

# UNIQUELY



# Financial Highlights

(\$ in millions except for per share amounts)

	2005	2004	% Change
<b>Consolidated</b>			
Gross operating revenue	\$ 7,774.6	\$ 7,153.6	8.7%
Earnings before income taxes and minority interest	527.7	460.9	14.5%
Income taxes	190.0	162.5	16.9%
Net earnings	330.1	291.5	13.3%
Cash generated from operations	721.2	630.4	14.4%
Cash generated from operating activities	438.1	413.1	6.1%
Dividends	45.7	38.5	19.0%
<b>Per share</b>			
Basic earnings	\$ 4.04	\$ 3.60	12.2%
Diluted earnings	3.98	3.53	12.7%
Cash generated from operations	8.82	7.78	13.3%
Cash generated from operating activities	5.36	5.10	5.1%
Dividends declared	0.58	0.50	16.0%
Shareholders' equity	30.83	27.75	11.1%
Number of shares outstanding - weighted average	81,764,082	80,983,467	
<b>Ratios<sup>1</sup></b>			
Current ratio	1.6	1.6	
Canadian Tire Retail inventory turnover	9.6	9.7	
Long-term debt to total capitalization	31.7%	28.9%	
Interest coverage	7.3	6.9	
Return on equity	13.9%	13.7%	

Strategic Plan key metrics <sup>1</sup>	2001-2005 Performance <sup>2</sup>	2005 Performance	2005-2009 Aspirational Targets
Canadian Tire Retail comparable store sales <sup>3</sup>	2.6%	3.0%	3%-4% per annum
Gross operating revenue <sup>4</sup>	8.3%	8.7%	7%-9% compound annual growth
EBITDA <sup>5</sup> and minority interest <sup>4</sup>	11.7%	12.2%	10%-15% compound annual growth
Basic earnings per share <sup>4</sup>	16.9%	12.2%	12% to 15% compound annual growth
After-tax return on invested capital <sup>3</sup>	8.7%	9.7%	10% after tax

<sup>1</sup> Formulae for certain ratios and metrics can be found in the glossary of this Annual Report on page 113.

<sup>2</sup> Performance from the beginning of fiscal 2001 to the end of fiscal 2005.

<sup>3</sup> For 2001 to 2005 Performance, results are an average of 2005, 2004, 2003, 2002 and 2001 percentages.

<sup>4</sup> Plan goals and performance for these metrics are expressed in terms of a compound annual growth rate (CAGR).

<sup>5</sup> Earnings before interest, income taxes, depreciation and amortization. See section 12 on non-GAAP measures in Management's Discussion and Analysis section of this Annual Report.

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Canadian Tire's unique business platform, market position and deep-rooted customer relationships provide the basis for sustainable long-term earnings growth. We have one of Canada's most recognized and trusted brands. We meet customers' needs through three retail banners, a vibrant financial services business and through Canada's largest independent gasoline retailer.

We are leveraging our customer relationships by taking advantage of significant opportunities for growth in each of our businesses and by leveraging synergies within our inter-related network of businesses.

# 24.7%

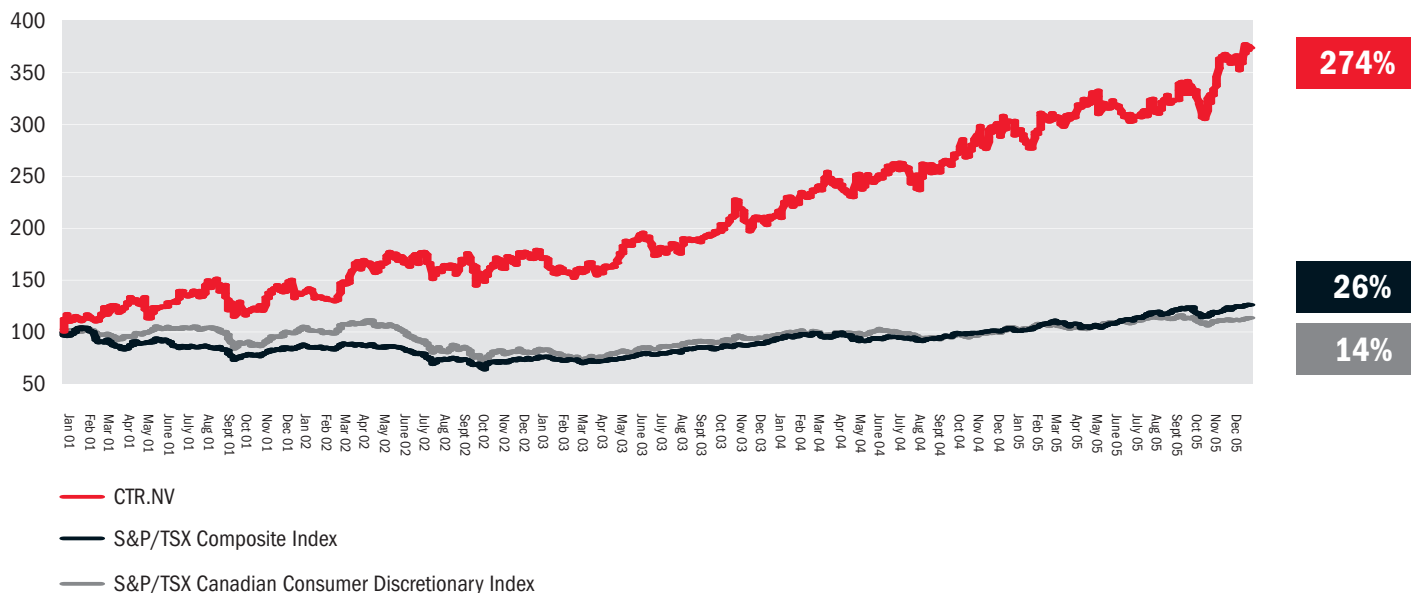
2005 total return to shareholders (TRS<sup>1</sup>)

<sup>1</sup> Total return to shareholders - TRS - consists of share price appreciation plus dividends.

Since December 29, 2000, Canadian Tire has delivered cumulative TRS of 286%, **ranking us in the top quartile of retailers in Canada and the United States.**

### Five Year Class A Non-Voting Shares (CTR.NV)

Stock price appreciation versus the S&P/TSX Composite Index and Canadian Consumer Discretionary Index (December 29, 2000 to December 31, 2005)



Canadian Tire Corporation, Limited is an inter-related network of businesses engaged in retail, petroleum and financial services, with more than 1,100 stores, gas bars and car washes.

# Uniquely Positioned for Growth



## Canadian Tire Retail: Positioned for growth

Canadian Tire Retail (CTR), Canada's most-shopped general merchandise retailer with 462 stores, offers a large selection of national and private label brands through three product divisions: Automotive Parts, Accessories and Service; Sports and Leisure Products; and Home Products. As of March 2006, we have approximately 15,500 products posted on [www.canadiantire.ca](http://www.canadiantire.ca), our online web store. CTR's store renewal program gives customers an inspiring place to shop for innovative products sourced worldwide. Canadian Tire Retail also operates 57 PartSource stores, including three recently acquired stores that will be re-branded to the PartSource brand in 2006, offering automotive parts and professional advice to commercial installers, serious "do-it-yourselfers" and automotive enthusiasts.



## Mark's Work Wearhouse: Creating a Superbrand

Mark's Work Wearhouse (Mark's) is one of the largest specialty retailers in Canada, offering men's and women's clothing, footwear and accessories for business casual and industrial work environments, as well as for recreational use or leisure. Mark's Work Wearhouse now operates 334 stores across Canada, including 37 under the L'Équipeur brand in Quebec. Mark's "Clothes That Work" marketing philosophy reinforces the quality and depth of their product offering and provides an exceptional opportunity to increase our market penetration.

### Canadian Tire Retail

2005

### Mark's Work Wearhouse

2005

% change versus 2004

% change versus 2004

Retail sales	<b>5.1%</b>
Same store sales	<b>3.4%</b>
Comparable store sales	<b>3.0%</b>
Net shipments	<b>4.2%</b>
Gross operating revenue	<b>4.3%</b>
Earnings before income taxes and minority interest	<b>6.8%</b>

Retail sales	<b>20.3%</b>
Same store sales	<b>17.4%</b>
Gross operating revenue	<b>21.7%</b>
Earnings before income taxes	<b>75.2%</b>

Our customer offering is unparalleled in terms of locations, products and services. Our unique businesses reach customers daily through innovative product and service offerings, and we build customer loyalty through Canada's most successful loyalty program, Canadian Tire 'Money'. Canadian Tire's market differentiation and business platform provide unique growth opportunities that support the Company's financial aspirations and performance objective of achieving top-quartile total return to shareholders among retailers in Canada and the United States.



### Canadian Tire Petroleum: Leveraging the brand

Canadian Tire Petroleum (Petroleum) is Canada's largest independent retailer of gasoline, operating 259 gasoline sites that pump, on average, twice the gasoline volume of competitor gas sites in Canada. Petroleum also operates 67 car washes, 247 convenience stores and kiosks, 13 Pit Stops and 77 sites with propane stations across the country. Our new premium convenience store centres that we call Q respond to customer needs for faster, more convenient service and a broad assortment of products. Petroleum is an integral part of our total value proposition as it drives customers to Canadian Tire stores with Canadian Tire 'Money' and encourages customers to use the Canadian Tire MasterCard® issued by our Financial Services business, which provides electronic Canadian Tire 'Money' on the card for instant redemption in Canadian Tire stores.



### Canadian Tire Financial Services: Capitalizing on deep customer roots

Canadian Tire Financial Services (Financial Services) offers Canadian Tire-branded credit cards that give customers increased rewards with Canadian Tire 'Money' on the card. The division also offers personal loans and markets a variety of insurance and warranty products, in addition to operating an emergency roadside service and award-winning call centres, providing daily opportunities to build strong relationships with customers. Financial Services' deep roots with customers and connections to our other businesses represent a tremendous opportunity to expand the breadth of our products and services to Canadian Tire customers.

#### Canadian Tire Petroleum

2005

% change versus 2004

Gasoline sales volume (in litres)	<b>6.4%</b>
Convenience sales	<b>12.7%</b>
Car wash sales	<b>26.3%</b>
Gross operating revenue	<b>20.3%</b>
Earnings before income taxes	<b>118.9%</b>

#### Canadian Tire Financial Services

2005

% change versus 2004

Net managed portfolio of loans receivable	<b>17.7%</b>
Gross operating revenue	<b>12.2%</b>
Earnings before income taxes	<b>11.1%</b>

# 2005 Performance Scorecard

## Canadian Tire Retail



**Mark Foote**  
President,  
Canadian Tire Retail

### Initiative

### 2005 Performance Goals

#### Revitalize store network

Build 20 new stores.

#### Concept 20/20 (C20/20)

Most of the new stores planned to open in 2005 will be C20/20 stores. Fifteen existing new-format stores will be retrofitted to the C20/20 format.

#### Customer values

Continue to improve our in-stock position on promotional products.

Continue to use eLearning as a key tool for developing employee product knowledge.

#### CustomerLink supply chain improvements

Complete the CustomerLink program in 2005 according to schedule and budget.

#### Exciting, New and Exclusive (ENE) products

Continue to increase sales of ENE products.

#### Enhance automotive infrastructure and grow Auto Parts and Service

Continue to make progress toward growing automotive service market share.

## Mark's Work Wearhouse



**Paul Wilson** (left)  
President and  
Chief Operating Officer,  
Mark's Work Wearhouse

**Mike Lambert** (right)  
President, Mark's Work Wearhouse  
and Executive Vice-President,  
Canadian Tire

#### Grow total same store sales

Increase total same store sales by 5.3 percent.

#### Continue network development by opening new stores, relocating existing locations and renovating older stores to the new Mark's format

Open up to 21 stores and increase retail square footage to 2.6 million.

#### Continued development of consumer awareness of the Mark's brand and their understanding of Mark's and "Clothes That Work"

Deliver 10 product launches, three incremental flyers, two incremental spend-and-save events and two events that marry gift cards and flyers to continue development of consumer awareness of Mark's and the "Clothes That Work" message.

**2005 Actual Performance<sup>1</sup>****2006 Performance Goals**

Built 18 new stores.

Build approximately 20 new stores.

Seventeen of the 18 new-format stores opened in 2005 were C20/20 stores and 11 existing stores were retrofitted to the same format. As of the end of 2005, 53 stores were C20/20 stores.

Substantially all new stores planned to open in 2006 will be C20/20 stores. Approximately 60 existing new-format stores are expected to be retrofitted to the C20/20 format.

Tracking studies continue to show improvements in both regular and promotional product in-stock performance.

CTR plans to continue making progress in regular and promotional product in-stock performance.

Two hundred and sixty-five Canadian Tire stores achieved Gold certification in 2005 through eLearning and retail initiatives. Currently there are 340 courses available in English and French and over 1.8 million lessons have been completed, leading to an improvement in product knowledge and customer satisfaction ratings. Canadian Tire University (CTU), a virtual learning environment, was launched for store and corporate team members.

Continue to offer and enhance CTU, an effective learning environment for all team members, focussing on product knowledge, employee development and creating lifetime customer relationships.

The major components of CustomerLink were substantially completed.

Implement the final CustomerLink components: Periodic Replenishment, Direct Ship, Yard and Dock Management.

Sales of ENE products in 2005 increased by 22 percent, compared to 2004, supported by the "Now That's Different" mini-catalogues in 2005.

The sales target for ENE in 2006 is an increase of 11.8 percent versus 2005.

Developed auto service strategy and deployed a team of Automotive Regional Managers to support stores with program execution. Continued our customer call back program. Implemented key enhancements to the in-store automotive parts assortment models. Continued to grow replenishment capability for the emergency supply of auto parts. Completed the analysis for future requirements for people, process and technology for the Automotive Parts and Service businesses.

Complete a comprehensive review of key infrastructure including process improvements and technology for Automotive Parts and Service businesses.

Increased total same store sales by 17.4 percent.

Increase total same store sales by 5.8 percent.

Opened 11 stores, renovated and/or relocated 34 Mark's stores to the latest format. At the end of 2005, Mark's had 334 stores, totalling 2.6 million square feet of retail selling space.



Open 15 to 21 new stores (including eight CTR-Mark's combination stores). Renovate and/or relocate up to 24 stores. Increase total system retail selling space to 2.8 million square feet.

Mark's successfully delivered all program elements required to build customer awareness and experienced correlating sales increases.

Deliver eight product launches, two incremental flyers, four incremental gift cards in flyer distributions and one incremental special event.

<sup>1</sup> See Management's Discussion and Analysis starting on page 34 for more detailed information on the Company's performance in 2005.

# 2005 Performance Scorecard

		Initiative	2005 Performance Goals
<b>Canadian Tire Petroleum</b>		<b>Expand chain of gas bars</b>	Open five new gas bars.
		<b>Re-brand competitor sites to Canadian Tire banner</b>	Re-brand 15 to 20 additional sites. Develop new re-branding partnerships.
		<b>Increase gasoline volume</b>	Increase total gasoline volume by approximately 10 percent.
		<b>Build incremental car washes</b>	Open a minimum of five new car washes in 2005. Increase total car wash sales by approximately 30 percent.
		<b>Increase high-margin convenience sales</b>	Open five or more convenience stores, including the first two premium Q convenience centres in early 2005. Increase convenience store sales by approximately 15 percent.
<b>PartSource</b>	<b>Mike Medline</b> Executive Vice-President, New Business Development	<b>Grow comparable store sales</b>	Increase comparable store sales by four percent to five percent.
		<b>Expand store chain</b>	Open 10 new stores primarily in the Greater Toronto Area.
<b>Canadian Tire Financial Services</b>		<b>Increase total managed portfolio</b>	Increase total managed portfolio to \$3.3 billion by the end of 2005.
		<b>Reduce operating expenses as a percentage of total managed portfolio (operating expense ratio)</b>	Continue to reduce operating expense ratio in 2005.
		<b>Maintain return on average total managed portfolio</b>	Maintain return on average total managed portfolio in the target range of 4.5 percent to 5.0 percent, excluding gain on sales of loans receivable.



**2005 Actual Performance<sup>1</sup>****2006 Performance Goals**

Opened six gas bars, bringing the total number of gas bars to 220 excluding re-branded sites and 259 including the re-branded sites.

Open a minimum of three new gas bars.

During 2005, three competitors' sites were converted to the Canadian Tire banner.

Re-brand up to 10 additional sites.

Increased gasoline volume by 6.4 percent.

Increase total gasoline volume by approximately five percent.

Opened 10 new car washes (including one re-branded car wash), bringing the total number of car washes to 67. Sales increased by 26.3 percent.

Open between 5 to 10 new car washes in 2006 (excluding re-branded sites), and increase total sales by 20 percent.

A total of eight convenience stores were opened in 2005, including two Q convenience centres and two re-branded convenience stores. Convenience sales increased by 12.7 percent.

Open a minimum of three new convenience stores (excluding re-branded sites) and increase total sales by approximately 10 percent.

Comparable store sales exceeded the target range.

PartSource comparable store sales are expected to increase by four percent to five percent.

Opened seven new stores and acquired three stores that are to be re-branded to the PartSource banner in 2006, bringing the total store count to 57.

PartSource plans to open eight new stores that will be located primarily in Ontario.

Increased total managed portfolio to \$3.4 billion at the end of 2005.

Increase total managed portfolio to \$3.6 billion.

Reduced operating expense ratio to 8.4 percent in 2005 from 9.3 percent in 2004.

Maintain operating expense ratio in the target range of 8.0 percent to 9.0 percent.

Delivered return on average total managed portfolio of 4.8 percent for 2005.

Maintain return on average total managed portfolio in the target range of 4.5 percent to 5.0 percent, excluding gain on sales of loans receivable.

<sup>1</sup> See Management's Discussion and Analysis starting on page 34 for more detailed information on the Company's performance in 2005.

# Message from the Chairman of the Board

**Gilbert S. Bennett** Chairman of the Board



**Advancing the practice of effective corporate governance adds value to Canadian Tire in ways that are not always clearly evident to our shareholders. During the course of 2005, the Board continued to make changes to strengthen its stewardship and supervision of the management of the Company's business, changes that I believe will ultimately improve business results.**

We increased our engagement in strategic planning, setting aside significant time at virtually every Board meeting for the Directors to deepen their understanding of Canadian Tire's customers, competitors, emerging trends, technology, risks, and opportunities to leverage synergies between our inter-related businesses. The substantial experience of our Directors, combined with the knowledge we have of Canadian Tire's operating environment, creates a competitive advantage for the Company when applied to the development of strategies that build shareholder value.

The Board also involved itself more actively in the succession planning process across the ranks of the senior leadership team. We put in place a special committee for CEO succession and we gave the Committee a mandate to recommend to the Board the steps that should be taken to identify, assess and select candidates for this most important role. Additionally, we stepped up our participation in the development of individuals who hold the potential for accession to Officer and other key leadership roles, meeting with those individuals in both formal and informal settings.

Our annual review of the Board Mandate resulted in a number of small changes that clarified Board obligations. The revised mandate has been published in the Company's Management Information Circular. In 2006, I intend to further clarify the duties of the Board by introducing a policy that describes in detail how our Directors must go about exercising a minimum standard of diligence in discharging their duties. When that task is complete, we will turn our attention to clarifying and restating our policy that delineates the roles of Management and of the Board and identify those decisions that require Board input and approval.

Shareholders will have noted the changes we have made to the Management Information Circular that is published concurrent with this annual report. We are fully complying with the disclosure rules of the Canadian Securities Administrators, which have superseded those of the Toronto Stock Exchange, and we have adopted many of the recommendations put forward by the Canadian Coalition for Good Governance. Of particular note is the enhanced disclosure and clarity for shareholders in connection with the compensation of the CEO and the four additional most highly compensated executives.

John Lacey and Kathy Misunas will not stand for re-election at the Annual General Meeting in May. As well, Earl Joudrie retired from the Board in the fall of 2005. On behalf of my fellow Directors, I thank them all for their unfailing dedication and their unique contributions to Canadian Tire. We are particularly indebted to Earl Joudrie, who served as a Director of Canadian Tire for 15 years and was my predecessor as Chairman. Earl laid a firm foundation for the Board to build upon, and the shareholders of Canadian Tire were well served by the broad and deep business experience Earl applied to his deliberations as Chairman and as a Director.

Another Director, Terry Douglas, was killed in January 2006 in a tragic airplane accident. Terry had been a Director less than a year but he had committed himself fully to the job and had made significant contributions during his brief tenure. As a Canadian Tire Associate Dealer for over 20 years, Terry had accumulated extensive front-line knowledge of the retail business, knowledge which he used to provide valuable insights to the Board. His loss has been profoundly felt across the enterprise.

In late 2005 and early 2006, Sue Perles and Keith Gostlin (an Associate Dealer) were appointed Directors by the Board to replace Earl Joudrie and Terry Douglas, respectively. Sue and Keith, along with Jim Neale and Jim Riley, have been nominated for the first time by the Board for election as Directors at the Annual General Meeting in May. Each of these individuals brings distinctive qualifications to the Board, qualifications which shareholders can review by reading the Director biographies provided in the Company's Management Information Circular.

On behalf of the Board of Directors and the Company's shareholders, I want to thank Wayne Sales, his management team and all of the employees at Canadian Tire for the superb job they have done in delivering on the objectives of the Company's first Strategic Plan and in developing a new Plan that will drive future growth for the Company.

(SIGNED)

**Gilbert S. Bennett**  
Chairman of the Board

# Leadership

Canadian Tire's executive leadership team is highly experienced in managing diverse and growing businesses and has deep knowledge of retail and financial services operations. Collectively, the team has substantial experience guiding Canadian Tire's strategic development and a strong track record of successfully executing initiatives to meet the Company's objectives.

Our leadership team is charged with the responsibility of creating a corporate culture that builds trust and confidence with stakeholders; supports innovation; takes balanced risks; promotes dignity, respect and open communication in the organization; and participates actively in responding to community needs.

*from left*

**Cameron D. Stewart**

*Senior Vice-President, Secretary and General Counsel*

**J. Huw Thomas**

*Executive Vice-President, Finance and Administration and Chief Financial Officer*

**Susan J. E. Rogers**

*Senior Vice-President, Corporate Affairs*

**Michael R. Lambert**

*President, Mark's Work Wearhouse and Executive Vice-President, Canadian Tire Corporation, Limited*

**Michael B. Medline**

*Executive Vice-President, New Business Development*

**Patrick R. Sinnott**

*Senior Vice-President, Supply Chain*

**Wayne C. Sales**

*President and Chief Executive Officer*

**Andrew T. Wnek**

*Senior Vice-President, Information Technology and Chief Information Officer*

**A. Mark Foote**

*President, Canadian Tire Retail*

**Stanley W. Pasternak**

*Senior Vice-President and Treasurer*

**Marco Marrone**

*President, Canadian Tire Financial Services (appointed February 9, 2006)*

**Kenneth Silver**

*Senior Vice-President, Real Estate and Construction*

**Thomas K. Gauld**

*President, Canadian Tire Financial Services (retired March, 2006)*

**Laura J. Dunne**

*Senior Vice-President, Human Resources*



# Message from the Chief Executive Officer

**Wayne C. Sales** President and Chief Executive Officer



**Of all that is unique about Canadian Tire, our brand – the ubiquitous red triangle – is surely our most distinctive and powerful asset. Canadian Tire is, in many respects, a national champion because our brand is very closely associated by Canadians with the characteristics that they define for themselves – trustworthy, resilient, good citizens, successful. Not surprisingly, these same characteristics are embodied in our culture, recognized in 2005 as one of the strongest corporate cultures in Canadian business.**

The Canadian Tire team is united by common goals: we seek to build customers for life, to sustain growth for our shareholders and to be responsible to our communities.

In many respects, 2005 was *the* year when the fruits of our collective labours were most evident. We reported the sixth consecutive year of earnings growth for the Company. We grew shareholder value in each year of our 2001–2005 Strategic Plan and achieved our over-riding objective with total return to shareholders (TRS) of 31 percent on an annualized basis and 286 percent over the life of the Plan.

We did what we set out to do in 2001 – we achieved top-quartile TRS performance among retailers in Canada and the United States. Contributing to our TRS performance over the Plan period was a 45 percent rise in dividends declared, from 40 cents per share annually in 2001 to 58 cents per share at the end of 2005.

Across the board, our divisions bonded more closely with their customers by delivering innovative products and better levels of service. They also leveraged the value of our inter-related network of businesses by successfully implementing initiatives that encourage multi-divisional shoppers. The greatest proof of these accomplishments is in the numbers; in 2005 all of our divisions recorded significant increases in revenues and earnings before tax over the previous year. Moreover, independent customer surveys showed improved rankings on the quality of service delivered by each of our businesses. One notable highlight was a top honour awarded to Canadian Tire Financial Services for call-centre excellence in 2005, an award they have won four of the last six years.

As a direct result of the Strategic Plan we introduced in 2001, and the stellar execution of key strategic initiatives contained in that Plan, Canadian Tire is today stronger, more financially sound and better positioned to compete in the highly competitive retail marketplace. We have great strengths to build upon and an abundance of opportunity, as was described when we publicly announced our new five-year Strategic Plan in April of 2005.

Our path forward is a natural evolution of our first Strategic Plan, building on the success of initiatives piloted and proven-out in the past few years and extending our brand into new products and services where our customers have indicated wide acceptance. The accelerated roll out of Canadian Tire Retail's new Concept 20/20 store format, more PartSource stores, expanding Mark's successful "Clothes That Work" brand umbrella, new retail banking products and credit cards from Financial Services, new-format convenience stores and gas bars from Petroleum, as well as an enhanced loyalty program, anchor our new Strategic Plan.

# Message from the Chief Executive Officer

In developing our new Plan, we undertook a comprehensive review of our organization's growth opportunities while listening very closely to our customers and our shareholders. As the planning process unfolded, we engaged our Board of Directors to challenge our assumptions, risks and opportunities. This collaborative process with the Board is invaluable to the oversight of key initiatives and to the work we have already begun on our next evolution of growth beyond the current five-year horizon.

Our ability to maintain top-quartile total return to shareholders will come from developing and sustaining our competitive advantage. The performance of our business units, which out-paced the market in many respects over the past five years, is expected to produce healthy but more moderate returns in 2006. However, we will invest significant capital this year on those initiatives that have the most potential to sustain the growth of Canadian Tire, including investments in supporting infrastructure.

We are embarking on a very aggressive agenda but I am satisfied that the investments we will make over the next few years will create long-term value for our shareholders, as will our continued efforts to exploit customer-facing and back-line synergies within our inter-related network of businesses.

I am also confident in Management's ability to lead Canadian Tire into a promising future. To that end, we welcome two new Officers to our executive team. Laura Dunne was appointed from within Canadian Tire's outstanding talent pool to Senior Vice-President of Human Resources. Marco Marrone, formerly the Chief Operating Officer of Canadian Tire Bank, was appointed to the helm of Canadian Tire Financial Services to replace Tom Gauld, who has retired after 13 remarkable years with Canadian Tire.

Tom served the Company and its shareholders exceptionally well. He developed and led a team that tripled the revenues and earnings of Financial Services during his tenure by following a powerful principle – build Customers for Life. Tom's vision for Financial Services is now embedded in the vision of Canadian Tire and is taking hold across the enterprise.

Among the many worthy charitable projects supported by Canadian Tire and its associates, one very significant program stands out: Canadian Tire JumpStart. In 2005, under the auspices of the Canadian Tire Foundation for Families, over 225 community chapters were created across Canada to give financially disadvantaged children the opportunity to participate in a sport or recreational activity. Over 24,000 children were assisted in 2005; our goal for 2006 is to help 35,000 children. We have received many accolades for creating Canadian Tire JumpStart and while the praise is satisfying, it surely speaks to a great need. Given the demographics of Canada, with the majority of our population over the age of 40 and a low birth rate, our country's future depends on strong and healthy children now more than ever. As Canadians, we must all try our very best to give every child the opportunity to live up to his or her full potential.

With all of the options we have before us, and the extraordinary team at Canadian Tire who have established a track record of delivering on commitments, we are well positioned to remain a competitive force in the retailing and financial services businesses. We will do so through sheer determination to remain *uniquely Canadian Tire*.

(SIGNED)

**Wayne C. Sales**

President and Chief Executive Officer

# 2001–2005 Report Card

With the creation of the 2001–2005 Strategic Plan, Canadian Tire established, for the first time, an integrated growth strategy for the Company with correlating imperatives and a set of five-year financial aspirations. We believed that successful execution of the strategic imperatives outlined in the Plan would enable us to achieve our aspirational targets and our over-riding objective for the Strategic Plan – top-quartile total return to shareholders (TRS) \*. Over the life of the 2001–2005 Strategic Plan, we achieved TRS of 286 percent, or 31.0 percent on an annualized basis, placing Canadian Tire squarely in the top-quartile of retailers in Canada and the United States.

Total return to shareholders remains the objective for the current Strategic Plan as the Company believes that TRS is the best long-term indicator of success for Canadian Tire.

\* TRS is defined as share price appreciation plus dividends

Financial Aspirations	2001–2005 Strategic Plan	2001–2005 Performance <sup>1</sup>
Comparable store sales (simple average of annual percentage growth, CTR stores only)	3% to 4%	2.6%
Gross operating revenue (compound annual growth rate)	at least 10%	8.3%
EBITDA <sup>2</sup> and minority interest (compound annual growth rate)	10% to 15%	11.7%
Basic earnings per share (compound annual growth rate)	12% to 15%	16.9%
After-tax return on invested capital (annual simple average)	at least 10%	8.7%

<sup>1</sup> Performance from the beginning of fiscal 2001 to the end of fiscal 2005.

<sup>2</sup> Earnings before interest, income tax, depreciation and amortization. See section 12 on non-GAAP measures in Management's Discussion and Analysis in this Annual Report.

see **page 16** for information on Strategic Plan Financial Aspirations for 2005 to 2009



# 2005-2009 Strategic Road Map

## PURPOSE & VISION

**We exist to create Customers for Life and shareholder value.**

**Our vision is to create sustainable growth by being a national champion and Canada's most trusted company. We will grow from our strengths - leveraging our brands, core capabilities, assets and extraordinary people.**

## STRATEGIC OBJECTIVE

Our objective is to achieve top-quartile total return to shareholders (TRS).

We compare our TRS performance against our peers - retailers in Canada and the United States listed in the major consumer product indices of the Toronto Stock Exchange, the NASDAQ stock market and the New York Stock Exchange. TRS is defined as share price appreciation plus dividends.

## FINANCIAL ASPIRATIONS

**3%–4%**

Comparable store sales<sup>1,2</sup>

**7%–9%**

Gross operating revenue<sup>3</sup>

**10%–15%**

EBITDA<sup>4</sup> - Earnings before interest, income taxes, depreciation and amortization and minority interest<sup>3</sup>

**12%–15%**

Basic earnings per share<sup>3</sup>

**10%**

After-tax return on invested capital<sup>2</sup>

<sup>1</sup> Represents sales growth at CTR only.

<sup>2</sup> Calculated as an annual simple average.

<sup>3</sup> Expressed in terms of a compound annual growth rate.

<sup>4</sup> See section 12 on non-GAAP measures in Management's Discussion and Analysis in this Annual Report.



## STRATEGIC IMPERATIVES

## STRATEGIC INITIATIVES

## COMPETITIVE STRENGTHS & CORE CAPABILITIES

### 1. Grow sales and revenues

- Replace traditional stores with Concept 20/20 (C20/20) stores and retrofit approximately 200 of CTR's existing new-format stores to the C20/20 design
- Expand Mark's network of stores and new, innovative product lines
- Expand Petroleum's network and expand the re-branding program
- Expand the network of PartSource stores
- Increase Financial Services' credit card average balances to industry norms
- Enhance Financial Services' insurance and warranty products and expand Financial Services' personal loan products
- Develop and test new credit cards, savings accounts and mortgage products

### 2. Improve earnings performance

- Increase the amount of products CTR sources globally
- Enhance CTR's inventory systems
- Increase the number of products Mark's sources globally
- Increase Mark's supply chain capacity
- Grow non-gas operations to approximately 30 percent of Petroleum's margins
- Identify opportunities to improve Petroleum's earnings performance
- Conduct a comprehensive PartSource operations review
- Reduce Financial Services' operating expense ratio

### 3. Embed a Customers for Life culture

- Reinforce a Customers for Life culture across the organization
- Develop comprehensive customer service benchmarks within each business unit
- Implement a customer feedback database

### 4. Extend growth and performance beyond 2009

- Consider growth opportunities within each existing business
- Consider growth opportunities in new retail, retail-related and financial services businesses

### 5. Enhance value creation through financial flexibility and maximization of real estate assets

#### Financial

- Maintain overall financial flexibility
- Continue focussed cost-reduction efforts
- Manage capital through an emphasis on low-cost, high-return investments

#### Real Estate

- Leverage redundant high-value properties for sale, and retain select properties to deliver a steady income stream
- Optimize funding by leveraging specific real estate assets

### > Unique platform of inter-related businesses

- Market-leading positions in each of our businesses
- Synergies and multi-divisional shoppers across businesses

### > Canadian Tire 'Money'

- Pioneered loyalty program over 45 years ago
- One of Canada's most popular and recognized loyalty programs

### > Brand recognition and trust

- Near universal brand awareness
- Ranked among Canada's most respected companies<sup>1</sup>

### > Innovative formats, products and services

- Transformational store renewal programs across our retail businesses
- Innovative and exclusive products from around the world

### > National reach and scale

- Unrivalled locational convenience
- Over 80 percent of Canadians shopped at Canadian Tire stores in 2005

### > Real estate capabilities

- Over \$2 billion in unencumbered assets
- Strategic placement of stores and efficient expansion of store network

<sup>1</sup> Canada's Most Respected Corporations study - KPMG.

# Strategic Plan Financial Aspirations 2005 to 2009

**We have established five financial aspirations to guide us in developing growth plans that will deliver above-average performance year after year. Our financial aspirations were determined after a review of our capabilities, our recent financial and operating performance, and by taking into consideration the performance of our peers.**

**We aim to meet our five aspirational targets through successful execution of our strategic imperatives. The importance that we have placed on striving to achieve our aspirational targets influences the decisions that we make and ensures that our entire organization is focussed on creating long-term shareholder value.**

## 2005–2009 Strategic Plan Financial Aspirations

Comparable store sales <sup>1,2</sup>	3%–4%
Gross operating revenue <sup>3</sup>	7%–9%
EBITDA <sup>4</sup> – Earnings before interest, income taxes, depreciation and amortization and minority interest <sup>3</sup>	10%–15%
Basic earnings per share <sup>3</sup>	12%–15%
After-tax return on invested capital <sup>2</sup>	10%

<sup>1</sup> Represents sales growth at CTR only.

<sup>2</sup> Calculated as an annual simple average.

<sup>3</sup> Expressed in terms of a compound annual growth rate.

<sup>4</sup> See section 12 on non-GAAP measures in Management's Discussion and Analysis in this Annual Report.

Our 2005–2009 Strategic Plan contains forward-looking statements, including our aspirations for sales and earnings growth of our businesses. While we believe that establishing financial targets is important to meeting our objective of top-quartile TRS, we cannot provide assurance of future financial results or performance. Further, there are many factors that are beyond our control that could impede our ability to achieve our results and that may impact our stock's market value. For more information on the risks associated with our businesses, refer to section 9 of Management's Discussion and Analysis in this Annual Report.

# 1

## GROW SALES AND REVENUES

STRATEGIC IMPERATIVE

**Canadian Tire's top priority is to grow sales and revenues during the outlook period, in order to deliver higher earnings in the future.**

- > Continue CTR's program to **replace traditional stores** with larger, more modern stores. A total of 100 replacement stores, most of which will feature the new Concept 20/20 (C 20/20) format, are expected to be built between 2005 to 2009, with the majority replacing traditional stores. In total, CTR's store count is expected to increase to 481 by the end of 2009.
- > **Retrofit approximately 200 of CTR's existing new-format stores to the C20/20 design** over the next five years. The first 53 C20/20 test stores have, on average, surpassed expectations of increasing store sales by 20 percent or more.
- > **Expand Mark's network of stores** to between 395 and 400 stores by the end of 2009. Expand, renovate and retrofit 20 percent to 30 percent of Mark's existing corporate stores during the Plan period.
- > Significantly **expand Mark's category offerings of new and innovative product lines** such as men's and women's private-label products, industrial wear and stain-resistant casual clothing, work wear for the health care and hospitality industries, and Imagewear, a business-to-business collection of work apparel.
- > **Expand Petroleum's network** by adding 25 to 35 new gas bars and retrofitting certain existing gas bars and convenience stores to increase Canadian Tire's brand presence in gasoline retailing across Canada. Increase non-gas sales at car washes and convenience stores and expand the re-branding program.
- > **Expand the network of PartSource stores.** Efforts will focus on building new stores and pursuing small-scale acquisitions in order to grow the customer base and expand the chain to more than 100 stores by the end of 2009.
- > **Increase Financial Services' credit card receivables** by increasing the number of accounts that have balances by three percent to four percent and, by increasing average balances. In order to achieve stated targets, Financial Services plans to continue its in-store customer acquisition program and balance transfer promotions, as well as introducing new types of credit cards.
- > **Enhance Financial Services' offerings of insurance and warranty products** to credit card customers. Revenues from insurance and warranty products associated with the credit card portfolio have grown significantly in the last four years and, over the outlook period of 2005 to 2009, are expected to increase by approximately six percent on a compound annual basis.
- > **Expand Financial Services' personal loan products** based on the successful launch of these products in 2005.
- > **Develop and test new financial products**, such as savings accounts and mortgages.

