%</b>
Terminal Operations			
Vancouver	2,641	2,571	3%
Thunder Bay	1,493	1,286	16%
Share of Affiliates	715	615	16%
<b>Total Terminal Operations</b>	<b>4,849</b>	<b>4,472</b>	<b>8%</b>

Pipeline margins (gross margin per tonne excluding other revenues and one-time items) in the Grain Handling and Marketing segment averaged \$17.72 per tonne for the year, in line with management's expectations, but below the \$21.00 achieved in fiscal 2004. The decline is related to two key factors. Feed grains represented approximately 27.0% of the Pool shipments in 2005, which is unusually high and compares to approximately 10.0% in fiscal 2004. In addition, because of significant harvest delays in the fall of 2004, the Pool was required to pay premiums to source quality commodities off-farm and incur additional shipping costs due to the temporary lack of supply during that period.

EBITDA for the twelve months was \$37.1 million (\$32.6 million net of one-time items) compared to \$59.7 million (\$49.7 million after one-time items) in fiscal 2004 with the decline directly related to weather events. EBIT was \$25.8 million in fiscal 2005 (\$21.3 million net of one-time items) versus \$50.8 million in 2004 (\$39.8 million net of one time items).

#### ***Agri-products Segment***

The Pool's Agri-products segment had a strong year. Growing conditions in the spring supported strong sales of all major product lines. Sales totaled \$514.2 million for the segment, up \$54.3 million or 11.8% from the \$459.9 million in sales generated in fiscal 2004. The Pool's retail operations generated sales growth of 8.4% year-over-year. Fertilizer sales grew 9.3%, seed sales were up 13.0% and crop protection products improved by 2.7%. Crop protection products and fertilizer represented 84.0% of the Pool's fiscal 2005 retail sales, on par with the previous year. Sales through WCFL were also strong, up 24.3% year-over-year reflecting both volume increases due to strong demand and higher overall pricing year-over-year.

EBITDA from this segment for the year was \$39.3 million and \$32.0 million in 2004. Despite a highly competitive market that pressured retail margins, strong demand and good growing conditions, coupled with disciplined marketing strategies drove the earnings improvement in 2005. Segment EBIT for the twelve months ended July 31, 2005 was \$29.3 million, up from \$22.4 million for fiscal 2004.

#### ***Agri-food Processing Segment***

Sales from the Agri-food Processing segment totaled \$118.5 million compared to \$110.6 million in 2004. Sales for Prairie Malt were up 8.0% year-over-year due to general market improvements and solid customer demand. At Can-Oat Milling, sales were 6.8% higher than 2004 reflecting a 15.3%

increase in sales volumes and a 7.4% decrease in sales prices. Can-Oat's sales mix changed relative to fiscal 2004. Sales of finished oat products were 72.6% of the mix last year, while in 2005 they represented over 77.1% of the total sales mix. Feed sales represented only 1.3% of sales volumes in 2005 versus 4.4% in fiscal 2004.

EBITDA from the Agri-food Processing segment for the year was \$16.5 million compared to \$14.3 million in 2004. Despite competitive pressures and the impact of the strong Canadian dollar on Can-Oat margins, strong demand for whole grain oat products led to EBITDA improvement of 10.7% year-over year. Prairie Malt also experienced strong earnings for the year. Sales volumes were up 21.3% over last year as a result of a plant shutdown in 2004 to allow for repairs and maintenance. Segment EBIT was \$11.3 million for the twelve months ended July 31, 2005 and \$9.2 million in fiscal 2004.

## **LIQUIDITY AND CAPITAL RESOURCES**

A number of developments occurred during the year ending July 31, 2005, which significantly improved the Pool's financial position and liquidity. These developments are summarized below and should be read in conjunction with the Notes to the Consolidated Financial Statements. They include:

- a new three year \$250.0 million revolving asset based loan facility which replaced an existing facility;
- \$100.0 million of Senior Secured Notes that were issued with \$78.7 million of the proceeds used to retire existing bank term debt;
- the Recapitalization, which included the issuance of new common voting shares to Class A and Class B shareholders and the exchange of \$171.7 million of Convertible Subordinated Notes into new common voting shares;
- receipt of net proceeds of \$142.3 million from a rights offering to Common Shareholders, and
- the repayment of the \$100.0 million of Senior Secured Notes from the proceeds of the rights offering.

The significant impact these transactions had on the Pool's shareholders' equity and long-term debt is illustrated below.

