

# EMPIRE

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## GROWING VALUE

Empire Company Limited Second Quarter Report | Six Months Ended October 31, 2002

## **Quarterly Report to Shareholders**

Empire Company Limited is a diversified Canadian Company whose key businesses include food distribution, real estate and corporate investment activities. Guided by conservative business principles, our primary goal is to grow long-term shareholder value through income and cash flow growth and equity appreciation. We accomplish this through direct ownership and equity participation in businesses that have the potential for long-term growth and profitability.

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Copies of this report are available on the Company's website ([www.empireco.ca](http://www.empireco.ca)) or by contacting the Vice President, Investor Relations at (902) 928-1725. A copy has also been filed on SEDAR.

The Company provided additional details concerning its second quarter results on a conference call held on Wednesday, December 11, 2002. Replay of the call is available on the Company's website ([www.empireco.ca](http://www.empireco.ca)).

### **Forward Looking Statements**

Certain forward-looking statements may be included in this quarterly report. Such statements are based on management's assumptions and beliefs in light of information currently available. These forward-looking statements are subject to inherent uncertainties and risks, including but not limited to: business and economic conditions generally in the Company's operating regions; pricing pressures and other competitive factors; results of the Company's ongoing efforts to reduce costs; equity price risk; and the availability and terms of financing. Consequently, actual results and events may vary significantly from those included in or contemplated or implied by such statements.

## Letter to Shareholders

On December 11, 2002, Empire Company Limited announced its financial results for the second quarter ending October 31, 2002.

### *Second Quarter Highlights (versus Q2 last year)*

- *Revenue of \$2.66 billion, up \$191 million or 7.7 percent*
- *Operating earnings (earnings before net capital gains and other items) of \$39.0 million, up \$4.7 million or 14 percent (with goodwill amortization excluded from last years earnings)*
- *Operating earnings per share (before net capital gains and other items) of \$0.59 versus \$0.52, a 13 percent increase (with goodwill amortization excluded from last year's earnings)*
- *Net capital loss of \$0.2 million in the quarter versus a net capital gain of \$10.9 million last year*
- *Net earnings of \$38.8 million versus \$42.3 million last year*

The Company recorded operating earnings (earnings before net capital gains and other items) of \$39.0 million or \$0.59 per share versus operating earnings before goodwill amortization in the second quarter last year of \$34.3 million or \$0.52 per share, a 14 percent increase. Second quarter earnings last year included earnings from the discontinued SERCA Foodservice operations of \$2.0 million or \$0.03 per share.

Revenue for the second quarter was \$2.66 billion compared to \$2.47 billion last year, a 7.7 percent increase. The food division reported revenue of \$2.61 billion, an increase of 7.7 percent over the second quarter last year. The increase in food division revenue is primarily attributed to same-store sales growth of 2.4 percent (3.6 percent including expanded stores) and from additional sales generated by new retail square footage as a consequence of capital spending. Food price inflation declined to the lowest quarterly rate in two years. Real estate and other operations reported revenue growth of 7.3 percent and 15.7 percent, respectively, over the second quarter last year. The growth in real estate revenues continues to reflect strong performance from our 35 percent interest in Genstar Limited Partnership.

Operating income (earnings before interest, income taxes and goodwill charges) in the second quarter totalled \$111.7 million, an increase of \$9.9 million or 9.7 percent compared to the second quarter last year. All operating companies recorded improvement in operating income over last year. The food division contributed operating income of \$82.7 million, an increase of 13.4 percent over the second quarter last year. The increase in food division operating income is attributed to the growth in revenue, disciplined cost management and continued improvements in regional marketing and merchandising programs. The real estate division contributed operating income of \$26.7 million, an increase of 6.8 percent over the second quarter last year. Trailing (last four quarters) funds from operations (net earnings plus depreciation) for the real estate division now equals \$52.5 million. Other operations' operating income equalled \$2.1 million, up \$0.3 million over last year.

Net earnings, including net capital gains and other items totalled \$38.8 million or \$0.59 per share versus \$42.3 million or \$0.64 per share last year. Included in last year's net earnings were \$10.9 million (\$0.16 per share) of net capital gains and other items primarily associated with the sale of investments in the second quarter last year. A net capital loss of \$0.2 million was recorded in the second quarter of the current fiscal year.

The financial condition of the Company remains strong. The ratio of net debt to capital at the end of the second quarter equalled 28.8 percent and our interest coverage ratio improved to 4.8 times from 3.6 times a year earlier.

Capital investment of \$112.3 million during the quarter and \$179.7 million year-to-date reflects the Company's ongoing commitment to invest cash flow back into growth opportunities in each of its core businesses. Investment by the food division in property and equipment, primarily related to new store development, totalled \$98.5 million of total capital investment. During the second quarter, seven corporate and franchised grocery stores were opened or replaced and one store was expanded. For the first six months of fiscal 2003, a total of nineteen corporate and franchised grocery stores were opened or replaced and another six stores were expanded. The Company also rebannered twenty-three stores in the quarter.

The Board of Directors declared a quarterly dividend of 8.25¢ per share on both the Class A and Class B common shares which will be payable on January 31, 2003 to shareholders of record on January 15, 2003. In addition, the Board declared regular dividends on the Company's outstanding preferred shares.

We are pleased with our operating earnings performance in the second quarter on both a consolidated basis and on an operating company level as each operating company delivered record second quarter operating earnings performance. The continued hard work and ongoing focus of our leadership on building sustainable long-term profitability in each of our operating companies is responsible for our progress to date in fiscal 2003. We will continue to work diligently towards continued growth in each of our businesses throughout the second half of fiscal 2003.

A handwritten signature in black ink, appearing to read "Paul D. Sobey", is written over a horizontal line.

Paul D. Sobey  
President & Chief Executive Officer

December 16, 2002

The table below presents summary financial performance for the second quarter and six months ended October 31, 2002. Per share data reflects the commencement of a 2-for-1 share split effective October 7, 2002.