## 2

### IMPROVE EARNINGS PERFORMANCE

STRATEGIC IMPERATIVE

**A key focus of the 2005–2009 Strategic Plan is to manage or reduce costs and to maximize productivity in order to enhance Canadian Tire's earnings performance and our return on invested capital.**

- > **Increase the amount of products CTR sources globally** in order to maintain product margins, increase sales and improve the customer value proposition by offering greater product innovation.
- > **Enhance CTR's inventory systems** to control or reduce operating costs, increase inventory turns and improve in-stock positions to raise customer satisfaction levels and sales.
- > **Increase the number of products Mark's sources globally** in order to maintain a competitive pricing strategy and expand core product categories.
- > **Increase Mark's supply chain capacity** and performance to support future growth.
- > **Grow non-gas operations to approximately 30 percent of Petroleum's margins** in order to reduce the impact of fluctuations in gasoline prices and margins. Growth plans include: adding new convenience stores, expanding and renovating existing stores, further testing the new Q retailing concept and expanding the network of car washes to approximately 90 sites by the end of 2009.
- > **Identify opportunities for Petroleum** to generate productivity improvements and to deliver superior earnings performance in the future.
- > **Conduct a comprehensive PartSource operations review** to identify ways of improving the supply chain and information technology systems.
- > **Reduce Financial Services' operating expense** as a percentage of gross average receivables through planned growth of the customer base and receivables.

## 3

### EMBED A CUSTOMERS FOR LIFE CULTURE ACROSS THE ENTIRE ORGANIZATION

STRATEGIC IMPERATIVE

**A key factor in Canadian Tire's success has been our ability to meet the needs of our customers. High customer satisfaction levels add long-term value for shareholders.**

- > **Reinforce a Customers for Life culture across the organization** by encouraging everyone who is part of Canadian Tire – from employees to Associate Dealers to franchisees and agents – to perform in a manner that develops lifelong relationships with our customers.
- > **Develop within each business unit comprehensive benchmarks** to evaluate progress toward sustaining a customer-centric culture.
- > **Implement a customer feedback database** which will allow customers' key concerns and ideas to be addressed, culminating in repeat traffic and overall customer loyalty to Canadian Tire.

# 4

## EXTEND GROWTH AND PERFORMANCE BEYOND 2009

STRATEGIC IMPERATIVE

**Canadian Tire will continue to explore new business opportunities and pursue channels of growth that leverage our core capabilities.**

- > **Review growth opportunities**, including potential acquisitions, joint ventures and/or strategic alliances.
- > **Consider growth opportunities within each existing business**, including development of new store formats and the introduction of innovative product categories and services.

# 5

## ENHANCE VALUE CREATION THROUGH FINANCIAL FLEXIBILITY AND MAXIMIZATION OF REAL ESTATE ASSETS

STRATEGIC IMPERATIVE

**Canadian Tire is committed to increasing revenue, and reducing operating costs and working capital needs to improve financial flexibility. Deriving the highest possible return from our real estate portfolio will also enhance value creation.**

### Financial

- > Employ effective risk management strategies to optimize returns to shareholders and **maintain overall financial flexibility**.
- > **Continue focussed cost-reduction efforts** across all business units.
- > **Manage capital through an emphasis on low-cost, high-return investments** and a working capital review.

### Real Estate

- > **Selectively review opportunities to leverage surplus high-value properties** to maximize proceeds and **retain select properties to deliver a steady income stream**.
- > **Optimize funding by leveraging specific real estate assets** and exploring a variety of funding options.

# What makes Canadian Tire *UNIQUE* in the marketplace

Canadian Tire has a unique business platform. Our distinctive business model cannot be easily compared with any other single retailer in North America. Our market differentiation, customer offerings and the nature of our inter-related businesses provide competitive advantages and drivers of growth.

# UNIQUELY



## Brand recognition and trust

With near universal brand recognition and a history of delivering a strong customer proposition, Canadian Tire is one of the most recognized and trusted names in Canadian retailing. We offer customers the products and services that they need and want, building increased loyalty and strengthening our competitive advantage.



## Reach and scale

Canadian Tire Retail continues to attract more shoppers than any other general merchandise retailer in Canada, with over 80 percent of Canadians visiting our stores in 2005. Our flyers and catalogues reach over 10 million households every year. Our Petroleum sites out-pump the industry average by twice as much fuel per site, as customers are drawn to our Canadian Tire 'Money' rewards. With more than 1.8 million active credit card accounts, Canadian Tire cardholders trust us to be their financial services provider. Our reach and breadth ensure that Canadian Tire offers value to Canadians each and every day.



## Unique business platform of inter-related businesses

Canadian Tire's retail, petroleum and financial services businesses enjoy market-leading positions in their respective segments and benefit from complementary customer opportunities that link the businesses. Synergies between the businesses such as cross-marketing programs, flyer and catalogue inserts, combination stores in select markets and the circulation of Canadian Tire 'Money' provide multi-divisional shopping opportunities and cost efficiencies.

## Canadian Tire 'Money' loyalty program

Canadian Tire 'Money' is a pioneer among loyalty programs. As one of the country's most-popular and recognized loyalty programs, Canadian Tire 'Money' rewards customers who shop at our stores, fill up at our gas bars or use our credit cards.



## Real estate

Canadian Tire manages over \$2 billion in unencumbered real estate. Our expertise in the development and management of real estate enables us to efficiently expand our store networks in advantageous locations, while also generating consistent gains from the sale of surplus properties.

## Innovative formats, products and services

Canadian Tire's history is steeped in innovation. Today, transformational store renewal programs are underway at CTR through the Concept 20/20 program, through store renovations at Mark's Work Warehouse and through the Q convenience centre test concept at Petroleum. As well, Financial Services continues to introduce new products and services, while PartSource's network expansion is meeting the needs of commercial installers and serious automotive enthusiasts.





# Canadian Tire Retail

## What makes us unique

There is no retailing format in Canada that shares Canadian Tire Retail's (CTR) unique assortment of products and services. Distinguishing ourselves in the marketplace and clearly defining our customer value proposition have been essential ingredients behind our success and are the pillars that support our retail strategy. Our ability to stand for something unique in the minds of our customers has resulted in market-leading positions in more than half of the lines of business in which we compete.



Debbie Travis, one of Canada's best known design personalities, is a great example of how we are creating an inspired shopping environment for our female customers with Exciting, New and Exclusive (ENE) products. The Debbie Travis Collection of products include paint, ready-to-assemble furniture and a wide range of décor items.

The first of two strategic pillars in CTR are our "differentiators" – Exciting, New and Exclusive products, inspiring events and promotions and impactful merchandising. We have made CTR a more recognized and relevant part of Canadians' everyday lives by bringing innovative and exclusive new products to market. We are communicating effectively to our customers through weekly promotional flyers, sales events, and demonstration-oriented television commercials that inspire our customers. We are also enhancing our merchandising, evidenced by initiatives such as our strategic alliance with home decorating expert Debbie Travis.

Our second strategic pillar is our focus on "retail imperatives", including the right product selection and quality, price assurance, friendly, quick and helpful assistance and in-stock merchandise. Semi-annual brand tracking surveys with customers show continued improvement on our retail imperatives which is a testament to our focus on global sourcing, employee training and improved category management among other initiatives.

Perhaps the most notable embodiment of our differentiation strategy is the Concept 20/20 store format – a strikingly different store design that encourages customers to visit Canadian Tire stores longer and more frequently. The stores are bigger, brighter, more open with wider aisles, and have a layout and displays that draw attention to featured merchandise.

In 2005, CTR continued to validate the customer appeal and business-building power of our Concept 20/20 store platform. Based on the strong performance of our 53 Concept 20/20 stores to date, we now plan to accelerate our roll-out in 2006 to exploit the market growth opportunity, with up to 80 new, replacement or retrofit projects that are estimated to add about 1.5 million square feet of retail space.

## How we are growing

Significant investment in our store network and supporting infrastructure is a foundation for future sustainable revenue and earnings growth. In all, we expect to have approximately 480 stores at the end of 2009.

We also expect to increase the purchases of goods sourced globally from approximately 35 percent in 2005 to approximately 50 percent by 2009. Global sourcing gives us access to a vast array of innovative and exclusive products to feed into our product development pipeline, while protecting margins, and offering customers excellent value.

With 345 stores renovated or built over the past decade, CTR is the youngest 83-year-old in the retail marketplace. We continue to re-invent the retail experience for our customers and, in so doing, are successfully driving growth to support our financial objectives.

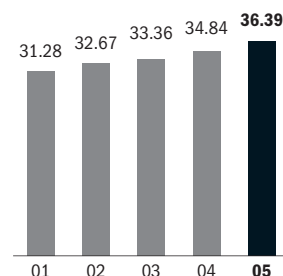
2005	Traditional stores	New-format stores (excluding Concept 20/20)	Concept 20/20 stores	Total
Store count	117	292	53*	462
Average transaction per customer (\$)	30.66	37.09	42.18	36.39

\* Including 11 combination Canadian Tire Retail-Mark's Work Wearhouse stores.

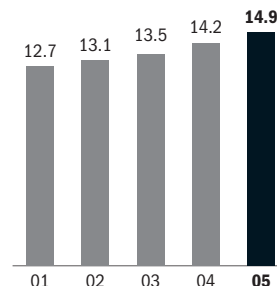
### CANADIAN TIRE RETAIL 2005 PERFORMANCE VERSUS 2004

Retail sales	5.1%
Same store sales	3.4%
Net shipments	4.2%
Gross operating revenue	4.3%
Earnings before income taxes and minority interest	6.8%

### AVERAGE TRANSACTION PER CUSTOMER (\$)



### RETAIL SQUARE FOOTAGE (millions of square feet)



Our very successful demonstration-style television commercials, which highlight the functional side of Exciting, New and Exclusive products, continue to be a critical element of our ENE advertising program.





# DRIVING FIXING LIVING

PLAYING



Canadian Tire Retail has a unique relationship with Canadians, who trust CTR as the place they go when starting a new season, sport or life event. With a clearly-defined strategy and the most significant store renewal program in our history now underway, we are emerging with one of the youngest and most dynamic retail chains in North America.







### What makes us unique

PartSource's market position, strategies and tactical initiatives focus on offering our retail and commercial customers "The Parts, The Pros, The Price" – a mantra for which we are becoming known in the communities where we operate.

PartSource targets the growing serious automotive do-it-yourself and professional installer segments, extending Canadian Tire's participation in the automotive sector. We offer our customers a comprehensive selection of recognizable brand-name parts and competitive prices. Our knowledgeable and professional staff are themselves automotive enthusiasts, and many are licenced mechanics.

The commercial automotive aftermarket represents a significant untapped opportunity. PartSource continues to strengthen its position in the market with a healthy sales mix of one-third commercial and two-thirds retail. PartSource benefits from the connection to Canadian Tire Retail's supply chain, which provides access to more products and achieves greater operating efficiencies.

During 2005, we continued the growth trajectory of PartSource, increasing both store count and geographic reach. In 2005, we further expanded in Ontario, concentrating on the Greater Toronto Area.



PartSource stores offer a leading array of branded products, providing our sophisticated customers with the choice they demand.

### How we're growing

PartSource had 57 stores at the end of 2005, including three acquired stores which will be converted to our brand in 2006. By the end of 2009, we expect to continue to grow our customer base and expand our business to more than 100 stores, building new stores and continuing to acquire and integrate small chains of stores, which can rapidly boost our regional visibility, brand presence and profitability.

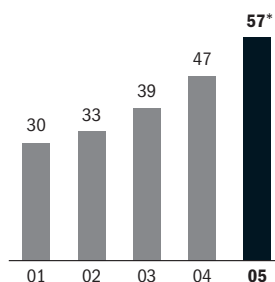


PartSource stores offer customers a broad assortment of automotive parts to get the job done right.

Our stores are staffed by knowledgeable pros including shop teachers and licenced mechanics, providing substantial experience for our customers.

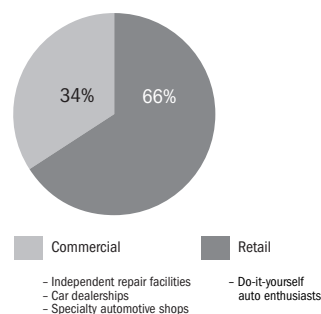
PartSource stores are characterized by their competitive prices – every day and for all products.

CONTINUOUS STORE GROWTH (number of stores)



\* Includes three recently acquired operations that will be converted to PartSource branded locations in 2006.

SALES MIX 2005



PartSource stores are a destination location for a customized retail experience.

# THE PARTS THE PROS THE PRICE



PartSource is an auto parts specialty store focussed on do-it-yourself automotive enthusiasts and the commercial auto parts segment.





**What makes us unique**

The essence of Mark's Work Wearhouse (Mark's) success is "Clothes That Work" – a brand strategy that has responded to Canadians' changing interests and needs.

In recent years, as the workplace has relaxed its view of what business wear and even business-casual means, Mark's has leveraged its brand strength as the provider of everyday workwear, from worksite jeans and footwear through weekend casual wear, and even to shirts and ties and 'dress up' clothes – and increasingly, a focus on women's apparel. At the same time, we have maintained the value proposition on which the business was built: providing customers with more functionality, more features and more style at a competitive price.

Commitment to value has also opened doors for Mark's in industries with specific clothing needs, including health care and hospitality, provided by Imagewear, a division of Mark's that sells directly to businesses. Our new avenues of growth have driven innovative product introductions such as improved safety footwear, comfort-fit clothing and stain-resistant clothing.

What makes Mark's unique is the wide range of products available to consumers, from respected private-label brands through to national brands.

Mark's also connects with Canadian Tire Retail on various levels, including select promotional activities and marketing events that build store traffic, leveraging real estate capabilities and supply chain expertise.

**How we are growing**

Mark's plans to continue growing and delivering strong financial performance by implementing multiple strategies. We will expand the store network from 334 at the end of 2005 to between 395 and 400 by the end of 2009, with an increased focus on under-served markets. In addition, we plan to renovate, retrofit and expand 20 percent to 30 percent of the current store base.

As consumers increasingly make purchases closer to the time of their intended use of the product, we plan to increase our promotional focus on seasonal apparel and attractively priced impulse purchases.

Ultimately, our objective is to achieve 'Superbrand' status, representing a significant share of overall apparel sales in each geographic market and in each product category where we compete.

Clothes That Work for a woman's lifestyle means comfort with style, fit and versatility.



Business casual for men is more than just the right look for the office. We add innovations like stain repellency and provide comfortable and durable clothing for men's wear that makes their clothing easier to care for.



**MARK'S WORK WEARHOUSE  
2005 PERFORMANCE VERSUS 2004**

Retail sales	20.3%
Same store sales	17.4%
Gross operating revenue	21.7%
Earnings before income taxes	75.2%

# “CLOTHES THAT WORK”



With its focus on new categories and innovative products, along with network expansion and development, Mark's Work Wearhouse continues to build sales and earnings growth.







# Canadian Tire Petroleum

## What makes us unique

Canadian Tire Petroleum (Petroleum) is a pioneer in the gasoline retailing business. Originator of the concept of combining a gasoline offering with retail stores and a loyalty program, Petroleum out-pumps the industry average by twice as much fuel per site. Petroleum also makes important contributions to the sales growth and performance of our retail and financial services businesses.

Petroleum continues to focus on growing non-gasoline sales which feature more stable margins, by growing our offering of complementary lines of business, including car washes and our new Q convenience centres.

Our new Q convenience centre concept is a unique retail offering that further differentiates us from our competitors. Time-starved customers can buy gas and a lot more – convenience items; grocery products; Starbucks coffee and restaurant meals – all in a single, highly convenient centre of up to 10,000 square feet. We currently have two Q convenience centre pilot locations in operation, with more planned in 2006 and 2007.

Petroleum customers are among Canadian Tire's most loyal customers. According to our research, consumers using their Canadian Tire credit cards and buying their gas at our gas bars, shop more often at Canadian Tire Retail, resulting in higher profitability for the Company. All of these transactions interconnect through the Canadian Tire 'Money' loyalty program.

## How we are growing

To serve customers better, we are increasing the size of our network of gas bars, Q convenience centres and car washes by developing new sites and by re-branding sites of other gasoline retailers. The cumulative effect of Canadian Tire's brand and the introduction of Canadian Tire 'Money' to re-branded locations has driven strong volume growth and made re-branding a very attractive way to grow.

We will maintain our focus on growing the non-gasoline sales by continuing to add larger convenience stores and remodelling existing ones. We will also continue to refine our Q convenience centre concept, securing high-traffic locations capable of generating significant fuel and convenience volumes, and developing the best strategic partnerships to deliver the complementary components of our offering in different regions across the country.

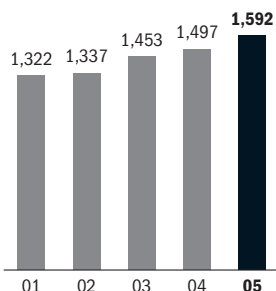


Our customer service offering ranges from small convenience stores at gas bars to our new Q convenience centre concept.

The success of our gas bars is a reflection not only of our Canadian Tire 'Money', but also of our customers' loyalty to the Canadian Tire brand.



GASOLINE SALES VOLUME (millions of litres)



CANADIAN TIRE PETROLEUM 2005 PERFORMANCE VERSUS 2004

Gasoline sales volume (in litres)	6.4%
Convenience sales	12.7%
Car wash sales	26.3%
Gross operating revenue	20.3%
Earnings before income taxes	118.9%

# LEVERAGING THE BRAND



Our Petroleum business epitomizes the competitive advantage inherent in our brand strength, the Canadian Tire 'Money' loyalty program, customer service and our inter-related businesses. Petroleum rewards customers with weekly product offers and Canadian Tire 'Money' that encourages them to shop at Canadian Tire Retail. Petroleum is also an important contributor to Financial Services – offering promotions tied to the use of Canadian Tire MasterCard.





### What makes us unique



Our Canadian Tire MasterCard represents approximately five percent of Canadian bank card receivables, and is the second largest MasterCard franchise in Canada as measured by number of active accounts.

Canadian Tire Financial Services (Financial Services) has successfully managed the transition from having only a retail credit card to developing, introducing and managing a growing suite of credit card and personal loan products. As a result, our MasterCard products now represent about five percent of the Canadian bank card market as measured by outstanding receivables – a major growth story since the launch of the 2001-2005 Strategic Plan. The Canadian bank card market is defined as all MasterCard and Visa branded credit cards that are reported by the Canadian Bankers Association. With the second largest MasterCard franchise in the country as measured by active accounts, we now have over \$3 billion in outstanding receivables.

Today, more than ever before, consumers have choice in credit products and services and, with their growing knowledge, are increasingly selective in choosing those products best suited to their needs. Our success in the financial services business is the result of the trust consumers have in the Canadian Tire brand and our ability to offer valued and innovative credit products. We have also leveraged our low-cost, high-volume customer acquisition channel – Canadian Tire Retail stores – and the many ways that Canadian Tire reaches out to customers: weekly promotional flyers, telephone, television and the Internet.



Our call centres consistently win awards for service excellence because our employees are committed, dedicated and enthusiastic about building Customers for Life.

Our success also rests on a highly experienced credit risk management team, advanced technology systems to manage our growing portfolio of products and services, as well as industry-leading customer care. In fact, our call centres have been awarded the Service Quality Excellence Award by Service Quality Measurement Group four times in the past six years.

We have been rewarded with significant growth in the average balance per account of our credit card customers, which has increased an average of 22 percent annually over the past three years, to reach almost \$1,700 at the end of 2005. We also continue to see very high customer acceptance of new credit cards, insurance and personal loan products. This is a testament to our approach of providing Canadian Tire customers with products and services that offer value.

### How we are growing

Financial Services will continue to grow as our credit card customers increase the balances they carry on their accounts – to the industry average of \$2,500 – and as we increase the number of cardholders and personal loans granted.

We will also continue to explore, design and conservatively test a targeted selection of financial services products, such as savings accounts and mortgages, products that are a natural extension of our current offering and well within our operating capabilities.

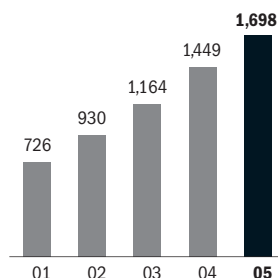
Cost control is a constant focus for Financial Services. As we grow and improve upon our financial performance, we witness declining operating expenses as a percentage of gross average receivables.

By leveraging both the trusted Canadian Tire brand and the broad relationship we have with our customers, we expect to continue generating significant opportunities to sustain our growth.

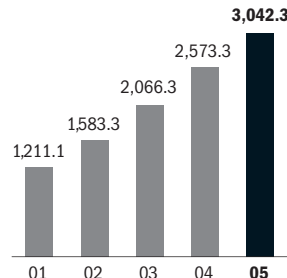
#### CANADIAN TIRE FINANCIAL SERVICES 2005 PERFORMANCE VERSUS 2004

Net managed portfolio of loans receivable	17.7%
Gross operating revenue	12.2%
Earnings before income taxes	11.1%

#### AVERAGE ACCOUNT BALANCE\* (\$)



#### GROSS AVERAGE RECEIVABLES\* (\$ millions)



\* Includes credit cards and personal loans.



# LEVERAGING OUR TRUSTED BRAND

Canadian Tire Financial Services is capitalizing on our unique position of trust with Canadians to build our business. We are working to leverage our strengths to provide greater value and services to Canadians.



## Message from the Chief Financial Officer

**Huw Thomas** Executive Vice-President, Finance and Administration and Chief Financial Officer



Dear Shareholder,

Financial success in business stems inherently from broad consumer acceptance of an organization's products and services and from the successful implementation of strategies.

The successful implementation of our business strategies and the strength of our consumer franchise have resulted in continuous improvement in our financial position over the course of our 2001–2005 Strategic Plan. Our financial strength serves as the underpinning for our next leg of growth as we further invest in strategies that have proven their ability to significantly contribute to our earnings performance and in new initiatives that we believe can build future growth.

In his letter to shareholders our CEO Wayne Sales articulated Canadian Tire's achievement of top-quartile total returns to shareholders. On behalf of our management team, I am pleased to report that Canadian Tire also continued to make progress on our strategic imperative of enhancing our financial flexibility. We are committed to growing in a measured way, and as we invest strategically to build our long-term growth platform, we also continue to make strides in building the strength of our balance sheet. In 2005 we generated \$438 million in cash from operating activities and put in place long-term financing at attractive rates. We continue to enjoy excellent liquidity and ready access to the capital markets. We also announced a 14 percent increase in our annual dividend payments – our third consecutive year of dividend increases – consistent with our policy that shareholders receive 15 percent to 20 percent of the prior year's normalized basic net earnings per share in dividend payments.

We fully recognize that delivering on our commitments and generating strong financial results are only part of the equation when it comes to attracting investors. We believe that our prudent management style which fosters balanced risk-taking, conservative financial management and progressive disclosure practices are equally important factors in creating long-term shareholder value and building trust.

Our commitment to earning your trust remains unwavering. Good disclosure practices, strategic focus and sound operational and financial management are tenets of our organization and will continue to guide our activities through the next leg of our growth journey.

(SIGNED)

**Huw Thomas**

Executive Vice-President, Finance and Administration and Chief Financial Officer

## Form 52-109F1 – Certification of Annual Filings

I, Wayne C. Sales, Canadian Tire Corporation, Limited, President and Chief Executive Officer, certify that:

1. I have reviewed the annual filings (as this term is defined in Multilateral Instrument 52-109 Certification of Disclosure in Issuers' Annual and Interim Filings) of Canadian Tire Corporation, Limited (the issuer) for the period ending December 31, 2005;
2. Based on my knowledge, the annual filings do not contain any untrue statement of a material fact or omit to state a material fact required to be stated or that is necessary to make a statement not misleading in light of the circumstances under which it was made, with respect to the period covered by the annual filings;
3. Based on my knowledge, the annual financial statements together with the other financial information included in the annual filings fairly present in all material respects the financial condition, results of operations and cash flows of the issuer, as of the date and for the periods presented in the annual filings;
4. The issuer's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures for the issuer, and we have:
  - (a) designed such disclosure controls and procedures, or caused them to be designed under our supervision, to provide reasonable assurance that material information relating to the issuer, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which the annual filings are being prepared; and
  - (b) evaluated the effectiveness of the issuer's disclosure controls and procedures as of the end of the period covered by the annual filings and have caused the issuer to disclose in the annual MD&A our conclusions about the effectiveness of the disclosure controls and procedures as of the end of the period covered by the annual filings based on such evaluation.

Date: March 9, 2006

(SIGNED)

**Wayne C. Sales**

President and Chief Executive Officer

## Form 52-109F1 – Certification of Annual Filings

I, J. Huw Thomas, Canadian Tire Corporation, Limited, Executive Vice-President, Finance and Administration and Chief Financial Officer, certify that:

1. I have reviewed the annual filings (as this term is defined in Multilateral Instrument 52-109 Certification of Disclosure in Issuers' Annual and Interim Filings) of Canadian Tire Corporation, Limited (the issuer) for the period ending December 31, 2005;
2. Based on my knowledge, the annual filings do not contain any untrue statement of a material fact or omit to state a material fact required to be stated or that is necessary to make a statement not misleading in light of the circumstances under which it was made, with respect to the period covered by the annual filings;
3. Based on my knowledge, the annual financial statements together with the other financial information included in the annual filings fairly present in all material respects the financial condition, results of operations and cash flows of the issuer, as of the date and for the periods presented in the annual filings;
4. The issuer's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures for the issuer, and we have:
  - (a) designed such disclosure controls and procedures, or caused them to be designed under our supervision, to provide reasonable assurance that material information relating to the issuer, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which the annual filings are being prepared; and
  - (b) evaluated the effectiveness of the issuer's disclosure controls and procedures as of the end of the period covered by the annual filings and have caused the issuer to disclose in the annual MD&A our conclusions about the effectiveness of the disclosure controls and procedures as of the end of the period covered by the annual filings based on such evaluation.

Date: March 9, 2006

(SIGNED)

**J. Huw Thomas**

Executive Vice-President, Finance and Administration and Chief Financial Officer



# Management's Discussion and Analysis

March 9, 2006

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## **Introduction**

This Management's Discussion and Analysis (MD&A) provides Management's perspective on our Company, our performance and our strategy for the future.

## **We, us, our, Company and Canadian Tire**

In this document, "we", "us", "our", "Company" and "Canadian Tire" refer to Canadian Tire Corporation, Limited and its business segments and subsidiaries.

## **Review and approval by the Board of Directors**

The Board of Directors, on the recommendation of the Audit Committee, approved the contents of this MD&A on March 9, 2006. This MD&A includes Canadian Tire's operating and financial results for 2005 and 2004 and should be read in conjunction with our Consolidated Financial Statements, which start on page 81 of this Annual Report.

## **Other important Company documents**

The following Canadian Tire public documents include additional information that will be of interest to investors:

- > Annual Information Form;
- > Management Information Circular; and
- > Quarterly reports.

These documents are available on SEDAR's web site at [www.sedar.com](http://www.sedar.com) and on the Investor Relations section of our web site at <http://investor.relations.canadiantire.ca>.

## **Quarterly and annual comparisons in this MD&A**

Unless otherwise indicated, all comparisons of the fourth quarter of 2005 are against the fourth quarter of 2004, and all comparisons to the full year of 2005 are against the full year of 2004.

## **Accounting estimates and assumptions**

The preparation of consolidated financial statements that conform with Canadian generally accepted accounting principles (GAAP) requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent liabilities at the date of the Consolidated Financial Statements and the reported amounts of revenue and expenses during the reporting period. We base our estimates on historical experience, current trends and other assumptions that are believed to be reasonable under the circumstances. Actual results could differ from those estimates. In our judgement, none of the estimates detailed in Note 1 of our annual Consolidated Financial Statements for the year ended December 31, 2005 requires us to make assumptions about matters that are highly uncertain. The methodology used in establishing each estimate is based either on models that we have used on a consistent basis for a significant period of time or on the detailed nature of the calculations used to establish the estimates. For these reasons, none of the estimates is considered a "critical accounting estimate" as defined in Form 51-102F1 published by the Ontario Securities Commission.

## **Forward-looking statements**

This disclosure contains statements that are forward-looking. Actual results or events may differ materially from those forecasted in this disclosure because of the risks and uncertainties associated with Canadian Tire's business and the general economic environment. In addition to the principal risks identified in section 9 of this MD&A, there are other external factors that could affect our results. These include, but are not limited to: changes in interest rates, currency exchange rates and tax rates; the ability of Canadian Tire to attract and retain quality employees, Associate Dealers, Petroleum agents and PartSource and Mark's Work Wearhouse store operators and franchisees; and the willingness of customers to shop at our stores or acquire our financial products and services.

# Management's Discussion and Analysis

Other specific risk factors that may cause actual results or events to differ materially from those forecasted in this MD&A include, but are not limited to:

- > expansion activity planned for Mark's Work Wearhouse (Mark's), PartSource, Canadian Tire Petroleum (Petroleum) and Canadian Tire Retail's (CTR) Concept 20/20 store format as well as the associated supply chain infrastructure could be affected by the Company's ability to acquire and develop real estate properties, obtain municipal and other required government approvals, access construction labour and lease suitable properties;
- > unseasonable weather patterns could affect the sales of seasonal merchandise at CTR and Mark's, particularly in the second and fourth quarters which historically are these divisions' largest selling periods;
- > adverse environmental occurrences could have the ability to damage the Company's reputation or threaten its licenses to operate, particularly in the Petroleum division;
- > changes in commodity prices could affect the profitability of Petroleum, CTR and Mark's; and customers' inability to repay their Canadian Tire credit card or personal loan balances could affect the earnings of Canadian Tire Financial Services (Financial Services).

We cannot provide any assurance that forecasted financial or operational performance will actually be achieved, or if it is, that it will result in an increase in the price of Canadian Tire shares.

## 1. Our Company

### 1.1 Overview of the business

Canadian Tire has been in business since 1922 and has evolved into a growing, innovative network of inter-related businesses. The Company operates over 1,100 stores, gas bars and car washes engaged in general merchandise, petroleum and clothing retailing and automotive and financial services.

The Company carries on four main businesses.

**Canadian Tire Retail (CTR)** is Canada's leading hard goods retailer with a network of 462 Canadian Tire stores that are operated by Associate Dealers who are independent business owners. Associate Dealers buy merchandise from us and sell it to consumers in Canadian Tire stores.

CTR also includes our online web-based shopping channel ("web store") and PartSource. PartSource is a chain of 57 specialty automotive hard parts stores that cater to serious "do-it-yourselfers" and professional installers of automotive parts. PartSource stores are operated primarily by franchisees.

**Mark's Work Wearhouse (Mark's)** is one of Canada's leading apparel and footwear retailers, operating 334 stores (280 corporate and 54 franchise stores). Mark's operates under the banners L'Équipeur in Quebec and Mark's Work Wearhouse and Work World in other parts of the country. In addition, Mark's conducts a business-to-business operation under the Imagewear by Mark's Work Wearhouse brand.

**Canadian Tire Petroleum (Petroleum)** is Canada's largest independent retailer of gasoline with a network of 259 gas bars, 247 convenience stores and kiosks, 67 car washes, 13 Pit Stops and 77 sites with propane stations. The convenience stores include two new Q store formats that were piloted in 2005. Substantially all of Petroleum's sites are operated by agents.

**Canadian Tire Financial Services (Financial Services)** markets the Canadian Tire MasterCard®, Canadian Tire retail credit card, Canadian Tire Commercial Link MasterCard, personal loans, insurance and warranty products and an emergency roadside assistance service called Canadian Tire Roadside Assistance. Canadian Tire Bank, a wholly-owned subsidiary of Financial Services, is a federally regulated bank that manages and finances Canadian Tire's MasterCard and retail credit card portfolios, as well as the personal loan portfolio.

## 2. Core capabilities

### 2.1 Brand equity

Canadian Tire's name and logo have been fixtures in Canadian retailing for over 80 years. The "red triangle" logo enjoys almost universal recognition among Canadian consumers. Canadian Tire has built a reputation for innovative products and services, attracting approximately 50 percent to 60 percent of all Canadians into Canadian Tire stores every month.

CTR has built upon its strong, long-standing private-label brands such as MotoMaster and Mastercraft by adding new brands on an ongoing basis, such as Yardworks and Simoniz, which are also becoming recognized and respected brands. Together, CTR's private-label products comprise approximately 30 percent of annual sales.

Mark's also has well established brand equity and established strong private-label brands, such as WindRiver, Denver Hayes and Dakota. At Mark's, private-label products represent approximately 75 percent of annual retail sales.

Petroleum's success is driven by its affiliation with the Canadian Tire brand. Petroleum's high-value reputation among customers is directly related to the successful Canadian Tire 'Money' loyalty program and cross-promotions with Canadian Tire stores. Petroleum's customer value proposition is one of the key factors that differentiates Petroleum from other gasoline retailers.

Financial Services' connection to the Canadian Tire brand contributes significantly to its success, which is enhanced by Financial Services' customer-focused culture. The Canadian Tire 'Money' on the Card program is one of the main incentives for customers to keep and use their Canadian Tire credit cards.

## **2.2 Loyalty program**

Canadian Tire's highly recognized 47-year-old loyalty program rewards customers with various forms of Canadian Tire 'Money'. The primary goal of the loyalty program is to encourage Canadians to shop at our stores, fill up at our gas bars and use our credit cards. Canadian Tire customers receive Canadian Tire 'Money' rewards when they pay with cash, debit card or cheque, or with one of Canadian Tire's credit cards.

Canadian Tire's 'Money' program originated as a customer traffic-builder for Canadian Tire's gas bars and today is still Petroleum's key loyalty program. Petroleum also offers several loyalty-building promotions, such as "multiplier" coupons that increase the amount of Canadian Tire 'Money' rewards customers receive when they buy gas at Petroleum's gas bars. Through effective use of marketing and promotional programs, Petroleum has become an industry leader in Canada in terms of the volume of gasoline pumped per site.

The Canadian Tire 'Money' on the Card program is an important part of Financial Services' value proposition. Customers earn Canadian Tire 'Money' on the Card rewards when they pay with their Canadian Tire MasterCard or retail card. They also earn Canadian Tire 'Money' on the Card rewards whenever they shop with their Canadian Tire MasterCard anywhere MasterCard is accepted.

## **2.3 Innovative product assortment**

CTR searches globally for innovative products for inclusion in the merchandise assortment carried in its stores. CTR provides strong advertising support, in the form of television commercials, in-store promotion and weekly flyers featuring these innovative new products to help drive consumer traffic into stores.

Mark's continues to introduce new apparel and footwear products to meet its customers' needs. In the last few years, Mark's introduced several innovative products such as metal-free safety boots and stain-resistant casual clothing. The introduction of these new products at Mark's increases sales by creating new customer demand and increasing store traffic.

## **2.4 Customer service**

Customer service is a key focus in all parts of our organization.

CTR enjoys a special relationship with its Associate Dealers, who have intimate knowledge of customer needs in local markets and use this knowledge to help determine the right product assortment and inventory levels to keep customers satisfied with their experience in Canadian Tire stores.

Financial Services' commitment to customer service is epitomized by its call centres, which have been recognized on a number of occasions by Service Quality Measurement Group Inc. as the best call centre in North America. In credit industry studies, credit cardholders cited customer service as one of the primary reasons for deciding which credit card they use.

Mark's commitment to customer service is reflected in its efforts to have the right inventory in the right place at the right time to service customer needs throughout the year.

Petroleum has also maintained a strong focus on customer service. Petroleum offers a special service to drivers who are physically challenged and need help refuelling their vehicles at our self-serve gas bars.

## **2.5 Real estate**

The Company has a core capability in identifying and securing, for purchase and development, strategic real estate properties. CTR has opened 345 new-format Canadian Tire stores since 1994, and has sold many of the surplus properties related to the traditional stores that were replaced during that period. Similarly, the Company actively manages the real estate assets of Petroleum, PartSource and Mark's. The Company employs a rigorous analysis and approval process to ensure that it places the right size store in the right market on a consistent and cost-effective basis and also works to maximize the proceeds realized on the sale of surplus properties, in order to re-deploy the cash raised more productively within the organization.