### **Impact of Significant Developments**

	<u>Date</u>	<u>Common Shares Outstanding</u>	<u>Shareholders' Equity</u>	<u>Long-term Debt (including portion due in one year)</u>
(in \$millions except for common shares)				
Balance at July 31, 2004		-	\$191	\$260
<b>Refinancing</b>				
Issuance of Senior Secured Notes	March 14, 2005			100
Repayment of Senior Secured Bank Term Loan	March 14, 2005			(79)
<b>Recapitalization</b>				
Conversion to Common Voting Shares				
Class A shares (1)	March 31, 2005	182,371	1	
Class B shares (2)	March 31, 2005	12,297,457		
Convertible Subordinated Notes (3)	March 31, 2005	22,591,731	31	(31)
Share Recapitalization costs			(13)	
<b>Rights Offering</b>				
Proceeds of rights offering	May 27, 2005	46,762,078	150	
Repayment of Senior Secured Notes	June 7, 2005			(100)

<b>Other</b>			
Net earnings		12	
Repayment of other debt			(7)
Accretion			11
Common Share stock options exercised	500		
Future income tax adjustments to retained earnings		9	
<hr/>			
Balance at July 31, 2005	81,834,137	\$381	\$154

- (1) 3.62 new Common shares for each \$25 Class A share held  
(2) one new Common share for each 20 Class B Shares held  
(3) 131.6 common shares for each \$1,000 principal

### **Key Financial Ratios**

	<u>2005</u>	<u>2004</u>
Current ratio	2.31	1.59
- current assets/current liabilities		
Total debt to equity	33:67	61:39
- total interest bearing debt/(total interest bearing debt + equity)		
Long-term debt to equity	29:71	58:42
-long-term debt/(long-term debt + equity)		

The improvement in financial ratios was primarily due to the Recapitalization and the rights offering.

### **Debt Ratings**

The following debt ratings were assigned by Dominion Bond Rating Services (DBRS) and Standard and Poors (NR means not rated):

<b>Rating Agency</b>	<b>Corporate Rating</b>	<b>Bank Debt</b>	<b>Senior Note</b>
DBRS	B high	NR	B
Standard & Poor's	B stable	BB-	CCC+

### **Revolving Asset Based Loan Facility**

The \$250.0 million revolving asset based loan facility is utilized at various times during the year to finance the Pool's operating requirements, which primarily consist of grain and agri-product inventory purchases and financing of accounts receivable from the Canadian Wheat Board and other trade accounts.

There were no cash drawings on the Pool's operating loan facilities at either July 31, 2005 or July 31, 2004. Short-term investments of \$29.0 million at July 31, 2005 supplemented by draws on the revolving asset based loan facility will be used for purchases of non-Board grain inventories and for working capital as Canadian Wheat Board receivables increase through the fall harvest period.

The facility is also used to post letters of credit and similar instruments related to operating an agri-business. These instruments effectively reduce the amount of cash that can be drawn on the revolving asset based loan facility.

The facility is secured by a first charge on inventory and accounts receivable and a second charge on all other assets of the company. Interest is payable monthly at a floating rate of bank prime plus 1.5%.

Certain of the Pool's subsidiaries and joint ventures have their own bank operating debt and long-term debt facilities. The company does not guarantee, nor does it have responsibility for the repayment of the subsidiaries' or joint ventures' loans.

**Selected Working Capital Changes**

	2005	2004	Change
	(in millions)		
Inventories:			
Non- Board grain	\$58	\$ 32	\$26
Agri-products	48	59	(11)
Agri-food processing	11	14	(3)
	117	105	12
Accounts receivable:			
Trade accounts, net	\$60	\$ 74	\$(14)
Canadian Wheat Board	48	71	(23)
Other accounts	19	19	-
	127	164	(37)
Prepaid expenses and deposits	21	10	11
Accounts payable and accrued liabilities	(115)	(151)	36
Total change in selected balance sheet items	\$150	\$ 128	\$22

The value of non-Board grain inventories increased year-over-year as the tonnes on hand were higher than at July 31, 2004. This increase was mitigated by a decrease in the average price per tonne.

The decrease in accounts receivable is due primarily to lower prices and volumes of grain held on behalf of the CWB and lower commercial grain receivables.

An improved working capital position allowed the Pool to place a \$10.0 million security deposit with the Canadian Grain Commission in lieu of a \$10.0 million letter of credit and resulted in increased prepaid expenses and deposits.

Accounts payable and accrued liabilities are lower primarily due to a \$17.0 million decrease in deferred cash tickets reflecting lower average prices per tonne as well as a reduction in the tonnes deferred for payment. This was accompanied by a decrease in general accounts payable and accrued liabilities of \$18.4 million due primarily to reduced agri-product inventory purchases.

**Cash Flow Information**

Cash flow from continuing operations was \$46.7 million for the year ending July 31, 2005 compared to \$58.5 million for the year ending July 31, 2004. Reduced cash flow from Grain Handling and Marketing was partially offset by improved results from both the Agri-products and Agri-food Processing.

Capital expenditures were \$12.9 million for the year ended July 31, 2005 with approximately 69.6% of the capital spending focused on Pool assets including \$3.2 million targeted to the Vancouver port terminal operation. Capital expenditures for fiscal 2006 are estimated to range from \$25.0 to \$30.0 million.

The Pool's proportionate share of short-term investments held by a joint venture was \$50.3 million at July 31, 2005 as compared to \$26.0 million at July 31, 2004.

### ***Dividends from Affiliates***

The company receives regular dividends from certain of its subsidiaries and joint ventures. The level of dividends is dependent on a number of factors, including profitability, cash flow and capital spending programs of those entities as well as covenants contained within their financing agreements.