(\$ in millions, except per share data)	Three Months Ended October 31		Six months Ended October 31	
	2002	2001	2002	2001
Segmented Revenue (net of elimination entries)				
Food Division	\$2,613.4	\$2,427.4	\$5,251.1	\$4,871.8
Real Estate Division	36.8	34.3	69.7	65.9
Other Operations	14.7	12.7	31.4	26.0
	<u>2,664.9</u>	<u>2,474.4</u>	<u>5,352.2</u>	<u>4,963.7</u>
Segmented Operating Income				
Food Division	\$82.7	\$72.9	\$167.0	\$140.3
Real Estate Division	26.7	25.0	49.2	47.3
Other Operations	2.3	3.9	10.7	11.8
	<u>111.7</u>	<u>101.8</u>	<u>226.9</u>	<u>199.4</u>
Earnings before net capital gains, other items and goodwill amortization	39.0	34.3	78.8	67.5
Earnings before net capital gains and other items	39.0	29.4	78.8	55.7
Operating earnings (after goodwill amortization)	39.0	31.4	78.8	61.7
Net capital gains (loss) and other items	(0.2)	10.9	(0.2)	29.2
Net earnings	<u>\$38.8</u>	<u>\$42.3</u>	<u>\$78.6</u>	<u>\$90.9</u>
<u>Per Share</u>				
Earnings before net capital gains, other items and goodwill amortization	\$0.59	\$0.52	\$1.19	\$1.12
Earnings before net capital gains and other items	0.59	0.45	1.19	0.85
Operating earnings (after goodwill amortization)	0.59	0.48	1.19	0.94
Net capital gains (loss) and other items	-	0.16	-	0.44
Net earnings	<u>\$0.59</u>	<u>\$0.64</u>	<u>\$1.19</u>	<u>\$1.38</u>
Weighted average number of common shares (in millions)	65.8	65.7	65.8	65.7

**EMPIRE COMPANY LIMITED**  
**CONSOLIDATED BALANCE SHEET**

(Unaudited, in millions)

	<u>October 31</u> <u>2002</u>	April 30 2002	<u>October 31</u> <u>2001</u>
<b>ASSETS</b>			
Current			
Cash and cash equivalents	\$ 182.5	\$ 302.6	\$ 105.4
Receivables	312.5	312.8	285.3
Inventories	500.4	425.7	468.7
Prepays	44.0	37.0	47.6
Future income taxes	2.2	5.4	13.9
Discontinued operations (Note 2)	<u>3.9</u>	<u>5.8</u>	<u>207.3</u>
	<b>1,045.5</b>	1,089.3	1,128.2
Investments, at cost (quoted market value \$331.0 April 30,2002 \$546.8; October 31,2001 \$508.2)	<b>418.4</b>	479.8	436.1
Investments, at equity (quoted market value \$29.9 April 30,2002 \$41.1; October 31,2001 \$33.5)	<u>41.2</u>	<u>41.1</u>	<u>63.6</u>
Current assets and marketable investments	<b>1,505.1</b>	1,610.2	1,627.9
Property and equipment	<b>1,988.3</b>	1,911.6	1,704.5
Other assets (Note 4)	<b>797.2</b>	796.2	803.5
Discontinued operations (Note 2)	<u>-</u>	<u>-</u>	<u>194.5</u>
	<b><u>\$ 4,290.6</u></b>	<b><u>\$ 4,318.0</u></b>	<b><u>\$ 4,330.4</u></b>
<b>LIABILITIES</b>			
Current			
Bank loans and notes payable	\$ 164.7	\$ 207.2	\$ 216.4
Payables and accruals	<b>948.0</b>	1,006.5	908.9
Income taxes payable	<b>61.8</b>	51.9	18.8
Long term debt due within one year	<b>181.8</b>	85.6	87.3
Discontinued operations (Note 2)	<u>-</u>	<u>-</u>	<u>210.5</u>
	<b>1,356.3</b>	1,351.2	1,441.9
Long term debt	<b>845.9</b>	975.0	1,074.1
Deferred revenue	<b>9.3</b>	12.8	12.8
Employee future benefit obligation	<b>72.7</b>	71.7	60.1
Minority interest	<b>513.6</b>	480.9	434.3
Future income taxes	<b>132.8</b>	135.8	112.2
Discontinued operations (Note 2)	<u>-</u>	<u>-</u>	<u>2.6</u>
	<b><u>2,930.6</u></b>	<b><u>3,027.4</u></b>	<b><u>3,138.0</u></b>
<b>SHAREHOLDERS' EQUITY</b>			
Capital stock	<b>195.8</b>	195.6	194.7
Retained earnings	<b>1,163.7</b>	1,094.5	996.0
Foreign currency translation	<u>0.5</u>	<u>0.5</u>	<u>1.7</u>
	<b><u>1,360.0</u></b>	<b><u>1,290.6</u></b>	<b><u>1,192.4</u></b>
	<b><u>\$ 4,290.6</u></b>	<b><u>\$ 4,318.0</u></b>	<b><u>\$ 4,330.4</u></b>

See accompanying notes to the unaudited interim period consolidated financial statements.

**EMPIRE COMPANY LIMITED**  
**CONSOLIDATED STATEMENT OF RETAINED EARNINGS**  
**SIX MONTHS ENDED OCTOBER 31, 2002**  
(Unaudited, in millions)

	<u>2002</u>	<u>2001</u>
Balance, beginning of period	<b>\$1,094.5</b>	\$ 923.1
Net earnings	<b>78.6</b>	90.9
	<u>1,173.1</u>	<u>1,014.0</u>
Refundable taxes		
Paid	-	11.7
Recovered	<u>(2.3)</u>	<u>(0.7)</u>
	<u>(2.3)</u>	<u>11.0</u>
Dividends paid		
Preferred shares	<b>0.2</b>	0.3
Common shares	<u>10.8</u>	<u>6.7</u>
	<u>11.0</u>	<u>7.0</u>
Excess of purchase price over average paid-up value of common shares purchased for cancellation	<u>0.7</u>	<u>-</u>
Retained earnings, end of period	<u><b>\$1,163.7</b></u>	<u><b>\$ 996.0</b></u>

*See accompanying notes to the unaudited interim period consolidated financial statements.*