# Management's Discussion and Analysis

## 3. Our strategy

### 3.1 Our overall strategic objective

In order to leverage our core capabilities and institute a platform for sustainable, profitable business growth, we develop company-wide long-term strategic plans. 2005 represented the final year of our 2001–2005 Strategic Plan, which outlined strategic imperatives for our Company and shaped the initiatives executed in our businesses during that period. With the conclusion of the 2001–2005 Strategic Plan in 2005, we also embarked upon a new Strategic Plan that will guide our efforts through to the end of 2009. This new Strategic Plan for 2005 to 2009, launched in the spring of 2005, is based upon a comprehensive review of our business performance and factors influencing our future ability to successfully compete. The 2005–2009 Plan builds on our progress over the last five years, refining our focus on the initiatives that will help us to meet our financial aspirations. Information regarding our progress to date against our new Strategic Plan objectives is highlighted in the business segment information found in section 5.

We measure our long-term success by our total return to shareholders (TRS). Our objective is to achieve TRS in the top-quartile of North American retailers listed in the major consumer product indices of three stock exchanges:

- > Toronto Stock Exchange (TSX);
- > NASDAQ stock market (NASDAQ); and
- > New York Stock Exchange (NYSE).

The following table shows Canadian Tire's TRS, as measured by the appreciation in Canadian Tire's Class A Non-Voting Shares, plus dividends.

Fiscal period	TRS	Ranking
2001	40.3%	Second quartile
2002	30.4%	Top quartile
2003	26.5%	Second quartile
2004	43.0%	Top quartile
<b>2005</b>	<b>24.7%</b>	<b>Top quartile</b>
<b>Annualized 2001 to 2005</b>	<b>31.0%</b>	<b>Top quartile</b>

Top-quartile TRS was the overall objective of Canadian Tire's 2001–2005 Strategic Plan and remains so for the Company's 2005–2009 Strategic Plan, discussed within each business segment in Section 5. In order to continue to achieve this objective, we have established five financial aspirations, which are outlined below, that guide our growth plans and our ability to deliver above-average long-term performance.

While we believe that establishing and striving to achieve our financial aspirations is important in order to meet our objective of top-quartile TRS, we cannot provide assurance that future financial results or performance will result in top-quartile TRS. For more information on the risks associated with our businesses, refer to section 9 of this MD&A.



### 3.2 Our financial aspirations

The 2001–2005 Strategic Plan introduced five financial aspirations that, if achieved, we believed, would help us deliver our TRS objective. Our financial aspirations were developed through a comprehensive review of our capabilities, our recent historical financial and operating performance and by taking into consideration the performance of our peers. We chose our financial aspirations based on their correlation to the top TRS achieved by our peer group of retailers in Canada and the United States. The importance we have placed on striving to attain our aspirations influences our decisions and ensures that our entire organization is aligned around our objective of creating long-term shareholder value.

The table below shows how we performed in respect of the financial aspirations of our 2001–2005 Strategic Plan and outlines our 2005 performance results:

Financial aspirations	2001–2005 Strategic Plan	Total 2001–2005 <sup>1</sup> performance	2005 year-over-year performance	2005 year-over-year performance, excluding non-operating items
Comparable store sales (simple average of annual percentage growth, CTR stores only)	3% to 4%	2.6%	3.0%	3.0%
Gross operating revenue (compound annual growth rate)	at least 10%	8.3%	8.7%	8.7%
EBITDA <sup>2</sup> and minority interest (compound annual growth rate)	10% to 15%	11.7%	12.2%	14.6%
Basic earnings per share (compound annual growth rate)	12% to 15%	16.9%	12.2%	16.2%
After-tax return on invested capital (annual simple average)	at least 10%	8.7%	9.7%	9.3%

<sup>1</sup> Performance from the beginning of fiscal 2001 to the end of fiscal 2005.

<sup>2</sup> Earnings before interest, income tax, depreciation and amortization. See section 12 on non-GAAP measures.

### 3.3 Strategic plans

As indicated above, 2005 was the final year of our 2001–2005 Strategic Plan. This Strategic Plan has served as a roadmap and solid foundation for sustained growth.

Our 2001–2005 Plan had four strategic imperatives:

- 1 – strengthen and accelerate growth and performance in Canadian Tire Retail;
- 2 – pursue unexploited growth in Petroleum, Financial Services and PartSource;
- 3 – develop and explore new business opportunities; and
- 4 – enhance financial flexibility.

The extent of our success in delivering against these strategic imperatives can be assessed by referring to the delivery of specific initiatives outlined in section 5 and the delivery of top-quartile TRS performance as highlighted above.

In April 2005, we announced the details of our new 2005–2009 Plan, which outlines the strategic imperatives for the next five years. Our 2001–2005 Plan and our 2005–2009 Plan overlap in one year, 2005.

Our 2005–2009 Plan builds on our progress over the previous five years, refining our focus on the initiatives that will help us meet our financial aspirations. Our 2005–2009 Plan has five strategic imperatives:

- 1 – grow sales and revenues;
- 2 – improve our earnings performance;
- 3 – embed a Customers for Life culture across our entire organization;
- 4 – extend growth and performance beyond 2009; and
- 5 – enhance value creation through financial flexibility and maximization of the value of real estate assets.

Each of these imperatives is supported by specific initiatives to help ensure we meet our long-term financial aspirations and strategic objectives.

Our performance in 2005 has been measured against the aspirations of both our 2001–2005 and 2005–2009 Strategic Plans. Please refer to the appropriate business segment discussion in section 5 of this MD&A for evaluation of business segment performance versus the targets and financial aspirations of both of the Strategic Plans.

# Management's Discussion and Analysis

## 4. Risk management

The Company approaches the management of risk strategically, within its enterprise risk management (ERM) framework, in order to preserve shareholder value prudently. Please refer to Section 9 for an in-depth discussion of the Company's risk management processes and accountabilities. Risks that may specifically affect an individual business segment are also identified in the information below relating to that business segment.

## 5. How we performed in 2005

### 5.1 Consolidated results

Our entire network of businesses contributed to earnings in the fourth quarter and for the full year of 2005.

#### Consolidated financial results

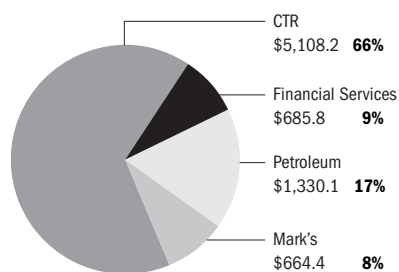
(\$ in millions except per share amounts)	Q4 2005	Q4 2004	Change	2005	2004	Change
Retail sales <sup>1</sup>	\$ 2,759.6	\$ 2,517.1	9.6%	\$ 9,090.5	\$ 8,389.6	8.4%
Gross operating revenue	2,319.2	2,095.9	10.7%	7,774.6	7,153.6	8.7%
EBITDA <sup>2</sup> and minority interest	260.1	221.5	17.4%	796.8	709.9	12.2%
Earnings before income taxes and minority interest	187.9	157.9	19.1%	527.7	460.9	14.5%
Effective tax rate	36.0%	35.3%		36.0%	35.3%	
Net earnings	\$ 118.2	\$ 100.4	17.7%	\$ 330.1	\$ 291.5	13.3%
Basic earnings per share	1.44	1.24	16.6%	4.04	3.60	12.2%

<sup>1</sup> Represents retail sales at CTR, as well as at Mark's corporate and franchise stores and at Petroleum's sites.

<sup>2</sup> See section 12 on non-GAAP measures.

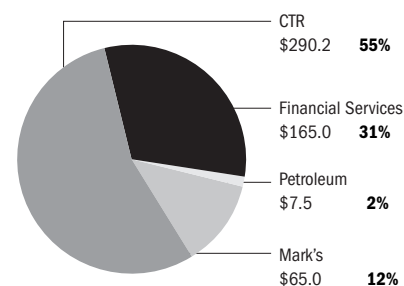
#### Gross operating revenue by business segment

(\$ millions)

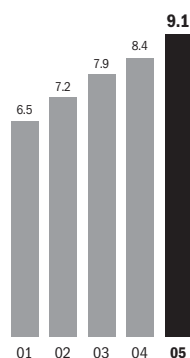


#### Earnings before income taxes and minority interest by business segment

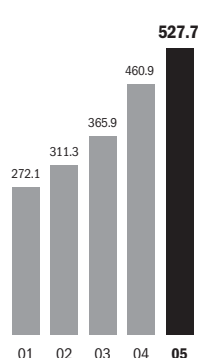
(\$ millions)



**Consolidated annual retail sales**  
(\$ billions)



**Consolidated earnings before income taxes and minority interest**  
(\$ millions)



**Robust fourth quarter retail sales contributed to strong full year top-line results** Highlights of our top-line performance in the fourth quarter and full year, on a year-over-year basis, include the following:

- > CTR's total retail sales increased 7.1 percent in the fourth quarter and 5.1 percent for the full year, while net shipments to CTR stores increased 7.8 percent in the fourth quarter and 4.2 percent for the full year;
- > Mark's retail sales increased 19.3 percent in the fourth quarter and 20.3 percent for the full year;
- > Petroleum's total retail sales increased 16.4 percent in the fourth quarter and 19.5 percent for the full year; and
- > Financial Services' total managed portfolio at year end increased 17.8 percent, including gross personal loan receivables, which now stand at \$221.1 million.

**Growth in gross operating revenue across all business segments** Consolidated gross operating revenue increased in the fourth quarter and year-to-date due to increased revenues across all business segments, including stronger shipments at CTR, higher gross receivables at Financial Services and continued strong sales at Mark's and Petroleum. Shipments to Canadian Tire stores accelerated in the fourth quarter due to the continued successful rollout of the Concept 20/20 store format and successful advertising and promotional programs, which led to solid retail sales in core product categories.

**Strong earnings growth in the fourth quarter fuelled by solid revenue gains and improved operating margins** Consolidated pre-tax earnings increased in the fourth quarter due to strong sales and earnings in CTR and Mark's along with growth in Financial Services profitability and an improvement in operating margins for Petroleum. The increase in pre-tax earnings was partially offset by lower gains on the sale of loans receivable than experienced in the fourth quarter of the prior year.

A higher effective tax rate in the fourth quarter and full year negatively impacted consolidated net earnings. The tax rate increased to 36.0 percent for the fourth quarter and the full year from 35.3 percent in the fourth quarter and the full year of 2004. This increase was primarily related to changes in the Ontario budget in the second quarter of 2005, which raised the tax rate on income earned by our Financial Services business for subsequent periods.

Full year 2005 consolidated pre-tax earnings increased year-over-year as a result of higher operating revenues, stronger margins and cost containment efforts. These factors overcame the impact of certain non-operating items, including the higher effective tax rate referred to in the previous paragraph, and the \$5.3 million cost of the early redemption of the May 2006 medium term notes, which occurred in the first quarter of 2005.

A comprehensive discussion of the factors that impacted each individual business segment's results is included in Section 5.2 of this MD&A.

**Impact of non-operating items** The following tables show our consolidated earnings on a pre-tax and after-tax basis, excluding gains and losses from the sales of loans receivable, the disposals of property and equipment and the impact of the early redemption of the May 2006 medium term notes.

**Adjusted consolidated earnings before income taxes and minority interest**

(\$ in millions)	Q4 2005	Q4 2004	Change	2005	2004	Change
Earnings before income taxes and minority interest	\$ 187.9	\$ 157.9	19.1%	\$ 527.7	\$ 460.9	14.5%
Less pre-tax adjustment for:						
Gain on sales of loans receivable <sup>1</sup>	13.0	14.2		19.9	22.6	
Gain on disposals of property and equipment <sup>2</sup>	5.9	2.9		10.9	14.4	
Loss on medium term notes redemption	-	-		(5.3)	-	
Adjusted earnings before income taxes and minority interest <sup>3</sup>	\$ 169.0	\$ 140.8	20.1%	\$ 502.2	\$ 423.9	18.5%

<sup>1</sup> Includes credit card and personal loans receivable. See section 5.2.4 on Financial Services' performance.

<sup>2</sup> See section 5.2.1 for CTR's performance and section 5.2.3 for Petroleum's performance.

<sup>3</sup> See section 12 on non-GAAP measures.

# Management's Discussion and Analysis

## Adjusted consolidated net earnings

(\$ in millions except per share amounts)	Q4 2005	Q4 2004	Change	2005	2004	Change
Net earnings	\$ 118.2	\$ 100.4	17.7%	\$ 330.1	\$ 291.5	13.3%
Less after-tax adjustment for:						
Gain on sales of loans receivable <sup>1</sup>	8.3	9.3		12.7	14.7	
Gain on disposals of property and equipment <sup>2</sup>	3.8	1.9		7.0	9.3	
Loss on medium term notes redemption	-	-		(3.4)	-	
Adjusted net earnings <sup>3</sup>	\$ 106.1	\$ 89.2	18.8%	\$ 313.8	\$ 267.5	17.3%
Basic earnings per share	\$ 1.44	\$ 1.24	16.6%	\$ 4.04	\$ 3.60	12.2%
Adjusted basic earnings per share <sup>3</sup>	1.30	1.10	17.6%	3.84	3.30	16.2%

<sup>1</sup> Includes credit card and personal loans receivable. See section 5.2.4 on Financial Services' performance.

<sup>2</sup> See section 5.2.1 for CTR's performance and section 5.2.3 for Petroleum's performance.

<sup>3</sup> See section 12 on non-GAAP measures.

## Selected annual consolidated financial information

(\$ in millions except per share amounts)	2005	2004	2003
Gross operating revenue	\$ 7,774.6	\$ 7,153.6	\$ 6,552.8
Net earnings	330.1	291.5	241.2
Basic earnings per share	4.04	3.60	2.99
Diluted earnings per share	3.98	3.53	2.95
Cash dividends declared per share	0.58	0.50	0.40
Total assets	5,955.6	5,243.2	4,893.1
Long-term debt (excluding current portion)	1,171.3	1,081.8	886.2

**Seasonal impact** We usually experience stronger revenues and earnings in the second and fourth quarters of each year because of the seasonal nature of a significant portion of our merchandise at CTR and Mark's. The following table shows our financial performance by quarter for the last two years.

## Consolidated quarterly results

(\$ in millions except per share amounts)	Q4 2005	Q3 2005	Q2 2005	Q1 2005	Q4 2004	Q3 2004	Q2 2004	Q1 2004
Gross operating revenue	\$ 2,319.2	\$ 1,904.2	\$ 2,032.4	\$ 1,518.8	\$ 2,095.9	\$ 1,715.5	\$ 1,927.3	\$ 1,414.9
Net earnings	118.2	84.4	92.2	35.3	100.4	69.4	80.8	40.9
Basic earnings per share	1.44	1.03	1.13	0.43	1.24	0.86	1.00	0.51
Diluted earnings per share	1.43	1.02	1.11	0.43	1.22	0.84	0.98	0.50

The proportion of annual gross operating revenue represented by the fourth quarter (29.8 percent) remained relatively consistent with that of the prior year (29.3 percent).

The proportion of annual net earnings represented by the fourth quarter (35.8 percent) is higher than the prior year (34.4 percent) due to the impact of first quarter charges in 2005, including the early redemption of MTNs referred to above. These factors were described in detail in our first quarter 2005 report.

## 5.2 How our business segments performed

### 5.2.1 Canadian Tire Retail

#### 5.2.1.1 2001–2005 Strategic Plan performance

The following outlines CTR's final results on the initiatives contained in our 2001–2005 Plan.

#### Canadian Tire Retail

Initiative	What was planned	2001–2005 What was delivered
<b>New-format/ Concept 20/20 store expansion</b>	<p>Revitalize store network by rolling out the new-format store concept and launch a store format renewal initiative to drive growth.</p> <p>The goal identified was to expand the retail network to between 480 and 490 stores by the end of 2005, of which 350 to 370 would be new-format stores.</p>	<p>Each year, the pace of new-store construction was evaluated to ensure that we were focussing on investing in the highest return projects. The Concept 20/20 format was created and now serves as CTR's growth platform for 2005 to 2009.</p> <p>At the end of 2005, there were 462 Canadian Tire stores in the CTR network, of which 345 were new-format stores. The total also included 53 Concept 20/20 stores and 11 combination Canadian Tire-Mark's Work Wearhouse stores.</p>
<b>Completing CustomerLink</b>	<p>Complete the multi-year supply chain upgrade program aimed at increasing supply chain capacity, improving productivity and improving customer service levels.</p>	<p>CustomerLink, which was a major investment in our supply chain capability, is substantially complete and contributing to improved capacity and productivity. Completion of the remaining program components is planned by mid 2006. Through this initiative we have been able to implement the technology to support multi-channel capabilities and have provided expanded capacity to improve customer service.</p>
<b>Expansion of Calgary distribution centre</b>	<p>440,000 square-foot expansion of the Calgary distribution centre capacity to support growth through 2009.</p>	<p>The building was completed on time in 2005. An additional project expansion, which includes material handling requirements, will be completed in early 2006.</p>
<b>Auto service</b>	<p>Grow our share of the automotive service market to 10 percent (from seven percent in 2001) and enhance our automotive infrastructure.</p>	<p>Our market share in 2005 remains at seven percent. We continue to aspire to achieving market share of 10 percent within the 2005–2009 Plan period.</p>
<b>PartSource network expansion</b>	<p>Continue to expand the PartSource network through opening new stores and through acquisitions as part of our ongoing initiative to build the network.</p>	<p>At the beginning of 2001, there were 28 PartSource locations and, at the end of 2005 there were a total of 57 locations in the network (three of which were recently acquired competitive businesses) demonstrating our commitment to continue expanding the network.</p> <p>The three new stores that were acquired in the fourth quarter of 2005 will be fully transitioned to the PartSource banner in 2006.</p>

# Management's Discussion and Analysis

## 5.2.1.2 Key performance indicators

The following are three key measures of CTR's sales productivity:

- > total retail, comparable and same store sales growth;
- > average retail sales per store; and
- > average sales per square foot of retail space.

### CTR retail, comparable and same store sales growth<sup>1</sup>

(year-over-year percentage change)	Q4 2005	Q4 2004	2005	2004
Total retail sales <sup>2</sup>	7.1%	3.7%	5.1%	4.4%
13 weeks compared to 13 weeks	7.1%	9.3%		
52 weeks compared to 52 weeks			5.1%	6.0%
Comparable store sales <sup>3</sup>	5.1%	1.1%	3.0%	1.8%
13 weeks compared to 13 weeks	5.1%	6.5%		
52 weeks compared to 52 weeks			3.0%	3.4%
Same store sales <sup>4</sup>	5.4%	N/A	3.4%	N/A

<sup>1</sup> The fiscal year of 2003 included 53 weeks, whereas 2004 and 2005 were normal 52-week fiscal years. To provide a more meaningful interpretation of our year-over-year results, we have identified where the 2004 calculations are adjusted based on the extra week in 2003.

<sup>2</sup> Includes sales from Canadian Tire stores, PartSource stores, sales from CTR's online web store and the labour portion of CTR's auto service sales.

<sup>3</sup> Comparable store sales include sales from stores that have been open for more than 53 weeks and that have not been expanded by more than 25 percent in the last year.

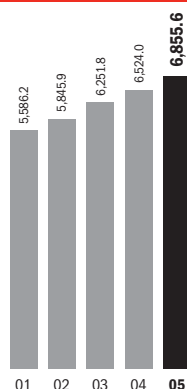
<sup>4</sup> Same store sales include sales from stores that have been open for more than 53 weeks, including stores that have been expanded by more than 25 percent in the last year. This metric was actively employed by CTR for the first time in 2005.

### CTR's same store sales

Same store sales comprise sales from stores that have been open for more than 53 weeks, including stores that have been expanded by more than 25 percent in the last year.

**Same store sales** With the large number of store expansions completed in the last year and those planned for the future, the same store sales metric has been included in this MD&A to enhance our disclosure.

### CTR's retail sales (\$ millions)



**Higher retail sales due to strong marketing programs and the continued success of the Concept 20/20 store program** The cumulative effect of 28 new Concept 20/20 stores opened in 2005 (including five combination CTR-Mark's stores and 11 retrofits), as well as compelling marketing and advertising programs, such as our flyer program and demonstration-style television commercials, and the strength of core categories, continued to play key roles in driving sales at Canadian Tire stores.

During the fourth quarter, sales in the Car Care and Accessories, Tools and Home Repair and Maintenance categories showed strong growth over the prior year, with Exciting, New and Exclusive (ENE) products such as, Reflex wiper blades, contributing to this growth. On a full year basis, sales in Tools, Car Care and Accessories and Kitchen and Home Appliances provided strong growth compared to last year. Both fourth quarter and year-to-date sales increases were partially offset by softness in the Auto Parts category due to the weak do-it-yourself auto parts market.

New Concept 20/20 stores continue to experience higher average sales per transaction and higher sales increases than new-format and traditional stores. CTR opened eight new stores (including two Concept 20/20 Mark's combination stores, one of which was a relocated Mark's store) and retrofitted 10 stores to the new Concept 20/20 format in the fourth quarter.

PartSource enjoyed a solid increase in sales in the fourth quarter and again experienced double-digit growth in commercial sales. Total sales growth was also supported by three new store openings during the fourth quarter and a total of seven new stores plus three acquired stores in 2005.

## Retail sales by product division<sup>1</sup>

(\$ in millions)	2005	2004	2003
Home	\$ 2,826.5	\$ 2,671.3	\$ 2,615.6
Leisure	1,930.5	1,835.7	1,682.2
Automotive	1,781.4	1,706.2	1,650.2
<b>Total</b>	<b>\$ 6,538.4</b>	<b>\$ 6,213.2</b>	<b>\$ 5,948.0</b>

<sup>1</sup> Retail sales are shown on a 52-week basis in each year and include sales from Canadian Tire and PartSource stores, and exclude sales from CTR's online web store and the labour portion of CTR's auto service sales.

The Home Products division, which at 43.2 percent of the total retail sales for CTR represents its largest division, grew at 5.8 percent in 2005 over 2004, representing the largest annual increase amongst the divisions. The increase was driven by strong sales of Tools and Kitchen and Home appliances.

## Average retail sales per Canadian Tire store<sup>1,2</sup>

(\$ in millions)	2005	2004	2003
Traditional stores	\$ 8.1	\$ 8.2	\$ 8.2
New-format stores	16.0	15.6	15.2

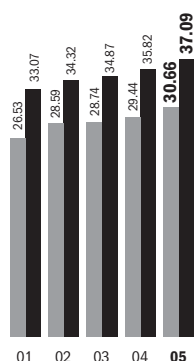
<sup>1</sup> Retail sales are shown on a 52-week basis in each year and exclude sales from PartSource stores, CTR's online web store and the labour portion of CTR's auto service sales.

<sup>2</sup> Only includes stores that have been open for a minimum of two years as of the beginning of the year.

Sales at new-format stores, including Concept 20/20 stores, are higher than at traditional stores as new-format stores are larger, have a more convenient layout and offer a broader selection of merchandise. The average dollar amount of each retail sale at new-format stores continues to increase partly because new-format stores allow for larger displays of promotional, seasonal and Exciting, New and Exclusive (ENE) products, which are key sales drivers.

## Average dollar amount of each retail sale<sup>1</sup>

(\$)



■ Traditional stores  
■ New-format stores

<sup>1</sup> Excludes sales from Concept 20/20 stores, PartSource stores, CTR's online web store and the labour portion of CTR's auto service sales.

## CTR store count

	2005	2004	2003	2002	2001
New-format stores	345	327	309	290	270
Concept 20/20 stores (included in new-format store count above)	53	25	4	-	-
Traditional stores	117	130	143	161	180
Total new-format stores and traditional stores	462	457	452	451	450
PartSource stores	57 <sup>1</sup>	47	39	33	30

<sup>1</sup> Including three recently acquired operations that will be converted to PartSource branded locations in 2006.

CTR continues to expand and retrofit the store network, consistent with the goals embodied in both the 2001-2005 and 2005-2009 Strategic Plans.

## Average sales per square foot of Canadian Tire retail space<sup>1,2</sup>

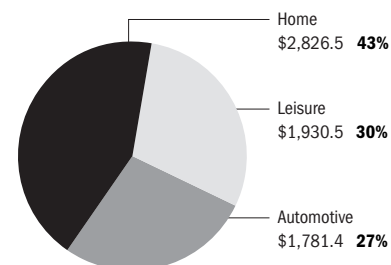
	2005	2004	2003
Retail square footage (millions of square feet)	14.9	14.2	13.5
Traditional stores (\$)	\$ 512	\$ 508	\$ 499
New-format stores (\$)	446	436	423

<sup>1</sup> Retail sales are shown on a 52-week basis in each year for those stores that have been open for a minimum of two years. Sales from PartSource stores, CTR's online web store and the labour portion of CTR's auto service sales are excluded.

<sup>2</sup> Retail space does not include warehouse, garden centre and auto service areas.

## CTR's retail sales by product division<sup>1</sup>

(\$ millions)



<sup>1</sup> Excludes sales from CTR's online web store and the labour portion of CTR's auto service sales.

Average sales per square foot of retail space in the larger new-format stores are lower than in our traditional stores because new-format stores are designed to utilize the additional space to display more merchandise, accommodate wider aisles and include more compelling product displays to create a more enjoyable shopping experience and thus increase total sales per store.

# Management's Discussion and Analysis

## 5.2.1.3 CTR's financial results

(\$ millions)	Q4 2005	Q4 2004	Change	2005	2004	Change
Retail sales	\$ 2,065.5	\$ 1,927.7	7.1%	\$ 6,855.6	\$ 6,524.0	5.1%
Net shipments (year-over-year % change)	7.8%	7.4%		4.2%	5.6%	
Gross operating revenue	\$ 1,520.7	\$ 1,409.4	7.9%	\$ 5,108.2	\$ 4,899.0	4.3%
EBITDA <sup>1</sup> and minority interest	151.1	133.8	12.9%	530.2	488.2	8.6%
Earnings before income taxes and minority interest	86.9	78.0	11.5%	290.2	271.9	6.8%
Less adjustment for:						
Gain on disposals of property and equipment	7.0	4.3		12.4	16.1	
Loss on medium term notes redemption	-	-		(5.3)	-	
Adjusted earnings before income taxes and minority interest <sup>1</sup>	\$ 79.9	\$ 73.7	8.5%	\$ 283.1	\$ 255.8	10.7%

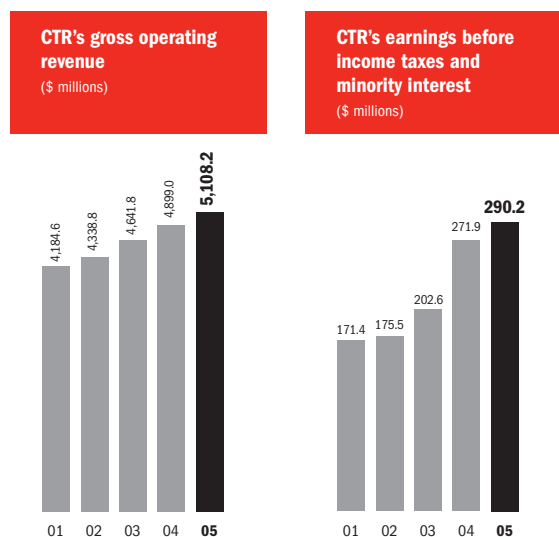
<sup>1</sup> See section 12 on non-GAAP measures.

## 5.2.1.4 Explanation of CTR's financial results

**Stronger shipments contributed to a solid rise in gross operating revenue** A 7.8 percent increase in net shipments in the fourth quarter and a 4.2 percent increase in the full year of 2005 led to higher gross operating revenue with shipment growth outpacing retail sales growth in the latter half of the year. For commentary on CTR's retail sales, see Section 5.2.1.2.

### CTR's net shipments

CTR's net shipments are the total value of merchandise shipped to Canadian Tire and PartSource stores, and through our online web store, less discounts and returns, recorded at the wholesale price that we charge to our Associate Dealers and PartSource franchisees.



**Fourth quarter earnings supported by higher shipments and margins** Earnings before tax and minority interest increased due to the volume impact of higher shipments, improved margins resulting from higher vendor rebates and global sourcing initiatives, as well as higher store rental revenue, consistent with the growth in retail sales. In addition, gains from the disposal of property and equipment were higher in the fourth quarter of 2005 versus the fourth quarter of 2004 by \$2.7 million.

These factors were partially offset by:

- > increased distribution costs due to additional offsite inventory storage costs and increases in utility rates and property taxes from the Calgary distribution centre expansion (\$2.1 million); and
- > increased depreciation from the CustomerLink project and IT capital expenditures (\$2.5 million)

**Full year earnings also supported by higher shipments and margins** On a full year basis, earnings before tax and minority interest increased primarily due to stronger shipments and improved margins resulting from the factors referred to in the previous paragraph as well as increased rental income from Associate Dealers stemming from stronger retail sales (\$11.3 million).

These factors were partially offset by:

- > lower gains from the disposal of property and equipment (\$3.7 million);
- > increased depreciation from the CustomerLink project (\$7.4 million); and
- > the net cost in the first quarter of the early redemption of the May 2006 medium term notes which was initiated to reduce financing costs over the long-term (\$5.3 million).

## 5.2.1.5 Business trends

Canada's retail industry has experienced significant change over the past 10 years. Competition in the retail market and individual sectors has intensified, with domestic retailers expanding and international retailers entering Canada. The industry has also experienced consolidation as department stores and other retailers have gone out of business or have been acquired.

Retail formats have continually increased in terms of store size and merchandise breadth, creating a situation where retailers are competing both within a specific industry segment (eg. Automotive and specialty) and across sectors (eg. general merchandise and grocery).



In order to grow in this increasingly competitive market, retailers must have a clear and unique value proposition and be able to respond to the changing demographics and lifestyles of Canadian consumers, who demand an optimum combination of choice, convenience, quality, value and service. Price competitiveness and promotional effectiveness are increasingly important factors in retail success.

The Home and Leisure markets are expected to grow in line with the growth in population and increases in consumers' disposable income that have resulted from a robust economy (particularly in western Canada) and the wealth effect from increasing property values.

After several years of flat performance, industry experts are forecasting the Canadian automotive parts market to expand in view of the automobiles purchased during the late 1990s (a high point in the automotive sales cycle) that are entering their prime repair years.

#### 5.2.1.6 2005–2009 Strategic Plan Outlook

Our 2005–2009 Strategic Plan consists of the following initiatives that represent a commitment to significant investment and will have a major impact on the delivery of our strategy and on our financial Outlook:

Initiative	Strategy	Key points
<b>New-format store roll-out</b>	CTR's strategy for the continued roll-out of new-format stores continues with a plan of approximately 20 new or replacement stores per year throughout the Outlook period.	New-format stores drive sales, enhance our brand image and are key to our growth. Replacement of traditional stores with new-format stores allows for continued renewal of store formats to better service customers.
<b>Concept 20/20 store roll-out</b>	<p>A critical aspect of CTR's Plan is to roll-out the Concept 20/20 format in existing new-format stores.</p> <p>Based on experience gained from the implementation of the first 53 Concept 20/20 stores, CTR has adjusted its roll-out approach. It has changed from a "Dealer-by-Dealer" approach to a "market-by-market" approach.</p>	<ul style="list-style-type: none"> <li>&gt; the Concept 20/20 format has proven to have a very positive impact on customers and retail sales;</li> <li>&gt; although individual store performance varies, the Plan assumes that, on average, new Concept 20/20 stores perform 10 percent to 20 percent better than typical new-format store performance;</li> <li>&gt; retrofit stores are assumed to have 10 percent to 15 percent gains in first year sales; and</li> <li>&gt; planned investment in the Concept 20/20 roll-out and continued replacement of traditional stores is anticipated to be between \$850 and \$900 million during the 2005–2009 period.</li> </ul>
<b>Global sourcing strategy</b>	Global sourcing is critical to CTR's Strategic Plan as it has proven to drive higher retail sales and margin protection.	<p>Offshore sourced products:</p> <ul style="list-style-type: none"> <li>&gt; provide margin protection;</li> <li>&gt; provide stronger retail sales results; and</li> <li>&gt; create new supply chain challenges.</li> </ul>
<b>Exciting, New and Exclusive (ENE) products</b>	ENE is one of CTR's critical long-term differentiators and we are investing in infrastructure to take the ENE concept to the next level.	<p>Key components of the ENE infrastructure will provide:</p> <ul style="list-style-type: none"> <li>&gt; world search capabilities;</li> <li>&gt; advanced consumer feedback methods;</li> <li>&gt; global sourcing infrastructure advancements;</li> <li>&gt; new "innovation" and "Style and Design" management teams; and</li> <li>&gt; trend and category innovation focus.</li> </ul>
<b>Inventory practices review</b>	The inventory practice program will be important to CTR's results and will involve short-term changes directed at improvements in promotional in-stock position and improved operational processes in forecasting and replenishment. It will also involve longer-term improvements directed at a smoother flow of goods among vendors, the Company and the Dealer network to improve promotional in-stock position, inventory turnover and sales.	<p>Key factors to consider in the implementation of the Plan are:</p> <ul style="list-style-type: none"> <li>&gt; continued focus on promotional effectiveness;</li> <li>&gt; the need to improve in-stock position for our customers; and</li> <li>&gt; increases in globally sourced goods.</li> </ul>

# Management's Discussion and Analysis

## 5.2.1.7 Strategic initiative status

The following summarizes CTR's progress to date against initiatives contained in the 2005–2009 Strategic Plan and current plans in place for continued progress in 2006.

### Schedule of new store openings, store retrofits and expansions

	Incremental square footage by quarter			New-format store openings <sup>1</sup>			Concept 20/20 retrofits/ store expansions		
	Plans for 2006	2005	2004	Plans for 2006	2005	2004	Plans for 2006	2005	2004
Q1	110,000	95,000	62,000	2	5	3	-	-	-
Q2	586,000	127,000	347,000	2	4	8	35	1	8
Q3	324,000	58,000	50,000	8	1	1	10	-	-
Q4	461,000	386,000	198,000	8	8	6	15	10	1
	1,481,000	666,000	657,000	20	18	18	60	11	9

<sup>1</sup> Includes combination Canadian Tire-Mark's Work Wearhouse stores.

## Canadian Tire Retail

### New-format stores

CTR began replacing traditional Canadian Tire stores with new-format stores in 1994 and, since then, has opened 345 new-format stores across the country.

Larger retail floor space, a more convenient layout and more room to display merchandise create a more enjoyable shopping experience for customers, which is why more customers visit new-format stores than traditional stores and, on average, spend a higher amount per visit. Also, new-format stores have consistent layouts to improve the efficiency of rolling out new merchandising programs and offer a more consistent customer experience across the chain.

In the fourth quarter of 2005, CTR:

- > replaced five traditional stores with new-format stores; and
- > opened three additional new-format stores.

Over the full year of 2005, CTR:

- > replaced 12 traditional stores with new-format stores; and
- > opened six additional new-format stores.

There are now 345 new-format stores in the CTR network, including 53 Concept 20/20 stores and 11 Canadian Tire-Mark's Work Wearhouse combination stores.

#### Plans for 2006

CTR's strategy for the ongoing roll-out of new-format stores will continue with a plan of opening approximately 20 new, expansion or replacement stores in 2006. As noted below, the major component of our Plan strategy involves an acceleration in the rollout of Concept 20/20 stores.

### Concept 20/20 store roll-out

In 2003, a new store merchandising format, Concept 20/20, was introduced featuring:

- > an updated store layout;
- > conversion of warehouse space to retail selling space;
- > expanded merchandise space for high growth categories;
- > a customer care centre;
- > new store signage; and
- > a revitalized exterior façade.

Expanding retail space by reducing the warehouse space within the store and adjusting merchandise space allocation are key elements of the concept, which is designed to boost sales in stores by 10 percent to 20 percent in the first year after the store has been converted to a C20/20 store and thereafter continuing to experience sales growth greater than traditional stores.

#### Plans for 2006 and beyond

Substantially all of the 20 new or replacement stores CTR plans to build in 2006 will be in the C20/20 format. CTR also plans to retrofit approximately 60 existing new-format stores to the C20/20 format.

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**Global sourcing strategy**

Global sourcing is critical to CTR's Strategic Plan as it provides access to a broader range of higher quality and innovative products to help drive stronger retail sales, as well as access to lower cost products, providing margin protection. Through the implementation of global sourcing, CTR will:

- > add to its portfolio of ENE products;
- > launch new and innovative promotional programs; and
- > achieve competitive price points, supported by lower inventory acquisition costs.

In 2005, approximately 35 percent of the value of purchases came from offshore sources, compared to 30 percent in 2004.

**Plans for 2006 and beyond**

CTR plans to increase the percentage of purchases sourced offshore from the current 35 percent level to a target level of approximately 50 percent by 2009.

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**Exciting, New and Exclusive products**

ENE products are one of CTR's critical long-term differentiators and a key component of CTR's strong marketing platform.

Aggressive advertising, including prominent placement in the Canadian Tire catalogue and flyers, demonstration-style television commercials, and compelling in-store displays continue to support the growth of ENE product sales.