Dividends from joint ventures are also dependent on the agreements with the joint venture partners. The Pool is not dependent on these dividends to fund its capital spending programs or to meet its financial obligations.

### ***Post Employment Benefits***

The company has three defined benefit plans: Hourly Employees' Retirement Plan (Hourly), Out of Scope Defined Benefit Plan (OSDB) and Supplementary Executive Retirement Plan (SERP). The Hourly and the OSDB plans each have surpluses, that when combined, total \$70 million, while the SERP is unfunded and the associated liability was \$4 million at July 31, 2005. As well, the company has a defined contribution plan for management employees hired after January 1, 2000 and unionized employees hired after May 1, 2001, covering 450 employees.

The SWP/GSU pension plan is a closed negotiated cost plan that provides defined benefits that are negotiated between the Pool and Grain Services Union to approximately 1,400 former employees and 600 active employees. The Pool's annual contribution in fiscal 2005 was 4.57% of members' payroll, or \$1.3 million. Active members contributed the same amount.

In its fiscal 2005, Second and Third Quarter Reports, the company identified an estimated potential deficit of \$1.9 million on a going concern basis and an estimated potential deficit of \$28 million on wind-up as at December 31, 2004. The plan has assets of approximately \$238 million.

The going concern basis of valuation assumes that the plan continues to operate until the last pensioner is paid out. The solvency basis assumes that the plan is wound up and annuities are purchased for all pensioners at today's historically low long-term interest rates.

The company and the GSU have met 21 times over the past 16 months in an attempt to resolve expected solvency deficit issues. No solution has been found. As a result, the Pool, the GSU and the Plan Trustees sought the guidance of the Office of Superintendent of Financial Institutions ("OSFI"), the federal pension regulator. On September 22, 2005, OSFI expressed concern about the solvency of the Plan and based on its own financial tests, OSFI restricted withdrawals by eligible individuals to 80% of the value of their benefit. The remaining portion would be paid over the following five-year period assuming the Plan does not wind-up.

On October 4, 2005, all four parties met. The Plan Trustees shared a preliminary actuarial estimate at December 31, 2005, which indicated that the Plan could have a going concern surplus of approximately \$8 million and a solvency deficit of approximately \$50 million. The solvency estimate is based on current rates of return on long-term bonds that are 0.75% lower than those at December 31, 2004. The actual going concern and solvency positions will be established in a formal actuarial valuation as of December 31, 2005. The result of this valuation may vary materially from the above preliminary estimates due to differences between actual and estimated interest rates, asset returns, and other assumptions.

Pension regulations will require any solvency deficit at December 31, 2005 to be addressed over a five-year period through quarterly installments. Assuming a \$50 million deficit, additional contributions would be approximately \$2.8 million per quarter until termination. One or more of the following actions may meet this requirement: amending the plan structure, reducing benefits, increasing employer contributions, or increasing employee contributions. The company has

received advice from external counsel that if the solvency deficiency is not addressed, the likely outcome will be the termination of the Plan.

The company has met all of its financial obligations in accordance with the pension plan text and collective agreement. There is a risk that the company may ultimately be responsible for an increase in contributions required by the formal valuation at December 31, 2005. The Pool's position is that it is not responsible for any payments beyond those negotiated with the GSU.

Readers should refer to Note 18 in the Notes to the Consolidated Financial Statements for additional information.

### **Off Balance Sheet Arrangements**

Under the terms of an agreement, Farm Credit Canada provides credit to the Pool's farming customers for the purchase of crop inputs. Please refer to the discussion under Credit Risk, Critical Accounting Estimates – Agri-products segment and Note 15b in the Notes to the Consolidated Financial Statements.

### **Related Party Transactions**

Transactions with joint ventures and subsidiaries are eliminated in accordance with consolidation accounting principles. There are no significant related party transactions with equity accounting or cost accounting investees.

### **Contractual Obligations**

(in thousands)

	Total	Less than 1 Year	Payments due by Period		After 5 years
			1–3 years	4–5 years	
Long-term debt	\$ 164,460	\$ 5,461	\$ 8,281	\$ 150,614	\$ 104
Operating leases	15,505	5,403	7,097	3,005	-
Purchase obligations*	81,567	81,567	-	-	-
Other long-term obligations	40,038	9,163	14,941	5,260	10,674
Total contractual obligations	\$ 301,570	\$ 101,594	\$ 30,319	\$ 158,879	\$ 10,778

\*The majority of purchase obligations relate to commodity purchase contracts for non-Board grains and oilseeds. The obligations under these contracts are largely offset by commodity sales contracts.

### **CONSOLIDATED RESULTS – FOURTH QUARTER**

Sales and other operating revenues for the quarter were \$546.7 million, up from \$542.5 million realized during last year's fourth quarter, driven by strong Agri-products and Agri-food sales that grew 15.3% and 9.0% respectively. Grain shipments for the quarter were slightly ahead of last year despite a decline in Canadian Wheat Board exports during the period. Fiscal 2005 sales also reflect significantly lower non-Board grain prices relative to the fourth quarter last year, when non-Board commodity prices were approximately 36.0% higher.