**EMPIRE COMPANY LIMITED**  
**CONSOLIDATED STATEMENT OF EARNINGS**  
**SIX MONTHS ENDED OCTOBER 31, 2002**  
(Unaudited, in millions, except per share amounts)

	<u>Three Months</u>		<u>Six Months</u>	
	<u>2002</u>	<u>2001</u>	<u>2002</u>	<u>2001</u>
Revenue	<b>\$ 2,664.9</b>	\$ 2,474.4	<b>\$ 5,352.2</b>	\$ 4,963.7
Cost of sales, selling and administrative expenses	<b><u>2,520.6</u></b>	<u>2,348.7</u>	<b><u>5,065.3</u></b>	<u>4,719.8</u>
	<b>144.3</b>	125.7	<b>286.9</b>	243.9
Depreciation	<b><u>34.7</u></b>	<u>27.7</u>	<b><u>69.3</u></b>	<u>56.0</u>
	<b>109.6</b>	98.0	<b>217.6</b>	187.9
Investment income (Note 5)	<b><u>2.1</u></b>	<u>3.8</u>	<b><u>9.3</u></b>	<u>11.5</u>
Operating income	<b><u>111.7</u></b>	<u>101.8</u>	<b><u>226.9</u></b>	<u>199.4</u>
Interest expense				
Long term debt	<b>22.0</b>	26.2	<b>44.3</b>	54.4
Short term debt	<b><u>1.4</u></b>	<u>1.7</u>	<b><u>2.5</u></b>	<u>4.0</u>
	<b><u>23.4</u></b>	<u>27.9</u>	<b><u>46.8</u></b>	<u>58.4</u>
	<b>88.3</b>	73.9	<b>180.1</b>	141.0
Capital gains and other items (Note 6)	<b><u>-</u></b>	<u>11.0</u>	<b><u>-</u></b>	<u>29.0</u>
	<b><u>88.3</u></b>	<u>84.9</u>	<b><u>180.1</u></b>	<u>170.0</u>
Income taxes				
Current income taxes	<b>32.2</b>	34.8	<b>63.5</b>	40.2
Future income taxes	<b><u>(0.1)</u></b>	<u>(6.5)</u>	<b><u>3.1</u></b>	<u>14.5</u>
	<b><u>32.1</u></b>	<u>28.3</u>	<b><u>66.6</u></b>	<u>54.7</u>
	<b>56.2</b>	56.6	<b>133.5</b>	115.3
Minority interest	<b><u>17.4</u></b>	<u>13.9</u>	<b><u>34.9</u></b>	<u>25.7</u>
Earnings before goodwill amortization	<b>38.8</b>	42.7	<b>78.6</b>	89.6
Goodwill amortization (Note 7)	<b><u>-</u></b>	<u>2.4</u>	<b><u>-</u></b>	<u>4.7</u>
Earnings from continuing operations	<b>38.8</b>	40.3	<b>78.6</b>	84.9
Earnings from discontinued operations	<b><u>-</u></b>	<u>2.0</u>	<b><u>-</u></b>	<u>6.0</u>
Net earnings	<b><u>\$ 38.8</u></b>	<u>\$ 42.3</u>	<b><u>\$ 78.6</u></b>	<u>\$ 90.9</u>
Earnings per share, basic and diluted (Note 3)				
Earnings from continuing operations	<b><u>\$ 0.59</u></b>	<u>\$ 0.61</u>	<b><u>\$ 1.19</u></b>	<u>\$ 1.29</u>
Earnings from discontinued operations	<b><u>\$ -</u></b>	<u>\$ 0.03</u>	<b><u>\$ -</u></b>	<u>\$ 0.09</u>
Net earnings	<b><u>\$ 0.59</u></b>	<u>\$ 0.64</u>	<b><u>\$ 1.19</u></b>	<u>\$ 1.38</u>

See accompanying notes to the unaudited interim period consolidated financial statements.



**EMPIRE COMPANY LIMITED**  
**CONSOLIDATED STATEMENT OF CASH FLOWS**  
**SIX MONTHS ENDED OCTOBER 31, 2002**

(Unaudited, in millions, except per share amounts)

	<u>Three Months</u>		<u>Six Months</u>	
	<u>2002</u>	<u>2001</u>	<u>2002</u>	<u>2001</u>
Cash provided by (used for) operations				
Earnings from continuing operations	\$ 38.8	\$ 40.3	\$ 78.6	\$ 84.9
Items not affecting cash (Note 8)	53.4	53.9	106.8	119.4
Payment of preferred dividends	(0.1)	(0.2)	(0.2)	(0.3)
	<u>92.1</u>	<u>94.0</u>	<u>185.2</u>	<u>204.0</u>
Net change in other current items	(28.0)	63.3	(129.2)	(14.7)
	<u>64.1</u>	<u>157.3</u>	<u>56.0</u>	<u>189.3</u>
Cash provided by (used for) financing				
Net increase (decrease) in bank loans	(54.8)	3.9	(42.5)	(12.8)
Net increase (decrease) in construction loans	(0.1)	(6.8)	0.4	(9.4)
Proceeds from issue of long term debt	4.1	4.4	8.0	17.6
Revolving securitization of accounts receivable	-	-	-	25.0
Repayment of long term debt	(24.3)	(23.9)	(41.3)	(42.7)
Increase in minority interest	0.7	0.1	3.3	4.6
Issue of Non-Voting Class A shares, net of costs	0.1	-	1.5	0.1
Purchase of Non-Voting Class A shares for cancellation	(1.6)	-	(1.6)	-
Payment of common dividends	(5.4)	(3.7)	(10.8)	(6.7)
Refundable taxes	1.2	(11.0)	2.3	(11.0)
	<u>(80.1)</u>	<u>(37.0)</u>	<u>(80.7)</u>	<u>(35.3)</u>
Total cash available (used)	<u>(16.0)</u>	<u>120.3</u>	<u>(24.7)</u>	<u>154.0</u>
Cash provided by (used for) investments				
Net decrease (increase) in investments	50.6	(29.2)	61.4	30.4
Purchase of property, equipment and other assets	(112.3)	(108.4)	(179.7)	(182.5)
Proceeds from sale of property	5.7	7.7	20.0	8.9
Increase in employee future benefit obligation	0.5	0.4	1.0	0.8
Increase in deferred foreign currency translation gains	-	0.8	-	3.5
	<u>(55.5)</u>	<u>(128.7)</u>	<u>(97.3)</u>	<u>(138.9)</u>
Total cash used	<u>(55.5)</u>	<u>(128.7)</u>	<u>(97.3)</u>	<u>(138.9)</u>
Increase (decrease) in cash from continuing operations	(71.5)	(8.4)	(122.0)	15.1
Discontinued operations (Note 2)	-	(10.2)	1.9	0.1
Cash and cash equivalents, beginning of period	254.0	124.0	302.6	90.2
Cash and cash equivalents, end of period	<u>\$ 182.5</u>	<u>\$ 105.4</u>	<u>\$ 182.5</u>	<u>\$ 105.4</u>