**Plans for 2006 and beyond**

CTR is investing in the infrastructure to take the ENE concept to the next level through its world search capabilities, consumer feedback mechanisms, growing global sourcing infrastructure, new "innovation" and "Style and Design" management teams and a trend and category innovation focus.

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**Inventory practice program**

The inventory practice program involves some key short-term and long-term changes that are expected to result in an improved flow of goods, both promotional and regular stock, to our Dealers.

The program will address the following during the implementation and planning process:

- > continued focus on promotional effectiveness;
- > the need to improve in-stock position especially of promotional items for our customers; and
- > increases in the proportion of globally sourced goods and consequent effect on lead times.

In 2005, our short-term plan involved changes directed at improvements in the promotional in-stock position and improved operational processes in forecasting and replenishment.

**Plans for 2006 and beyond**

Longer-term plans for the inventory practice program include directing a smoother flow of goods from vendors to the Company and on to the Dealers to improve in-stock position, inventory turns and sales.

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**5.2.1.8 Business risks**

CTR is exposed to a number of risks in the normal course of its business that have the potential to affect its operating performance. The following are some of the business risks specific to CTR's retail and other operations. Please also refer to Section 9 of this MD&A for a discussion of some other industry-wide and company-wide risks affecting us.

**Supply chain disruption risk** An increasing portion of CTR's product assortment is being sourced globally and the supply chain lengthens and consequently the time between order point and delivery point to our distribution centres has been extended. CTR is exposed to potential supply chain disruptions due to foreign supplier failures, geopolitical risk and risks of delays/losses of inventory in transit. The Company mitigates this risk through effective supplier selection and procurement practices supplemented by marine insurance coverage. CTR has demonstrated its ability to mitigate this risk, to the extent possible, in the past.

**Seasonality risk** CTR derives a significant amount of its revenues from the sale of seasonal merchandise and accordingly bears a degree of risk from unseasonable weather patterns. We mitigate this risk, to the extent possible, through effective procurement and inventory management practices.

**Environmental risk** Environmental risk within CTR is primarily associated with the handling and recycling of certain materials, such as tires, paint, oil and lawn chemicals, sold in Canadian Tire and PartSource stores. CTR established and follows comprehensive environmental policies and practices to avoid putting its reputation and license to operate at risk. CTR's procedures for the identification and mitigation of environmental risk are supplemented by environmental insurance coverage.

# Management's Discussion and Analysis

## 5.2.2 Mark's Work Wearhouse

### 5.2.2.1 2001–2005 Strategic Plan performance

The following outlines Mark's final results on the initiatives contained in our 2001–2005 Strategic Plan.

#### Mark's Work Wearhouse

Initiative	What was planned	2001–2005 What was delivered
<b>Network expansion and store expansions</b>	Build new stores, renovate select stores to the newest Mark's format, and convert identified Work World stores to the Mark's Work Wearhouse banner.	<p>At the time of Canadian Tire's acquisition of Mark's in February 2002, there were 323 stores in the Mark's chain (167 Mark's, 148 Work World and eight DOCKERS). During the 2001–2005 Strategic Plan period, Mark's added 72 new stores, closed 46 stores, discontinued relationships with 15 Work World franchise stores and converted 95 Work World banner stores and one DOCKER'S banner store to Mark's banner stores to end the Plan period with 334 stores (324 Mark's and 10 Work World stores). Mark's also renovated or relocated 77 stores in order to revitalize the store network.</p> <p>Based on initial targets established and communicated in our 2003 Annual Report, Mark's fell short of the targeted store count of 363 stores, but attained its goal of 2.6 million total system retail square feet. At the end of 2005, included in the total store count were 11 combination CTR-Mark's stores developed over the last two years.</p>
<b>Category growth</b>	Continue to expand the women's casual wear, business-to-business and health care apparel categories.	Mark's has continued to expand its women's wear, business-to-business and health care apparel categories. Corporate store sales increased in 2005 in all three of these high-potential categories by over 20 percent versus the same period in 2004, exceeding Mark's target of 15 percent growth for these categories.

### 5.2.2.2 Key performance indicators

The following are key performance indicators for Mark's:

- > retail and same store sales growth;
- > average sales per corporate store; and
- > average sales per square foot of retail space.

#### Mark's retail and same store sales growth<sup>1,2</sup>

(year-over-year percentage change)	Q4 2005	Q4 2004	2005	2004
Total retail sales	<b>19.3%</b>	15.7%	<b>20.3%</b>	17.8%
13 weeks compared to 13 weeks	<b>19.3%</b>	20.0%		
52 weeks compared to 52 weeks			<b>20.3%</b>	19.6%
Same store sales	<b>17.4%</b>	11.3%	<b>17.4%</b>	13.4%
13 weeks compared to 13 weeks	<b>17.4%</b>	15.4%		
52 weeks compared to 52 weeks			<b>17.4%</b>	15.1%

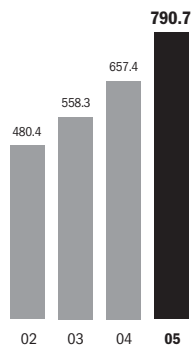
<sup>1</sup> Mark's same store sales exclude new stores, stores not open for the full period in each year and store closures.

<sup>2</sup> The fiscal year of 2003 included 53 weeks, whereas 2004 and 2005 were normal 52-week fiscal years. To provide a more meaningful interpretation of our year-over-year results, we have identified where the 2004 calculations are adjusted based on the extra week in 2003.



**Mark's retail sales** represent total merchandise sales to consumers, net of returns across Mark's entire network of stores, recorded at retail prices.

**Mark's retail sales<sup>1</sup>**  
(\$ millions)



<sup>1</sup> Mark's was acquired on February 1, 2002. Performance prior to that has been excluded.

**Higher total retail sales in major product categories and in all regions in the fourth quarter** Mark's delivered another quarter of double-digit total retail sales increases in all regions across Canada, with particularly strong sales in the prairies, which rose 23.1 percent, and British Columbia, which increased 21.0 percent. By product category, the largest sales increases, in percentage terms, occurred in:

- > accessories (men's and women's), 31.7 percent;
- > casual footwear (men's and women's), 24.2 percent; and
- > industrial footwear (men's and women's), 24.1 percent.

In addition, Mark's also delivered full year double-digit total retail sales increases in all regions across Canada for 2005. The strongest sales were reported in the prairies, which rose 24.2 percent, and Ontario, which increased 20.5 percent. By product category, the largest sales increases, in percentage terms, occurred in:

- > women's casual wear, 39.6 percent;
- > accessories (men's and women's), 29.5 percent; and
- > casual footwear (men's and women's), 26.4 percent.

Both fourth quarter and full year sales were driven by category initiatives, a higher investment in inventory during the first half of the year, ongoing implementation of Mark's "Clothes That Work" marketing strategy, cross-promotions with other Canadian Tire business segments and the cumulative effect of store replacements, expansions and conversions over the past several quarters. The increasing popularity of Mark's innovative products, such as stain-resistant clothing, metal-free safety footwear and socks for diabetics, again contributed to Mark's overall sales performance in the fourth quarter and full year.

**Average corporate store sales**

	2005	2004	2003
Sales per store (\$ thousands) <sup>1</sup>	\$ <b>2,406</b>	\$ 2,061	\$ 1,929
Sales per square foot (\$) <sup>2</sup>	<b>313</b>	276	254

<sup>1</sup> Average sales per corporate store include corporate stores that have been open for 12 months or more.

<sup>2</sup> Sales per square foot is based on sales from corporate stores. We have prorated square footage for corporate stores that have been open for less than 12 months.

Mark's corporate sales productivity, as measured by sales per store and sales per square foot, has increased significantly since Mark's was acquired by Canadian Tire in 2002. The increase in sales productivity in 2005 over the prior year was due to:

- > higher inventory in-stock position during 2005;
- > introduction of innovative products into the product line; and
- > effective marketing and advertising programs designed to increase customer visits and raise awareness of Mark's brands.

**5.2.2.3 Mark's financial results**

(\$ millions)	Q4 2005	Q4 2004	Change	2005	2004	Change
Retail sales <sup>1</sup>	\$ <b>326.6</b>	\$ 273.7	19.3%	\$ <b>790.7</b>	\$ 657.4	20.3%
Gross operating revenue <sup>2</sup>	<b>275.0</b>	227.8	20.7%	<b>664.4</b>	546.1	21.7%
EBITDA <sup>3</sup>	<b>47.2</b>	35.2	34.1%	<b>82.2</b>	53.8	52.9%
Earnings before income taxes	<b>42.2</b>	30.9	36.7%	<b>65.0</b>	37.1	75.2%

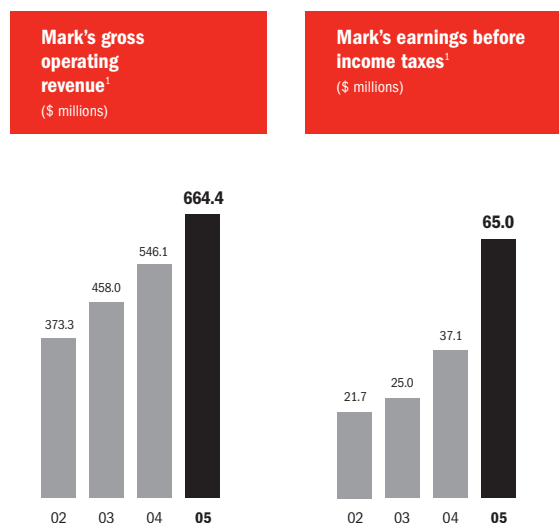
<sup>1</sup> Includes retail sales from corporate and franchise stores.

<sup>2</sup> Gross operating revenue includes retail sales at corporate stores only.

<sup>3</sup> See section 12 on non-GAAP measures.

# Management's Discussion and Analysis

## 5.2.2.4 Explanation of Mark's financial results



<sup>1</sup> Mark's was acquired on February 1, 2002. Performance prior to that has been excluded.

**Higher sales drove Mark's increase in pre-tax earnings** The significant year-over-year improvement in Mark's pre-tax earnings in the fourth quarter and full year was due to a double-digit increase in same store sales and improved gross margin. Mark's gross margin rate improved in the fourth quarter as compared to the fourth quarter of the prior year primarily due to improved purchase markup due to ongoing global sourcing initiatives and reduced customer adjustments and inventory shrinkage, which more than offset higher markdowns and freight costs. The full year improvement was due to the same factors. Mark's robust top-line growth was supported by increased investments in personnel, advertising and infrastructure. Mark's, however, also incurred higher store closure costs. Even with these additional costs, Mark's total expenses, as a percentage of gross operating revenue, improved in both the fourth quarter and year-to-date.

## 5.2.2.5 Business trends

Two long-term trends that have impacted Canada's \$19 billion to \$20 billion apparel market are:

- > the move from traditional business attire to business casual clothing in the workplace; and
- > the increasing number of Canadians who are leading more active lifestyles outside the office.

Traditional apparel retailers are facing a challenging market. Consumers are spending a smaller percentage of disposable income on clothing. The apparel market in Canada has also experienced price deflation due to intensifying competition from other retailers, including foreign and non-traditional apparel retailers that are increasing the number of products they procure from overseas suppliers. Nevertheless, growth opportunities still exist for Canadian retailers that are positioned to anticipate and meet the changing preferences and lifestyle needs of customers.

## 5.2.2.6 2005–2009 Strategic Plan Outlook

Our 2005–2009 Strategic Plan consists of the following initiatives that represent a commitment to significant investment and will have a major impact on the delivery of our strategy to our customers and on our financial Outlook:

Initiative	Strategy	Key points
Grow sales and revenue	Continue network development through opening new stores, relocating or expanding existing stores and renovating older stores to the new Mark's format.	Continue growth of the retail network to between 395 and 400 stores by the end of the 2005–2009 Strategic Plan period.
	Continue to expand key product categories.	Focus on expanding key category product lines with a focus on: <ul style="list-style-type: none"> <li>&gt; women's casual and business wear;</li> <li>&gt; business-to-business work apparel;</li> <li>&gt; footwear;</li> <li>&gt; dressier clothing; and</li> <li>&gt; health care wear.</li> </ul>
	Continue to identify ways to take advantage of synergies available through existing Canadian Tire channels.	Focus on identifying ways to further leverage synergistic opportunities through: <ul style="list-style-type: none"> <li>&gt; cross-promotions;</li> <li>&gt; marketing distribution efficiencies; and</li> <li>&gt; opening combination CTR-Mark's stores.</li> </ul>

Initiative	Strategy	Key points
<b>Improve earnings</b>	Continued margin improvement.	Improve margins through identifying and creating: <ul style="list-style-type: none"> <li>&gt; sourcing initiatives; and</li> <li>&gt; price optimization.</li> </ul>
	Continued operational efficiency improvements to reduce expenses as a percentage of sales.	Reduce expenses, as a percentage of sales by taking advantage of: <ul style="list-style-type: none"> <li>&gt; operational efficiency improvements; and</li> <li>&gt; supplier programs.</li> </ul>
<b>Develop Customers for Life</b>	Establish a solid foundation for the Customers for Life strategy.	Identify, and develop reporting on, key metrics and measures in order to assess progress with the strategic goals.
	Focus on promoting a growth culture through strategic campaigns such as “Clothes That Work”.	“Clothes That Work” is a more customer-focussed strategy that focusses on better engineered clothing.
	Establish a solid foundation for strong brand recognition of Mark’s and the “Clothes That Work” campaign.	Create a “Superbrand” for Mark’s to meet Mark’s aspiration of \$1 billion of total system sales by 2009 through: <ul style="list-style-type: none"> <li>&gt; building a favourite brand that customers recognize, use and value; and</li> <li>&gt; building a brand that achieves a role in the everyday life and closets of Canadians.</li> </ul>

#### 5.2.2.7 Strategic initiative status

The following summarizes Mark’s progress to date against initiatives contained in the 2005–2009 Plan and current plans in place for continued progress in 2006.

#### Mark’s Work Wearhouse

##### Grow sales and revenue

Mark’s continues to focus on growing sales and revenue through implementation of its network development program, expansion of key product categories, and taking advantage of synergies available in the existing Canadian Tire network.

Mark’s will continue network development through opening new stores, relocating or expanding existing locations and renovating older stores to the new Mark’s format.

At the end of 2005, Mark’s total store count was 334, totaling 2.6 million retail square feet.

In the fourth quarter, Mark’s:

- > opened two new stores, including one combination CTR-Mark’s store;
- > renovated two stores;
- > relocated 14 stores, including one combination CTR-Mark’s store; and
- > closed three stores.

In 2005, Mark’s:

- > opened 11 new stores, including two combination CTR-Mark’s stores;
- > renovated eight stores;
- > relocated 26 stores (including three combination CTR/Mark’s stores); and
- > closed 10 stores, four of which were closed as part of the Work World conversion program.

# Management's Discussion and Analysis

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<b>Expand category growth</b>	<p>Mark's will continue to expand key categories.</p> <p>Mark's has continued to expand its women's wear, business-to-business and health care apparel categories. Corporate store sales increased in 2005 in all three of these high-potential categories, exceeding Mark's target of 15 percent growth.</p>
<b>Utilize existing synergies</b>	<p>Mark's has continued to identify ways to take advantage of synergies with other Canadian Tire business units by opening combination CTR-Mark's stores. At the end of 2005, there were a total of 11 combination stores in the network.</p> <p><b>Plans for 2006 and beyond</b></p> <p>Mark's plans to continue expanding its network of stores from 334 at the end of 2005 to between 395 and 400 stores by the end of 2009. Mark's also plans to expand, renovate or retrofit 20 percent to 30 percent of Mark's Work Wearhouse corporate stores over the 2005-2009 Plan period to ensure that they have a consistent appearance and provide support for the execution of effective marketing and merchandising programs, which are desired to enhance Mark's strong brand.</p>
<b>Improve earnings</b>	<p>Mark's has continued to focus on improving margins through global sourcing and effective inventory management and, as a result, saw margin improvement in 2005. The full year gross margin improved to 43.3 percent in 2005 from 42.1 percent for the same period last year.</p> <p><b>Plans for 2006 and beyond</b></p> <p>Mark's plans to expand the men's and women's dress wear and work wear for the health care and hospitality businesses categories over the Strategic Plan period. In addition, Imagewear, Mark's growing business-to-business collection of work apparel, is a category that is also planned for expansion.</p> <p>Mark's has targeted an average annual growth rate of four percent to six percent for same store sales and an eight percent average annual growth rate for total retail sales over the Plan period.</p>
<b>Develop enhanced consumer awareness of the Mark's brand</b>	<p>Mark's has continued to focus on category initiatives and marketing of "Clothes That Work".</p> <p>In the fourth quarter:</p> <ul style="list-style-type: none"><li>&gt; total retail sales increased 19.3 percent; and</li><li>&gt; same store sales increased 17.4 percent.</li></ul> <p>In 2005:</p> <ul style="list-style-type: none"><li>&gt; total retail sales increased 20.3 percent; and</li><li>&gt; same store sales increased 17.4 percent.</li></ul> <p><b>Plans for 2006 and beyond</b></p> <p>Mark's Plan entails a strong focus on making Mark's Work Wearhouse a national brand that people recognize and value for serving all of their everyday clothing needs.</p>

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## 5.2.2.8 Business risks

Mark's is exposed to a number of risks in the normal course of its business that have the potential to affect its operating performance. The following are some of the business risks specific to Mark's retail and other operations. Please also refer to Section 9 of this MD&A for a discussion of some other industry-wide and company-wide risks affecting us.

**Seasonality risk** Mark's business remains very seasonal, with the fourth quarter typically producing a disproportionate share of sales and profits. In 2005, for example, the fourth quarter produced about 40 percent of total annual retail sales and approximately 65 percent of the annual profits. This results from the general increase in consumer spending in that quarter for winter clothing and Christmas-related purchases. Detailed sales reporting and merchandise planning modules assist Mark's in mitigating the risk and uncertainty associated with unseasonable weather and consumer sentiment during the important Christmas selling season, but cannot remove it completely, as inventory orders, especially for a significant portion of merchandise purchased offshore, must be placed well ahead of the season.

**Market obsolescence risk** All clothing retailers are exposed, to varying degrees, to the vagaries of consumers' fashion preferences. Mark's mitigates this risk through its brand positioning, consumer preference monitoring, demand forecasting and merchandise selection efforts. Mark's specifically targets consumers of durable everyday wear and is arguably less exposed to changing fashions than apparel retailers targeting high end fashion wear and accessories.

### 5.2.3 Canadian Tire Petroleum

#### 5.2.3.1 2001–2005 Strategic Plan performance

The following outlines Petroleum's final results on the initiatives contained in our 2001–2005 Strategic Plan.

#### Canadian Tire Petroleum

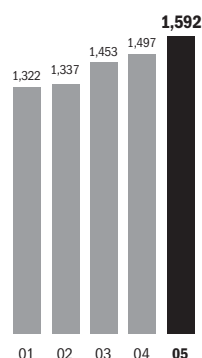
Initiative	What was planned	2001–2005 What was delivered
<b>Network expansion/re-branding</b>	Pursue and accelerate unexploited growth and profit opportunities by opening new sites and re-branding competitor sites.	During the Strategic Plan period, Petroleum took advantage of opportunities to extend the network by opening new sites and re-branding certain competitor sites. At the end of 2005, there were a total of 39 re-branded sites in the Petroleum network.  In total, Petroleum grew its network of gas bar locations from 206 at the end of 2000 to 259 at the end of 2005.
<b>Growth of gasoline sales volume (litres)</b>	Focus on the goal of increasing gasoline sales volume through the Canadian Tire 'Money' loyalty program and other promotions.  Specific targets included an increase in gasoline sales volume to over 2.2 billion litres in 2005.	Petroleum's total sales volume reached 1.6 billion litres in 2005, realizing an increase of 6.4 percent in sales volume over the previous year.  Total sales volumes at the end of the strategic period were lower than planned due to market conditions and a lower number of sites than originally planned at the end of the Plan period.
<b>Non-gas business growth – convenience stores</b>	Increase the on-site presence of convenience stores in order to leverage the high customer traffic at Petroleum's gas bars and provide one-stop shopping for customers.  Develop new business opportunities by launching the Q convenience concept.	Petroleum expanded their network of convenience stores to a total of 247 at the end of 2005. Convenience stores at the gas bars are now larger, on average, and offer a broader assortment of convenience items.  After the successful pilot of the Q store concept, with two locations in operation at the end of 2005, Petroleum intends to open an additional store in 2006 in the Toronto urban market.
<b>Non-gas business growth – car washes</b>	Increase convenience to customers and create another incentive to purchase gas at Canadian Tire, while increasing Petroleum's overall margins.	Car wash sales grew 26.3 percent in 2005, continuing a trend of growing sales over the Strategic Plan period as more locations were built and added to the car wash network.  At the end of 2005, there were 67 car washes at select Petroleum sites.



# Management's Discussion and Analysis

Gasoline pump prices and margins remain volatile due to global supply and competitive retail conditions. As part of a number of initiatives to improve profitability in 2005, Petroleum implemented changes to the financial terms of the existing agency agreement between Petroleum and the agents who operate the Petroleum sites, which is expected to have a positive impact on Petroleum's future profitability.

## Petroleum's gasoline sales volume (millions of litres)



### 5.2.3.2 Key performance indicators

Gasoline sales volume is a key top-line performance indicator for Petroleum, as measured by the number of gasoline litres sold. On average, Petroleum sells approximately twice as much gasoline per site as the industry average. The following are the main factors that contribute to Petroleum's gasoline sales volume:

- > the attractiveness of the Canadian Tire 'Money' loyalty program;
- > the success of cross-merchandising programs with Canadian Tire stores; and
- > strong customer service.

Wholesale and retail prices of gasoline are two other key factors that have a significant impact on Petroleum's earnings. From period to period, however, wholesale and retail gasoline prices can fluctuate widely and are, therefore, difficult to predict.

### Gasoline sales volume

	Q4 2005	Q4 2004	Change	2005	2004	Change
Sales volume (millions of litres)	<b>396.3</b>	389.0	1.9%	<b>1,592.3</b>	1,496.7	6.4%

**Gasoline volume gains supported by new site openings** The cumulative effect of Petroleum's expansion plan over the past year, including the re-branding of a number of competitors' sites and a strong response to our customer loyalty program, contributed to the increase in total gasoline sales volume in 2005. For the full year, gasoline volume increased 6.4 percent, while sales volume at comparable sites increased by 2.5 percent. The fourth quarter experienced a slowdown, however, with total volume increasing only 1.9 percent and comparable site sales declining by 1.7 percent.

### 5.2.3.3 Petroleum's financial results

(\$ in millions)	Q4 2005	Q4 2004	Change	2005	2004	Change
Retail sales	\$ <b>367.5</b>	\$ 315.7	16.4%	\$ <b>1,444.2</b>	\$ 1,208.2	19.5%
Gross operating revenue	<b>339.3</b>	289.2	17.3%	<b>1,330.1</b>	1,105.9	20.3%
EBITDA <sup>1</sup>	<b>7.0</b>	6.0	16.7%	<b>21.9</b>	16.4	33.8%
Earnings before income taxes	<b>3.0</b>	2.5	22.5%	<b>7.5</b>	3.4	118.9%
Less adjustment for:						
Gain/(loss) on disposals of property and equipment	<b>(0.2)</b>	(0.1)		<b>0.1</b>	(0.7)	
Adjusted earnings before income taxes <sup>1</sup>	\$ <b>3.2</b>	\$ 2.6	23.6%	\$ <b>7.4</b>	\$ 4.1	77.2%

<sup>1</sup> See section 12 on non-GAAP measures.

### 5.2.3.4 Explanation of Petroleum's financial results

**Increase in gross operating revenue due to higher gasoline prices and non-gas sales** The following factors were the main contributors to Petroleum's increase in gross operating revenue in the period:

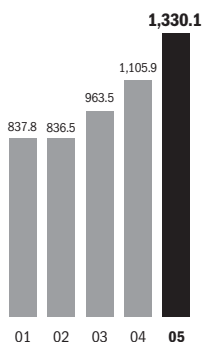
- > higher gasoline prices at the pump;
- > higher sales volume; and
- > increases in sales from our convenience stores and car washes.

#### Gasoline pricing

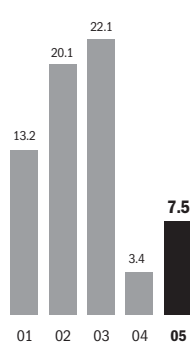
*Petroleum buys gasoline at wholesale prices and sells the gasoline at retail prices that are competitive in the geographic area of each Petroleum site. Higher retail pump prices across Canada in 2005 had a negative effect on gasoline sales volume throughout the industry. The higher pump prices in the latter part of the year, also had a dampening effect on non-gas sales.*

Petroleum's continued focus on increasing its non-gasoline sales resulted in a 14.7 percent increase in convenience store sales for the quarter and a 12.7 percent increase for the full year. Car wash sales climbed 27.9 percent in the fourth quarter and 26.3 percent over the prior full year.

**Petroleum's gross operating revenue**  
(\$ millions)



**Petroleum's earnings before income taxes**  
(\$ millions)



#### **Stronger fourth quarter pre-tax earnings due to improved gas margins and non-gas sales**

After a period of margin volatility and weakness, caused by global supply and demand conditions and intense price competition in the industry, margins strengthened in the fourth quarter over the third quarter of 2005 and helped to improve the full year margin, on a cents per litre and total dollar basis. This was partially offset by higher operating costs necessary to support the network expansion program over the past year. In addition, Petroleum incurred environmental monitoring and clean up costs during the year of approximately \$3.8 million, an increase of \$1.2 million over the prior year.

### 5.2.3.5 Business trends

Canada's petroleum market is mature and exhibiting modest growth, but margins can be unpredictable because of the volatility of wholesale and retail gasoline prices. Within this market, gasoline retailers are evolving in response to changing lifestyles such as Canadians spending more time in their cars and valuing greater convenience. Growth prospects within the market are being shaped by the development of other services that generate higher margins, such as car washes, and convenience stores that leverage gas bar real estate and customer visits. Key drivers of success in this market are perceptions of value, convenience and trust, providing an advantage to chains with well-known brands.

# Management's Discussion and Analysis

## 5.2.3.6 2005–2009 Strategic Plan Outlook

Our 2005–2009 Plan consists of the following initiatives that represent a commitment to significant investment and will have a major impact on the delivery of our strategy to our customers and on our financial Outlook:

Initiative	Strategy	Key points
<b>Grow sales and revenue</b>	Pursue and accelerate unexploited growth and profit opportunities by opening new sites and re-branding competitor sites.	<p>Network expansion to include:</p> <ul style="list-style-type: none"> <li>&gt; 25–35 new-to-industry gas bars by the end of 2009; and</li> <li>&gt; 25–35 new car wash locations by the end of 2009.</li> </ul> <p>Site retrofits to include:</p> <ul style="list-style-type: none"> <li>&gt; an increase in gas bars to approximately 290 locations by the end of 2009.</li> </ul>
	As a result of new site openings, increase higher margin growth opportunities for non-gas sales.	<p>Non-gas operations are targeted to represent approximately 30 percent of network business by 2009. This will result in:</p> <ul style="list-style-type: none"> <li>&gt; increased ancillary margins;</li> <li>&gt; reduction in reliance on gasoline margins;</li> <li>&gt; an increase in car wash locations to approximately 90 locations by the end of 2009; and</li> </ul>
	Continue to take advantage of and promote loyalty and cross-promotion programs.	<ul style="list-style-type: none"> <li>&gt; a new “Gas Advantage” card (a Financial Services product), piloted in 2005, to be launched in Ontario in the first quarter of 2006.</li> </ul>
<b>Improve earnings</b>	Implement a thorough business model review to target areas where earnings and margins can be improved.	Operating costs are monitored and controlled. Petroleum will continue to look for ways to drive costs out of its operations.
<b>Embed Customers for Life culture</b>	Implement a customer feedback database which will allow customers’ key concerns and ideas to be addressed, culminating in repeat traffic and overall customer loyalty to Canadian Tire.	Increasing customer loyalty will contribute to increased volume, stronger margins and additional cross-selling opportunities.

### 5.2.3.7 Strategic initiative status

The following summarizes Petroleum's progress to date against initiatives contained in the 2005–2009 Strategic Plan and current plans in place for continued progress in 2006.

#### Canadian Tire Petroleum

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##### Network expansion

Petroleum continued to expand its network by re-branding and opening new gas bars in 2005.

In the fourth quarter, Petroleum:

- > added three incremental gas bars; and
- > re-branded three competitor gas bars.

In 2005, Petroleum:

- > added six incremental gas bars, two of which had adjacent Q stores;
- > replaced three gas bars;
- > re-branded three competitor gas bars; and
- > closed three gas bars.

At the end of 2005, Petroleum had 259 gas bars, including 39 re-branded gas bars.

##### Plans for 2006

Petroleum plans to expand the network in 2006 by opening a minimum of three new gas bars and by continuing the successful re-branding program, described in more detail below.

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##### Re-branding

Petroleum's program to re-brand competitors' petroleum sites to the Canadian Tire brand continued to deliver strong sales performance. In addition to the benefits of higher sales and earnings, re-branding is an effective way for Canadian Tire to increase market presence in gasoline retailing with less capital investment than is required to build new sites.

##### Re-branding business model

The re-branding program provides benefits to Canadian Tire and the re-branding partner. In most cases, we incur the relatively low cost of converting the gas bar and convenience store to the Canadian Tire brand, while our re-branding partner participates in the profits of the converted site.

To date, 39 competitor petroleum sites have been re-branded to Canadian Tire sites, of which three sites were re-branded in 2005.

##### Plans for 2006

Petroleum plans to re-brand approximately 10 additional sites in 2006 and develop new re-branding partnerships.

Although the re-branding program is considered a success to date, a limited number of competitive sites are available for future re-branding.

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##### Non-gas business growth

Convenience stores and car washes leverage the high customer traffic at Petroleum's gas bars and provide one-stop shopping for busy customers. Increasing convenience store and car wash sales also enhances gross margin and reduces the impact of gasoline margin volatility on Petroleum's earnings. By the end of 2005, there were 247 convenience stores and kiosks and 67 car washes in the Petroleum network.

##### Convenience stores

Three main initiatives are underway to grow sales at convenience stores:

- > adding new convenience stores;
- > expanding and renovating existing stores; and
- > building Q convenience stores.

Petroleum has expanded its non-gas business through adding convenience stores to existing Petroleum gas bar locations as well as newly re-branded sites. In 2005, Petroleum added eight convenience stores, five of which were added in the fourth quarter.

# Management's Discussion and Analysis

Expanding and renovating existing convenience stores has been ongoing for several years. Convenience stores at our gas bars are now larger and offer a broader assortment of convenience items.

Petroleum's new Q premium convenience centres are co-located with other leading retailers in the same building, to add value and convenience for customers. Our first two test stores opened in early 2005 and are co-located with Starbucks coffee shops, Sobey's Express and a restaurant. The combined retail space is more than 10,000 square feet. Results of the test phase will determine the full potential of this initiative.

Convenience store sales rose 12.7 percent in 2005. The table below shows details of Petroleum's convenience store sales increases in 2004 and 2005.

(percent increase over prior period)	Q4 2005	Q4 2004	2005	2004
Total convenience sales	14.7%	14.2%	12.7%	21.6%

#### Plans for 2006

Petroleum plans to add a minimum of three new convenience stores in 2006 (excluding re-branded sites), including an additional Q premium convenience store. Convenience store sales are targeted to grow by approximately 10 percent in 2006, including the expected sales contribution from re-branded convenience stores.

#### Car wash sales

Car washes offer added convenience to customers and create another incentive to purchase gas at Canadian Tire, while increasing Petroleum's overall margins.

Petroleum added two car washes in the fourth quarter and 10 car washes for the full year of 2005.

Car wash sales increased 26.3 percent in 2005. The table below shows Petroleum's car wash sales increases in 2004 and 2005.

(percent increase over prior period)	Q4 2005	Q4 2004	2005	2004
Total car wash sales	27.9%	1.1%	26.3%	20.5%

#### Plans for 2006

Petroleum plans to add 5 to 10 car washes in 2006, excluding re-branded sites.

#### 5.2.3.8 Business risks

Petroleum is exposed to a number of risks in the normal course of its business that have the potential to affect its operating performance. The following are some of the business risks specific to Petroleum's operations. Please also refer to Section 9 of this MD&A for a discussion of some other industry-wide and company-wide risks affecting us.

**Commodity price risk** The operating performance of petroleum retailers can be affected by the fluctuations of the commodity cost of oil. The wholesale price of gasoline is subject to global oil price supply and demand conditions, which are increasingly a function of rising demand from fast-developing countries such as India and China, political instability in the Middle East, potential supply chain disruptions from natural disasters and commodity speculation. To mitigate this risk to profitability, Petroleum tightly controls its operating costs and enters into long-term contractual purchase arrangements with integrated gasoline wholesalers. Petroleum recently signed a long-term contract with a major supplier to secure its supply of gasoline.

**Environmental risk** Environmental risk within Petroleum is primarily associated with the handling of gasoline, oil and propane. Environmental contamination, if not controlled and addressed, can result in fines, significant cleanup costs and/or sanctions and can be damaging to our reputation. Petroleum mitigates this risk through complying with all environmental laws and carrying out site environmental investigations, as required, and remediating any matters requiring action on a timely basis. In addition, Petroleum has environmental insurance coverage in effect.



#### 5.2.4 Canadian Tire Financial Services

The strategic plans, key performance indicators, financial results, business trends and risks of the Financial Services segment also include those of Canadian Tire Bank, a wholly-owned subsidiary of Financial Services.

##### 5.2.4.1 2001–2005 Strategic Plan performance

The following outlines Financial Services' final results on the initiatives contained in our 2001–2005 Plan.

#### Canadian Tire Financial Services

Initiative	What was planned	2001–2005 What was delivered
<b>Grow credit card receivables</b>	Grow credit card receivables to \$3.1 billion by 2005 by increasing the average number of accounts with a balance and increasing the average account balance.	Gross credit card receivables were \$3.2 billion at the end of the Strategic Plan period.  The average account balance grew 12.5 percent in 2005 over 2004.
<b>Increase revenues from insurance premiums and warranty products</b>	As part of the initiative to include additional products in Financial Services' portfolio, a focus was placed on increasing revenues from insurance premiums and warranty products.	In 2005, revenue from insurance and warranty products increased 7.9 percent over 2004.
<b>Develop personal financial services</b>	Expanding on the success of our pilot program to test personal loans, Financial Services targeted to generate personal loan receivables of up to \$200 million in 2005.	Gross personal loans were \$221 million at the end of the 2001–2005 Strategic Plan period.
<b>Reduce operating expense ratio<sup>1</sup></b>	Operating expense reduction has been a key component of our Strategic Plan and measures are in place to monitor expenses on an ongoing basis.	As a result of tight controls on operating expenses during the quarter and full year, operating expenses, as a percentage of gross average receivables, declined from 9.3 percent in 2004 to 8.4 percent in 2005.
<b>Maintain return on total managed portfolio</b>	Financial Services set the target of achieving a return on the total managed portfolio of between 4.0 percent to 5.0 percent.	The return on the total managed portfolio was 4.8 percent for the year ended December 31, 2005.

<sup>1</sup> Operating expenses as a percentage of gross average receivables (GAR)

##### 5.2.4.2 Key performance indicators

The following are key indicators of Financial Services' performance:

- > size of the total managed portfolio;
- > profitability of the portfolio; and
- > quality of the portfolio.

# Management's Discussion and Analysis

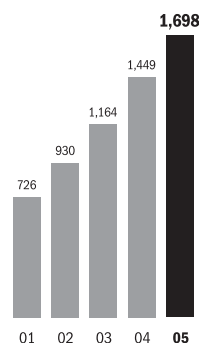
## Total managed portfolio

### Financial Services' total managed portfolio of loans receivable<sup>1</sup>

(\$ in millions except where noted)	Q4 2005	Q4 2004	Change	2005	2004	Change
Average number of accounts with a balance (thousands)	1,826.7	1,772.0	3.1%	1,791.9	1,775.7	0.9%
Average account balance (\$)	\$ 1,776	\$ 1,557	14.1%	\$ 1,698	\$ 1,449	17.2%
Gross average receivables (GAR)	3,244.2	2,758.6	17.6%	3,042.3	2,573.3	18.2%
Total managed portfolio (end of period)				3,395.1	2,881.4	17.8%
Net managed portfolio (end of period)				3,359.1	2,853.2	17.7%

<sup>1</sup> Includes credit card and personal loans receivable.

**Financial Services' average account balance<sup>1</sup>**  
(\$)



<sup>1</sup> Includes credit card and personal loans receivable.

### Net managed portfolio

The net managed portfolio managed by Financial Services is the total value, after allowances, of loans receivable. A significant portion of the loans receivable that Financial Services manages is securitized.