Consolidated earnings before interest, taxes and amortization (EBITDA) were \$47.1 million, up from the \$41.0 million recorded in the final quarter of 2004. All three segments posted improved results on a comparable basis relative to last year's final quarter. The Agri-products segment generated EBITDA of \$34.4 million, up from \$29.7 million quarter-over-quarter. The Grain Handling and Marketing segment earned \$17.2 million in EBITDA compared to \$16.3 million in 2004's fourth quarter. Excluding one-time items included in both years' quarters, EBITDA from Grain Handling and Marketing improved by 12.2% quarter-over-quarter. The Agri-food Processing's EBITDA was \$3.6 million in the final three months, which is an improvement from the \$2.5 million earned in the same period a year earlier.

Prior to interest and taxes, the Pool recorded earnings (EBIT) of \$40.4 million in the quarter. During the last quarter of 2004, EBIT was \$41.0 million. Excluding one-time items in each period, the Pool's fourth quarter EBIT performance exceeded the previous year's quarter by 17.9%.

Interest for the quarter was \$9.9 million compared to \$9.2 million last year. Cash interest expenses were down over 46.2% for the quarter to \$3.4 million compared to \$6.4 million in the final quarter of 2004. This improvement reflects the Pool's substantially lower debt levels in the final quarter of 2005.

The Pool recorded non-cash interest of \$6.5 million in the fourth quarter, which compares to \$2.8 million recorded during the same period of 2004. The variance reflects \$3.9 million of financing costs that would have amortized over three years, but were written off in the fourth quarter when the Pool repaid its \$100.0 million term loan. The remainder of the non-cash interest this quarter relates to approximately \$1.0 million of deferred financing costs for the asset backed operating loan that amortizes quarterly, together with ongoing accretion of the Pool's Senior Subordinated Notes. These two non-cash expenses were partially offset by a decline in accretion related to the debt component of the Pool's Convertible Subordinated Notes, which were retired in March of 2005. Accretion is an accounting concept where discounted debt balances are increased on a systematic basis to eventually equal their face value at maturity.

Earnings from continuing operations for the final three months of fiscal 2005 were up 26.0% to \$25.7 million from \$20.4 million earned in the same period a year ago.

This year's fourth quarter included a \$3.9 million net recovery from discontinued operations, which included the Pool's previously held investments in hog production, aquaculture, and feed milling. The recovery primarily reflects a \$3.8 million after-tax recovery related to filings under the Canadian Agricultural Income Stabilization (CAIS) Program, a joint federal/provincial business risk management program. A portion of the losses incurred by this segment in prior years qualified under this program and were therefore recoverable. Last year, discontinued operations for the quarter reflected a net recovery of \$8.4 million primarily related to corporate taxes resulting from the wind-up of that segment.

Net earnings for the quarter were \$29.5 million primarily reflecting a strong spring selling season and more normal weather conditions in the critical May to July growing period. Last year, net earnings were \$28.8 million. Net earnings from continuing operations for the fourth quarter of fiscal 2005 were \$23.1 million, up \$10.6 million from last year's final quarter of \$12.5 million after excluding one-time items in both periods.

Fourth quarter cash flow from continuing operations grew 11.4% to \$41.2 million from \$37.0 million in last year's fourth quarter.

### ***Operating Results - Fourth Quarter***

The Pool's Grain Handling and Marketing segment shipped 1.9 million tonnes during the quarter, slightly ahead of shipments in the fourth quarter of 2004. The Pool's shipping performance for the quarter outperformed the western Canadian industry, which experienced a 10.5% decline in shipments of the six major grains in the final three months of the year.

The Pool's wholly owned port terminals received approximately 1.2 million tonnes compared to 1.0 million tonnes in the final three months of last year, an 11.2% increase quarter-over-quarter, despite a 10.3% decrease in CWB shipments through Vancouver. Stronger volumes through the Pool's pipeline reflect higher crop production in Saskatchewan and an increase in farmer deliveries and market share in the Pool's primary handling business.

Pipeline margins per tonne (excludes other revenue and one-time items for the quarter) were \$18.40 up from the \$18.38 per tonne generated in the fourth quarter of 2004. Poor grain quality, an

issue throughout the entire fiscal year limited margin potential and challenged export opportunities for the Canadian Wheat Board.

This quarter's segment EBITDA from Grain Handling and Marketing of \$17.2 million included \$2.9 million of one-time items. The Pool recognized approximately \$2.0 million in interest revenue related to manufacturing and processing tax credits for prior year filings as a result of a positive Revenue Canada ruling related to the processing capabilities of the Pool's prairie grain handling network. Last year in the final quarter, the Pool generated \$16.3 million, which included \$3.5 million in positive one-time items. Excluding one-time items in both periods, performance in this segment improved by 12.2% reflecting market share increases on the Prairies, higher grain shipments and increased volumes through the Pool's wholly owned port terminal facilities. Segment EBIT for the quarter was \$14.3 million versus \$14.7 million last year, a \$1.2 million improvement after excluding non-recurring items.