See accompanying notes to the unaudited interim period consolidated financial statements.

**EMPIRE COMPANY LIMITED**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**  
**OCTOBER 31, 2002**

(Unaudited, in millions, except per share amounts)

**1. Significant Accounting Policies**

**Interim financial statements**

Effective during the first quarter of the previous fiscal year, the Company adopted the Canadian Institute of Chartered Accountants handbook section 1751 relating to interim financial statements. The accounting policies used in the preparation of these interim consolidated financial statements conform with those used in the Company's annual consolidated financial statements. These interim consolidated financial statements do not include all of the disclosures included in the Company's annual consolidated financial statements. Accordingly, these interim consolidated financial statements should be read in conjunction with the consolidated financial statements for the year ended April 30, 2002, as set out in the Annual Report 2002.

**Goodwill**

Effective May 1, 2002, the Company prospectively implemented the recommendations of the new handbook section 3062 issued by the Canadian Institute of Chartered Accountants on goodwill and other intangible assets. Under the new standard, goodwill and intangible assets with indefinite useful lives are no longer amortized but are subject to an annual impairment review. Any permanent impairment in the book value of goodwill and intangible assets will be written off against earnings. The Company has completed its review and has determined that no adjustment is required to the carrying value of goodwill.

**Stock-based compensation plans**

Effective May 1, 2002, the Company adopted the Canadian Institute of Chartered Accountants new handbook section 3870 relating to stock-based compensation plans. This section has been implemented retroactively without restatement of the prior period financial statements. No adjustment to retained earnings is required as a result of implementing this section.

The Directors of the Company and its subsidiary, Sobeys Inc., can choose to defer the receipt of their compensation and have the ultimate amount to be received tied to the market value of their respective Company's stock. The deferred amounts are to be paid when they cease to be a Director. The Company records a liability based on the current market value of the Companies' stock. At October 31, 2002 the liability recorded under the plans is \$1.3.

The Company has a stock option plan that allows holders to purchase Non-Voting Class A shares at \$6.555 per share. Options expire at dates from April 2003 to October 2006. At October 31, 2002 81,074 options were outstanding and no new options were granted during the quarter. During the six months ended October 31, 2002 13,600 options were exercised resulting in 13,600 Non-Voting Class A shares being issued for \$0.1.

**2. Discontinued Operations**

On April 1, 2002 the Company's subsidiary, Sobeys Inc., announced completion of the sale of substantially all of the assets of its SERCA Foodservice operations. SERCA Foodservice distributed foodservice products to primarily hospitality, institutional and commercial customers throughout Canada.

The revenues of the discontinued operations were \$1,156.4 for the six months ended October 31, 2001.

Earnings from discontinued operations during the six months ended October 31, 2001 were \$6.0.

Interest on other debt that is not directly attributable to the discontinued operations was not allocated to the discontinued operations.

Current assets of discontinued operations at April 30, 2002 and October 31, 2002 were comprised of assets for resale. Noncurrent assets of discontinued operations at October 31, 2001 were comprised principally of fixed assets and goodwill.

Cash flow from discontinued operations for the six months ended October 31, 2002, included cash generated by investing activities of \$1.9. Cash flow from discontinued operations for the six months ended October 31, 2001, included cash used by operating activities by SERCA Foodservice of \$1.9, cash generated by investing activities of \$2.2 and cash used by financing activities of \$0.2.

**EMPIRE COMPANY LIMITED**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**  
**OCTOBER 31, 2002**

(Unaudited, in millions, except per share amounts)

**3. Net Earnings Per Share**

Net earnings per share amounts are calculated on the weighted average number of shares outstanding (2002-65,805,000 shares; 2001-65,670,000 shares) after providing for preference share dividends accrued to the balance sheet date. Diluted earnings per share have been calculated on the assumption that all the outstanding stock options were exercised at the beginning of the period. Effective October 7, 2002 both the Class A shares and Class B shares were split on the basis of two-for-one.

Earnings applicable to common shares is comprised of the following:

	<u>Three Months</u>		<u>Six Months</u>	
	<u>2002</u>	2001	<u>2002</u>	2001
Earnings before goodwill amortization	\$ 38.8	\$ 42.7	\$ 78.6	\$ 89.6
Goodwill amortization	-	2.4	-	4.7
Earnings from continuing operations	38.8	40.3	78.6	84.9
Capital gains and other items, net of taxes of \$0.2 (2001 \$(0.2))	<u>(0.2)</u>	10.9	<u>(0.2)</u>	29.2
	39.0	29.4	78.8	55.7
Earnings from discontinued operations	-	2.0	-	6.0
Operating earnings	39.0	31.4	78.8	61.7
Capital gains and other items	<u>(0.2)</u>	10.9	<u>(0.2)</u>	29.2
Net earnings	38.8	42.3	78.6	90.9
Preferred share dividends	<u>0.1</u>	0.2	<u>0.2</u>	0.3
Earnings applicable to common shares	<u>\$ 38.7</u>	<u>\$ 42.1</u>	<u>\$ 78.4</u>	<u>\$ 90.6</u>

Earnings per share is comprised of the following:

Earnings before goodwill amortization applicable to common shares	\$ 0.59	\$ 0.64	\$ 1.19	\$ 1.36
Goodwill amortization	-	0.03	-	0.07
Earnings from continuing operations	0.59	0.61	1.19	1.29
Capital gains and other items, net of taxes	-	0.16	-	0.44
	0.59	0.45	1.19	0.85
Earnings from discontinued operations	-	0.03	-	0.09
Operating earnings	0.59	0.48	1.19	0.94
Capital gains and other items	-	0.16	-	0.44
Net earnings per share	<u>\$ 0.59</u>	<u>\$ 0.64</u>	<u>\$ 1.19</u>	<u>\$ 1.38</u>

**4. Other Assets**

	<u>October 31</u>	April 30	October 31
	<u>2002</u>	2002	2001
Mortgages and loans	\$ 105.8	\$ 109.0	\$ 121.5
Goodwill (less accumulated amortization of \$56.1; April 30, 2002 \$56.1; October 31, 2001 \$48.0)	565.1	565.8	561.3
Deferred charges	<u>126.3</u>	<u>121.4</u>	<u>120.7</u>
	<u>\$ 797.2</u>	<u>\$ 796.2</u>	<u>\$ 803.5</u>

**EMPIRE COMPANY LIMITED**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**  
**OCTOBER 31, 2002**

(Unaudited, in millions, except per share amounts)

**5. Investment Income**

	<u>Three Months</u>		<u>Six Months</u>	
	<u>2002</u>	<u>2001</u>	<u>2002</u>	<u>2001</u>
Dividend and interest income	\$ 2.5	\$ 3.0	\$ 9.2	\$ 9.3
Share of income of companies accounted for by the equity method	<u>(0.4)</u>	<u>0.8</u>	<u>0.1</u>	<u>2.2</u>
	<u>\$ 2.1</u>	<u>\$ 3.8</u>	<u>\$ 9.3</u>	<u>\$ 11.5</u>

**6. Capital Gains and Other Items**

	<u>Three Months</u>		<u>Six Months</u>	
	<u>2002</u>	<u>2001</u>	<u>2002</u>	<u>2001</u>
Gain on sale of investments	\$ -	\$ 11.8	\$ -	\$ 30.3
Foreign currency translation loss	-	(1.2)	-	(1.2)
Loss on disposal of properties	-	0.4	-	(0.1)
	<u>\$ -</u>	<u>\$ 11.0</u>	<u>\$ -</u>	<u>\$ 29.0</u>

**7. Goodwill Amortization**

	<u>Three Months</u>		<u>Six Months</u>	
	<u>2002</u>	<u>2001</u>	<u>2002</u>	<u>2001</u>
Amortization of goodwill	\$ -	\$ 4.0	\$ -	\$ 8.0
Income taxes	-	(0.1)	-	(0.3)
Minority interest	-	(1.5)	-	(3.0)
	<u>\$ -</u>	<u>\$ 2.4</u>	<u>\$ -</u>	<u>\$ 4.7</u>

**8. Supplementary Cash Flow Information**

	<u>Three Months</u>		<u>Six Months</u>	
	<u>2002</u>	<u>2001</u>	<u>2002</u>	<u>2001</u>
<b>a.) Items not affecting cash</b>				
Depreciation	\$ 34.7	\$ 27.7	\$ 69.3	\$ 56.0
Goodwill amortization	-	4.0	-	8.0
Future income taxes	(0.3)	10.4	0.2	31.4
Amortization of deferred items	3.5	2.7	7.0	7.4
Equity in earnings of other companies, net of dividends received	0.4	(0.8)	(0.1)	(2.2)
Minority interest	15.1	9.9	30.4	18.8
	<u>\$ 53.4</u>	<u>\$ 53.9</u>	<u>\$ 106.8</u>	<u>\$ 119.4</u>
<b>b.) Other cash flow information</b>				
Interest paid	<u>\$ 24.2</u>	<u>\$ 34.3</u>	<u>\$ 39.0</u>	<u>\$ 59.1</u>
Income taxes paid	<u>\$ 18.3</u>	<u>\$ 24.3</u>	<u>\$ 64.9</u>	<u>\$ 69.7</u>

**EMPIRE COMPANY LIMITED**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**  
**OCTOBER 31, 2002**

(Unaudited, in millions, except per share amounts)

**9. Segmented Information**

	<u>Three Months</u>		<u>Six Months</u>	
	<u>2002</u>	<u>2001</u>	<u>2002</u>	<u>2001</u>
<b>Revenue</b>				
Food distribution	<b>\$ 2,613.4</b>	\$ 2,427.4	<b>\$ 5,251.1</b>	\$ 4,871.8
Real estate				
Outside	<b>36.8</b>	34.3	<b>69.7</b>	65.9
Inter-segment	<b>11.4</b>	11.7	<b>23.3</b>	22.9
	<b>48.2</b>	46.0	<b>93.0</b>	88.8
Other operations	<b>14.7</b>	12.7	<b>31.4</b>	26.0
	<b>2,676.3</b>	2,486.1	<b>5,375.5</b>	4,986.6
Elimination	<b>(11.4)</b>	(11.7)	<b>(23.3)</b>	(22.9)
	<b>\$ 2,664.9</b>	\$ 2,474.4	<b>\$ 5,352.2</b>	\$ 4,963.7
<b>Operating income</b>				
Food distribution	<b>\$ 82.7</b>	\$ 72.9	<b>\$ 167.0</b>	\$ 140.3
Real estate	<b>26.7</b>	25.0	<b>49.2</b>	47.3
Other operations	<b>2.1</b>	1.8	<b>5.1</b>	4.0
Investment income	<b>2.1</b>	3.8	<b>9.3</b>	11.5
Corporate expenses	<b>(1.9)</b>	(1.7)	<b>(3.7)</b>	(3.7)
	<b>\$ 111.7</b>	\$ 101.8	<b>\$ 226.9</b>	\$ 199.4

**10. Comparative Figures**

Comparative figures have been reclassified, where necessary, to reflect the current period's presentation, including disclosure for discontinued operations.