The total managed portfolio of loans receivable, as at the end of the year, grew by 17.8 percent over the prior year end. Canadian Tire's MasterCard receivables grew in the quarter, and for the year, due to increases in average account balances and an increase in the number of accounts carrying a balance. The personal loan product, which was initially tested in the third quarter of 2004 and expanded during the first and second quarters of this year, also contributed to the total portfolio growth. Gross receivables from personal loans were \$221.1 million at the end of the year or approximately 6.5 percent of total managed receivables.

### Securitization of receivables

Securitization is a term that refers to the process by which financial assets are sold to a third party. At Financial Services, both credit card and personal loan receivables are routinely financed by selling an interest in the assets to trusts involved in the business of handling receivables portfolios. In the case of credit card receivables, a co-ownership interest is sold to Glacier Credit Card Trust. For personal loans, the loans are sold to a third party trust for consideration that includes cash and a retained interest in the assets. We record these transactions as a sale, and as a result, these assets are not included on our Consolidated Balance Sheets.

## Gross average receivables (GAR)

GAR is calculated as the monthly average of Financial Services' loans receivable averaged over a specified period of time.

## Financial Services' profitability

Financial Services' profitability measures are tracked as a percentage of gross average receivables, shown in the table below.

### Profitability of total managed portfolio<sup>1</sup>

	2005	2004	2003
Total revenue as a % of GAR <sup>2</sup>	25.47%	26.76%	27.12%
Gross margin as a % of GAR <sup>2</sup>	13.14%	14.18%	15.09%
Operating expenses as a % of GAR <sup>2</sup>	8.37%	9.29%	10.28%
Return on average total managed portfolio <sup>2,3</sup>	4.77%	4.89%	4.81%

<sup>1</sup> Figures are calculated on a rolling 12-month basis and include the total managed portfolio of loans receivable.

<sup>2</sup> Excludes gain on sales of loans receivable.

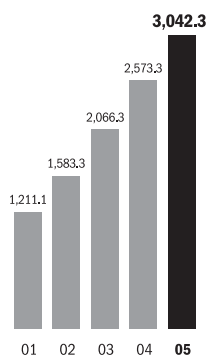
<sup>3</sup> Return is calculated as earnings before taxes as a percentage of GAR.

Financial Services' total revenue and gross margin as a percentage of gross average receivables are expected to continue to decline with the introduction of lower priced credit cards and personal loans. We expect that the lower gross margin rate will be largely offset through continued reductions in our operating expense ratio. In 2006, Financial Services plans to maintain the pre-tax return on its total managed portfolio in the target range of 4.5 percent to 5 percent.

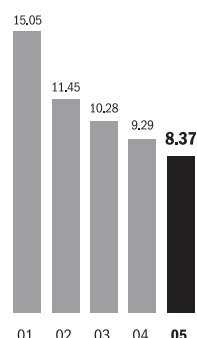
## Portfolio quality

	2005	2004	2003
Net write-off rate (rolling 12-month basis)	5.99%	5.82%	5.90%
Account balances less than 30 days overdue at end of period	96.31%	96.46%	96.45%
Allowance rate	2.52%	2.34%	2.15%

**Financial Services' gross average receivables**  
(\$ millions)



**Financial Services' operating expense ratio**  
(%)



Net write-offs for the total managed portfolio were 5.99 percent on a 12-month rolling basis, an increase of 17 basis points over the 12-month period ending in the fourth quarter of 2004 but still within the targeted range of five percent to six percent. The 18 basis point increase in the portfolio allowance rate reflects the impact of a slight deterioration in portfolio aging and the increase in write-off rates. Periodic fluctuations in write-offs, aging and allowances will occur as a result of a variety of economic influences such as job growth/losses, personal debt levels and personal bankruptcy rates.

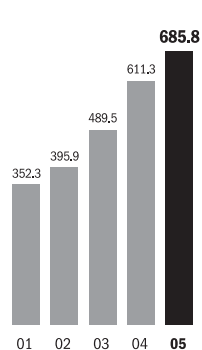
**5.2.4.3 Financial Services' financial results**

(\$ in millions)	Q4 2005	Q4 2004	Change	2005	2004	Change
Gross operating revenue	\$ 190.6	\$ 171.6	11.1%	\$ 685.8	\$ 611.3	12.2%
EBITDA <sup>1</sup>	62.9	52.6	19.5%	191.0	172.0	11.0%
Earnings before income taxes	55.8	46.5	19.8%	165.0	148.5	11.1%
Less adjustment for:						
Gain on sales of loans receivable <sup>2</sup>	13.0	14.2		19.9	22.6	
Adjusted earnings before income taxes <sup>1</sup>	\$ 42.8	\$ 32.3	32.2%	\$ 145.1	\$ 125.9	15.3%

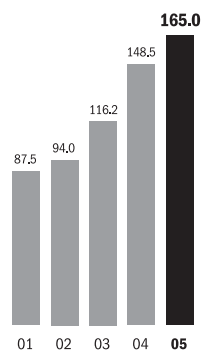
<sup>1</sup> See section 12 on non-GAAP measures.

<sup>2</sup> Includes credit card and personal loans receivable.

**Financial Services' gross operating revenue**  
(\$ millions)



**Financial Services' earnings before income taxes**  
(\$ millions)



**5.2.4.4 Explanation of Financial Services' financial results**

**Gross operating revenue increased due to growth in the total managed portfolio of loans receivable** The 17.6 percent increase in gross average receivables was the major contributor to the growth in Financial Services' revenue during the quarter which was also in line with the 18.2 percent increase in gross average receivables for the year. As expected, fourth quarter revenue growth of 11.1 percent and full year growth of 12.2 percent lagged receivables growth due to the changing mix of the portfolio towards lower rate cards and personal loans. Related growth in ancillary services including creditor insurance and warranty products also contributed to Financial Services' revenue increase in both the quarter and the full year.

**Earnings growth was driven by increased receivables and reduced operating expense ratio** Financial Services' pre-tax earnings increased 19.8 percent in the fourth quarter due to higher revenue and an improvement in the operating expense ratio versus the same quarter of last year. The positive impact of these factors was partially offset by the increase in the write-off and allowance rates and a lower gain on the sales of loans receivable than in the fourth quarter of last year. Excluding the impact of the gain on the sales of loans receivable, pre-tax earnings in the quarter were up 32.2 percent versus the fourth quarter of 2004 and increased 15.3 percent in 2005 versus 2004.

# Management's Discussion and Analysis

## 5.2.4.5 Business trends

The total Canadian bank card market now represents over \$60 billion in outstanding loans and has grown consistently over the past three years, offering an attractive growth opportunity despite intense competition. While Canada's major banks are the market leaders, U.S. based credit card issuers are gaining market share and are redefining customer expectations. With the increasing number of credit cards available, consumers are looking for relationships with organizations that offer strong value, exceptional service and programs that reward them for their loyalty.

## 5.2.4.6 2005–2009 Strategic Plan Outlook

Our 2005–2009 Plan consists of the following initiatives that represent a commitment to significant investment and will have a major impact on the delivery of our strategy to our customers and on our financial Outlook:

Initiative	Strategy	Key points
<b>Increase market share of credit cards</b>	Grow the number of credit card accounts (three percent to four percent per annum).	<p>Financial Services plans to introduce new cards as part of its program to grow the total number of credit card accounts through the following initiatives:</p> <ul style="list-style-type: none"> <li>&gt; premium cards;</li> <li>&gt; low rate cards; and</li> <li>&gt; new loyalty based cards.</li> </ul> <p>To further increase the market share of the credit card portfolio, Financial Services plans to increase average balances to industry norms through the following initiatives:</p> <ul style="list-style-type: none"> <li>&gt; targeted credit limit increases;</li> <li>&gt; balance transfer offers; and</li> <li>&gt; reduced pricing for low risk accounts.</li> </ul>
<b>Expand personal loan business</b>	Expand personal loans to Canadian Tire MasterCard customers.	<p>The following initiatives are planned to further expand the personal loan portfolio:</p> <ul style="list-style-type: none"> <li>&gt; customer acquisition via convenient direct mail and inbound phone call sales channels;</li> <li>&gt; pre-approved offers to qualified customers; and</li> <li>&gt; leverage credit card operating platforms and risk management.</li> </ul> <p>Financial Services plans to grow the personal loan portfolio to over \$240 million by the end of 2006.</p>
<b>Test new financial services</b>	<p>In order to increase its total managed portfolio, Financial Services plans to test the following services for possible rollout to existing and new customers:</p> <ul style="list-style-type: none"> <li>&gt; high-rate savings accounts;</li> <li>&gt; mortgages; and</li> <li>&gt; new warranty and insurance products.</li> </ul>	<p>As part of the plan to test new products, Financial Services will capitalize on the Canadian Tire brand, customer data and new and existing marketing channels to further explore and assess customer acceptance of these products.</p>
<b>Customers for Life</b>	<p>To ensure the continued satisfaction of our customers, we have established a key imperative to reinforce a customer-centric culture across our entire organization. Customers for Life extends beyond store merchandising and marketing programs and encourages all employees to perform in a way that encourages lifelong relationships with our customers. High customer satisfaction levels add long-term value for shareholders and will enable Canadian Tire to stay competitive in the future.</p>	<p>Financial Services plans to continue enhancing our Customers for Life plan through the following initiatives:</p> <ul style="list-style-type: none"> <li>&gt; monthly customer service satisfaction tracking;</li> <li>&gt; "Voice of the Customer" feedback systems;</li> <li>&gt; extensive customer retention training/offers; and</li> <li>&gt; recognition and reward systems for frontline employees.</li> </ul>

#### 5.2.4.7 Strategic initiative status

The following summarizes Financial Services' progress to date against initiatives contained in the 2005–2009 Strategic Plan and current plans in place to continue progress in 2006.

#### Canadian Tire Financial Services

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##### **Increase market share of credit cards**

Credit card receivables are driven by the number of accounts that carry a balance, and by the average balance per account. We believe that increasing the average account balance is Financial Services' most significant opportunity to increase its earnings in the short-term.

Financial Services uses low-cost, in-store acquisition programs to add new accounts, and then uses a variety of marketing methods to encourage cardholders to use their cards, which often results in higher account balances, including:

- > offering low interest rates to customers to transfer credit card balances from other financial institutions; and
- > offering increased credit limits to qualified customers.

Increasing credit card receivables, the number of accounts with balances and average account balances are key performance indicators for Financial Services.

At the end of 2005:

- > the 12 month average credit card account balance was \$1,614, an increase of 12.5 percent from the previous year; and
- > gross average credit card receivables balance was \$2.8 billion, an increase of 12.0 percent from 2004.

##### **Plans for 2006**

Financial Services plans to increase the gross credit card receivables balance to \$3.4 billion by the end of 2006.

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##### **Insurance and warranty products**

Revenues from insurance and warranty products have grown significantly over the last four years. Financial Services plans to continue to increase revenues from related products by attracting new customers and adding additional complementary products.

In 2005 revenue generated from insurance and warranty products increased 7.9 percent over 2004.

Financial Services expects revenues from insurance and warranty products to increase as the credit card portfolio grows.

##### **Plans for 2006**

Financial Services plans to increase revenues on insurance and warranty products by seven percent in 2006.

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##### **Introduction and growth of personal loans**

Financial Services introduced personal loans in 2004 through an initial test offering to qualified Canadian Tire MasterCard customers and further expanded the program in 2005.

At the end of 2005:

- > the 12 month average number of personal loan accounts had increased to approximately 28,500; and
- > gross average personal loan receivables had increased to \$195.3 million compared to \$30.4 million from 2004.

##### **Plans for 2006**

Financial Services plans to increase gross receivables for the personal loan portfolio to over \$240 million by the end of 2006.

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##### **Test new financial products and services**

As a natural extension of its existing products and services, and based on the success of previous test products (i.e. personal loans, insurance and warranty products), Financial Services plans to test new products and services during the Strategic Plan period. These may include:

- > high-rate savings accounts;
- > mortgages; and
- > new warranty and insurance products.

##### **Plans for 2006**

Financial Services plans to test these products and services in the second half of 2006.



# Management's Discussion and Analysis

## 5.2.4.8 Business risks

Financial Services is exposed to a number of risks in the normal course of its business that have the potential to affect its operating performance. The following are some of the business-specific risks to Financial Services' operations. Please also refer to section 9 of this MD&A for a discussion of some other industry-wide and company-wide risks affecting us.

**Consumer credit risk** Canadian Tire, through its financial services business, grants credit to its customers on Canadian Tire MasterCard and retail credit cards and personal loans. With the granting of credit, Financial Services assumes certain risks that include the failure or inability to accurately predict the creditworthiness of its customers or their ability to repay debt. Financial Services minimizes credit risks to maintain and improve the quality of its consumer lending portfolio by:

- > employing sophisticated credit-scoring models to constantly monitor the creditworthiness of customers;
- > using the latest technology to make informed credit decisions for each customer account to limit credit risk exposure;
- > adopting technology to improve the effectiveness of the collection process; and
- > monitoring the macro-economic environment, especially with respect to consumer debt levels, interest rates, employment levels and income levels.

**Securitization funding risk** Financial Services has used securitization as a source of funding over the past several years as a normal part of financing growth in loans receivable. At the end of 2005, Financial Services had securitized 77 percent of its total managed portfolio. Securitization involves the sale of credit card receivables to Glacier Credit Card Trust (GCCT) and the sale of personal loans receivable to a third party trust, and is an important source of funding for Canadian Tire.

**Interest rate risk** The Company's sensitivity to movements in interest rates is substantially limited to its cash and short-term investments, commercial paper and medium term notes. A one percent change in interest rates would not materially affect its earnings, cash flow or financial position.

Most of Financial Services' revenue is not interest rate sensitive as it is generated from the Canadian Tire MasterCard and Canadian Tire retail cards, each of which carries fixed interest rates appropriate to customer groups with common credit ratings. Financial Services' funding requirements were reduced during 2005 primarily by the sale of loans receivable through the securitization program described in section 7 of this MD&A. However, the balance of Financial Services' funding requirements in 2005 was met with the issuance of floating rate debt, which makes the Company's earnings somewhat sensitive to changes in interest rates. Canadian Tire constantly monitors the potential impact of interest rate fluctuations on its fixed versus floating rate exposure, and has managed its overall balance between fixed and floating rate debt to reduce the magnitude of this exposure. As the success of Financial Services is dependent upon its ability to access capital markets at favourable rates, and given the rapid growth of the total managed portfolio, maintaining the quality of the securitized receivables is a key priority of Financial Services.

## 6. New business development

While we believe that we can achieve our financial aspirations by effectively executing our strategic initiatives, we will continue to identify and evaluate domestic opportunities to enhance our growth and profitability beyond 2009. Our business development team is focussed on identifying potential retail and retail-related business opportunities that can leverage our core capabilities and that fit within our existing network of businesses.

New business opportunities may include acquisitions, joint ventures and strategic alliances. Canadian Tire will assess new business opportunities using rigorous operating and financial parameters and defined acquisition criteria, including strategic fit and risk, as well as financial, business and shareholder impact to create a focussed list of opportunities that offer the greatest potential.

## 7. Capital structure and financing

### 7.1 Capital structure

Improving our financial flexibility is one of our long-term goals and one of the imperatives of our new Strategic Plan.

We regularly review our funding plan and capital structure to ensure that we have sufficient funding options to provide us with the financial flexibility to implement the growth initiatives and meet the targets of our Strategic Plan.

We ended 2005 in a strong financial position, with:

- > \$838 million of cash and cash equivalents;
- > no short-term debt;
- > less than 15 percent of our long-term debt due in 2006;
- > long-term debt at less than 32 percent of total capitalization;
- > \$570 million in committed lines of credit;
- > the flexibility to access capital markets to refinance corporate debt at more favourable rates; and
- > over \$2 billion of book value in unencumbered real estate.

For the years indicated, our capital structure was as follows:

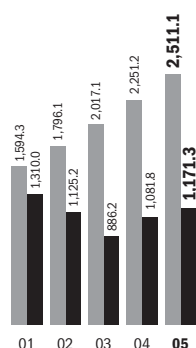
### Capital structure

(composition of total structure)

	2005	2004
Shareholders' equity	57.8%	59.8%
Minority interest	6.9%	8.0%
Long-term debt <sup>1</sup>	31.7%	28.9%
Other long-term liabilities	1.5%	1.5%
Future income taxes	2.1%	1.8%
	100.0%	100.0%

<sup>1</sup> Long-term debt includes current portion.

#### Shareholders' equity and long-term debt (\$ millions)



■ Shareholders' equity  
■ Long-term debt (excludes current portion)

**Equity** The book value of Common and Class A Non-Voting Shares at the end of 2005 was \$30.83 per share compared to \$27.75 at the end of 2004.

We have a policy of purchasing Class A Non-Voting Shares to offset the dilutive effects of shares issued to fulfill our obligations under various employee profit sharing, stock option and share purchase plans and the dividend reinvestment plan. In the long-term, these purchases are expected to offset the issuance of new shares.

On February 9, 2006, we announced our intention to initiate a normal course issuer bid (NCIB) to purchase up to 2.0 million of the issued and outstanding Class A Non-Voting Shares over the 12-month period ending February 18, 2007.

An NCIB is a bid by a listed company to buy back its own shares on a stock exchange, subject to certain rules that protect investors, but without complying with all of the requirements applicable to issuer bids because the bid is made for a number of shares that is below a prescribed threshold. A total of approximately 1.3 million Class A Non-Voting Shares were purchased in 2005 under the previous NCIB.

### Shares outstanding

	2005	2004
<b>Class A Non-Voting Shares (CTR.NV)</b>		
Shares outstanding at beginning of year	77,699,631	77,337,718
Shares issued under plans <sup>1</sup>	1,617,593	1,903,013
Shares purchased under NCIB	(1,284,500)	(1,541,100)
Shares outstanding at end of year	78,032,724	77,699,631
<b>Common Shares (CTR)</b>		
Shares outstanding at beginning and end of year	3,423,366	3,423,366

<sup>1</sup> We issue shares under stock purchase, stock option, dividend reinvestment and various employee profit-sharing plans.

**Dividends** Dividends of \$47.4 million were declared on Common and Class A Non-Voting Shares in 2005 compared with \$40.5 million in 2004. The increase in dividends declared reflected the Board of Directors' decision in February 2005 to increase the annual dividend rate by 16 percent from \$0.50 per share to \$0.58 per share. The first quarterly dividend at the new rate was declared on March 10, 2005 in the amount of \$0.145 per share payable on June 1, 2005 to shareholders of record as of April 29, 2005. On February 9, 2006, the Board of Directors approved a further increase in the annual dividend rate, from \$0.58 per share to \$0.66 per share.

**Short-term debt** We have a program in place that allows us to issue commercial paper up to an authorized limit of \$800 million. We had no commercial paper outstanding at the end of 2005 or 2004.

Credit ratings for our commercial paper are R-1(low) from Dominion Bond Rating Service Limited (DBRS) and A-1(low) from Standard & Poor's (S&P).

At the end of 2005, we had \$570 million in committed lines of credit, unchanged from 2004. None of the committed lines were drawn upon at the end of these periods. In January 2006 we added a \$75 million committed line of credit, bringing the total available to \$645 million in committed lines of credit.

# Management's Discussion and Analysis

**Long-term debt** To allow for timely access to debt markets, we filed a shelf prospectus with provincial and territorial securities commissions on March 14, 2005 for the issuance of up to \$750 million of medium term notes (MTNs). As described below, we issued \$500 million of MTNs in 2005 under the shelf prospectus.

Long-term debt was \$1.38 billion at the end of 2005, which included the current portion of \$204 million, including \$5 million in capital leases. This compared to \$1.09 billion of long-term debt at the end of 2004, including \$8 million in capital leases.

On April 1, 2005, we redeemed \$225 million of MTNs with an annual interest rate of 7.05 percent that were due on May 18, 2006. The early redemption, at a net cost of \$5.3 million, was undertaken due to favourable market conditions and to reduce the amount of debt refinancing that would have otherwise occurred in 2006.

On May 20, 2005, we issued \$300 million of MTNs under the shelf prospectus. The MTNs have an annual interest rate of 4.95 percent and mature on June 1, 2015.

On September 2, 2005, we issued \$200 million of MTNs under the shelf prospectus. The MTNs have an annual interest rate of 5.61 percent and mature on September 4, 2035.

Like most borrowers, we provide covenants to our lenders. We are in compliance with all of these debt covenants.

Our long-term debt is currently rated A (low) by DBRS and BBB+ by S&P.

## 7.2 Funding program

**Funding requirements** We fund our capital expenditures, working capital needs, dividend payments and other financing needs, such as debt repayments and share purchases under the normal course issuer bid, from a combination of sources. In 2005, the primary sources of funding were:

- > \$802 million of cash on hand at the beginning of 2005;
- > \$516 million from increasing long-term debt;
- > \$721 million of cash generated from operations;
- > \$395 million from the securitization of loans receivable; and
- > \$78 million from the sale of property and equipment.

**2005 Capital program** Canadian Tire's 2005 capital expenditures totaled \$391 million, a 14.8 percent increase from the \$341 million spent in 2004.

Our capital investment in 2005 was slightly more than the \$380 million planned and greater than our updated third quarter forecast of \$350-\$370 million.

Capital expenditures during the year included:

- > \$191 million for real estate projects, including \$173 million associated with the roll out of CTR's new-format stores;
- > \$20 million for the expansion of CTR's Calgary, Alberta distribution centre;
- > \$5 million for CTR's CustomerLink program;
- > \$33 million for Mark's;
- > \$29 million for Petroleum gas bars and car washes;
- > \$15 million for Financial Services; and
- > \$98 million for other purposes.

In the fourth quarter of 2005, we invested \$143 million in property and equipment for our various businesses, as follows:

- > \$38 million for real estate projects, including \$35 million associated with the roll out of CTR's new-format stores;
- > \$1 million for the expansion of CTR's Calgary, Alberta distribution centre;
- > \$1 million for CTR's CustomerLink program;
- > \$16 million for Mark's;
- > \$14 million for Petroleum gas bars and car washes;
- > \$7 million for Financial Services; and
- > \$66 million for other purposes.

**Sources of liquidity** We have the following sources from which to fund our 2006 capital program:

- > existing cash reserves;
- > cash flow from operations;
- > \$800 million of authorized commercial paper;
- > \$250 million available in MTNs under our \$750 million shelf prospectus;
- > additional sales of loans receivable; and
- > proceeds from the dispositions of surplus property and equipment.

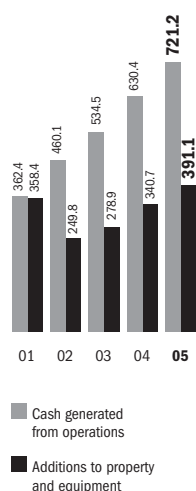
**2006 Capital program** The Company expects to invest approximately \$500 to \$525 million in capital expenditures in 2006. Financial Services expects to securitize approximately \$590 million of loans receivable in 2006. Financial Services' securitization program is discussed in more detail at the end of this section.

**Working capital** As part of our financial flexibility imperative, reducing our working capital continues to be a long-term priority. The table below shows the change in the value of working capital components for the Company at the end of 2005 and 2004.

### Comparable working capital components

(\$ in millions)	2005	2004	Increase/ (decrease) in working capital
Accounts receivable	\$ 652.8	\$ 370.7	\$ 282.1
Merchandise inventories	675.5	620.6	54.9
Prepaid expenses and deposits	42.4	24.1	18.3
Income taxes payable	(71.2)	(44.2)	(27.0)
Accounts payable and other	(1,545.5)	(1,437.6)	(107.9)
			\$ 220.4

### Cash flow versus capital expenditures (\$ millions)



The most significant change in working capital components was an increase in accounts receivable that was partially offset by an increase in accounts payable.

**Accounts receivable** At the end of 2005 accounts receivable totaled \$701 million, of which \$48 million have been sold to independent investors. The remaining \$653 million of accounts receivable were recorded on our 2005 Consolidated Balance Sheet. Of our total \$694 million of accounts receivable at the end of 2004, we had sold \$323 million and reported \$371 million on our 2004 Consolidated Balance Sheet.

The largest portion of accounts receivable was comprised of the monies owed to us from Associate Dealers for merchandise we shipped to them. Of the \$653 million of year-end receivables, Dealer receivables was \$570 million compared to \$543 million a year earlier. The increase in Dealer receivables was a result of increased shipments to the Dealers in the fourth quarter.

**Merchandise inventories** CTR increased its inventory levels by \$60 million or 13.0 percent at the end of 2005 compared to the end of 2004. The increase in value of the products in transit from overseas suppliers was approximately \$9 million at the end of 2005. The balance of the increase in inventory was to prepare for strong promotional activity that CTR is planning in early 2006.

Mark's decreased its inventory levels by \$8.6 million or 5.8 percent at the end of 2005 compared to a year earlier. The decrease was related to the combination of very strong sales in 2005 and a focus on reducing inventory levels from 2004.

**Accounts payable** The increase in accounts payable was primarily comprised of normal trade payables related to the increase in merchandise inventories.

**Cash and cash equivalents** At December 31, 2005, the Company held \$838 million of cash or cash equivalents compared to \$802 million at January 1, 2005.

**Loans receivable** Our loans receivable securitization programs are designed to provide cost-effective, alternative sources of funding for Financial Services.

# Management's Discussion and Analysis

## Net managed loans receivable

(\$ in millions)	2005	2004
Securitized <sup>1</sup>	\$ 2,599.1	\$ 2,209.3
Unsecuritized	760.1	643.9
Net managed loans receivable	\$ 3,359.2	\$ 2,853.2

<sup>1</sup> Net of seller's interest in personal loan securitization in 2005 of \$29.1 million (2004 - nil).

Net managed loans receivable continued to increase in 2005 as customers' use of the Canadian Tire MasterCard and participation in personal loans grew. At the end of 2005, net managed loans receivable were 17.7 percent higher than at the end of 2004.

Canadian Tire Bank (CTB) transfers co-ownership interests in credit card receivables to Glacier Credit Card Trust (GCCT). In 2005, CTB also sold a portion of its personal loan portfolio to a third party trust. CTB continues to service both credit card and personal loan receivables. The Company does not have a controlling interest in GCCT or the third party trust, so we do not include the financial results of either in our Consolidated Financial Statements.

Following the provisions of the Canadian Institute of Chartered Accountants' (CICA)'s Accounting Guideline 12 (AcG-12), "Transfers of Receivables", which came into effect on July 1, 2001, we record the transfers of co-ownership interests in credit card receivables to GCCT as sales. The proceeds of the sales are deemed to be the cash we receive, plus the estimated fair value of our portion of the service charges that will be paid on the receivables, less our servicing liability. We estimate fair value by discounting our expected future cash flows from the receivables sold. We record a gain or loss on the date of the sale in the amount that the estimated fair value of the proceeds we receive differs from the carrying value of our ownership share in receivables sold. We record gains or losses from sales made before July 1, 2001 when we receive the service charges. As at December 31, 2005, all receivables sold are accounted for under AcG-12.

The securitization of personal loans operates and is accounted for in similar, though not identical fashion as the credit card securitizations. Please see note 2 to the Consolidated Financial Statements found in this Annual Report.

In 2005, we recognized a pre-tax gain of \$19.9 million (2004 - \$22.6 million gain) on such securitization transactions.

## Cash flows from loan securitizations

(\$ in millions)	Q4 2005	Q4 2004	2005	2004
Proceeds from new securitizations	\$ 541.1	\$ 625.0	\$ 541.1	\$ 625.0
Proceeds from collections reinvested in previous securitizations	1,754.1	1,512.1	6,723.0	5,601.0
Other cash flows received on retained interest	424.1	398.4	1,286.7	1,335.3

We expect the growth in the number and average balances of Canadian Tire MasterCards to lead to an increase in total credit card receivables in 2006. Financial Services expects to fund most of this increase from the sale of credit card receivables to GCCT.

The success of the securitization program is mainly due to GCCT's ability to obtain funds from third parties by issuing debt instruments with high credit ratings. As of December 2005, GCCT had the following ratings:

- > a rating of R-1(high) from DBRS for the asset-backed commercial paper program;
- > ratings of AAA by DBRS and S&P for the asset-backed senior notes; and
- > ratings of A from DBRS and A from S&P for the asset-backed subordinated notes.

We expect the personal loan portfolio to increase due to growth in the number of accounts. Financial Services expects to fund this increase from the sale of personal loans to other third party trusts.

The Canada Trust Company is the trustee and custodian for GCCT, manages the co-ownership interests and acts as agent for, and on behalf of, Canadian Tire Bank and GCCT, as the owners of the co-ownership interests. BNY Trust Company of Canada acts as indenture trustee with respect to GCCT and manages the security interests of the holders of the senior and subordinated notes. We are currently not aware of any events, commitments, trends or uncertainties that may have a negative impact on our arrangement with GCCT.



The table below lists the details of the outstanding asset-based notes issued by GCCT.

#### Glacier Credit Card Trust asset-backed notes outstanding

(\$ in millions)	At December 31, 2005	At January 1, 2005	Repayment of principal begins	Estimated final dates for payment
Series 1997-1 Commercial Paper Notes <sup>1</sup>	\$ 75	\$ 90		
6.665% Series 2000-1 Senior Notes <sup>2</sup>	-	200	Nov. 22, 2004	fully repaid
6.163% Series 2001-1 Senior Notes <sup>2</sup>	300	300	Apr. 1, 2006	July 21, 2006
4.82% Series 2002-1 Senior Notes <sup>2</sup>	450	450	Sep. 1, 2007	Dec. 20, 2007
4.444% Series 2003-1 Senior Notes <sup>2</sup>	542	542	Aug. 1, 2008	Nov. 20, 2008
4.274% Series 2004-1 Senior Notes <sup>2</sup>	591	591	Aug. 1, 2009	Nov. 20, 2009
4.187% Series 2005-1 Senior Notes <sup>2</sup>	345	-	Aug. 1, 2010	Nov. 19, 2010
Floating Rate Series 2000-1 Subordinated Notes <sup>3,4</sup>	-	4		
7.203% Series 2001-1 Subordinated Notes <sup>3</sup>	15	15		
5.88% Series 2002-1 Subordinated Notes <sup>3</sup>	23	23		
5.034% Series 2003-1 Subordinated Notes <sup>3</sup>	28	28		
4.674% Series 2004-1 Subordinated Notes <sup>3</sup>	34	34		
4.507% Series 2005-1 Subordinated Notes <sup>3</sup>	20	-		
<b>Total</b>	<b>\$ 2,423</b>	<b>\$ 2,277</b>		

<sup>1</sup> Commercial paper notes mature on a business day within one year of the date of issue.

<sup>2</sup> Repayment of principal begins from allocations to GCCT in the previous month. In some instances, earlier prepayment may be required. Final payment dates are estimated based on assumptions about the performance of the credit card receivables and other factors.

<sup>3</sup> Repayment of principal for subordinated notes begins after all principal owing under the related series of senior notes has been repaid in full.

<sup>4</sup> Interest on the Series 2000-1 Subordinated Notes is payable at the rate of Bankers' Acceptances plus 1.25 percent.

**Sale and leaseback of distribution centres** Subsequent to year end, on January 31, 2006, we closed the sale and leaseback of two distribution centres, located in Brampton, Ontario and Calgary, Alberta, to a third party for total proceeds of \$229 million. These proceeds will be used to fund strategic initiatives outlined in our 2005-2009 Strategic Plan.

### 7.3 Financial ratios

We have ready access to funding from the financial markets because of our relatively strong balance sheet and healthy financial ratios.

We have a long-standing policy of keeping our ratio of long-term debt to total capitalization below 50 percent. The actual ratio, while below 50 percent, was higher at the end of 2005 than it was a year earlier mainly because there was an increase of \$288.2 million in long-term debt, partially offset by an increase of \$265.7 million in retained earnings.

The following table shows the changes in financial ratios over the past year.

	At December 31, 2005	At January 1, 2005
Ratio of long-term debt to total capitalization <sup>1</sup>	31.7%	28.9%
Ratio of current assets to current liabilities	1.6:1	1.6:1
Interest coverage <sup>2</sup>	7.3 times	6.9 times

<sup>1</sup> Long-term debt includes current portion.

<sup>2</sup> We calculate interest coverage on a rolling 12-month basis using earnings before interest, income taxes and minority interest.

### 7.4 Funding costs

The table below shows total funding costs, not including those of GCCT. The figures include the impact of interest rate swaps, which are part of our interest rate risk management program.

#### Interest expense<sup>1</sup>

(\$ in millions)	2005	2004
Long-term interest expense	\$ 79.5	\$ 76.0
Short-term interest expense	4.6	2.4
<b>Total</b>	<b>\$ 84.1</b>	<b>\$ 78.4</b>
Effective blended cost of debt	6.8%	6.4%

<sup>1</sup> Interest expense is increased or decreased by the interest rate differentials paid or received on interest rate swap contracts.

# Management's Discussion and Analysis

The effective average blended cost of debt was higher in 2005 due to the net redemption premium of \$5.3 million paid on the early redemption of \$225 million, 7.05 percent May 2006 MTNs.

## **8. Off-balance sheet arrangements**

We had the following off-balance sheet arrangements at the end of 2005:

### **8.1 Glacier Credit Card Trust**

As previously described in section 7.2 of this MD&A, GCCT was formed to buy our credit card receivables, and issues debt instruments to third party investors to fund its credit card receivables purchases.

### **8.2 Personal loan securitization**

As previously described in section 7.2 of this MD&A, we sold a portion of our personal loans portfolio to a third party trust.

### **8.3 Trust financing for Associate Dealers**

A financing program has been established to provide an efficient and cost-effective way for Associate Dealers to access the majority of the financing they require for their store operations, with specified support from us as described below.

**Trust** In 1995, a major Canadian bank set up a trust (the Trust) to provide financing to retail franchisees, and in 1997, began providing loans to Associate Dealers to help them buy core-level inventory and fixed assets. Each of these loans is secured by the assets of the applicable Associate Dealer. The loans totaled \$784 million at December 31, 2005, compared to \$794 million at January 1, 2005. In addition, Dealers use their own equity, as well as subordinated operating lines of credit from Canadian banks, to manage seasonal fluctuations in inventory levels and meet other regular business needs. We do not normally loan money directly to Associate Dealers, but we have done so on rare occasions.

**Co-owner trusts** In the fourth quarter of 2004, the Trust sold all of its rights in the Associate Dealer loans to independent trusts (the Co-owner Trusts) that were set up by major Canadian banks. The Trust continues to advance new loans to Associate Dealers that are immediately sold to the co-owner trusts. The Co-owner Trusts raise funds in the capital markets to fund their initial and ongoing purchases of loans from the Trust.

Each bank administers its Co-owner Trust, provides it with a liquidity line, and in one case is a counterparty to the Co-owner Trusts in interest rate swaps. The interest rate swaps are used to effectively convert the interest payments the Co-owner Trusts receive from Associate Dealers on fixed-rate loans into variable rate interest payments to match the Co-owner Trusts' variable rate debt raised in the capital markets.

Major Canadian trust companies are the trustees of the Co-owner Trusts and are accountable for the interests of the third party beneficiaries.

Most of our Associate Dealers participate in this program, and have individual loan agreements that are ultimately with the Co-owner Trusts.

**Program support** We provide support to this financing program in two ways:

- > we provide credit enhancement in the form of guarantees of standby letters of credit provided by several banks;
- > we indemnify the Co-owner Trusts and certain other parties they deal with against certain events, such as changes in laws and regulations (including tax legislation), and shortfalls in certain payments owed by the Trust. The terms of these indemnification agreements do not put a limit on our total potential liability. To date, we have made only a nominal payment under these indemnifications, and we have not accrued any amount for these indemnifications in our 2005 Consolidated Financial Statements;
- > we have also provided a waiver to the Trust of certain statutory rights that we have with respect to the Associate Dealers as landlord and merchandise supplier; and
- > we indemnify the interest rate swap counterparty for amounts owing to the counterparty which the Trust cannot collect from an Associate Dealer who has a fixed rate loan.

As consideration for this support, the Co-owner Trusts pay us a program support amount after they have paid all expenses, but before any distribution to their beneficiaries. The amount we receive from the Co-owner Trusts depends on how much the Associate Dealers borrow from them and the prevailing market interest rates.

We also pay fees to the banks that provide the letters of credit. The following table summarizes the program support amounts received and letters of credit fees paid.

(\$ in millions)	Q4 2005	Q4 2004	2005	2004
Program support amount received (net)	\$ 2.6	\$ 2.4	\$ 9.8	\$ 9.3
Letters of credit fees paid	0.2	0.2	0.6	0.9

Our guarantees of the standby letters of credit provided as credit enhancement by banks totaled \$117 million at December 31, 2005 compared to \$134 million at January 1, 2005. The letters of credit benefit the Co-owner Trusts by helping them achieve a high credit rating on the debt they issue to fund their initial and ongoing purchases of the Associate Dealer loans from the Trust.

The amount of credit enhancement required is based on a defined formula that considers the value of the assets of the participating Associate Dealers, and will increase if the value of the Associate Dealers' assets goes down or the Associate Dealers increase the amount they borrow through this financing program.