Sales from the Pool's retail agri-products operations combined with its share of revenue from joint venture affiliate, Western Co-operative Fertilizers Limited (WCFL), were \$320.3 million, a 15.3% increase over 2004 fourth quarter sales of \$278 million. The Pool's retail operations performed well with a 15.1% increase in fertilizer sales, a 4.3% increase in crop protection product sales and a 16.0% increase in seed sales. WCFL generated sales growth of 36.4% reflecting strong demand for fertilizer due to improved moisture levels and an abbreviated anhydrous ammonia program in the fall that pushed a portion of those sales into the Pool's fourth quarter.

EBITDA from the Agri-products segment for the quarter was \$34.4 million compared to \$29.7 million in the fourth quarter last year, a 15.9% increase. The improvement reflects higher sales volumes in all of the Pool's product lines, particularly fertilizer, higher miscellaneous revenues and a reduction in bad debt expenses. These positive business results more than offset the overall reduction in retail margins caused by heightened competition and lower supplier rebates. Agri-products EBIT was \$31.8 million for the quarter compared to \$27.2 million for the same quarter of fiscal 2004.

For the Agri-food Processing segment, quarterly sales increased by 9.0% to \$28.8 million compared to \$26.4 million in the last quarter of fiscal 2004. Prairie Malt's sales were on par with the previous year's quarter while Can-Oat sales grew 12.8%. Can-Oat's sales growth was attributable to strong demand from destination customers who have begun to respond to changing consumer buying patterns that are driving increased demand for whole grain oat products. This is in contrast to 2004 when industry-wide demand softened temporarily because of the low carbohydrate diet fad that was popular at the time.

EBITDA for the final quarter of fiscal 2005 for the Agri-food Processing segment reflected an 18.4% increase from Can-Oat. Prairie Malt's earnings improved over the previous year's quarter as a result of lower processing costs and lower barley handling costs. EBITDA for the quarter totaled \$3.6 million compared to \$2.5 million in the same quarter last year and EBIT was \$2.4 million versus \$1.3 million for the same periods.

## **OUTLOOK**

Based on the October 5, 2005 Statistics Canada report, western Canadian production is estimated to be 52.5 million tonnes, which is on par with the five-year average. Production in Saskatchewan is expected to be 29.0 million tonnes, up from 26.1 million tonnes produced for fiscal 2005. Should these estimates hold, this is positive for the Pool because of its dominant market share in Saskatchewan. In Manitoba, production is estimated to be down by 40% year-over-year to 5.0 million tonnes and in Alberta on par at 18.2 million tonnes relatively unchanged from 18.4 million tonnes to last year. The impact of the Manitoba crop situation will not be significant for the Pool given its relatively small presence in that Province. Based on October 11, 2005 crop reports, approximately 70 to 75% of the harvest on the Prairies was complete.

Recent damp weather in certain regions of the Prairies will impact quality, however, it is not expected to damage the crop to the same extent as last year. A complete picture of the quality available in 2006 will be determined once harvest is complete and samples have been tested. Grain movement is expected to improve for the Pool in 2006 given the larger than average crop in Saskatchewan and estimates by the Canadian Wheat Board that they intend to export between 17 and 18 million tonnes, a significant improvement from the 14.8 million tonnes exported in fiscal 2005. Margins too, are expected to improve over fiscal 2005, however, given the probability that some deterioration in the quality of cereal grains will occur this year, the Pool expects the amount of feed grains shipped in 2006 to be higher than normal.

Recent weather conditions in the northern regions could limit fall fertilizer applications. Overall, however, moisture conditions on the Prairies are good and should set the stage for strong fertilizer demand in the spring. Weather conditions throughout the crop cycle are key to the Agri-products segment since the majority of its sales and earnings are generated during the spring and summer months.

Whole grain oat consumption is expected to continue to drive demand for Can-Oat products into 2006 and the Pool will continue to assess expansion opportunities in that business to meet their growing customer base.

### ***CRITICAL ACCOUNTING ESTIMATES***

In preparing the company's consolidated financial statements, management is required to make assessments and estimates as to the outcome of events in the future. This assessment is made using the best information available to management at the time. The following is an analysis of the critical accounting estimates.

#### ***Grain Handling and Marketing Segment***

The Grain Handling and Marketing segment contains a \$4.0 million allowance related to a receivable for product delivered to a customer in Mexico. Due to steps taken by the company to mitigate this potential loss as at July 31, 2005, the allowance of \$4.0 million completely covers the exposure. To the extent that the company is successful in recovering this receivable, earnings would increase in future years.

#### ***Agri-products Segment***

Under the terms of an agreement, Farm Credit Canada provides credit for the purchase of crop inputs to producer customers of the Pool. Loans are stratified based on program years and are generally due to this financial institution on January 31 of the following year. Loans under the program are secured by a general security agreement granted by the customer covering the crop and farm assets. Under the agreement, the Pool has agreed to reimburse this financial institution in December for loan losses in excess of a reserve.

At July 31, 2005, \$185.0 million of producer loans were outstanding, of which \$174.0 million relate to the 2005 loan program and \$11.0 million related to the 2004 loan program. The loan loss provision, net of the total reserve, is \$7.4 million, with the net portion due within one year estimated to be \$4.1 million. This provision has been established based on historical results from fiscal 2003 and 2004 and the Pool's assessment of outstanding loans. The Pool expects that loan losses will not differ significantly from those provided for previously. Any differences will be reflected in future years.