## **Empire Company Limited**

### **Management's Discussion and Analysis**

#### **Interim Report**

Empire Company Limited ("Empire" or the "Company") is a diversified Canadian company headquartered in Stellarton, Nova Scotia. Empire's key businesses are retail food distribution (through majority ownership of Sobeys Inc. ("Sobeys")), real estate (primarily through wholly-owned Atlantic Shopping Centres Limited ("ASC") and Sobey Leased Properties Limited ("SLP") managing 12.1 million square feet of leasable space), and corporate investment activities and other operations (which includes wholly-owned Empire Theatres Limited). With \$4.3 billion in assets, Empire employs approximately 34,000 people directly and through its subsidiaries.

The following is a discussion and analysis of the interim consolidated financial condition and results of operations of Empire for the three-month period ended October 31, 2002. This discussion may contain forward-looking statements about the future performance of the Company. The statements are based on management's assumptions and beliefs in light of the information herein. These forward-looking statements are subject to uncertainties and other factors that could cause actual results to differ materially from such statements. Additional financial information has been filed electronically with various securities commissions in Canada through SEDAR.

This document should be read in conjunction with: the Interim Consolidated Financial Statements of Empire Company Limited and notes thereto for the three-month period ended October 31, 2002; Management's Discussion and Analysis included in the Annual Report of the Company for the year ended April 30, 2002; and the Consolidated Financial Statements and notes thereto for the year ended April 30, 2002.

The financial information presented in this report includes the contribution of Sobeys Inc.'s retail grocery distribution business. SERCA Foodservice ("SERCA") operations are not reflected in Empire's consolidated sales, cost of sales, selling and administrative expense, depreciation, interest expense or income tax expense. SERCA has been accounted for as a discontinued operation, reflecting the sale of substantially all of the net assets of SERCA on March 30, 2002.

## Consolidated Operating Results

For the three month period ended October 31, 2002, Empire reported operating earnings before net capital gains, other items and goodwill amortization (“operating earnings”) of \$39.0 million or \$0.59 per share, up 14 percent in dollar terms and 13 percent on a per share basis over the previous fiscal year. All operating companies recorded improved earnings over the second quarter of fiscal 2002. For the six months ended October 31, 2002, operating earnings totalled \$78.8 million, up \$11.3 million or 17 percent over the comparable period of the previous fiscal year.

Second quarter revenue reached \$2.66 billion, an improvement of 7.7 percent over the second quarter of fiscal 2002. The Food Division contributed revenue of \$2.61 billion versus \$2.43 billion contributed in the second quarter last year. Real estate revenues (net of inter-company elimination) improved 7.3 percent and Other Operations reported revenue growth of 15.7 percent. Revenue for the first half of the current fiscal year equalled \$5.35 billion versus \$4.96 billion in fiscal 2002.

Operating income for the three month period ended October 31, 2002 totalled \$111.7 million, an increase of \$9.9 million or 9.7 percent compared to the same period of the previous fiscal year. All operating companies recorded improvement in EBITDA margin (earnings before interest, taxes, depreciation and amortization charges over revenue) over last year. Improved EBITDA dollars more than offset a 25 percent increase in depreciation expense in the quarter. The higher depreciation expense is primarily the result of the food division’s capital spending program. Operating income for the first six months of fiscal 2003 reached \$226.9 million, an increase of \$27.5 million or 14 percent compared to the same period last year.

Interest expense declined \$4.5 million or 16 percent in the second quarter of fiscal 2003 and \$11.6 million or 20 percent year-to-date. Interest on long-term debt amounted to \$22.0 million, down 16 percent from the same period last year, while interest on short-term debt decreased 17 percent from last year. The decrease was due primarily to a reduction in funded debt coincident with the application of a portion of SERCA sale proceeds to reduce indebtedness.

The effective income tax rate applicable to the Company’s operating earnings for the second quarter was 36.4 percent versus 38.3 percent in quarter two of fiscal 2002. The decrease in rate is primarily the result of statutory rate reductions.

Empire recorded a net capital loss of \$0.2 million in the second quarter of fiscal 2003 compared to a net capital gain of \$10.9 million in the second quarter of fiscal 2002, primarily from the sale of investments. A net capital loss of \$0.2 million has been recorded year-to-date in the current fiscal year, while net capital gains for the first half of the previous fiscal year totalled \$29.2 million.

Net earnings totalled \$38.8 million or \$0.59 per share for the three month period ended October 31, 2002 versus \$42.3 million or \$0.64 for the same period last year. The difference is the result of net capital gains of \$10.9 million generated in quarter two of fiscal 2002, partially offset by stronger operating earnings recorded in the second quarter of fiscal 2003 against fiscal 2002. Net earnings for the first half of fiscal 2003 amounted to \$78.6 million, down \$12.3 million from the \$90.9 million recorded in the six months ended October 31, 2001. The decline is a result of the net capital gains recorded from the sale of investments in the first half of fiscal 2002; partially offset by stronger year-to-date operating results in fiscal 2003.

## **Operating Overview & Performance by Segment**

### **FOOD DISTRIBUTION**

Empire's food distribution business is carried on through its 62 percent ownership in Sobeys. Sobeys recorded second quarter sales of \$2.61 billion, an increase of 7.7 percent compared to the second quarter of fiscal 2002. Same store sales (excluding expanded stores) grew by 2.4 percent during the quarter and by 3.6 percent when including expanded stores. Sobeys' second quarter sales growth was driven by favorable sales increases in all regions, resulting from the combined impact of real growth generated by executing a number of program initiatives directed at satisfying the unique needs of each of our customer segments, increased square footage added to Sobeys' retail store network during the past 12 months, and inflation of approximately 1.0 percent. Year-to-date performance exhibited similar trends: total sales were 7.8 percent higher than the prior year, with same store sales growth of 2.9 percent (4.2 percent including expanded stores).