No amount has ever been drawn on the letters of credit. The Co-owner Trusts can, however, draw on the letters of credit in various situations, including the following:

- > if an Associate Dealer defaults on a loan held by the Co-owner Trusts. If we choose not to buy the defaulted loan, the Co-owner Trusts can draw on the letters of credit for the loan amount (including any unpaid interest and costs) and then must assign the Associate Dealer's loan agreement and related security documentation to us;
- > to cover shortfalls in related fees and expenses owing to them;
- > if we do not provide sufficient credit enhancement. In this situation, the Co-owner Trusts can fully draw on the letters of credit, and realize on the loans' underlying security; and
- > upon termination of the program.

We must reimburse the banks for any amounts the Co-owner Trusts draw from the letters of credit.

**Terminating the arrangement** The Company, the Trust and the Co-owner Trusts cannot unilaterally terminate this financing program before December 2007, and, after that date, anyone deciding to terminate participation in the program must provide six months written notice to the other parties.

The arrangement will automatically be terminated if:

- > we become insolvent;
- > we do not meet our obligations to provide sufficient credit enhancement or indemnify against certain events; and
- > the Co-owner Trusts' debt rating goes down significantly.

If the arrangement is terminated, the Associate Dealers will need to replace the loans with alternative financing. We are under no contractual obligation to provide financial support in this situation.

We are not currently aware of any events, commitments, trends or uncertainties that are expected to have a negative impact on this arrangement.

#### **8.4 Associate Dealers and PartSource franchisees**

We have also guaranteed bank debt of some Associate Dealers. If an Associate Dealer fails to make scheduled debt payments on loans we have guaranteed, we may be required to pay the amount guaranteed. The majority of these credit guarantees expire by the end of 2006, and can be extended on their expiry at our option.

As of December 31, 2005, the maximum amount we may be required to pay under these guarantees is \$8.5 million, compared to \$4.9 million at January 1, 2005. The increase is due to an increase in the number of Dealer loans outstanding. We have not accrued any specific amount for these guarantees, over any general provision for bad debts, in our Consolidated Financial Statements.

#### **8.5 Derivative financial instruments**

We use derivative financial instruments to manage our exposure to changes in interest rates and foreign currency exchange rates. We also use equity derivative contracts to hedge certain future stock-based compensation expenses. We do not use hedging to speculate, but rather as a risk management tool.

To manage the credit and market risks associated with these instruments, we:

- > deal only with counterparties that are highly rated financial institutions; and
- > restrict the amount of hedging we can transact with any one counterparty.

# Management's Discussion and Analysis

If we sell or terminate a hedged item, or it matures before the related hedging instrument is terminated, we recognize in income any realized or unrealized gain or loss on the derivative instrument.

Our credit exposure to hedges and other derivatives is the current replacement value of contracts that are in a gain position. As at December 31, 2005, our credit exposure from interest rate swap, foreign exchange and equity derivative contracts was \$25.4 million.

## **9. Enterprise risk management**

The Company approaches the management of risk strategically, within its enterprise risk management (ERM) framework, in order to preserve shareholder value prudently.

In 2003, we introduced an ERM framework that sets out principles, processes and tools for evaluating, prioritizing and managing risk effectively and consistently across the organization. In developing our ERM, our intent was to develop an integrated approach to managing risks to help us achieve our strategic objectives. Our ERM is:

- > designed to provide an understanding of risks across the organization, and the impacts of risks on every part of the organization;
- > cross-functional in its perspective and employs a consistent discipline for assessing, managing and measuring risk;
- > designed to allow for improved capital allocation decisions to optimize risk and reward; and
- > designed to incorporate a number of tools for managing risk, including avoidance, mitigation, insurance and acceptance.

Our first steps were to develop a process for identifying and assessing our principal risks, and to carry out an initial risk assessment. We completed the assessment in 2004, and identified 15 principal risks. We define a principal risk as a risk that 1) can have a significant adverse impact on Canadian Tire's performance, reputation or ability to service its customers, and 2) has, in the absence of controls, a reasonable possibility of occurring.

Each principal risk:

- > has been assigned to at least one of our executives or management committees who have reporting, executive oversight and operational accountability for the risk;
- > is reviewed by one or more Board committees which have Board oversight accountability for the risk; and
- > is reviewed by the Company executive and the Board on a regular basis.

The table in Section 9.2 below lists our principal risks and the nature of the potential impact of these risks.

### **9.1 Board accountability**

The Board of Directors has overseen the development of an enterprise risk management process (ERM) and has delegated to the Social Responsibility and Risk Governance Committee (SRRG) and, in certain instances, the Audit Committee, the task of gaining and maintaining reasonable assurance that we:

- > appropriately identify and manage risks;
- > develop a policy which accurately sets out our risk philosophy and risk tolerance and the expectations and accountabilities for identifying, assessing, monitoring and managing risks;
- > fully implement and sustain the ERM process in compliance with the ERM policy and that the policy continues to set out accurately our risk philosophy and risk tolerance as well as the expectations and accountabilities for managing risks;
- > identify in a timely manner the most significant risks – principal risks – including those related to or arising from any weaknesses or threats to our business, and our assumptions underlying our Strategic Plan; and
- > effectively assess, monitor and manage principal risks in compliance with the ERM policy.

The SRRG is responsible for the oversight of the broad ERM framework and risk management process, as well as most elements of risk, including health and safety, environmental and operational.

The Audit Committee is responsible for the oversight of financial risk and financial reporting risk.

## 9.2 Principal risks

Category	Risk	Potential impacts		
		Performance	Ability to service customers	Reputation
Business processes/execution	Technology – critical business systems <sup>1,2</sup>		✓	✓
	Product quality <sup>1</sup>			✓
Credit	Consumer credit <sup>2,3</sup>	✓		
External	Competitive <sup>4</sup>	✓		
	Economic <sup>4</sup>	✓		
	Hazards, disasters and business interruptions <sup>1</sup>	✓	✓	✓
	Legislative compliance <sup>1,2,3</sup>			✓
	Geopolitical events <sup>2</sup>	✓		
Finance	Accounting, valuation and reporting <sup>2</sup>	✓		✓
	Disclosure <sup>2</sup>	✓		✓
	Capital <sup>4</sup>	✓		
	Financial instruments <sup>2</sup>	✓		
People	Effective management <sup>5</sup>	✓	✓	✓
	Ethical business practice <sup>1,2</sup>			✓
	Quality of workplace <sup>1,5</sup>	✓	✓	✓

### Board/Committee Oversight Accountability

<sup>1</sup> Social Responsibility and Risk Governance Committee

<sup>2</sup> Audit Committee

<sup>3</sup> Canadian Tire Bank Board

<sup>4</sup> Board of Directors

<sup>5</sup> Management Resources and Compensation Committee

The following commentary provides a high-level perspective on the nature of each identified principal risk and describes the main practices that we have in place to mitigate the impacts of these risks on our business activities.

**Technology** The integrity, reliability and availability of technology and the data processed and stored by that technology are critical to the daily requirements of our business and finance operations. The inability to process customer transactions directly affects sales. Loss of our critical technology systems – those that support shipments and sales – would shut down our Operations Planning processes and impact our ability to move product through our distribution centres. Numerous controls are in place to manage technology risk, including disaster recovery procedures and monitoring of inappropriate external access attempts. Since the beginning of 2003, our Information Technology group has been implementing a strategy designed to operate a simpler technical environment with the appropriate standardized processes to minimize the risks associated with operating on a number of differing technology platforms.

**Product quality** Our brand equity and reputation are integrally linked to the quality of the products we sell to our customers, particularly our proprietary products and those which could pose a risk to the health and safety of our customers. We have a Quality Engineering group that proactively tests products for durability, safety and functionality. We analyze product returns and review consumer reports and use the resulting information to include quality provisions in contract negotiations with vendors. All of our vendors are required to carry insurance to cover product liability and indemnify us.

**Consumer credit** With a growing portfolio of credit card customers and the granting of credit, our Financial Services business assumes certain risks that include the failure or inability to accurately predict the creditworthiness of our customers or their ability to repay debt. Financial Services minimizes credit risks to maintain and improve the quality of its consumer lending portfolio by:

- > employing sophisticated credit-scoring models to constantly monitor the creditworthiness of customers;
- > using the latest technology to make informed credit decisions for each customer account to limit credit risk exposure;
- > adopting technology to improve the effectiveness of the collection process; and
- > monitoring the macro-economic environment, especially with respect to interest rates, employment levels and income levels.

**Competitive** We compete against international, national and regional retailers such as department stores, mass merchandisers, home-improvement warehouses, petroleum retailers and specialty marketers, which currently operate in one or more of our business segments. These retailers and new entrants represent a competitive risk to our ability to attract customers and operate successfully in our markets.

We actively monitor and analyze developments in our markets to determine our competitiveness within each market or business segment. Each of our businesses has core strengths and initiatives that provide differentiation in the marketplace and enhance its competitive position, reducing our overall competitive risk. The unique strengths and strategies of our businesses are described in more detail in sections 2 and 5 respectively of this MD&A.



# Management's Discussion and Analysis

**Economic** Shifts in the economic health of the environment in which we operate – such as economic growth, inflation, exchange rates and levels of taxation – can impact consumer confidence and spending and impact our ability to source products at a competitive cost. We constantly monitor economic developments in the markets where we operate and where we source our products. We use this information in our continuous strategic and operational reviews to adjust our initiatives as economic conditions dictate and to facilitate ongoing innovation of stores, merchandising concepts and products.

**Hazards, disasters and business interruptions and geopolitical events** Risks arising from natural disasters, war, or random occurrences or acts can result in a material change to economic and market performance, consumer behaviour and business conditions or operations. We have established emergency response protocols and business continuity plans, and our emergency response teams have been trained to properly respond to situations as they arise. Our Business Continuity Management team assesses business continuity plans to ensure that they are adequately prepared and tested for all of our critical processes and systems. We also maintain insurance coverage to offset physical loss and loss of profits to mitigate the financial impact of an unusual event. The outcome of any insurance claim is subject to limitations set by the insurer.

**Legislative compliance** In operating our business, we must comply with a variety of laws and regulations to meet our corporate and social responsibilities and to avoid the risk of financial penalties and/or criminal and civil liability for our Officers and Directors. Areas of compliance include environment, health and safety, competition law, transportation of dangerous goods, customs and excise and regulations governing financial institutions.

Changes to regulations that govern Financial Services could affect us, for example, by increasing the ability of competitors to compete with products and services we provide or by increasing compliance costs. A failure to comply with applicable regulations could result in sanctions and financial penalties by regulatory bodies that could impact our earnings and reputation.

We have in place a number of policies and programs – such as our environmental, health and safety management system – to ensure ongoing compliance, and we carry out regular assessments of facilities and procedures to determine whether our operations meet regulatory and corporate requirements. Our Financial Services division has in place a compliance department to assist Canadian Tire Bank in addressing the requirements of the Office of the Superintendent of Financial Institutions. At the corporate level, we have established a compliance department to provide a framework for compliance oversight with laws and regulations applicable to our businesses.

**Tax compliance** In the ordinary course of business, the Company is subject to ongoing audits by tax authorities. While the Company believes that its tax filing positions are appropriate and supportable, the possibility exists that certain matters may be reviewed and challenged by the tax authorities. The Company regularly reviews the potential for adverse outcomes and the adequacy of its tax provisions and believes it has adequately provided for these matters. Should the ultimate outcomes materially differ from the provisions, the Company's effective tax rate and/or its earnings could be affected positively or negatively in the period in which the matters are resolved. The Company mitigates this risk through ensuring tax staff are well trained and supervised and that tax filing positions are carefully scrutinized by Management and external consultants, as appropriate.

**Accounting, valuation and reporting** Risks can arise from changes in the rules or standards governing accounting or financial reporting. We employ numerous professionally accredited accountants throughout our finance group and all of our divisional financial officers have a dotted line reporting relationship to our Chief Financial Officer (CFO). Senior finance representatives are assigned to all significant projects that impact financial accounting and reporting systems. Policies are in place to ensure the completeness and accuracy of reported transactions. Key transaction controls are in place, and there is a segregation of duties between transaction initiation, processing and cash disbursement, and restricted physical access to the Treasury and cash settlements area. Accounting, measurement, valuation and reporting of accounts, which involve estimates and/or valuations, are reviewed quarterly by the CFO, external auditor and the Audit Committee. Significant accounting and financial topics and issues are presented to and discussed with the Audit Committee, and a presentation of quarterly scorecards on operational results and Officer objectives is made to the Audit Committee and Board of Directors.

**Disclosure** We are required to comply with securities reporting legislation and accounting standards that are intended to ensure the full, accurate and timely communication of financial and other material information to the public. To ensure that we meet our obligations and mitigate risks associated with the disclosure of inaccurate or incomplete information – or a failure to disclose required information – we have put in place a Disclosure Policy and a Disclosure Committee to guide compliance:

- > the Disclosure Policy sets out our accountabilities, authorized spokespersons, and our approach to the determination, preparation and dissemination of material information. The policy also defines restrictions on insider trading and the handling of confidential information; and
- > the Disclosure Committee reviews all financial information prepared for communication to the public to ensure it meets requirements and is responsible for raising all outstanding issues it believes require the attention of the Audit Committee prior to recommending disclosures for that Committee's approval.

The CEO, CFO, Senior Vice-President, Secretary and General Counsel, Senior Vice-President Corporate Affairs, Chairman of the Board and Chairman of the Audit Committee review all financial disclosures prior to submission to the Audit Committee for the Audit Committee's review and recommendation for approval by the Board.

**Capital** We must maintain sufficient capital to operate our business and absorb the potential impact of unexpected losses.

We maintain adequate access to debt markets to meet our funding requirements. Our Treasurer is responsible for the effective management of capital within the target limits approved by the Board. To monitor our adherence to established policies, a Financial Risk Management Report – which sets out targets and performance on debt to capital ratios, liquidity ratios and foreign exchange management – is provided to the Audit Committee on

a quarterly basis. Our Financial Risk Management group approves financial risk management policies for recommendation to the Audit Committee and monitors compliance with those policies. The Funding Plan for the Company is prepared by our Treasury department and approved by the Board.

**Financial instruments** The use of derivative financial products to hedge currency, interest rates and equity exposures, as well as the use of other complex financial instruments pose certain risks.

To reduce our risk, our Treasury department does not operate as a profit centre. Controls are in place to detect and prevent speculative activity.

It is our policy to identify and manage currency and interest-rate risk proactively and conservatively. To ensure that any counterparty to our financial transactions has the ability to meet its financial commitments, we deal only with highly rated financial institutions. We also ensure that there is no undue concentration with any single counterparty.

**Effective management** Lack of effective recruitment programs, succession planning, compensation structures, as well as performance management and development would present risks to our ability to implement our strategic initiatives and to attract, motivate and retain talented people.

We have well-established recruitment and performance management practices that are facilitated and monitored by our Human Resources group. Our compensation structure emphasizes employee share ownership and profit sharing, and is reviewed regularly to ensure it is competitive with the marketplace. Twice annually, the executive team undertakes a Leadership Review Process to identify high-potential individuals for development and to ensure that there are viable successors for all key management positions.

**Ethical business practices** Any violation of law, breach of Company policy or unethical behaviour poses significant risk to our reputation, our brand name and our ability to operate.

Commitment to ethical business practices is core to our values and is reflected in a number of policies and practices which have been strengthened over the past year to ensure that our employees and Directors uphold the highest standards of ethical behaviour. In 2004, our Board reviewed and approved updates to our Code of Business Conduct that all employees must sign annually as a condition of their employment. Directors are also required to annually provide consent to that Code. We introduced a separate Supplier Code of Business Conduct and established a Business Conduct Compliance Office to oversee compliance with our Code of Business Conduct and to provide channels for people to report, confidentially and anonymously, breaches of that code for subsequent investigation. The Office became fully operational in 2005.

**Quality of workplace** Ensuring a healthy and safe workplace minimizes injuries and other risks employees may face in carrying out their duties, improves productivity and avoids penalties or other liabilities for our Officers and Directors.

We have a number of practices in place to ensure a quality workplace, including guidelines for physical and ergonomic workspaces and shared facilities. Our environment, health and safety compliance and management system and policies ensure that procedures are followed to minimize workplace injuries and we offer programs to promote healthy lifestyles. The incidence of workplace injuries is monitored regularly and reports are reviewed by the Social Responsibility and Risk Committee on a quarterly basis.

## 10. Contractual obligations

### Contractual obligations due by period

(\$ in millions)	Total	2006	In years 2007-2008	In years 2009-2010	After 2010
Long-term debt	\$ 1,370.8	\$ 201.8	\$ 153.4	\$ 152.3	\$ 863.3
Capital lease obligations	4.8	2.5	2.3	-	-
Operating leases	1,267.4	160.0	275.4	224.4	607.6
Purchase obligations	361.0	335.0	22.3	3.7	-
Other obligations	58.9	52.7	5.0	1.2	-
<b>Total contractual obligations</b>	<b>\$ 3,062.9</b>	<b>\$ 752.0</b>	<b>\$ 458.4</b>	<b>\$ 381.6</b>	<b>\$ 1,470.9</b>

## 11. Changes in accounting policies

### 11.1 Vendor rebates restatement

Effective July 4, 2004, we retroactively implemented the accounting policy issued by the Canadian Institute of Chartered Accountants (CICA) in EIC-144, "Accounting by a Customer (Including a Reseller) for Certain Consideration Received from a Vendor", and restated the Consolidated Financial Statements for 2004 and prior periods. Vendor rebates are payments CTR receives from suppliers to support advertising and marketing programs that promote products CTR buys from these suppliers. This policy provides guidance on how a customer (including a reseller) of a vendor's products should account for rebates it receives from the vendor.

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As a result of the implementation of EIC-144, CTR's earnings before income taxes and minority interest for the fourth quarter of 2004, decreased by \$5.1 million to \$78.0 million, and for the full year of 2004, increased by \$2.1 million to \$271.9 million. In the fourth quarter of 2005, earnings before income taxes and minority interest were \$9.1 million lower, and for the full year of 2005, were \$5.2 million lower, as a result of EIC-144.

The following table shows CTR's earnings before and after the implementation of the new accounting policy, EIC-144.

## Impact of vendor rebates on CTR's earnings

(\$ in millions)	Q4 2005	Q3 2005	Q2 2005	Q1 2005	Q4 2004	Q3 2004	Q2 2004	Q1 2004
Earnings before income taxes and minority interest prior to the implementation of EIC-144	\$ 96.0	\$ 84.3	\$ 96.2	\$ 18.9	\$ 83.1	\$ 69.7	\$ 84.6	\$ 32.4
Impact of EIC-144	(9.1)	1.8	(4.0)	6.1	(5.1)	1.5	(3.1)	8.8
Earnings before income taxes and minority interest adjusted to include the impact of EIC-144	\$ 86.9	\$ 86.1	\$ 92.2	\$ 25.0	\$ 78.0	\$ 71.2	\$ 81.5	\$ 41.2

### 11.2 Amendment to EIC-144

In January 2005, the CICA amended EIC-144. The amendment clarifies when and how to recognize those vendor rebates that are payable only if the customer completes a specified cumulative level of purchases or remains a customer for a specified period of time. EIC-144 now requires companies to recognize those rebates that are at the vendor's discretion when the vendor either pays the rebates or becomes obligated to pay them. For binding agreements, EIC-144 now requires that vendor rebates be recognized when and to the extent that they are probable and reasonably estimable.

Effective April 3, 2005, we retroactively implemented the amended policy EIC-144. As there was no material impact from implementing the amendment, no restatements were made to the Consolidated Financial Statements for prior periods.

### 11.3 Consolidation of variable interest entities

In June 2003, the CICA issued Accounting Guideline 15, "Consolidation of Variable Interest Entities", (AcG-15). This guideline was amended in September 2004 to harmonize with the related U.S. accounting standard, which had been revised in December 2003. AcG-15 requires companies to include certain variable interest entities in their annual or interim consolidated financial statements beginning on or after November 1, 2004.

In the fourth quarter of 2004, we made structural changes to the arrangements involving the independent trusts described in section 8. Consequently, we were not required to include the financial results of the trusts in our 2005 Consolidated Financial Statements.

A number of the corporations owned and operated by independent Associate Dealers and Mark's Work Wearhouse and PartSource franchisees are variable interest entities. Although a few of these corporations required some subordinated financial support from us during the year, none of these corporations have been included in our Consolidated Financial Statements as the impact of consolidating them was not material.

### 11.4 Foreign currency translation of foreign subsidiaries

Due to a change in the nature and extent of certain foreign subsidiaries' operations, we have determined that these subsidiaries are now considered to be integrated operations under the definition provided in Section 1650 of the CICA Handbook. Accordingly, effective from the third quarter of 2005, the accounts of those affected subsidiaries, previously translated using the current rate method, are now translated using the temporal method. Under this method exchange gains or losses resulting from translating the foreign currency denominated financial statements to Canadian dollars are included in income during the period instead of being treated as a separate component of shareholders' equity. The change in the method of translation, which was accounted for prospectively, was not material.

### 11.5 Consideration to customers

During 2005, the CICA issued EIC-156, "Accounting by a Vendor for Consideration Given to a Customer (Including a Reseller of the Vendor's Products)". This standard provides guidance on the presentation, recognition and measurement of consideration given to customers. This EIC is effective for interim and annual financial statements for fiscal years beginning on or after January 1, 2006. We are currently determining the potential impact of this new standard on our Consolidated Financial Statements for 2006.

## 11.6 Financial instruments

During 2005, the CICA issued three new Handbook Sections: Section 3855, "Financial Instruments – Recognition and Measurement", Section 3865, "Hedges" and Section 1530, "Comprehensive Income". These standards provide guidance on the recognition, measurement and classification of financial assets and financial liabilities. The new standards also establish new accounting requirements for hedges. Any ineffectiveness of designated hedges will be recognized immediately in income. These standards also provide guidance for reporting items in other comprehensive income, which will be included on the Consolidated Balance Sheets as a separate component of shareholders' equity. These accounting standards are to be applied no later than the fiscal years beginning on or after October 1, 2006. We are currently evaluating the potential impact of these new standards on our Consolidated Financial Statements for 2007.

## 12. Non-GAAP measures

The following measures included in this MD&A do not have a standardized meaning under Canadian generally accepted accounting principles (GAAP):

- > EBITDA (earnings before interest, income taxes, depreciation and amortization) and minority interest;
- > all references made to adjusted earnings; and
- > same store and comparable store sales.

**EBITDA and minority interest** With the exception of Financial Services, we consider EBITDA and minority interest to be an effective measure of the contribution of each of our businesses to our profitability on an operational basis, before allocating the cost of income taxes and capital investments. EBITDA and minority interest is also commonly regarded as an indirect measure of operating cash flow, a significant indicator of the success of any business.

A reconciliation of EBITDA and minority interest to the most comparable GAAP measure (earnings before income taxes and minority interest) is provided as follows:

### Reconciliation of EBITDA to GAAP measures<sup>1</sup>

(\$ in millions)	Q4 2005	Q4 2004	2005	2004
<b>EBITDA and minority interest</b>				
CTR	\$ 151.1	\$ 133.8	\$ 530.2	\$ 488.2
Financial Services	62.9	52.6	191.0	172.0
Petroleum	7.0	6.0	21.9	16.4
Mark's	47.2	35.2	82.2	53.8
Eliminations	(8.1)	(6.1)	(28.5)	(20.5)
<b>Total EBITDA and minority interest</b>	<b>\$ 260.1</b>	<b>\$ 221.5</b>	<b>\$ 796.8</b>	<b>\$ 709.9</b>
<b>Less: Depreciation and amortization expense</b>				
CTR	\$ 38.1	\$ 33.1	\$ 143.5	\$ 129.6
Financial Services	3.1	3.4	12.5	14.1
Petroleum	4.0	3.5	14.4	13.0
Mark's	4.0	3.6	14.6	13.9
<b>Total depreciation and amortization expense</b>	<b>\$ 49.2</b>	<b>\$ 43.6</b>	<b>\$ 185.0</b>	<b>\$ 170.6</b>
<b>Interest expense</b>				
CTR	\$ 26.1	\$ 22.7	\$ 96.5	\$ 86.7
Financial Services	4.0	2.7	13.5	9.4
Mark's	1.0	0.7	2.6	2.8
Eliminations	(8.1)	(6.1)	(28.5)	(20.5)
<b>Total interest expense</b>	<b>\$ 23.0</b>	<b>\$ 20.0</b>	<b>\$ 84.1</b>	<b>\$ 78.4</b>
<b>Earnings before income taxes and minority interest</b>				
CTR	\$ 86.9	\$ 78.0	\$ 290.2	\$ 271.9
Financial Services	55.8	46.5	165.0	148.5
Petroleum	3.0	2.5	7.5	3.4
Mark's	42.2	30.9	65.0	37.1
<b>Total earnings before income taxes and minority interest</b>	<b>\$ 187.9</b>	<b>\$ 157.9</b>	<b>\$ 527.7</b>	<b>\$ 460.9</b>

<sup>1</sup> Differences may occur due to rounding.

# Management's Discussion and Analysis

**References to adjusted earnings** In several places in this MD&A, we refer to adjusted pre-tax and after-tax earnings before the impact of non-operating items. Historically, non-operating items have included gains and losses on the sales of loans receivable and dispositions of surplus property and equipment. The timing and amount of gains and losses from these items are not consistent from quarter to quarter. In the first quarter of 2005, non-operating items also included the \$5.3 million net charge for the early redemption of MTNs, which was included in CTR's long-term debt interest expense.

We believe the adjusted figures allow for a clearer assessment of earnings for each of our businesses, and provide a more meaningful measure of our consolidated and segmented operating results.

**Same store and comparable store sales**

Same store sales include sales from stores that have been open for more than a year, including stores that have been expanded by more than 25 percent in the last year.

Comparable store sales include sales from stores that have been open for more than 53 weeks and that have not been expanded by more than 25 percent in the last year.

### **13. Management's evaluation of disclosure controls and procedures**

Management is responsible for establishing and maintaining a system of controls and procedures over the public disclosure of financial and non-financial information regarding the Company. Such controls and procedures are designed to provide reasonable assurance that all relevant information is gathered and reported, on a timely basis, to senior management, including the Chief Executive Officer (CEO) and the Chief Financial Officer (CFO), so that appropriate decisions can be made by them regarding public disclosure.

Our system of disclosure controls and procedures includes, but is not limited to, our Disclosure Policy, our Code of Business Conduct, the effective functioning of our Disclosure Committee, procedures in place to systematically identify matters warranting consideration of disclosure by the Disclosure Committee and verification processes for individual financial and non-financial metrics and information contained in annual and interim filings, including the financial statements, MD&As, Annual Information Forms and other documents and external communications.

As required by CSA Multilateral Instrument 52-109, Certification of Disclosure in Issuers' Annual and Interim Filings, an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures was conducted, under the supervision of Management, including the CEO and CFO, as of December 31, 2005. The evaluation included documentation review, enquiries and other procedures considered by Management to be appropriate in the circumstances.

Based on that evaluation, the CEO and the CFO have concluded that the design and operation of the system of disclosure controls and procedures was effective as of December 31, 2005.

The CEO and CFO are also required, under Multilateral Instrument 52-109, to file certifications of our annual filings. Copies of these certifications may be found on page 33 of the 2005 Annual Report.



# Management's Responsibility for Financial Statements

The Management of Canadian Tire Corporation, Limited is responsible for the accompanying Consolidated Financial Statements and all other information in the Annual Report. The financial statements have been prepared by Management in accordance with Canadian generally accepted accounting principles, which recognize the necessity of relying on some best estimates and informed judgements. All financial information in the Annual Report is consistent with the Consolidated Financial Statements.

To discharge its responsibilities for financial reporting and safeguarding of assets, Management depends on the Company's systems of internal accounting control. These systems are designed to provide reasonable assurance that the financial records are reliable and form a proper basis for the timely and accurate preparation of financial statements. Management meets the objectives of internal accounting control on a cost-effective basis through the prudent selection and training of personnel, adoption and communication of appropriate policies, and employment of an internal audit program.

The Board of Directors oversees Management's responsibilities for the Consolidated Financial Statements primarily through the activities of its Audit Committee, which is composed solely of directors who are neither officers nor employees of the Company. This Committee meets with Management and the Company's independent auditors, Deloitte & Touche LLP, to review the Consolidated Financial Statements and recommend approval by the Board of Directors. The Audit Committee is also responsible for making recommendations with respect to the appointment of and for approving remuneration and the terms of engagement of the Company's auditors. The Audit Committee also meets with the auditors, without the presence of Management, to discuss the results of their audit, their opinion on internal accounting controls, and the quality of financial reporting.

The Consolidated Financial Statements have been audited by Deloitte & Touche LLP, who were appointed by shareholder vote at the annual shareholders' meeting. Their report is presented below.

(SIGNED)

**Wayne C. Sales**  
President and  
Chief Executive Officer  
March 9, 2006

(SIGNED)

**J. Huw Thomas**  
Executive Vice-President, Finance and Administration and  
Chief Financial Officer

## Auditors' Report

To the Shareholders, Canadian Tire Corporation, Limited

We have audited the consolidated balance sheets of Canadian Tire Corporation, Limited as at December 31, 2005 and January 1, 2005 and the consolidated statements of earnings and retained earnings and of cash flows for the years then ended. These financial statements are the responsibility of the Company's Management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2005 and January 1, 2005 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Deloitte & Touche LLP (SIGNED)

**Chartered Accountants**  
Toronto, Ontario  
March 9, 2006

# Consolidated Statements of Earnings and Retained Earnings

For the years ended (Dollars in millions except per share amounts)	<b>December 31, 2005</b>	January 1, 2005
<b>Gross operating revenue</b>	<b>\$ 7,774.6</b>	\$ 7,153.6
<b>Operating expenses</b>		
Cost of merchandise sold and all other operating expenses except for the undernoted items	<b>6,949.1</b>	6,416.9
Interest		
Long-term debt	<b>79.5</b>	76.0
Short-term debt	<b>4.6</b>	2.4
Depreciation and amortization	<b>185.0</b>	170.6
Employee profit sharing plan (Note 10)	<b>28.7</b>	26.8
<b>Total operating expenses</b>	<b>7,246.9</b>	6,692.7
<b>Earnings before income taxes and minority interest</b>	<b>527.7</b>	460.9
<b>Income taxes</b> (Note 11)		
Current	<b>187.2</b>	150.8
Future	<b>2.8</b>	11.7
<b>Total income taxes</b>	<b>190.0</b>	162.5
<b>Net earnings before minority interest</b>	<b>337.7</b>	298.4
<b>Minority interest</b> (Note 17)	<b>7.6</b>	6.9
<b>Net earnings</b>	<b>\$ 330.1</b>	\$ 291.5
<b>Basic earnings per share</b>	<b>\$ 4.04</b>	\$ 3.60
<b>Diluted earnings per share</b> (Note 9)	<b>\$ 3.98</b>	\$ 3.53
<b>Weighted average number of Common and Class A Non-Voting Shares outstanding</b>	<b>81,764,082</b>	80,983,467
<b>Retained earnings, beginning of year</b>	<b>\$ 1,546.9</b>	\$ 1,318.0
<b>Net earnings</b>	<b>330.1</b>	291.5
<b>Dividends</b>	<b>(47.4)</b>	(40.5)
<b>Repurchase of Class A Non-Voting Shares</b> (Note 9)	<b>(17.0)</b>	(22.1)
<b>Retained earnings, end of year</b>	<b>\$ 1,812.6</b>	\$ 1,546.9

# Consolidated Statements of Cash Flows

For the years ended (Dollars in millions)	<b>December 31, 2005</b>	January 1, 2005
<b>Cash generated from (used for):</b>		
<b>Operating activities</b>		
Net earnings	\$ 330.1	\$ 291.5
Items not affecting cash		
Net provision for loans receivable	222.1	184.4
Depreciation and amortization of property and equipment	182.0	166.2
Other	9.2	6.5
Amortization of other assets	5.8	7.1
Future income taxes	2.8	11.7
Gain on disposals of property and equipment	(10.9)	(14.4)
Gain on sales of loans receivable (Note 2)	(19.9)	(22.6)
<b>Cash generated from operations</b>	<b>721.2</b>	<b>630.4</b>
<b>Changes in other working capital components</b> (Note 12)	<b>(283.1)</b>	<b>(217.3)</b>
<b>Cash generated from operating activities</b>	<b>438.1</b>	<b>413.1</b>
<b>Investing activities</b>		
Investment in loans receivable	(717.6)	(592.3)
Additions to property and equipment	(391.1)	(340.7)
Long-term receivables and other assets	(24.7)	(16.2)
Purchases of stores	(4.9)	(1.3)
Asset retirement obligations	(1.3)	(0.3)
Sale of Associate Dealer receivables (Note 12)	47.8	321.1
Proceeds on disposition of property and equipment	78.2	38.2
Securitization of loans receivable	395.2	349.4
<b>Cash used for investing activities</b>	<b>(618.4)</b>	<b>(242.1)</b>
<b>Financing activities</b>		
Issuance of long-term debt	516.4	201.5
Class A Non-Voting Share transactions, net (Note 9)	(23.3)	(13.6)
Dividends	(45.7)	(38.5)
Repayment of long-term debt	(231.3)	(244.8)
<b>Cash generated from (used for) financing activities</b>	<b>216.1</b>	<b>(95.4)</b>
<b>Cash generated in the year</b>	<b>35.8</b>	<b>75.6</b>
<b>Cash and cash equivalents, beginning of year</b>	<b>802.2</b>	<b>726.6</b>
<b>Cash and cash equivalents, end of year</b> (Note 12)	<b>\$ 838.0</b>	<b>\$ 802.2</b>

# Consolidated Balance Sheets

As at (Dollars in millions)	<b>December 31, 2005</b>	January 1, 2005
<b>ASSETS</b>		
<b>Current assets</b>		
Cash and cash equivalents (Note 12)	\$ 838.0	\$ 802.2
Accounts receivable (Note 12)	652.8	370.7
Loans receivable (Note 2)	728.7	592.4
Merchandise inventories	675.5	620.6
Prepaid expenses and deposits	42.4	24.1
Future income taxes (Note 11)	43.6	24.6
<b>Total current assets</b>	<b>2,981.0</b>	2,434.6
<b>Long-term receivables and other assets</b> (Note 3)	<b>132.1</b>	129.7
<b>Goodwill</b> (Note 4)	<b>46.2</b>	41.7
<b>Intangible assets</b> (Note 4)	<b>52.4</b>	52.0
<b>Property and equipment</b> (Note 5)	<b>2,743.9</b>	2,585.2
<b>Total assets</b>	<b>\$ 5,955.6</b>	\$ 5,243.2
<b>LIABILITIES</b>		
<b>Current liabilities</b>		
Accounts payable and other	\$ 1,545.5	\$ 1,437.6
Income taxes payable	71.2	44.2
Current portion of long-term debt (Note 6)	204.3	5.6
<b>Total current liabilities</b>	<b>1,821.0</b>	1,487.4
<b>Long-term debt</b> (Note 6)	<b>1,171.3</b>	1,081.8
<b>Future income taxes</b> (Note 11)	<b>89.0</b>	67.2
<b>Other long-term liabilities</b> (Note 7)	<b>63.2</b>	55.6
<b>Total liabilities</b>	<b>3,144.5</b>	2,692.0
<b>Minority interest</b> (Note 17)	<b>300.0</b>	300.0
<b>SHAREHOLDERS' EQUITY</b>		
<b>Share capital</b> (Note 9)	<b>702.7</b>	709.0
<b>Contributed surplus</b>	<b>1.5</b>	1.3
<b>Accumulated foreign currency translation adjustment</b>	<b>(5.7)</b>	(6.0)
<b>Retained earnings</b>	<b>1,812.6</b>	1,546.9
<b>Total shareholders' equity</b>	<b>2,511.1</b>	2,251.2
<b>Total liabilities, minority interest and shareholders' equity</b>	<b>\$ 5,955.6</b>	\$ 5,243.2

(SIGNED)

**Gilbert S. Bennett**  
Director

(SIGNED)

**Maureen J. Sabia**  
Director

# Notes to the Consolidated Financial Statements

## 1. SIGNIFICANT ACCOUNTING POLICIES

**Basis of consolidation** The Consolidated Financial Statements include the accounts of Canadian Tire Corporation, Limited and its subsidiaries and partnership (the "Company").

**Fiscal year** The fiscal year of the Company consists of a 52- or 53-week period ending on the Saturday closest to December 31. The fiscal years for the Consolidated Financial Statements and Notes presented for 2005 and 2004 are the 52-week periods ended December 31, 2005 and January 1, 2005, respectively.

The results of certain subsidiaries which have different year ends from the Company have been included in the Consolidated Financial Statements for the 12 months ended December 31.

**Consolidation of variable interest entities** Effective January 2, 2005, the Company implemented the Canadian Institute of Chartered Accountants' ("CICA") Accounting Guideline 15 ("AcG-15") "Consolidation of Variable Interest Entities", which is effective for years beginning on or after November 1, 2004. A variable interest entity ("VIE") is any type of legal structure not controlled by voting equity, but rather by contractual or other financial arrangements. AcG-15 requires a VIE to be consolidated by the primary beneficiary, who is the party that will absorb the majority of the VIE's expected losses, receive a majority of the VIE's expected residual returns, or both.