In 1987, WCFL closed two facilities that manufactured phosphate and nitrate fertilizers. The joint venture has provided for the costs of the reclamation process. Reclamation involves the demolition of the manufacturing facilities and reclamation of the phosphogypsum stacks. The Pool's share of the estimated costs included in long-term liabilities is \$11.5 million. WCFL reviews the provision on a regular basis to ensure that the costs to complete the work are appropriately reflected in its

financial statements. To the extent that the estimate for reclamation changes in the future, the earnings of the joint venture will be impacted.

### ***Agri-food Processing Segment***

There are no critical accounting estimates in this segment.

### ***Corporate and Other***

The Pool follows the liability method of tax allocation in accounting for income taxes. Essentially this means that future income tax assets and liabilities are recorded based on the temporary differences between the tax and accounting balances for these assets and liabilities, multiplied by the tax rate that is projected to be in effect when the differences are expected to reverse. For the Pool the primary temporary differences are between the book value of property, plant and equipment compared to the tax cost of these assets as well as non-capital tax losses that are available for carry-forward over a finite period.

The Pool records future tax assets, net of a valuation allowance, to reflect an amount the company considers is more likely than not to be realized. At July 31, 2005, the Pool recorded a \$102.7 million future tax asset, which is net of a \$69.4 million valuation allowance. The amount recorded may change based on future events and circumstances.

### ***Discontinued Operations***

In fiscal 2005, the Pool recorded a \$3.8 million after-tax recovery related to filings under the Canadian Agricultural Income Stabilization Program (CAIS), a joint federal/provincial risk management program. The CAIS filings represent a recovery of a portion of the losses incurred by operations discontinued in prior years. The \$3.8 million after-tax recovery may change based on future events and management assessments.

### ***CHANGES IN ACCOUNTING POLICIES***

The only accounting policy change in fiscal 2005 relates to the new Canadian Institute of Chartered Accountants (CICA) standard regarding Asset Retirement Obligations (ARO) (CICA 3110). The accounting for the environmental obligations of one of the company's affiliates was amended to reflect CICA 3110 effective August 1, 2004. This standard applies to the recognition and measurement of legal obligations on the acquisition, construction, development or normal use of property, plant or equipment owned by the company or its affiliates. The standard requires the obligation be recognized in the financial statements in the period incurred provided a reasonable estimate of the fair value can be determined. As time passes, accretion is charged to earnings to recognize the fair value of the obligation.

The impact of retroactively transitioning to the new ARO standard is as follows:

- no impact on reclamation provision or retained earnings at July 31, 2004; and
- negligible impact on earnings for fiscal 2005.

### ***FINANCIAL AND OTHER INSTRUMENTS***

The Pool is involved in the purchase, sale and processing of raw agricultural commodities. Agricultural commodities are subject to price fluctuations due to numerous unpredictable factors that may create price risk. The company enters into derivative contracts, exchange-traded futures and options contracts and forward purchase and sales contracts, with the objective of managing the exposure to adverse price movements in agricultural commodities. The daily net commodity position consists of inventory, related forward purchase and sales contracts, and exchange-traded futures and options contracts.

The Pool uses these derivative contracts to minimize the effects of changes in the prices of hedgable agricultural commodities. Exchange-traded futures and options contracts and forward purchase and sales contracts are marked to market at market values, which are based on quoted market prices adjusted for freight and handling costs. The unrealized gains and losses for hedgable commodity positions are recognized as cost of sales in the consolidated statements of earnings and retained earnings (deficit).

The company has practices and policies in place to limit the amount of unhedged fixed-price commodity positions the company is allowed to maintain. On a daily basis the company measures the combination of quantity and value at risk.

The Pool is exposed to fluctuations in foreign currency exchange rates on transactions denominated in foreign currencies.

The company uses derivative financial instruments, such as foreign currency forward contracts and futures contracts, to limit exposures to changes in foreign currency exchange rates with respect to its recorded foreign currency denominated assets and liabilities and forecast transactions. These derivative instruments are marked to market value. In certain areas of the company not related to the handling and marketing of grain, the company commenced application of the CICA Accounting Guideline 13. Hedge accounting is same period recognition, in income, of the gains, losses, revenues and expenses associated with a hedged item and the hedging instrument. In the remaining areas of the company, unrealized gains and losses on forward foreign exchange and futures contracts are marked to market and recognized as sales and other operating revenues in the consolidated statements of earnings and retained earnings (deficit).

The company has established policies that measure and review the company's exposure to foreign currency risk on a daily basis. Further information is provided in the July 31, 2005 Notes to the Consolidated Financial Statements – Note 23.

## ***FUTURE ACCOUNTING STANDARDS***

### ***Comprehensive Income and Equity***

The new CICA standards Comprehensive Income (CICA 1530) and Equity (CICA 3251) are effective for fiscal years beginning on or after October 1, 2006. CICA 1530 establishes standards for reporting comprehensive income. CICA 3251 establishes standards for presentation of equity and changes in equity during the reporting period.