Sobeys reported net earnings of \$46.6 million (\$0.71 per share), 33 percent higher than the \$35.1 million (\$0.53 per share) earned in the same period of fiscal 2002. Effective the first quarter of fiscal 2003 Sobeys discontinued the amortization of goodwill consistent with the new accounting standard issued by the CICA on goodwill and other intangible assets. Had goodwill not been amortized in quarter two of fiscal 2002, net operating earnings in quarter two last year would have been \$4.7 million higher or \$39.8 million (\$0.60 per share). Adjusting for goodwill amortization in the second quarter last year, Sobeys' earnings grew by 17 percent. This performance represents a continuation of the positive trend established in the first quarter and exceeds Sobeys' fiscal 2003 objective of 12 to 16 percent growth in net operating earnings.



The year-over-year earnings growth in the Food Division is the result of a number of factors, including EBITDA improvement, lower interest expense, and a decline in the Company's effective tax rate.

Sobeys' EBITDA for the three month period ended November 2, 2002, was \$113.9 million, which is 18 percent higher than the \$96.4 million recorded in the same period last year. EBITDA as a percentage of sales increased 39 basis points to 4.36 percent. This represents the fifth consecutive quarter of year-over-year margin improvement. The EBITDA margin gain was due to a continuation of the Food Division's margin development and disciplined cost management initiatives throughout the entire supply chain which were implemented in fiscal 2002. The programs implemented in the areas of national merchandising, distribution and logistics, and selling, general and administrative ("SG&A") cost streamlining were primarily responsible for the second quarter EBITDA growth, and they are expected to further contribute to operating margin throughout the second half of fiscal 2003.

Operating income or earnings before interest and taxes ("EBIT") amounted to \$84.1 million, an increase of 15 percent over the second quarter of fiscal 2002. Operating income for the first half of fiscal 2003 increased \$28.1 million or 20 percent compared to the same period in fiscal 2002. The increase in the second quarter and year-to-date is attributable to the increase in EBITDA dollars partially offset by an increase in depreciation expense. The increased depreciation expense in the quarter and for the first half of fiscal 2003 is a result of Sobeys' capital spending program.

Second quarter interest expense declined \$3.6 million or 26 percent versus the same period in the previous fiscal year, while interest expense for the first half of the fiscal year declined \$9.3 million or 32 percent. The decline for the second quarter and year-to-date is primarily the result of a decline in borrowing levels due to the use of a portion of the SERCA sale proceeds, received in quarter four of fiscal 2002. Interest coverage (operating income divided by interest expense) on a twelve month trailing basis for the Food Division improved to 8.4 times at October 31, 2002 compared to 5.4 times last year.

The Food Division's effective tax rate for the second quarter was 37.1 percent versus 39.8 percent for the same period last year. The decline is primarily the result of statutory tax rate reductions.

## **REAL ESTATE**

Empire's real estate operations are primarily conducted through wholly-owned Atlantic Shopping Centres Limited and Sobey Leased Properties Limited, and a 35 percent ownership position in Genstar Development Partnership ("Genstar").

Operating income in the three month period ended October 31, 2002 was \$26.7 million, relatively unchanged from the \$25.0 million recorded in the comparable period last year. Real estate contributed 24 percent of Empire's second quarter consolidated operating income. For the first half of fiscal 2003, the real estate division reported operating income of \$49.2 million, up 4% over the comparable period last year.

Real estate earnings improvement is primarily the result of continued strong financial performance from Genstar and ASC. ASC improved its operating performance primarily through the benefits of its on-going development activity. Total occupancy rate at the end of the quarter was 92.2 percent versus 94.4 percent at the same time last year.

Funds from operations ("FFO"), or earnings before net capital gains and other items plus depreciation, generated in the second quarter totalled \$13.1 million, up 25 percent or \$2.6 million over the same quarter of fiscal 2002. Year-to-date FFO reached \$23.1 million versus \$18.8 million generated in the first half of fiscal 2002. The twelve month trailing Real Estate group FFO have increased to \$52.5 million versus \$34.7 million in the prior twelve month period. The improved year-to-date and twelve month trailing FFO performance is primarily as a result of increased FFO from Genstar as a result of strong lot sales.

#### **INVESTMENTS AND OTHER OPERATIONS**

The third component of Empire's business is its investments, consisting of a portfolio of equity investments, and other operations. At October 31, 2002 Empire's total investments at the holding company level carried a market value, excluding cash and cash equivalents, of \$360.9 million on a carrying value of \$459.6 million, resulting in an unrealized loss of \$98.7 million. For the first six months of fiscal 2003, the total return on Empire's portfolio was down approximately 30 percent, below the total return performance of the S&P 500 index (down approximately 18 percent) and the S&P/TSX index (down approximately 19 percent) over the same period. This downturn in Empire's investment portfolio performance is primarily the result of the decline in the share price of Empire's Delhaize Group investment. On October 31, 2002 Delhaize Group shares closed at a price of 15.75 Euro, down 59 percent from the July 31, 2002 closing share price of 38.80 Euro. This price decline is responsible for about three-quarters of the change in unrealized losses from \$16 million at July 31, 2002 to \$98.7 million at October 31, 2002. Excluding the negative 62.8 percent total return recorded by Delhaize in the first half of fiscal 2003, the total return on Empire's investment portfolio is negative 17.7 percent, relatively consistent with the major market indices previously mentioned. At October 31, 2002, the Company continued to hold 1.7 million shares of Delhaize.

The other contributing factor to the Company's negative investment portfolio performance continues to be the general decline in equity markets, with the S&P/TSX index off 5.4 percent and the S&P 500 index off 2.8 percent from August 1, 2002 through October 31, 2002.

Investment income of \$2.1 million for the quarter was below last year's result of \$3.8 million. The decline of \$1.7 million is attributable to a decrease in equity accounted earnings contribution from Empire's only equity accounted investment, Wajax Limited ("Wajax") of \$1.2 million combined with a decrease of \$0.5 million in interest and dividend income from other portfolio investments.

Other operation's contribution to Empire's operating income increased by \$0.3 million in the second quarter of fiscal 2003. This increase is primarily the result of strong revenue growth, good film quality and continued expense control at wholly-owned Empire Theatres Limited.