Upon implementation of AcG-15, the Company reviewed all legal structures in which the Company has a potential financial interest including Associate Dealer corporations, Petroleum Agent corporations, PartSource and Mark's Work Wearhouse ("Mark's") franchisee corporations, financing trusts referred to in Notes 2 and 14 and external suppliers. The Company has identified that some of the corporations owned and operated by Associate Dealers and Mark's and PartSource franchisees are VIEs.

The Company enters into various forms of agreements with independent owner-operators of Canadian Tire Associate Stores (Associate Dealers) and franchisees of Mark's and PartSource stores.

The Company's agreement with each Associate Dealer generally permits the Associate Dealer to own and operate the retail business of a Canadian Tire Associate Store under the Canadian Tire trademark. The Company has a policy to offer new Associate Dealers smaller Canadian Tire Associate Stores and, based upon successful operation of their Canadian Tire Associate Stores, to offer Associate Dealers larger locations from time to time pursuant to the Associate Dealer mobility system. When eligible, Associate Dealers may obtain financing through a structure involving independent trusts to facilitate the purchase of core-level inventory and fixed assets. These trusts are administered by independent major Canadian banks. Associate Dealers may also obtain financing through traditional financial institutions. The Company monitors the financial condition of its Associate Dealers and provides for estimated losses when appropriate.

The Company's agreements with each Mark's and PartSource franchisee also permit the franchisees to own and operate retail businesses under their respective trademarks. Franchisees obtain financing through traditional financial institutions. The Company monitors the financial condition of its franchisees and provides for estimated losses when appropriate.

The Company is the primary beneficiary of a small number of these corporations. These VIEs have not been consolidated in these financial statements, as the impact was not material.

**Translation of foreign currencies** Transactions in foreign currencies are translated into Canadian dollars at rates in effect at the date of the transaction. Assets and liabilities denominated in foreign currencies are translated at the exchange rates in effect at each accounting period end date. Exchange gains or losses are included in income.

For foreign subsidiaries that are considered self-sustaining the current rate method of translating foreign currencies has been used. Under this method, assets and liabilities are translated into Canadian dollars at the exchange rates in effect at each accounting period end date and revenues and expenses are translated at average exchange rates during the period. Gains or losses arising from the translation of the financial statements of these foreign subsidiaries are included in a separate component of shareholders' equity.

For foreign subsidiaries that are considered integrated the temporal method of translating foreign currencies has been used. Under this method, monetary items are translated into Canadian dollars at the exchange rates in effect at each accounting period end date. Non-monetary items and their related amortization are translated at their historical exchange rates. Revenues and expenses are translated at average exchange rates during the period. Gains or losses arising from the translation of the financial statements of these foreign subsidiaries are included in income.

During the year, the Company determined that certain foreign subsidiaries ceased to meet the criteria of being self-sustaining and are now considered to be integrated operations. Accordingly, the method of translating these foreign subsidiaries was changed from the current rate method to the temporal method. The change, which was made prospectively, was not material.

**Revenue recognition** The Company's shipments of merchandise to Canadian Tire Retail's ("CTR") Associate Dealers and PartSource franchisees (retail store owner-operators) are recorded as revenue when delivered and are net of returns. Revenue on the sale of gasoline by Canadian Tire Petroleum ("Petroleum") is recorded upon sale to the customer. Revenue for Mark's is recognized at the time goods are sold by its corporate-owned stores to its customers and is net of returns. Royalties, based on sales by Mark's franchisees, are recorded in income as they are earned. Interest income and service charges on loans receivable are accrued each month according to the contractual provisions of the credit agreements. Merchant fees on credit card loans receivable are taken into revenue at the time new loans are recorded. Revenue from separately-priced extended warranty contracts is recorded on a straight-line basis over the term of the contracts.

**Stock-based compensation plans** Stock-based awards are measured and recognized using a fair-value based method. Stock options granted after December 28, 2002 are measured on grant date using a fair-value based method and expensed over the vesting period. The counterpart is recorded as contributed surplus. When employees exercise their stock options, share capital is increased by the sum of the consideration paid by employees together with the related portion previously added to contributed surplus when compensation costs were charged against income. For stock options granted to employees prior to December 29, 2002, the Company recorded no compensation cost. Accordingly, the Company discloses pro forma net earnings and earnings per share as if the fair-value based method had been used for stock options granted between December 30, 2001 and December 28, 2002 (see Note 10).



# Notes to the Consolidated Financial Statements

## 1. Significant Accounting Policies (continued)

Compensation expense is recognized for the Company's contributions under the Employee Profit Sharing Plan, the Employee Stock Purchase Plan, the Deferred Share Unit Plan, the Restricted Share Unit Plan, the Performance Share Unit Plan, the Performance Conditioned Share Unit Plan, the Performance Driven Share Unit Plan and the Deferred Share Unit Plan for an Executive (see Note 10 and Note 15).

**Earnings per share** Basic earnings per share is calculated using the weighted average number of shares outstanding during the accounting period. The diluted earnings per share calculation uses an increased number of shares, determined using the treasury stock method.

**Cash and cash equivalents** Cash and cash equivalents are defined as cash and short-term investments less bank indebtedness. Short-term investments held include Canadian and United States government securities and notes of other creditworthy parties due within three months.

**Loans receivable** Loans receivable include credit card and personal loans receivable. Loans receivable are recorded at cost net of unearned interest income and of allowances established for credit losses. Interest income is recorded on an accrual basis, except for impaired loans, the treatment of which is described below.

An allowance for credit losses is calculated using the historical loss experience of account balances based on aging and arrears status, with certain adjustments for other relevant circumstances influencing the recoverability of the loans. Personal loans are considered impaired when principal or interest payments are over 90 days past due and are written off when they are one year past due. Revenue on personal loans which are over 90 days past due and classified as impaired is not recognized. Credit card loans are written off when they are in arrears for over 180 days. Payments received on loans that have been written off are recorded first against any previous write-offs or allowances, and then as revenue.

When a personal loan has been identified as impaired, the carrying amount of the loan is reduced to its estimated realizable amount, measured by discounting the expected future cash flows at the effective interest rate inherent in the loan. In subsequent periods, recoveries of amounts previously written off and any increase in the estimated realizable value of the loan is credited to the provision for credit losses. Where a portion of a loan is written off and the remaining balance is restructured, the new loan is carried on an accrual basis when there is no longer any reasonable doubt regarding the collectibility of principal or interest, and payments are not 90 days past due.

Effective July 1, 2001, the Company adopted the CICA's Accounting Guideline 12 ("AcG-12"), "Transfers of Receivables". Under this policy, the Company is required to recognize gains or losses on its loans receivable securitizations subsequent to June 30, 2001 that qualify as sales. The gain or loss on the sale of the loans receivable depends in part on the previous carrying amount of the loans involved in the sale. The carrying amount is allocated between the assets sold and the retained interests based on their relative fair values at the date of sale. The Company estimates fair value based on the present value of future expected cash flows using management's estimates of the key assumptions (see Note 2).

**Merchandise inventories** Merchandise inventories are valued at the lower of cost and estimated net realizable value, with cost being determined using the average cost method, except for the merchandise inventories of Mark's, which are accounted for by the retail method and are carried at the lower of the anticipated selling price (less an expected average gross margin) and the estimated cost.

**Vendor rebates** The Company records cash consideration received from vendors as a reduction in the price of vendors' products and reflects it as a reduction to cost of goods sold and related inventory when recognized in the Consolidated Statements of Earnings and Consolidated Balance Sheets. Certain exceptions apply where the cash consideration received is either a reimbursement of incremental selling costs incurred by the reseller, or is a payment for assets or services delivered to the vendor.

In January 2005, the CICA Emerging Issues Committee's Abstract 144 "Accounting by a Customer (Including a Reseller) for Certain Consideration Received from a Vendor" (EIC-144) was amended to clarify when and how to recognize those vendor rebates that are payable only if the customer completes a specified cumulative level of purchases or remains a customer for a specified period of time. EIC-144 now requires companies to recognize those rebates that are at the vendor's discretion when the vendor either pays the rebates or agrees to pay them. For binding agreements, EIC-144 now requires that vendor rebates be recognized to the extent that they are probable and reasonably estimable.

Effective April 3, 2005, the Company retroactively implemented the amended EIC-144. As there was no material impact from implementing the amendment, no restatements were made to the Consolidated Financial Statements for prior periods.

**Income taxes** Income taxes are accounted for using the asset and liability method. Under this method, future income tax assets and liabilities are recognized for temporary differences between financial statement carrying amounts of assets and liabilities and their respective income tax bases. A future income tax asset or liability is estimated for each temporary difference using income tax rates and laws expected to be in effect when the asset is realized or the liability is settled. A valuation allowance is established, if necessary, to reduce any future income tax asset to an amount that is more likely than not to be realized.

**Interest-only strip** The interest-only strip represents the present value of the Company's share of the spread to be earned over the collection period on the loans receivable sold (see Note 2). The spread is equal to the yield earned, less the net write-offs and interest expense on the loans receivable sold. The interest-only strip is amortized into income over the collection period based on the projected collection rate.

**Debt discount and other issue expenses** Debt discount and other issue expenses are included in "Long-term receivables and other assets" on the Consolidated Balance Sheets and are amortized over the term of the respective debt issues.

**Deferred expenses** The Company capitalizes both direct and indirect costs with respect to certain ventures which are in the development stage. Capitalization of costs continues until formal operations have commenced, at which time the deferred costs are amortized over a three-year period. Should a venture be abandoned during the development stage, all capitalized costs are immediately expensed. The Company also defers acquisition expenses related to non-retail services and amortizes them into income over the terms of the related contracts. All of the above costs are included in "Long-term receivables and other assets" on the Consolidated Balance Sheets.

**Goodwill and intangible assets** Goodwill represents the excess of the purchase price over the fair value of net assets of acquired businesses. Goodwill is not amortized and is tested for impairment annually, or more frequently if events or changes in circumstances indicate that the asset might be impaired. When the carrying amount of a reporting unit's goodwill exceeds the estimated fair value of the goodwill, an impairment loss is recognized in an amount equal to the excess, if any.

### 1. Significant Accounting Policies (continued)

Intangible assets which have indefinite lives are not amortized, and are tested for impairment annually, or more frequently if events or changes in circumstances indicate that the asset might be impaired. The impairment test compares the carrying amount of the intangible asset with its fair value, and an impairment loss is recognized in an amount equal to the excess, if any. Intangible assets with finite useful lives are amortized over their useful lives and are also subjected to an assessment for impairment.

**Property and equipment** Property and equipment are stated at cost. The cost of real estate includes all direct costs, financing costs on specific and general corporate debt relating to major projects until project completion and certain pre-development costs. Depreciation is provided for using the declining balance method commencing in the month that the equipment or facilities are placed into service. Amortization of leasehold improvements and lease inducements, and lease expense are recognized on a straight-line basis over the terms of the respective leases. Purchased computer software, including direct implementation costs, is amortized on a straight-line basis over a period of up to five years. Depreciation relating to each capital lease for fixtures and equipment and computer software is provided for on a straight-line basis over the term of the lease.

Property and equipment are subjected to an assessment for impairment. Property and equipment assets are grouped with other assets and liabilities to form an asset group at the lowest level for which identifiable cash flows are largely independent of cash flows of other assets and liabilities. An impairment loss is recognized when the carrying amount of property and equipment is not recoverable and exceeds its fair value.

**Asset retirement obligations** Legal obligations associated with site restoration costs on the retirement of property and equipment are recognized in the period in which they are incurred if a reasonable estimate of fair value can be made. The obligations are initially measured at fair value and discounted to present value. A corresponding amount equal to that of the initial obligation is added to the capitalized costs of the related asset. Over time, the discounted asset retirement obligation amount accretes due to the increase in the fair value resulting from the passage of time. This accretion amount is charged to income for the period. The initial costs are depreciated over the useful lives of the related property and equipment.

**Actuarial liabilities** Actuarial liabilities for reinsurance of coverages provided to the Company's credit cardholders include an amount determined from loss reports and individual cases and an amount, based on past experience, for losses incurred but not reported. These estimates are continually reviewed and are necessarily subject to the impact of future changes in such factors as claim severity and frequency. While management believes that the amount is adequate, the ultimate liability may be in excess of, or less than, the amounts provided and any adjustments will be reflected in the periods in which they become known. These amounts are included in "Accounts payable and other" in the Consolidated Balance Sheets.

**Employee future benefits** The Company provides certain health care, dental care, life insurance and other benefits, but not pensions, for certain retired employees pursuant to Company policy. The Company accrues the cost of these employee future benefits over the periods in which the employees earn the benefits. The cost of employee future benefits earned by employees is actuarially determined using the projected benefit method prorated on length of service and management's best estimate of salary escalation, retirement ages of employees, employee turnover and expected health and dental care costs. The discount rate used is based on market rates as at the measurement date. The net actuarial gains and losses that exceed 10% of the accrued benefit obligation are amortized on a straight-line basis over the expected average remaining service life of employees.

**Derivative financial instruments** Derivative financial instruments are utilized by the Company in the management of its foreign currency and interest rate exposures. The Company also enters into equity derivative contracts to hedge certain future stock-based compensation expenses.

The Company assesses all existing derivative financial instruments and designates those that are effective economic hedges of identified risk exposures as hedges. Any gains or losses on these instruments are offset against the item being hedged. The Company documents the relationships between hedging instruments and hedged items, as well as its risk management objectives and strategy for undertaking various hedge transactions. This process includes linking all derivatives to specific assets and liabilities on the Consolidated Balance Sheets or to forecasted transactions. The Company also assesses, both at the hedge's inception and on an ongoing basis, whether the derivatives that are used in hedging transactions are effective in offsetting changes in fair values or cash flows of hedged items.

All derivative financial instruments that do not meet the criteria for hedge accounting are marked to market. The related gains and losses are included in earnings for the period with an offsetting asset or liability being recorded.

The Company enters into foreign exchange contracts, primarily in U.S. dollars, to hedge future purchases of foreign currency denominated goods and services. Foreign exchange translation gains and losses on foreign currency denominated derivative financial instruments used to hedge future purchases are recognized as an adjustment of cost when the purchase is recorded.

Interest rate swap agreements are used as part of the Company's program to manage the fixed and floating interest rate mix of the Company's total debt portfolio and related overall cost of borrowing. The interest rate swap agreements involve the periodic exchange of payments without the exchange of the notional principal amount upon which the payments are based, and are recorded as an adjustment of interest expense on the hedged debt instrument. The related amount payable to or receivable from counterparties is included as an adjustment to accrued interest. Interest to be paid or received under such swap contracts is recognized over the life of the contracts as adjustments to interest expense. Unrealized gains or losses resulting from market movements are not recognized.

Equity derivative contracts are used to hedge the anticipated exposure relating to certain stock-based compensation plans. With respect to equity forwards, the amount to be paid at the expiration of the performance period is included in compensation expense over the life of the hedge period. Unrealized gains or losses resulting from market movement are not recognized.

Realized and unrealized gains or losses associated with derivative instruments, which have been terminated or cease to be effective prior to maturity, are deferred under other current or non-current assets or liabilities on the Consolidated Balance Sheets and are recognized in income in the period in which the underlying hedged transaction is recognized. In the event a designated hedged item is sold, extinguished or matures prior to the termination of the related derivative instrument, any realized or unrealized gain or loss on such derivative instrument is recognized in income immediately.

# Notes to the Consolidated Financial Statements

## 1. Significant Accounting Policies (continued)

**Use of estimates** The preparation of the Consolidated Financial Statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the Consolidated Financial Statements and the reported amount of revenue and expenses during the reporting period. Actual results could differ from these estimates. Estimates are used when accounting for items such as income taxes, impairment of assets, employee benefits, product warranties, inventory provisions, amortization, uncollectible loans receivable, environmental reserves, asset retirement obligations and the liability for the Company's loyalty programs.

## 2. LOANS RECEIVABLE

The Company sells pools of loans receivable ("the Loans") to third party trusts ("the Trusts") in transactions known as securitizations. Loans include both credit card and personal loans receivable. The transactions are accounted for as sales in accordance with Accounting Guideline 12, "Transfers of Receivables" ("AcG-12"), and the Loans are removed from the Consolidated Balance Sheets. The Company retains the interest-only strip, and for the personal loan securitization, a subordinated interest in the loans sold (the "seller's interest") and cash deposited with one of the Trusts (the "securitization reserve"), all of which are retained interests. The seller's interest and securitization reserve provide that Trust with a source of funds in the event that the interest and principal collected on the Loans is not sufficient to pay the Trust's creditors. The Trusts' recourse to the Company is limited to the retained interests. The Company also assumes responsibility for servicing the Loans, for which it does not receive any direct compensation.

The proceeds of the sale are deemed to be the cash received, interest-only strip and securitization reserve, less any servicing obligation assumed. The proceeds are allocated between the Loans, interest-only strip, seller's interest and securitization reserve based on their relative fair value at the date of sale, with any excess or deficiency recorded as a gain or loss on sale respectively. The Company estimates fair values by discounting future cash flows or comparing the appropriate yield curves to matching maturity terms. Retained interests are measured at fair value and are reviewed for impairment on a quarterly basis. For the year ended December 31, 2005, the Company recognized pre-tax gains of \$19.9 million (2004 - \$22.6 million) on the securitization of the Loans.

As the Company does not control the Trusts, they have not been consolidated in these financial statements.

Quantitative information about loans receivable managed and securitized by the Company is as follows:

(Dollars in millions)	Total principal amount of receivables <sup>1</sup>		Average balances <sup>1</sup>	
	2005	2004	2005	2004
Total net managed credit card portfolio	\$ 3,143.4	\$ 2,789.2	\$ 2,818.2	\$ 2,512.6
Credit card receivables sold	(2,422.8)	(2,209.3)	(2,224.2)	(1,889.5)
Credit card receivables held	720.6	579.9	594.0	623.1
Total net managed personal loan portfolio <sup>2</sup>	215.8	64.0	190.0	29.6
Personal loans sold <sup>3</sup>	(176.3)	-	(7.3)	-
Personal loans held	39.5	64.0	182.7	29.6
Total loans receivable	760.1	643.9	\$ 776.7	\$ 652.7
Less: long-term portion <sup>4</sup>	31.4	51.5		
Current portion of loans receivable <sup>5</sup>	\$ 728.7	\$ 592.4		

<sup>1</sup> Amounts shown are net of allowance for credit losses.

<sup>2</sup> Personal loans are unsecured loans that are provided to qualified existing credit cardholders for terms of three to five years. Personal loans have fixed monthly payments of principal and interest; however, the personal loans can be repaid at any time without penalty.

<sup>3</sup> Personal loans totaling \$205.4 million were sold, net of the seller's interest on securitization of \$29.1 million.

<sup>4</sup> The long-term portion of loans receivable is included in "Long-term receivables and other assets". It includes the long-term portion of the seller's interest on securitization of \$21.2 million (2004 - nil).

<sup>5</sup> The current portion of loans receivable includes the current portion of the seller's interest on securitization of \$7.9 million (2004 - nil).

Net credit losses for the year ended December 31, 2005, were \$182.1 million (2004 - \$149.6 million). Net credit losses are charge-offs net of recoveries and are based on the total managed portfolio of loans receivable.

The book value and fair value of the retained interests based on future cash flows are as follows:

(Dollars in millions)	2005		2004	
	Book value	Fair value	Book value	Fair value
Credit card loans	\$ 91.7	\$ 92.6	\$ 80.5	\$ 81.3
Personal loans	47.2	50.1	-	-
Total fair value of retained interests	\$ 138.9	\$ 142.7	\$ 80.5	\$ 81.3

For both the credit card and personal loans, the retained interests include the allowance on securitized receivables and the interest-only strip. For the personal loan securitization, retained interests also include the seller's interest and the securitization reserve.

## 2. Loans Receivable (continued)

The following tables show the key economic assumptions used in measuring the fair value of retained interests at the date of securitization. The tables also display the sensitivity of the current fair value of residual cash flows to immediate 10 percent and 20 percent adverse changes in those assumptions at year end.

### Credit card loans

(Dollars in millions)	Assumptions	Impact of adverse changes on fair value of retained interest <sup>1</sup>		Assumptions
		2005	10%	
Yield <sup>2</sup>	<b>16.55%</b>	\$ (12.9)	\$ (25.7)	16.50%
Liquidation rate <sup>3</sup>	<b>24.05%</b>	(10.3)	(18.9)	23.01%
Expected credit losses <sup>2</sup>	<b>6.01%</b>	(0.1)	(0.3)	5.60%
Discount rate <sup>2</sup>	<b>12.00%</b>	(1.5)	(3.1)	12.00%
Servicing rate <sup>2,4</sup>	<b>2.00%</b>	(0.1)	(0.2)	2.00%

### Personal loans

(Dollars in millions)	Assumptions	Impact of adverse changes on fair value of retained interest <sup>1</sup>		Assumptions
		2005	10%	
Yield <sup>2</sup>	<b>12.53%</b>	\$ (3.0)	\$ (6.0)	N/A
Pre-payment rate <sup>3</sup>	<b>55.48%</b>	(0.4)	(0.7)	N/A
Expected credit losses <sup>2</sup>	<b>3.60%</b>	(0.8)	(1.7)	N/A
Discount rate <sup>2</sup>	<b>8.00%</b>	(0.3)	(0.6)	N/A
Servicing rate <sup>2,4</sup>	<b>1.00%</b>	(0.1)	(0.2)	N/A

<sup>1</sup> These sensitivities are hypothetical and should be used with caution. As the figures indicate, changes in fair value based on a 10 percent or 20 percent variation in assumptions generally cannot be extrapolated because the relationship of the change in assumption to the change in fair value may not be linear. Also, in these tables, the effect of a variation in a particular assumption on the fair value of the retained interest is calculated without changing any other assumption; in reality, changes in one factor may result in changes in another (for example, increases in market interest rates may result in lower payments and increased credit losses), which might magnify or counteract the sensitivities.

<sup>2</sup> Yield, expected credit losses and discount and servicing rates are based on historical patterns.

<sup>3</sup> Based on historical patterns, credit card loans are estimated to be collected in 12 months. Personal loans are collected over terms of three to five years.

<sup>4</sup> The servicing liability as at December 31, 2005 was \$18.2 million (2004 - \$13.5 million).

### Details of cash flows from securitizations:

(Dollars in millions)	2005	2004
Proceeds from new securitizations	\$ <b>541.1</b>	\$ 625.0
Proceeds from collections reinvested in previous securitizations	<b>6,723.0</b>	5,601.0
Other cash flows received on retained interests	<b>1,286.7</b>	1,335.3

## 3. LONG-TERM RECEIVABLES AND OTHER ASSETS

(Dollars in millions)	2005	2004
Interest-only strip	\$ <b>55.6</b>	\$ 41.3
Personal loans (Note 2)	<b>31.4</b>	51.5
Other assets	<b>24.0</b>	15.3
Other receivables	<b>11.9</b>	12.2
Long-term debt issue costs	<b>7.5</b>	7.5
Mortgages receivable	<b>1.7</b>	1.9
	\$ <b>132.1</b>	\$ 129.7

## 4. GOODWILL AND INTANGIBLE ASSETS

The change in the carrying amount of goodwill is as follows:

(Dollars in millions)	CTR	Mark's	Total
Balance, January 1, 2005	\$ 8.8	\$ 32.9	\$ 41.7
Goodwill acquired	0.8	3.7	4.5
Balance, December 31, 2005	\$ <b>9.6</b>	\$ <b>36.6</b>	\$ <b>46.2</b>

# Notes to the Consolidated Financial Statements

## 4. Goodwill and Intangible Assets (continued)

Intangible assets were acquired in February 2002 and March 2005:

(Dollars in millions)	2005	2004
Mark's Work Wearhouse/L'Équipeur store banner	\$ 46.0	\$ 46.0
Mark's private label brands	4.4	4.0
Mark's Franchise Agreements	2.0	2.0
	<b>\$ 52.4</b>	<b>\$ 52.0</b>

These intangible assets are considered to have indefinite lives because they are expected to generate cash flows in perpetuity. There were no writedowns of goodwill or intangible assets due to impairment during 2005 and 2004.

## 5. PROPERTY AND EQUIPMENT

(Dollars in millions)	2005			2004			Depreciation amortization rate/term
	Cost	Accumulated depreciation and amortization	Net book value	Cost	Accumulated depreciation and amortization	Net book value	
Land	\$ 700.5	\$ -	\$ 700.5	\$ 672.1	\$ -	\$ 672.1	
Buildings	2,094.4	704.4	1,390.0	1,987.5	652.5	1,335.0	4%-10%
Fixtures and equipment	528.4	347.5	180.9	470.2	316.4	153.8	10%-33%
Leasehold improvements	265.6	91.3	174.3	201.0	69.0	132.0	Term of lease
Computer software	353.4	209.3	144.1	293.3	173.7	119.6	Up to 5 years
Assets under capital lease	30.3	26.4	3.9	24.8	18.0	6.8	Term of lease
Construction in progress	150.2	-	150.2	165.9	-	165.9	
	<b>\$ 4,122.8</b>	<b>\$ 1,378.9</b>	<b>\$ 2,743.9</b>	<b>\$ 3,814.8</b>	<b>\$ 1,229.6</b>	<b>\$ 2,585.2</b>	

Included in property and equipment are land and buildings held for sale with a cost of \$21.8 million (2004 - \$44.3 million) and accumulated depreciation of \$9.6 million (2004 - \$21.0 million). The Company capitalized interest of \$4.6 million (2004 - \$3.8 million) on indebtedness related to property and equipment under construction.

## 6. LONG-TERM DEBT

(Dollars in millions)	2005	2004
Medium term notes		
5.65% due January 16, 2006	\$ 200.0	\$ 200.0
7.05% due May 18, 2006	-	225.0
5.70% due June 9, 2008	150.0	150.0
4.95% due June 1, 2015	300.0	-
6.25% due April 13, 2028	150.0	150.0
6.32% due February 24, 2034	200.0	200.0
5.61% due September 4, 2035	200.0	-
Debentures, 12.10% maturing May 10, 2010	150.0	150.0
Mortgage payable	14.4	-
Capital lease obligations	4.8	7.9
Other	6.4	4.5
Total long-term debt	<b>1,375.6</b>	<b>1,087.4</b>
Less: amounts due within one year	<b>204.3</b>	<b>5.6</b>
Total - net of current portion	<b>\$ 1,171.3</b>	<b>\$ 1,081.8</b>

**Medium term notes** Certain of the medium term notes are redeemable by the Company, in whole or in part, at any time, at the greater of par and a formula price based upon interest rates at the time of redemption.



6. Long-Term Debt (continued)

**Debentures** The debentures are redeemable by the Company, in whole or in part, at any time, at the greater of par and a formula price based upon interest rates at the time of redemption. Commencing with the quarter ended October 1, 1994 and for each subsequent quarter, the Company may (subject to availability and pricing) be required to purchase up to 1.15 percent of the debentures outstanding at the beginning of such quarter. To date, no such purchases have been made.

**Mortgage payable** A mortgage payable with a maturity date of October 2011 and an interest rate of 7.6 percent was assumed in 2005.

**Capital lease obligations** The fixtures and equipment and computer software under capital leases are the security for the respective obligations. The leases have an average interest rate of 7.99 percent and an average remaining term of 18 months.

**Debt covenants** The Company has provided covenants to certain of its lenders. All of the covenants were complied with during 2005 and 2004.

**Repayment requirements**

(Dollars in millions)	2006	2007	2008	2009	2010	Thereafter	Total
Medium term notes	\$ 200.0	\$ -	\$ 150.0	\$ -	\$ -	\$ 850.0	\$ 1,200.0
Debentures	-	-	-	-	150.0	-	150.0
Mortgage payable	0.3	0.3	0.3	0.4	0.4	12.7	14.4
Capital lease obligations	2.5	1.5	0.8	-	-	-	4.8
Other	1.5	1.5	1.3	0.8	0.7	0.6	6.4
	\$ 204.3	\$ 3.3	\$ 152.4	\$ 1.2	\$ 151.1	\$ 863.3	\$ 1,375.6

On April 1, 2005, the Company completed redemption of \$225.0 million of medium term notes, which were to mature on May 18, 2006, and bore interest at 7.05 percent. As a result of this redemption, the Company paid a contractual make-whole amount, expensed the unamortized balance of related issuance costs and realized a gain from unwinding the related swaps. The net expense of \$5.3 million is included in long-term debt interest expense in 2005.

On May 20, 2005, the Company completed an issuance of \$300.0 million of medium term notes, which mature on June 1, 2015, and bear interest at 4.95 percent.

On September 2, 2005, the Company completed an issuance of \$200.0 million of medium term notes, which mature on September 4, 2035, and bear interest at 5.61 percent.

Subsequent to the end of the fiscal year, on January 16, 2006, medium term notes totaling \$200.0 million, with an interest rate of 5.65%, matured and were repaid.

**7. OTHER LONG-TERM LIABILITIES**

(Dollars in millions)	2005	2004
Employee future benefits (Note 8)	\$ 42.1	\$ 37.6
Asset retirement obligations	12.1	12.9
Other	9.0	5.1
	\$ 63.2	\$ 55.6

# Notes to the Consolidated Financial Statements

## 8. EMPLOYEE FUTURE BENEFITS

The Company provides certain health care, dental care, life insurance and other benefits for certain retired employees pursuant to Company policy. The Company does not have a pension plan. Information about the Company's defined benefit plan is as follows:

(Dollars in millions)	2005	2004
Accrued benefit obligation, beginning of year	\$ 50.1	\$ 44.8
Current service cost	1.8	1.6
Interest cost	3.5	2.8
Benefits paid	(1.7)	(1.6)
Actuarial losses	17.3	2.5
Accrued benefit obligation, end of year <sup>1</sup>	71.0	50.1
Unamortized net actuarial losses	(28.9)	(12.5)
Accrued benefit liability	\$ 42.1	\$ 37.6
Elements of benefit plan costs recognized		
Current service cost	\$ 1.8	\$ 1.6
Interest cost	3.5	2.8
Actuarial losses	17.3	2.5
Elements of employee future benefit costs before adjustments to recognize the long-term nature of employee future benefit costs	\$ 22.6	\$ 6.9
Difference between actuarial loss recognized for the year and actual actuarial loss on accrued benefit obligation for the year	(16.4)	(2.0)
Benefit costs recognized	\$ 6.2	\$ 4.9

<sup>1</sup> The accrued benefit obligation is not funded as funding is provided when benefits are paid. Accordingly, there are no plan assets.

Significant actuarial assumptions used:

	2005	2004
Accrued benefit obligation		
Discount rate	5.00%	5.75%
Benefit costs recognized		
Discount rate	5.75%	6.25%

For measurement purposes, a 10.0 percent annual rate of increase in the per capita cost of covered health care benefits was assumed for 2005 (2004 - 9.5 percent). The rate was assumed to decrease gradually to 4.5 percent for 2014 (2004 - decrease gradually to 4.5 percent for 2009) and remain at that level thereafter. A 4.5 percent annual rate of increase in the per capita cost of covered dental costs was assumed for 2005 and thereafter (2004 - 4.5 percent and thereafter). The expected average remaining service period of the active employees covered by the benefit plan is 16 years (2004 - 12 years).

The most recent actuarial valuation of the obligation was performed as of January 2, 2005. The next required valuation will be as of January 1, 2008.

Sensitivity analysis:

Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plans. A one-percentage-point change in assumed health care cost trend rates would have the following effects for 2005:

(Dollars in millions)	Increase	Decrease
Total of service and interest cost	\$ 1.0	\$ (0.8)
Accrued benefit obligation	12.1	(9.4)

## 9. SHARE CAPITAL

(Dollars in millions)		2005	2004
Authorized			
3,423,366	Common Shares		
100,000,000	Class A Non-Voting Shares		
Issued			
3,423,366	Common Shares (2004 – 3,423,366)	\$ 0.2	\$ 0.2
78,032,724	Class A Non-Voting Shares (2004 – 77,699,631)	702.5	708.8
		\$ 702.7	\$ 709.0

During 2005 and 2004, the Company issued and repurchased Class A Non-Voting Shares. The net excess of the repurchase price over the issue price is allocated to retained earnings.

The following transactions occurred with respect to Class A Non-Voting Shares during 2005 and 2004:

(Dollars in millions)	2005		2004	
	Number	\$	Number	\$
Shares outstanding at the beginning of the year	77,699,631	\$ 708.8	77,337,718	\$ 700.3
Issued				
Dividend reinvestment plan	33,910	2.0	30,843	1.4
Stock option plan	1,032,445	25.9	1,213,062	28.4
Employee stock purchase plan	386,119	22.7	449,186	20.8
Employee profit sharing plan	52,900	3.2	65,958	3.0
Associate Dealer profit sharing plans	112,219	6.6	143,964	6.6
Repurchased	(1,284,500)	(83.7)	(1,541,100)	(73.8)
Excess of repurchase price over issue price	-	17.0	-	22.1
Shares outstanding at the end of the year	78,032,724	\$ 702.5	77,699,631	\$ 708.8

Since 1988 the Company has followed an anti-dilution policy. The Company repurchases shares to substantially offset the dilutive effects of issuing Class A Non-Voting Shares pursuant to various corporate programs.

Subsequent to the end of the fiscal year, from January 1, 2006 to March 9, 2006, the Company issued 113,715 Class A Non-Voting Shares for proceeds of \$6.5 million and repurchased 36,300 Class A Non-Voting Shares for \$2.4 million.

The reconciliation of the number of shares used in the diluted earnings per share calculation is as follows:

	2005	2004
Average number of shares for basic earnings per share calculations	81,764,082	80,983,467
Dilutive options	1,132,320	1,523,889
Average number of shares for diluted earnings per share calculations	82,896,402	82,507,356

**Conditions of Class A Non-Voting Shares and Common Shares** The holders of Class A Non-Voting Shares are entitled to receive a preferential cumulative dividend at the rate of \$0.01 per share per annum. After payment of a dividend on each of the Common Shares at the same rate, the holders of the Class A Non-Voting Shares and the Common Shares are entitled to further dividends declared and paid in each year in equal amounts per share. In the event of liquidation, dissolution or winding-up of the Company, the Class A Non-Voting Shares and Common Shares rank equally with each other on a share-for-share basis.

The holders of Class A Non-Voting Shares are entitled to receive notice of and to attend all meetings of the shareholders but, except as provided by the *Business Corporations Act* (Ontario) and as hereinafter noted, are not entitled to vote thereat. Holders of Class A Non-Voting Shares, voting separately as a class, are entitled to elect the greater of: (i) three Directors or (ii) one-fifth of the total number of the Company's Directors.

Common Shares can be converted, at any time, into Class A Non-Voting Shares on a share-for-share basis. The authorized number of shares of either class cannot be increased without the approval of the holders of the other class. Neither the Class A Non-Voting Shares nor the Common Shares can be changed by way of subdivision, consolidation, reclassification, exchange or otherwise unless at the same time the other class of shares is also changed in the same manner and in the same proportion.

Should an offer to purchase Common Shares be made to all or substantially all of the holders of Common Shares (other than an offer to purchase both Class A Non-Voting Shares and Common Shares at the same price and on the same terms and conditions) and should a majority of the Common Shares then issued and outstanding be tendered and taken up pursuant to such offer, the Class A Non-Voting Shares shall thereupon be entitled to one vote per share at all meetings of the shareholders.

# Notes to the Consolidated Financial Statements

## 9. Share Capital (continued)

The foregoing is a summary of certain of the conditions attached to the Class A Non-Voting Shares of the Company and reference should be made to the Company's articles for a full statement of such conditions.

As at December 31, 2005, the Company had dividends payable to Class A Non-Voting and Common shareholders of \$11.8 million (2004 - \$10.1 million).

## 10. STOCK-BASED COMPENSATION PLANS

The following describes the Company's stock-based compensation plans.

**Employee Profit Sharing Plan** The Company offers its employees a Deferred Profit Sharing Plan ("DPSP"). The amount of the award is contingent on the Company's profitability. The maximum contribution is 6.75 percent of earnings before income taxes and minority interest, after certain adjustments. The maximum amount of the Company's contribution to the DPSP per employee per year is subject to limits set by the Canada Revenue Agency. The DPSP is required to invest and maintain 10 percent of its holdings in the Company's Class A Non-Voting Shares. The Company's contributions to the DPSP vest 20 percent after one year of continuous service and 100 percent after two years of continuous service.

In 2005, of the employee profit sharing plan expense for the prior year, the Company contributed \$15.6 million (2004 - \$15.0 million) under terms of the DPSP, towards the Trustee-managed investment portfolio. As of December 31, 2005, the DPSP held 419,280 Common Shares (2004 - 419,280) and 1,031,090 Class A Non-Voting Shares (2004 - 1,317,407) of the Company.