The impact of the adoption of these standards on the presentation of the company's consolidated financial statements has not yet been determined.

### ***Financial Instruments – Recognition and Measurement***

The new CICA standard Financial Instruments – Recognition and Measurement (CICA 3855) is effective for fiscal years beginning on or after October 1, 2006. CICA 3855 establishes the basis of initial measurement (fair value) and subsequent measurement (fair value or cost) of financial instruments. It also specifies how financial instrument gains and losses are to be presented.

The impact of the adoption of this standard on the consolidated results of operations or financial position has not yet been determined.

### ***Non-monetary Transactions***

The new CICA standard Non-monetary Transactions (CICA 3831) is effective for periods beginning on or after January 1, 2006. The standard requires all non-monetary transactions to be measured at fair value unless they meet one of four specific criteria.

The impact of the adoption of this standard on the company's financial statements is not expected to be significant.

## ***RISK MANAGEMENT***

The Pool faces certain risks, including weather, strategic, market, financial restriction, credit and foreign exchange risk that can impact its financial performance. For additional information on other general business and environmental risks, readers should review the 2005 Annual Information Form.

### ***Governance and Oversight***

The Pool's Risk Management Committee (the "Committee") is a senior management committee responsible for assessing enterprise risks and implementing strategies to reduce the company's exposure. The Committee meets regularly to assess risks and direct risk mitigation activities. Regular reports are provided to the Audit Committee of the Board of Directors.

### ***Weather Risk***

The Pool's most significant risk, as an agri-business company, is the weather. The effects of weather conditions on crop quality and production volumes present significant operating and financial risk to the Pool's Grain Handling and Marketing segment. Volumes are a key driver of earnings for the Pool's grain operations. Fixed costs in the Pool's primary elevator system represent approximately 75% to 80% of its total costs and, as a result, reduced volume and inventory turns negatively impact the margin/earnings per tonne the Pool can achieve.

Crop quality is also an important factor because the majority of the higher quality grains and oilseeds move into export position and as a result the Pool is able to generate margins at each stage of its pipeline through to its port terminals. Grains destined to domestic markets, on average, generate lower margins, particularly feed grains that require little processing and handling. Therefore the mix of grains and oilseeds that the Pool manages in any given year is an important factor in its ability to generate strong margins and earnings. The Pool offers a number of programs, including drying and blending opportunities to its primary customers in an attempt to mitigate some of the quality risk.

The level and mix of agri-product sales are also dependent on weather. Weather is a determining factor in crop selection by producers at seeding time, the variety of seeds sown, and the amount of proprietary seed sold. Crop selection decisions also impact the amount of fertilizer and crop protection products that are sold since certain crops require significantly more inputs than others. Weather, throughout the growing season, will determine how much product is applied to the land. The Pool's Agri-products group works closely with its Grain group to assist in anticipating producers' seeding intentions in order to manage agri-product inventories accordingly.

The Pool has attempted over the years to mitigate some of this exposure to weather with its expansion of grain handling and agri-products facilities into Alberta and Manitoba to reduce the impacts of localized growing conditions. The Pool has also secured grain volume insurance for fiscal 2006 that provides a level of protection against a dramatic reduction in grain receipts (producers' deliveries). It is the company's objective to develop a long-term volume insurance program as part of its overall risk management strategies.

### ***Market Risk***

A significant portion of the company's sales are derived from its Grain Handling and Marketing segment. Earnings for this segment fluctuate based on the volume of grain handled and the margins earned on the purchase and sale of non-Board grains. In the case of CWB grain, the Pool earns storage and handling tariffs from the CWB, which are established independently of the market price for grain.

Approximately 60% of the grain shipped by the Pool is Board grain – wheat and barley sold by or on behalf of the CWB – into the export and domestic markets. For these grains, the company's risks are reduced in part through the terms of formal legal arrangements between the Pool and the CWB. The arrangements provide for full reimbursement of the price paid to producers for grain as well as certain costs incurred by the Pool. Adverse impacts may be experienced by the Pool where handling of Board grain results in a loss of grade or, in the case of the CWB's tendering program, if the Pool fails to meet the requirements under the tendering contract. The Pool employs grain grading, handling procedures and quality testing throughout the pipeline to help mitigate these risks.

For other non-Board grains and oilseeds purchased by the Pool, the Pool faces the risk of movement in price between the time the grain is purchased and the time that it is sold. Financial risk management activities commonly referred to as "hedging," where such opportunities exist, can reduce this risk. Not all such activities, however, necessarily qualify for hedge accounting or are accounted for as hedges. Hedging is the placing of an opposite position in the futures market to that held in the cash market to reduce the risk of financial loss from an adverse price change.

The Pool hedges non-Board grain purchases and sales to the extent possible. This is accomplished by hedging purchases and sales of non-Board grains through regulated futures markets. Because of the size of future contracts and certain time constraints, it may not be possible to be fully hedged at all times. Special crops are more difficult to hedge, as no regulated futures market exists for these commodities and the hedging instruments available lack liquidity. Where possible, financial exposure to un-hedged purchases and sales is reduced by back-to-back buying and selling.

