Adding value

Empire delivered growth in earnings in fiscal 2004, despite a challenging year for our food division. A decline in Sobeys' operating earnings was offset by the continued strong performance for our real estate, theatre and investment operations.

In fiscal 2004 Empire revenues increased by 6%, operating earnings grew by 2% to reach $2.49 per share, and the common dividend rate per share increased by 21%.

This is a good indication of the value of our diversified business base and our business and investment balance, which has contributed over the long term to ongoing growth and profitability. While both real estate and food distribution are basic and complementary businesses, they are driven by different market dynamics and economic cycles. Having both sectors in our business mix reduces volatility and stabilizes growth trends over time.

Sobeys faced a number of unplanned events during the year, but maintained national market share and posted sales growth of 6% in a highly competitive marketplace. Unplanned events ranged from SARS, an Ontario power failure and recovery from a labour disruption at an Ontario operation, among others. All businesses face unanticipated events and challenges from time to time; the real test of management is the ability to withstand short term challenges and build a healthy, competitive and sustainable business for the future by executing on their strategic plan. Sobeys' strategic direction is sound and progress is being made. We are confident that management will continue to focus on improving the operations of the business and grow profitability in fiscal 2005.

Growing diversity

Our business balance and diversity has been enhanced over the past few years by growing the geographic diversity of our operating businesses as we have expanded steadily and carefully beyond our traditional core markets in Atlantic Canada. Sobeys gained a national platform in Canada with the acquisition of the Oshawa Group in December 1998, and has built on that, growing in every region. In real estate, Crombie has been increasing its presence in Ontario – and, through Genstar, we are participating in high growth residential markets principally in Western Canada. As well, in our theatre business, we have developed a new platform for growth through an established theatre operator in Western Canada.

This geographic expansion is important for two reasons – it has broadened growth opportunities, and it has provided us with greater resilience to regional downturns.

Supporting this diversification is one of the ways that Empire has added value as a holding company. At Empire, we don't micromanage our operating businesses, nor do we attempt to manage the other businesses in which we invest. Our primary role is to ensure excellent

ABOVE: **PAUL SOBEY,** President and Chief Executive Officer, Empire Company Limited

management is in place and that they remain focused on executing day-to-day improvements to the business with care, passion and integrity. In assessing management, we have learned over time not to confuse good markets with good management or difficult and challenging markets with poor management. We don't get concerned with short-term fluctuations based on changing market conditions, and we don't have a lot of time for quick fix "flavours of the week" in terms of management strategies and theory. We look to the long term, we look for steady progress on the execution of each operating company's strategic plan, and we are not disappointed. Empire's long-term track record reflects the benefit of this approach.

With strong operating management in place, we strive to add value through our stewardship role – reviewing strategies, monitoring progress, determining capital allocation in support of growth initiatives, strengthening our financial resources, and providing guidance and stability – as owners with a long-term perspective, broad business experience and a profound and passionate commitment to our businesses.

Managing growth in 2004

Sobeys, while not meeting our earnings expectations in 2004, made significant progress in very tough competitive markets. Sobeys continued to invest in pricing, while pursuing its highly focused strategies for strengthening the value proposition for customers, enhancing and expanding the store network, improving merchandising, and investing in operations. Sobeys focused on top line performance and delivered top line improvements with a strong increase in sales.

Our real estate business had another strong year with a 9.4% increase in operating earnings, supported by continued earnings growth from Genstar and from our commercial retail business. Genstar continued to perform above our expectation with an 8.1% growth in operating

LEFT: **CROMBIE PROPERTIES MANAGEMENT DISCUSS REAL ESTATE DEVELOPMENT.** *PICTURED FROM LEFT:* **SCOTT MACLEAN,** Vice-President Operations; **STUART BLAIR,** President and Chief Executive Officer; **PAUL WIGGINTON,** Comptroller; **FRANK SOBEY,** Chairman; **ALLAN MACDONALD,** Vice-President Leasing

RIGHT: **SOBEYS' MANAGEMENT MEET TO DISCUSS REGULATORY REQUIREMENTS.** *PICTURED FROM LEFT:* **JAMES DICKSON,** Executive Vice-President, Chief Development Officer and Secretary; **JANE McDOW,** Assistant Secretary; **PAUL JEWER** Vice-President, Finance and Treasury OPPOSITE PAGE: **EMPIRE COMPANY MANAGEMENT MEET TO DISCUSS RISK MANAGEMENT CONTROLS.** *PICTURED FROM LEFT:* **STUART FRASER,** President and Chief Executive Officer (Empire Theatres Limited); **JOHN MORROW,** Vice-President and Comptroller; **CAROL CAMPBELL,** Vice-President, Risk Management

earnings over the past year. While we believe that kind of growth rate is not sustainable year-over-year, Genstar has a very focused strategic approach and has shown an ongoing ability to outperform in its market sector.

Crombie's commercial retail business also had positive year-over-year results, posting improvements in occupancy and rental rates, while increasing future value with the acquisition of seven strip plaza properties in Ontario.

Empire Theatres' performance continued to be strong, expanding with three new theatres in Atlantic Canada and one joint venture in Western Canada, enhancing its offering and delivering record revenues and earnings.

We also achieved first quartile return performance from our investments including a solid turnaround by our equity accounted investment in Wajax Limited ("Wajax").

Emerging synergies

Our operating businesses are distinct and autonomous, but some synergies have emerged. Clearly, real estate strategies are vital to both the ongoing development and expansion of the food distribution business and the theatre business, while knowledge of retail and consumer trends is vital to the real estate business. Our businesses all benefit from the pool of market and industry knowledge that we collectively represent, and this has been extremely beneficial as each has expanded beyond Atlantic Canadian markets.

Clear evidence of this was the joint approach to the acquisition of Commisso's – a regional grocery business in Southwestern Ontario. Both Sobeys and Crombie had identified Commisso's

"The management teams are supported by the diligence and efforts of thousands of dedicated people who have the passion, the integrity, the knowledge and the will to succeed. That has driven our performance in the past and will continue in the future."

as an attractive acquisition candidate. Together, they were able to determine the full and potential value of the acquisition and through a joint approach, Sobeys was able to acquire Commisso's grocery business assets, while Crombie was able to buy the real estate assets.

Accounting for value

As Empire has grown, we have worked hard to identify and measure the value of our businesses and to report accurately to our shareholders. While this will be more challenging going forward given that the new accounting principles will impact all of our operating companies, we remain committed to ensuring transparency to the investment community.

New accounting principles, both enacted and pending, will affect depreciation charges, revenue recognition, accounting for acquisitions of rental properties, and potentially consolidation of franchising arrangements, to name a few. While these accounting changes will not impact the cash position of the corporation or its underlying economic value, they risk making the financial statements more confusing for our shareholders, masking actual improvements in fundamental values, particularly for our real estate business.

While complying with the new rules, we will endeavour to provide commentary that will give as accurate a picture of underlying value as possible.

Looking forward

Going forward, we intend to stay the course by supporting and encouraging the management of our operating businesses towards continued progress on the successful execution of their respective business plans. In doing so we are confident that the fundamentals of each of our core operating businesses – food distribution, real estate and theatres – will improve.

We enter fiscal 2005 in a strong financial position and with strong and balanced operating businesses that know where they are going and have the business plans, leadership teams and people to get them there.

PAUL D. SOBEY
PRESIDENT AND C.E.O.
JULY 19, 2004