## **Consolidated Financial Position**

### **ASSETS**

Total assets at the end of the second quarter totalled \$4,290.6 million, relatively unchanged from the \$4,317.1 million reported at July 31, 2002 and \$4,318.0 million reported at the previous year-end, April 30, 2002.

### **NET ASSET VALUE**

At October 31, 2002 management calculates Empire's consolidated net asset value ("NAV") at \$2,145 million or \$32.59 per share, compared to \$2,362 million or \$35.89 per share at July 31, 2002. The decrease is primarily attributable to a decline in the market value of the Company's investment in Sobeys of \$135 million and a decline in the market value of Empire's Delhaize Group investment of \$69 million.

## **Capital Resources and Liquidity**

Empire's net debt to capital ratio was 28.8 percent at October 31, 2002, consistent with the ratio reported at July 31, 2002. Interest coverage (operating income divided by interest expense) at October 31, 2002 was 4.8 times, relatively unchanged from July 31, 2002.

Short-term liquidity remains strong as a result of internally generated cash flow, net cash on hand, and unutilized bank credit lines for operating, general and corporate purposes of \$325 million. Bank lines were 41 percent utilized at October 31, 2002. Including subsidiaries, the Company's consolidated authorized bank credit facilities exceeded borrowings by \$629.1 million at October 31, 2002.

## **CASH FLOWS**

Second quarter cash flow from operating activities was \$64.1 million compared to \$157.3 million in the comparable period last year, a decrease of \$93.2 million. The decline was due to a net change in other current items of negative \$91.3 million, resulting primarily from an increase in inventory in the quarter while payables declined. The increase in inventory is largely the result of Sobeys recording higher inventories due to seasonal factors and expansion of their store network.

For the three month period ended October 31, 2002, cash flows used for investment activities equalled \$55.5 million versus \$128.7 million in the same period last year. The decrease in cash used for investments is largely the result of increased cash provided by the sale of investments in the second quarter of fiscal 2003.

Financing activities during the second quarter of fiscal 2003 used cash of \$80.1 million compared to \$37.0 million in the same period of fiscal 2002. The year-over-year difference is primarily the result of the Company paying short-term bank loans with cash on hand.

## **Risk and Risk Management**

Risk and uncertainties related to economic and industry factors and Empire's management of this risk, as discussed in detail in the "Management's Discussion and Analysis" section of the Company's fiscal 2002 annual report, remain substantially unchanged.

## **Accounting Policy Changes**

In the first quarter ended July 31, 2002, the Company implemented the CICA accounting standard pertaining to goodwill and other intangible assets, Section 3062. Under this standard, goodwill and intangible assets with indefinite useful lives are no longer amortized, but are subject to impairment tests on at least an annual basis. Empire and its operating companies have completed their review and have determined that the book value of existing goodwill is not impaired.

Also effective in the first quarter, the Company adopted CICA accounting standard, Section 3870, "Stock-based Compensation and Other Stock-based Payments". While the Company's long-term incentive plan for executives provides for the issuance of stock options, the Company ceased issuing options in 1996, and as of October 31, 2002 had 81,074 options outstanding. Adopting this standard does not have an effect on Empire's financial statements.

## **Outlook**

As a result of the Company's second quarter results, Empire's trailing (last four quarters) operating earnings (before goodwill amortization) per share now equal \$2.32 per share versus \$1.67 per share last year, a 39 percent increase. Empire remains well positioned to continue its earnings growth through fiscal 2003.

Empire projects stronger financial performance in fiscal 2003, primarily as a result of continued growth in contribution from each of its operating businesses. Management has assumed the continuation of the current competitive environment and has factored in conservative cost of capital assumptions. The Company is committed to growing value in each of its divisions and, thereby growing value in Empire Company Limited on behalf of all shareholders.

## **INVESTOR INFORMATION**

### **EMPIRE COMPANY LIMITED**

Head Office  
115 King Street  
Stellarton, Nova Scotia  
B0K 1S0  
Telephone: (902) 755-4440  
Fax: (902) 755-6477  
Internet: [www.empireco.ca](http://www.empireco.ca)

### **INVESTOR RELATIONS**

For additional information please write to the Company, c/o Stewart H. Mahoney, CFA Vice President, Treasury and Investor Relations  
E-mail: [investor.relations@empireco.ca](mailto:investor.relations@empireco.ca)

### **STOCK EXCHANGE LISTINGS**

The Toronto Stock Exchange

### **STOCK SYMBOLS**

Non-voting Class A shares - EMP.A  
Preferred shares:  
Series 2 - EMP.PR.B

### **AVERAGE DAILY TRADING VOLUME (TSE)**

22,813

### **COMMON DIVIDEND RECORD AND PAYMENT DATES FOR FISCAL 2003**

Record Date	Payment Date
Jan. 15th, 2003	Jan. 31st, 2003
Apr. 15th, 2003*	Apr. 30th, 2003*
July 15th, 2003*	July 31st, 2003*
Oct. 15th, 2003*	Oct. 31st, 2003*

\*subject to approval by Board of Directors

### **OUTSTANDING SHARES**

As of December 12, 2002	
Non-Voting Class A common	30,859,602
Options exercisable with Class A common shares	68,874
Class B common, voting	34,897,456

### **TRANSFER AGENTS**

Computershare Trust Company of Canada  
Telephone: (800) 564-6253  
Non-voting Class A shares

CIBC Mellon Trust Company  
Telephone: (902) 420-3821  
Series 2 Preferred shares

### **MULTIPLE MAILINGS**

If you have more than one account, you may receive a separate annual report for each. If this occurs, please contact Computershare at (902) 420-3557 to eliminate the multiple mailings.

### **INVESTOR INQUIRIES**

Communications regarding investor records including changes of address or ownership, should be directed to the Company's transfer agent, Computershare Trust Company of Canada, at the above contact information.

Shareholders, analysts and investors should direct their financial inquiries or requests to Stewart H. Mahoney.

### **EXEMPLAIRE FRANÇAIS**

Vous pouvez obtenir un exemplaire français de ce rapport annuel en écrivant à:  
Empire Company Limited  
Investor Relations  
115 King Street  
Stellarton, Nova Scotia  
B0K 1S0