The Pool employs a comprehensive Commodity Risk Management Policy, in which position limits are utilized to restrict its exposure to changes in commodity prices. Position limits set out the amount of market exposure the company is willing to tolerate by commodity. The Policy defines these tolerance levels based on the size of the original position, liquidity in the futures market along with a number of other factors. Various authorization levels are also set out in the Policy. The Risk Management Committee, an executive management committee may approve temporary changes to the authorization levels upon the request of the CEO. Any such changes are reported to the Board's Audit Committee.

### ***Credit Risk***

The Pool is exposed to credit risk in connection with credit provided to its customers, including credit provided on agri-products purchases through a third party. Credit defaults by the Pool's customers could have a material adverse effect on the Pool's financial results and financial condition. The Pool shares responsibility for defaulted accounts and loan losses with Farm Credit Canada, its partner in the FarmSmart agri-products credit program. The allowance for doubtful accounts under this program averaged less than 2.0% of sales per program year in its first two years of operation.

The Pool manages credit risk through adherence to its established Credit and Collection Policies. The Credit Policy outlines the terms and conditions for granting credit to customers and continuing credit sales. The Collection Policy provides the framework for collections of past due accounts. Any exceptions to the Credit and Collection Policies require the written approval of the Pool's executive management. These policies cover the Pool's agri-products and commercial grain credit facilities, as well as the credit facilities for Can-Oat Milling.

The Pool pursues a payment and country risk reduction strategy for offshore customers through the use of export financing arrangements, strategic business alliances and country risk reporting. Export financing payment arrangements include cash prior to unloading, cash against documents

and obtaining confirmed letters of credit. Activity is continually monitored to ensure the Pool's exposure is within acceptable limits.

### ***Foreign Exchange Risk***

Significant portions of Can-Oat's oat products and the Pool's non-Board grains are sold into the export market and are priced in American dollars. Can-Oat and the Pool hedge substantially all foreign currency transactions using options, futures currency contracts or forward exchange contracts, and through the use of natural hedges created by offsetting transactions. To the extent that the companies have not fully hedged this foreign exchange risk, an appreciation of the Canadian dollar against the American dollar or other relevant currencies could have a material adverse effect on the Pool's financial results.

### ***EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES***

Management, including the President and Chief Executive Officer and Chief Financial Officer, have evaluated the effectiveness of the Pool's disclosure controls and procedures (as defined in National Instrument 52-109 of the Canadian Securities Administrators) as of July 31, 2005. Management has concluded that, as of July 31, 2005, the Pool's disclosure controls and procedures were adequate and effective to provide reasonable assurance that material information relating to the Pool and its consolidated subsidiaries would be made known to them by others within those entities, particularly during the period in which this report was being prepared.

### ***EBIT AND EBITDA DATA***

The EBIT and EBITDA data provided herein is intended to provide further insight with respect to the company's financial results, including its results on a segment-by-segment basis and to supplement its earnings (loss) as determined in accordance with GAAP. The Pool's method of calculating EBIT and EBITDA may not be comparable to other companies in the industry. EBIT should therefore not be used as an alternative to net earnings (loss) as determined in accordance with GAAP. Similarly, EBITDA should not be used as an alternative to cash provided by operating activities as determined in accordance with GAAP.

### ***FORWARD-LOOKING INFORMATION***

Certain statements in this Management's Discussion and Analysis are forward-looking and reflect the Pool's expectations regarding future results of operations, financial condition and achievements. All statements included or incorporated by reference therein that address activities, events or developments that the company or its management expects or anticipates will or may occur in the future, including such things as the company's comments in the "Outlook" section of the Management's Discussion and Analysis, the growth of its business and operations, competitive strengths, strategic initiatives, planned capital expenditures, plans and references to future operations and results of the company and other such matters, are forward-looking statements. Such forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause the actual results, performance and achievements of the Pool to be materially different from any future results, performance and achievements expressed or implied by those forward-looking statements. A number of factors could cause actual results to differ materially from expectations, including weather conditions, crop production and crop quality in Western Canada; world agricultural commodity prices and markets; producers' decisions regarding total seeded acreage, crop selection, and utilization levels of farm inputs such as fertilizers and crop protection products; credit risk; foreign exchange risk; changes in the grain handling and agri-products competitive environments, including pricing pressures; Canadian grain export levels; changes in government policy and transportation deregulation; international trade matters; global political and economic conditions, including grain subsidy actions and tariffs of the United States and the European Union; competitive developments in connection with the Pool's grain handling, agri-products, agri-food processing businesses and other operations; and environmental risks and unanticipated expenditures relating to environmental and other matters. Many of these risks and

uncertainties are beyond the control of the company. All of the forward-looking statements made in this annual report and this Management's Discussion and Analysis are qualified by these cautionary statements and the other cautionary statements and factors contained therein, and there can be no assurance that the actual developments or results anticipated by the company and its management will be realized or, even if substantially realized, that they will have the expected consequences for, or effects on, the company.