**Employee Stock Purchase Plan** The Company offers an Employee Stock Purchase Plan ("ESPP") to its employees, whereby employees can choose to have up to 10 percent of their annual base earnings withheld to purchase Class A Non-Voting Shares of the Company. The purchase price of the shares is calculated monthly and is equal to the weighted average share price at which Class A Non-Voting Shares of the Company trade on the Toronto Stock Exchange for a given month. The Company may elect to match up to 50 percent of employee contributions to the ESPP. The Company's matching contribution vests in increments of 10 percent for every year of an employee's service.

In return for employee contributions, the Company issued to employees 386,119 Class A Non-Voting shares in 2005 (2004 - 449,186). The Company's matching contribution of \$10.1 million in 2005 (2004 - \$9.4 million) was used to purchase Class A Non-Voting shares on the Toronto Stock Exchange. In addition, the Company recorded as compensation expense \$5.8 million (2004 - \$5.8 million) for reimbursement of employee income tax liabilities relating to the ESPP.

**Deferred Share Unit Plan** The Company offers a Deferred Share Unit Plan ("DSUP") for members of the Board of Directors. Under the DSUP, each Director may elect to receive all or a percentage of his or her annual compensation in the form of notional Class A Non-Voting Shares of the Company called deferred share units ("DSUs"). The issue price of each DSU is equal to the weighted average share price at which Class A Non-Voting Shares of the Company trade on the Toronto Stock Exchange during the 10-day period prior to the last day of the quarter in which the DSU is issued. A Director must elect to participate or change his or her participation in the DSUP prior to the beginning of a fiscal quarter. The DSU account of each Director includes the value of dividends, if any, as if reinvested in additional DSUs. The Director is not permitted to convert DSUs into cash until retirement from the Board. The value of the DSUs, when converted to cash, will be equivalent to the market value of the Class A Non-Voting Shares at the time the conversion takes place. The value of the outstanding DSUs as at December 31, 2005, was \$5.5 million (2004 - \$3.8 million).

**Restricted Share Unit Plan** The Company has granted restricted share units ("RSUs") to certain employees which entitle the participant to receive a cash payment in an amount equal to the weighted average closing price of Class A Non-Voting shares traded on the Toronto Stock Exchange for the 20-day period prior to and including the last day of the restriction period, multiplied by an applicable multiplier if specific performance-based criteria are met. The restriction period is a maximum of three years less 30 days from the date of grant. Compensation expense related to the RSUs is accrued over the term of the RSU based on the expected total compensation to be paid out at the end of the restriction period, factoring in the impact of the probability of any performance-based criteria being met during the restriction period and the impact of the equity derivative contracts used to hedge the anticipated exposure relating to RSUs. As the end of the restriction period was October 3, 2003 and all RSUs were settled with cash payments, no compensation expense was recorded for the year ended December 31, 2005, in respect of this plan (2004 - nil).

**Performance Share Unit Plan** The Company has granted performance share units ("PSUs") to certain employees. Each PSU entitles the participant to receive a cash payment in an amount equal to the weighted average closing price of Class A Non-Voting shares traded on the Toronto Stock Exchange for the 20-day period prior to and including the last day of the performance period, multiplied by an applicable multiplier determined by specific performance-based criteria. The performance period is a maximum of three years less 45 days from the date of grant. Compensation expense related to the PSUs is accrued over the term of the performance period based on the expected total compensation to be paid out at the end of the performance period, factoring in the probability of any performance-based criteria being met during that period. The compensation expense recorded for the year ended December 31, 2005 in respect of this plan was \$6.4 million (2004 - \$14.4 million).

**Performance Conditioned Share Unit Plan** The Company has granted performance conditioned share units ("PCSUs") to certain employees. Each PCSU entitles the participant to receive a cash payment in an amount equal to the weighted average closing price of Class A Non-Voting shares traded on the Toronto Stock Exchange for the 20-day period prior to and including the last day of the performance period, multiplied by applicable multipliers determined by specific performance-based criteria. Compensation expense related to PCSUs is accrued over the term of the performance period based on the expected total compensation to be paid out at the end of the performance period, factoring in the probability of any performance-based criteria being met during that period. Compensation expense for PCSUs for the year ended December 31, 2005 was \$6.4 million (2004 - \$1.6 million).

10. Stock-based Compensation Plans (continued)

**Performance Driven Share Unit Plan** In 2005, the Company granted performance driven share units (PDSUs) to certain employees. Each PSU entitles the participant to receive a cash payment in an amount equal to the weighted average share price of Class A Non-Voting shares traded on the Toronto Stock Exchange for the 20-day period prior to and including the last day of the performance period. Compensation expense related to PDSUs is accrued over the term of the performance period based on the expected total compensation to be paid out at the end of the performance period. The compensation expense recorded for PDSUs for the year ended December 31, 2005 was \$4.5 million (2004 - nil)

**Deferred Share Unit Plan for an Executive** In 2005, the Company granted deferred share units (DSUs) to an Executive. The DSU account for the Executive includes the value of dividends, if any, as if reinvested in additional DSUs. Each DSU entitles the Executive to receive a cash payment in an amount equal to the weighted average share price of Class A Non-Voting shares traded on the Toronto Stock Exchange on the tenth business day prior to the settlement date. Compensation expense related to these DSUs for the year ended December 31, 2005 was \$1.6 million (2004 - nil).

**Stock options** The Company has granted options to certain employees for the purchase of Class A Non-Voting Shares, with vesting occurring on a graduated basis over a four-year period. The exercise price of each option equals the weighted average closing price of Class A Non-Voting shares on the Toronto Stock Exchange for the 10-day period preceding the date of grant. Options are exercisable over a term of 10 years. The aggregate number of Class A Non-Voting Shares issuable under the stock option plan may not exceed 11.0 million Class A Non-Voting Shares.

The compensation expense recorded for the year ended December 31, 2005, in respect of stock options granted on or after December 29, 2002 was \$0.7 million (2004 - \$0.8 million). The counterpart is recorded as contributed surplus. Any consideration paid by employees on exercise of stock options is credited to share capital.

No stock options were granted in 2005 or 2004. The weighted average grant-date fair value of options granted in 2003 was estimated at \$6.99 per option using the Black-Scholes model for valuing options. The following weighted average assumptions were used: expected dividend yield of 1.47 percent per annum, risk-free interest rate of 4.5 percent per annum, expected stock price volatility of 27.4 percent and expected option life of 3.5 years.

The outstanding options as at December 31, 2005 were granted at prices between \$16.47 and \$41.47 and expire between March 2007 and November 2013.

Stock option transactions during 2005 and 2004 were as follows:

	2005		2004	
	Number of options	Weighted average exercise price	Number of options	Weighted average exercise price
Outstanding at beginning of year	2,733,588	\$ 26.95	4,032,126	\$ 25.79
Granted	-	-	-	-
Exercised	(1,032,446)	24.53	(1,213,062)	23.23
Forfeited and expired	(51,165)	28.02	(85,476)	24.84
Outstanding at end of year	1,649,977	\$ 28.43	2,733,588	\$ 26.95
Stock options exercisable at end of year	1,280,801		1,884,558	

The following table summarizes information about stock options outstanding at December 31, 2005:

Range of exercise prices	Options outstanding			Options exercisable	
	Number of outstanding options	Weighted average remaining contractual life <sup>1</sup>	Weighted average exercise price	Number exercisable	Weighted average exercise price
\$ 33.07 to 41.47	370,925	3.73	\$ 38.42	352,025	\$ 38.58
28.84 to 31.61	406,525	6.37	29.93	195,290	30.18
25.42 to 28.55	521,315	5.36	25.97	402,274	26.13
16.47 to 25.32	351,212	4.88	19.78	331,212	19.48
\$ 16.47 to 41.47	1,649,977	5.14	\$ 28.43	1,280,801	\$ 28.45

<sup>1</sup> Weighted average remaining contractual life is expressed in years.



# Notes to the Consolidated Financial Statements

## 10. Stock-based Compensation Plans (continued)

**Pro forma stock option disclosure** Had the fair-value based method been used to expense stock options granted between December 30, 2001 and December 28, 2002, the Company's net earnings would have decreased to the pro forma amounts indicated below:

(Dollars in millions except per share amounts)	2005	2004
Net earnings:		
As reported	\$ 330.1	\$ 291.5
Pro forma	328.8	290.1
Basic earnings per share:		
As reported	4.04	3.60
Pro forma	4.02	3.58
Diluted earnings per share:		
As reported	3.98	3.53
Pro forma	3.97	3.52

## 11. INCOME TAXES

Income taxes in the Consolidated Statements of Earnings vary from amounts that would be computed by applying the statutory income tax rate for the following reasons:

(Dollars in millions)	2005	2004
Income taxes based on a combined Canadian federal and provincial income tax rate of 35.51% (2004 - 35.42%)	\$ 187.4	\$ 163.3
Adjustment to income taxes resulting from:		
Large corporations tax	1.6	2.6
Lower income tax rate on earnings of foreign subsidiaries	(4.1)	(9.3)
Other (including non-deductible items and prior year tax adjustments)	5.1	5.9
Income tax expense	\$ 190.0	\$ 162.5

The following are the components of the income tax provision:

(Dollars in millions)	2005	2004
Current tax expense	\$ 187.2	\$ 150.8
Future income tax expense relating to the origination and reversal of temporary differences	2.5	11.5
Future income tax expense resulting from change in tax rate	0.3	0.2
Income tax expense	\$ 190.0	\$ 162.5

The tax-effected temporary differences which result in future income tax assets and (liabilities) are as follows:

(Dollars in millions)	2005	2004
Current		
Reserves and deferred income	\$ 52.2	\$ 31.4
Deferred items	(11.8)	(9.0)
Other	3.2	2.2
Current future income taxes	\$ 43.6	\$ 24.6
Long-term		
Reserves and deferred income	\$ 2.6	\$ 6.4
Employee future benefits	15.1	13.4
Property and equipment	(75.1)	(51.8)
Deferred items	(23.5)	(29.8)
Intangible assets	(9.5)	(9.3)
Other	1.4	3.9
Long-term future income taxes	\$ (89.0)	\$ (67.2)

11. Income Taxes (continued)

In the ordinary course of business, the Company is subject to ongoing audits by tax authorities. While the Company believes that its tax filing positions are appropriate and supportable, the possibility exists that certain matters may be reviewed and challenged by the tax authorities. The Company regularly reviews the potential for adverse outcomes and the adequacy of its tax provisions. The Company believes that it has adequately provided for these matters. Should the ultimate outcome materially differ from the provisions, the Company's effective tax rate and its earnings could be affected positively or negatively in the period in which the matters are resolved.

**12. NOTES TO THE CONSOLIDATED STATEMENTS OF CASH FLOWS**

**Working capital components**

(Dollars in millions)	<b>2005</b>	2004
Cash generated from (used for):		
Accounts receivable	\$ (329.3)	\$ (185.6)
Merchandise inventories	(50.9)	(154.3)
Prepaid expenses and deposits	(18.3)	3.8
Accounts payable and other	88.1	175.8
Income taxes payable	27.0	(53.1)
Other	0.3	(3.9)
Change in other working capital components	\$ (283.1)	\$ (217.3)

**Cash and cash equivalents**

The components of cash and cash equivalents are:

(Dollars in millions)	<b>2005</b>	2004
Cash	\$ (70.5)	\$ (34.3)
Short-term investments	908.5	836.5
Cash and cash equivalents	\$ 838.0	\$ 802.2

**Supplementary information** For the year ended December 31, 2005, the Company paid income taxes amounting to \$155.8 million (2004 - \$200.0 million) and interest payments of \$83.5 million (2004 - \$78.3 million).

**Sale of Associate Dealer receivables** During 2005 and 2004, the Company sold certain Associate Dealer receivables to independent investors. According to the terms of the sale, the Company retained full servicing responsibilities for which it received no compensation. For the year ended December 31, 2005, the Company recognized a loss of \$0.1 million (2004 - \$2.1 million) on the sale of Associate Dealer receivables, which assumes no expected credit losses and a servicing liability of 1.0 percent. Quantitative information about accounts receivable managed by the Company is as follows:

(Dollars in millions)	Total principal amount of receivables	
	<b>2005</b>	2004
Associate Dealer receivables	\$ 570.2	\$ 543.3
Associate Dealer receivables sold	(47.9)	(323.2)
Other accounts receivable	130.5	150.6
Accounts receivable	\$ 652.8	\$ 370.7

# Notes to the Consolidated Financial Statements

## 13. OPERATING LEASES

The Company is committed to minimum annual rentals (exclusive of taxes, insurance, and other occupancy charges) for equipment and properties under leases with termination dates extending to 2043. Under sublease arrangements with Associate Dealers, the majority of the properties are income-producing.

The minimum annual rental payments for equipment and property are as follows:

(Dollars in millions)

2006	\$	160.0
2007		143.3
2008		132.1
2009		117.7
2010		106.7
2011-2043		607.6
	\$	1,267.4

## 14. GUARANTEES, COMMITMENTS AND CONTINGENCIES

**Guarantees** In the normal course of business, the Company enters into numerous agreements that may contain features that meet the definition of a guarantee. A guarantee is defined to be a contract (including an indemnity) that contingently requires the Company to make payments to the guaranteed party based on (i) changes in an underlying interest rate, foreign exchange rate, equity or commodity instrument, index or other variable, that is related to an asset, a liability or an equity security of the counterparty, (ii) failure of another party to perform under an obligating agreement, or (iii) failure of a third party to pay its indebtedness when due.

The Company has provided the following significant guarantees to third parties:

**Standby letters of credit and performance guarantees** The Company has arranged for several major Canadian banks to provide standby letters of credit (the "LCs") to an independent trust (the "Independent Trust"), which provides loans to Associate Dealers for their purchase of inventory and fixed assets (the "Associate Dealer Loans"). During 2004, the Independent Trust sold all of its rights in the LCs and the then outstanding Associate Dealer Loans to other independent trusts set up by major Canadian banks (the "Co-owner Trusts") that raise funds in the capital markets to finance their purchase of these undivided co-ownership interests. As a result, the Independent Trust's only remaining role is that of originator, seller and servicer of the Associate Dealer Loans. Total Associate Dealer Loans as at December 31, 2005 were \$784.4 million (2004 - \$793.6 million).

In the event that an Associate Dealer defaults on a loan, the Company has the right to purchase such loan from the Co-owner Trusts, at which time the Co-owner Trusts will assign such Associate Dealer's debt instrument and related security documentation to the Company. The assignment of this documentation provides the Company with first priority security rights over all of such Associate Dealer's assets, subject to certain prior ranking statutory claims. In most cases, the Company would expect to recover any payments made to purchase a defaulted loan, including any associated expenses. In the event the Company does not elect to purchase a defaulted Associate Dealer Loan, the Co-owner Trusts may draw against the LCs.

The Co-owner Trusts may also draw against the LCs to cover any shortfalls in certain related fees owing to them. In any case where a draw is made against the LCs, the Company has agreed to reimburse the bank issuing the LCs for the amount so drawn. In the unlikely event that all the LCs were fully drawn simultaneously, the maximum payment by the Company under this reimbursement obligation would have been \$117.0 million at December 31, 2005 (2004 - \$133.5 million). The Company has not recorded any liability for these amounts, due to the credit quality of the Associate Dealer Loans and to the nature of the underlying collateral, represented by the inventory and fixed assets of the borrowing Associate Dealers.

**Business and property dispositions** In connection with agreements for the sale of all or a part of a business and in addition to indemnifications relating to failure to perform covenants and breach of representations and warranties, the Company has agreed to indemnify the purchasers against claims from its past conduct of the business, including environmental remediation. Typically, the term and amount of such indemnification will be determined by the agreement. The nature of these indemnification agreements prevents the Company from estimating the maximum potential liability it would be required to pay to counterparties. Historically, the Company has not made any significant indemnification payments under such agreements and no amount has been accrued in the Consolidated Financial Statements with respect to these indemnification agreements.

**Lease agreements** The Company has entered into agreements with certain of its lessors that guarantee the lease payments of certain sub-lessees of its facilities to lessors. Generally, these lease agreements relate to facilities the Company has vacated prior to the end of the term of its lease. These lease agreements require the Company to make lease payments throughout the lease term if the sub-lessee fails to make the scheduled payments. These lease agreements have expiration dates through July 2010. The Company has also guaranteed leases on certain franchise stores in the event the franchisees are unable to meet their remaining lease commitments. These lease agreements have expiration dates through January 2016. The maximum amount that the Company may be required to pay under both of these types of agreements is \$9.7 million (2004 - \$11.6 million), except for one lease agreement for which the maximum amount cannot be reasonably estimated. In addition, the Company could be required to make payments for percentage rents, realty taxes and common area costs. No amount has been accrued in the Consolidated Financial Statements with respect to these lease agreements.

**Third party debt agreements** The Company has guaranteed the debt of certain PartSource franchisees and Associate Dealers. These third party debt agreements require the Company to make payments if the franchisee or Associate Dealer fails to make scheduled debt payments. The majority of these third party debt agreements have expiration dates extending to January 31, 2006. The maximum amount that the Company may be required to pay under these types of debt agreements is \$8.5 million (2004 - \$4.9 million). No amount has been accrued in the Consolidated Financial Statements with respect to these debt agreements.

14. Guarantees, Commitments and Contingencies (continued)

**Indemnification of lenders and agents under credit facilities** In the ordinary course of business, the Company has agreed to indemnify its lenders under various credit facilities against costs or losses resulting from changes in laws and regulations which would increase the lenders' costs and from any legal action brought against the lenders related to the use of the loan proceeds. These indemnifications generally extend for the term of the credit facilities and do not provide any limit on the maximum potential liability. Historically, the Company has not made any significant indemnification payments under such agreements and no amount has been accrued in the Consolidated Financial Statements with respect to these indemnification agreements.

**Other indemnification commitments** In the ordinary course of business, the Company provides indemnification commitments to counterparties in transactions such as leasing transactions, service arrangements, investment banking agreements, securitization agreements, indemnification of trustees under indentures for outstanding public debt, director and officer indemnification agreements, escrow agreements, price escalation clauses, sales of assets (other than dispositions of businesses discussed above) and the arrangements with the Independent Trust and Co-owner Trusts discussed above. These indemnification agreements require the Company to compensate the counterparties for certain amounts and costs incurred, including costs resulting from changes in laws and regulations (including tax legislation) or as a result of litigation claims or statutory sanctions that may be suffered by a counterparty as a consequence of the transaction. The terms of these indemnification agreements will vary based on the contract and do not provide any limit on the maximum potential liability. Historically, the Company has not made any significant payments under such indemnifications and no amount has been accrued in the Consolidated Financial Statements with respect to these indemnification commitments.

**Other commitments and contingencies** As at December 31, 2005, the Company had the following other commitments and contingencies. In accordance with Canadian generally accepted accounting principles, the Company has not recognized a liability relating to these commitments and contingencies except for a provision for legal proceedings:

The Company has obtained documentary and standby letters of credit aggregating \$34.9 million (2004 - \$33.2 million) relating to the importation of merchandise inventories and to facilitate various real estate activities for the Company's merchandise operations.

The Company has commitments of approximately \$72.4 million (2004 - \$37.9 million) for the acquisition of property and equipment and the expansion of retail store facilities during 2006.

The Company has committed to pay a minimum of \$39.7 million (2004 - \$47.0 million) in total to third parties for credit card processing services (to 2009) and information technology services (to 2008).

The Company has committed to pay a minimum of \$15.7 million (2004 - \$18.4 million) for various commitments and contingent liabilities including merchandise inventory buy-back agreements, a customs bond, and the guarantee of a franchisee's total indebtedness.

The Company has an agreement to buy back one Mark's franchise store at an estimated total amount of \$0.9 million if that franchisee defaults on its bank indebtedness or becomes insolvent (2004 - general obligation to buy back eight stores at an estimated total amount of \$3.8 million).

The Company and certain of its subsidiaries are party to a number of legal proceedings. The Company believes that each such proceeding constitutes routine litigation incidental to the business conducted by the Company and that the ultimate disposition of the proceedings will not have a material adverse effect on its consolidated earnings, cash flow or financial position.

## 15. FINANCIAL INSTRUMENTS

The purpose of this Note is to disclose the Company's exposure related to financial instruments.

The Company enters into interest rate swap contracts with approved creditworthy counterparties to manage the Company's current and anticipated exposure to interest rate risks. The Company has also entered into interest rate swap contracts ("Trust Swaps") with an independent trust to manage the interest rate exposure of the trust during the period in advance of repayment by the trust of fixed rate debt used to finance the purchase of the Company's loans receivable. The Company also enters into foreign exchange contracts, primarily in U.S. dollars, to hedge future purchases of foreign currency denominated goods and services with an emphasis on those purchases that are expected to be completed within a six-month period. Neither the notional principal amounts nor the current replacement value of these outstanding financial instruments is carried on the Consolidated Balance Sheets. The Company also enters into equity derivative contracts to hedge certain future stock-based compensation expenses. The Company does not hold or issue derivative financial instruments for trading or speculative purposes, and controls are in place to detect and prevent these activities.

During 2004, the Company entered into an equity derivative contract to hedge a portion of the PCSUs (Note 10). The premium paid of \$6.9 million will be amortized over the term of the contract. As at December 31, 2005, the unamortized portion of the premium was \$3.1 million (2004 - \$5.6 million) and is included in "Long-term receivables and other assets". The contract terminates on March 9, 2007, at which time the Company will be entitled to receive an amount based on the share price of the Class A Non-Voting Shares of the Company. Since the contract is considered a hedge for accounting purposes, as at December 31, 2005, a derivative asset in the amount of \$6.6 million (2004 - \$1.2 million) is included in "Long-term receivables and other assets". This asset offsets the accrued compensation liability that is being recorded for PCSUs.

As at December 31, 2005, outstanding off-balance sheet financial instruments of the Company are summarized as follows:

(Dollars in millions)	Notional amounts maturing				2005 Total	2004 Total
	Within 1 year	Over 1 to 5 years	Over 5 to 10 years	Over 10 years		
Interest rate swap contracts	\$ 316.6	\$ 674.8	\$ -	\$ 100.0	\$ 1,091.4	\$ 1,470.4
Foreign exchange contracts <sup>1</sup>	1,661.7	67.0	-	-	1,728.7	1,358.3

<sup>1</sup> May include both forward contracts and options.

# Notes to the Consolidated Financial Statements

## 15. Financial Instruments (continued)

For the year ended December 31, 2005, interest expense included a net receipt of approximately \$6.5 million (2004 - \$8.1 million) relating to interest rate swaps. Any unsettled interest differentials outstanding at year end were accrued for and included in "Accounts payable and other". For the year ended December 31, 2005, the Company recorded a net gain of \$0.4 million (2004 - \$1.8 million net loss) in gross operating revenue relating to the Trust Swaps.

The estimated fair values of financial instruments as at December 31, 2005 and January 1, 2005 are based on relevant market prices and information available at that time. The fair-value estimates below are not necessarily indicative of the amounts that the Company might receive or pay in actual market transactions. For financial instruments which are short-term in nature, carrying value approximates fair value.

The fair values of other financial instruments are as follows:

(Dollars in millions)	2005		2004	
	Book value	Fair value	Book value	Fair value
<b>Financial assets and liabilities</b>				
Interest-only strip	\$ 55.6	\$ 60.1	\$ 41.3	\$ 42.2
Long-term personal loans, mortgages and other receivables	45.0	41.8	65.6	59.1
Equity derivative contracts	11.8	20.6	6.8	8.4
Securitization reserve	4.1	3.4	-	-
Long-term debt (excluding current portion)	(1,171.3)	(1,257.4)	(1,081.8)	(1,163.4)
<b>Off-balance sheet financial instruments</b>				
Interest rate swap contracts	\$ -	\$ (15.5)	\$ -	\$ (4.6)
Foreign exchange contracts <sup>1</sup>	-	(29.6)	-	(60.3)

<sup>1</sup> The average effective rate of Canadian to U.S. dollars at December 31, 2005 was \$1.1871 (2004 - \$1.2856).

The fair values of the interest-only strip, long-term personal loans, mortgages and other receivables, securitization reserve, long-term debt (excluding current portion) and interest rate swap contracts were estimated based on: quoted market prices (when available); discounted cash flows, using discount rates based on prevailing market interest rates and the Company's credit rating; or by comparing the appropriate yield curves to matching maturity terms as at year end. The foreign exchange contracts were valued based on the differential between contract rates and year-end spot rates, and reflect the time value of money. The equity derivative contracts were valued by the counterparties based on year-end market interest rates, implied Company volatility values and the year-end closing share price of the Class A Non-Voting Shares of the Company on the Toronto Stock Exchange. For interest rate swap, foreign exchange and equity derivative contracts, the fair values reflect the estimated amounts that the Company would receive or pay if it were to unwind the contracts at the reporting date.

**Interest rate risk** The following table identifies the Company's financial assets and liabilities which are sensitive to interest rate movements and those which are non-interest rate sensitive as they are either non-interest bearing or bear interest at fixed rates.

(Dollars in millions)	2005		2004	
	Interest sensitive	Non-interest sensitive	Interest sensitive	Non-interest sensitive
Cash and cash equivalents	\$ 838.0	\$ -	\$ 802.2	\$ -
Loans receivable	-	728.7	-	592.4
Long-term personal loans, mortgages and other receivables	-	45.0	-	65.6
Long-term debt (including current portion)	-	(1,375.6)	-	(1,087.4)
	\$ 838.0	\$ (601.9)	\$ 802.2	\$ (429.4)

The Company enters into interest rate swap contracts to manage its exposure to interest rate risk. As at December 31, 2005, the Company had entered into contracts that exchanged a net notional amount of \$591.4 million from floating to fixed rate debt (2004 - \$ 720.4 million exchanged from floating to fixed). These contracts hedge the Company's net balance sheet interest rate sensitivity position. A one percent change in interest rates would not materially affect the Company's earnings, cash flow or financial position.

**Credit risk** The Company's exposure to concentrations of credit risk is limited. Accounts receivable are primarily from Associate Dealers who individually comprise less than one percent of the total balance outstanding and are spread across Canada. Similarly, loans receivable are generated by credit card and personal loan customers, a large and geographically dispersed group. Current credit exposure is limited to the loss that would be incurred if all of the Company's counterparties were to default at the same time.

The credit exposure with respect to hedges and similar financial instruments is the current replacement value of only those contracts which are in a gain position. As at December 31, 2005, the credit exposure due to interest rate swap and foreign exchange contracts was \$25.4 million (2004 - \$11.0 million). The Company believes that its exposure to credit and market risks for these instruments is negligible.

## 16. SEGMENTED INFORMATION

The Company's reportable operating segments are strategic business units that offer different products and services. The Company has four reportable operating segments: Canadian Tire Retail ("CTR"), Canadian Tire Financial Services ("Financial Services"), Canadian Tire Petroleum ("Petroleum") and Mark's Work Wearhouse ("Mark's"). CTR derives its revenue primarily from shipments of merchandise to Associate Dealers and PartSource franchisees. Financial Services is primarily engaged in financing and managing customer credit accounts that arise from customers' use of their Canadian Tire credit cards and also derives revenue from a personal loan portfolio and from ancillary products such as extended warranty contracts. Petroleum revenue arises primarily from the sale of petroleum products through its agents. Mark's revenue arises from the sale of merchandise to customers from its corporate-owned stores.

The accounting policies of the segments are the same as those described in the significant accounting policies in Note 1. The Company evaluates each segment's performance based on earnings before income taxes and minority interest. The only significant non-cash item included in segment earnings before income taxes and minority interest is depreciation and amortization.

(Dollars in millions)	CTR		Financial Services		Petroleum		Mark's		Eliminations		Total	
	2005	2004	2005	2004	2005	2004	2005	2004	2005	2004	2005	2004
Gross operating revenue <sup>1</sup>	\$ 5,108.2	\$ 4,899.0	\$ 685.8	\$ 611.3	\$ 1,330.1	\$ 1,105.9	\$ 664.4	\$ 546.1	\$ (13.9)	\$ (8.7)	\$ 7,774.6	\$ 7,153.6
Earnings before income taxes and minority interest	290.2	271.9	165.0	148.5	7.5	3.4	65.0	37.1	-	-	527.7	460.9
Income taxes											(190.0)	(162.5)
Minority interest											(7.6)	(6.9)
Net earnings											\$ 330.1	\$ 291.5
Interest revenue <sup>2</sup>	\$ 24.6	\$ 18.5	\$ 13.6	\$ 10.2	\$ -	\$ -	\$ -	\$ -	\$ (28.5)	\$ (20.5)	\$ 9.7	\$ 8.2
Interest expense <sup>2</sup>	96.5	86.7	13.5	9.4	-	-	2.6	2.8	(28.5)	(20.5)	84.1	78.4
Depreciation and amortization	143.5	129.6	12.5	14.1	14.4	13.0	14.6	13.9	-	-	185.0	170.6
Total assets	4,604.7	3,988.0	1,350.9	1,174.7	494.5	509.8	342.9	333.1	(837.4)	(762.4)	5,955.6	5,243.2
Capital expenditures	315.1	289.0	14.8	7.2	28.6	26.6	32.6	17.9	-	-	391.1	340.7

<sup>1</sup> Gross operating revenue includes dividend and interest revenue.

<sup>2</sup> Interest revenue and expense are not allocated to Petroleum.

## 17. MINORITY INTEREST

In November 2001, the Company formed a limited partnership for the purpose of raising \$300 million of capital in relation to a portfolio of its retail properties. The Company is the general partner in this partnership. A third party investor group invested \$300 million in the partnership for a limited partnership interest with preferential rights to distribution of income and capital. The limited partnership interest is entitled to a cumulative, quarterly preferred distribution on its capital account (approximately 3.98% for the 52 weeks ended December 31, 2005 (2004 - 3.59%)) and the partnership intends to follow a full distribution policy. The partnership invested in the retail properties by way of a note and equity in an entity that owns the portfolio of properties. The note matures in November 2006 and may be renewed. The partnership has an indefinite life, but could be liquidated in certain circumstances including shortfalls in cash flows generated by the retail properties and repayment of the note. The assets and liabilities, results of operations and cash flows of the partnership are included in the financial statements of the Company. The preferred interest is treated as minority interest on the Consolidated Balance Sheets and in the Consolidated Statements of Earnings. The Company has not recognized a gain or loss on the formation of the partnership.

## 18. COMPARATIVE FIGURES

Certain of the prior period's figures have been reclassified to conform to the current year presentation.

## 19. SUBSEQUENT EVENT

On November 29, 2005, the Company announced its agreement to sell and leaseback two distribution centres to a third party. On January 31, 2006, the Company and the third party completed the sale and leaseback agreements for the two distribution centres. The proceeds from the sale of the two distribution centres totaled \$229 million, resulting in a net pre-tax gain of approximately \$50 million. As the Company entered into a long-term lease arrangement with the third party, the gain will be amortized over the lease term.

## Supplementary Information: Interest Coverage

The Company's long-term interest requirements for the 52 weeks ended December 31, 2005, after annualizing interest on long-term debt issued and retired during this period, amounted to \$84.8 million. The Company's earnings before interest on long-term debt, income taxes and minority interest for the 52 weeks then ended were \$592.9 million, which is 7.0 times the Company's long-term interest requirements for this period.



# 2005 Quarterly Information

	First Quarter (January 2, 2005 to April 2, 2005)	Second Quarter (April 3, 2005 to July 2, 2005)	Third Quarter (July 3, 2005 to October 1, 2005)	Fourth Quarter (October 2, 2005 to December 31, 2005)	Total
<b>Canadian Tire Retail</b>					
Gross operating revenue	\$ 968.8	\$ 1,386.4	\$ 1,232.3	\$ 1,520.7	\$ 5,108.2
Earnings before income taxes and minority interest	25.0	92.2	86.1	86.9	290.2
<b>Canadian Tire Petroleum</b>					
Gross operating revenue	286.2	333.1	371.5	339.3	1,330.1
Earnings before income taxes	1.6	0.1	2.8	3.0	7.5
<b>Mark's Work Wearhouse</b>					
Gross operating revenue	114.8	145.3	129.3	275.0	664.4
Earnings before income taxes	4.2	12.7	5.9	42.2	65.0
<b>Canadian Tire Financial Services</b>					
Gross operating revenue	151.2	170.2	173.8	190.6	685.8
Earnings before income taxes	25.8	43.4	40.0	55.8	165.0
<b>Total</b>					
Gross operating revenue	\$ 1,518.8	\$ 2,032.4	\$ 1,904.2	\$ 2,319.2	\$ 7,774.6
Cost of merchandise sold and all expenses except for the undernoted items	1,390.7	1,813.5	1,694.9	2,050.0	6,949.1
Interest					
Long-term debt	23.5	15.7	19.0	21.3	79.5
Short-term debt	1.0	1.7	0.2	1.7	4.6
Depreciation and amortization	44.0	44.8	47.0	49.2	185.0
Employee profit sharing plan	3.0	8.3	8.3	9.1	28.7
Earnings before income taxes and minority interest	56.6	148.4	134.8	187.9	527.7
Income taxes	19.4	54.4	48.5	67.7	190.0
Minority interest	1.9	1.8	1.9	2.0	7.6
Net earnings	35.3	92.2	84.4	118.2	330.1
Basic earnings per share <sup>1</sup>	0.43	1.13	1.03	1.44	4.04
Diluted earnings per share <sup>2</sup>	0.43	1.11	1.02	1.43	3.98
<b>Canadian Tire Retail</b>					
Retail sales growth	4.8%	4.2%	3.9%	7.1%	5.1%
Comparable store sales growth	2.5%	2.2%	2.0%	5.1%	3.0%
Net shipments growth	1.5%	1.3%	5.5%	7.8%	4.2%
Number of new-format stores	332	336	337	345	
Number of traditional stores	126	122	122	117	
Cumulative number of Canadian Tire stores	458	458	459	462	
Number of PartSource stores	47	48	51	57 <sup>3</sup>	
<b>Canadian Tire Petroleum</b>					
Gasoline sales volume (millions of litres)	382.8	411.6	401.6	396.3	1,592.3
Number of gas bars	254	253	253	259	
Number of car washes	62	62	65	67	
Number of convenience stores	242	242	242	247	
<b>Mark's Work Wearhouse</b>					
Retail sales growth	26.9%	20.1%	17.0%	19.3%	20.3%
Same store sales growth	23.5%	16.4%	13.9%	17.4%	17.4%
Number of Mark's Work Wearhouse stores	332	333	335	334	
<b>Class A Non-Voting Shares</b>					
High	\$ 57.99	\$ 62.24	\$ 64.00	\$ 70.60	\$ 70.60
Low	50.81	56.00	55.75	56.34	50.81
Close	57.00	56.62	62.89	69.54	69.54
Volume (thousands of shares)	13,234	9,983	10,771	12,652	46,640
<b>Common Shares</b>					
High	\$ 86.01	\$ 104.00	\$ 97.25	\$ 118.00	\$ 118.00
Low	66.34	87.00	89.01	91.50	66.34
Close	86.01	94.00	92.00	118.00	118.00
Volume (thousands of shares)	61	60	39	45	205

<sup>1</sup> Quarterly basic earnings per share are calculated using the weighted average number of Common and Class A Non-Voting Shares outstanding for the quarter, while annual basic earnings per share are calculated using the weighted average number of Common and Class A Non-Voting Shares outstanding for the full year.

<sup>2</sup> Quarterly diluted earnings per share are calculated using the diluted weighted average number of Common and Class A Non-Voting Shares outstanding for the quarter, while annual diluted earnings per share are calculated using the average of the quarterly weighted average numbers of diluted Common and Class A Non-Voting Shares outstanding.

<sup>3</sup> Includes three acquired stores that will be re-branded to the PartSource banner in 2006.

# 2004 Quarterly Information

	First Quarter (January 4, 2004 to April 3, 2004)	Second Quarter (April 4, 2004 to July 3, 2004)	Third Quarter (July 4, 2004 to October 2, 2004)	Fourth Quarter (October 3, 2004 to January 1, 2005)	Total
<i>(Dollars in millions, except per share amounts)</i>					
<i>(Store numbers are cumulative at end of period)</i>					
<b>Canadian Tire Retail</b>					
Gross operating revenue	\$ 952.3	\$ 1,367.0	\$ 1,170.3	\$ 1,409.4	\$ 4,899.0
Earnings before income taxes and minority interest	41.2	81.5	71.2	78.0	271.9
<b>Canadian Tire Petroleum</b>					
Gross operating revenue	243.9	288.3	284.5	289.2	1,105.9
Earnings before income taxes	0.1	0.8	—	2.5	3.4
<b>Mark's Work Wearhouse</b>					
Gross operating revenue	89.6	119.8	108.9	227.8	546.1
Earnings before income taxes	(1.0)	5.5	1.7	30.9	37.1
<b>Canadian Tire Financial Services</b>					
Gross operating revenue	131.3	154.3	154.1	171.6	611.3
Earnings before income taxes	25.8	39.5	36.7	46.5	148.5
<b>Total</b>					
Gross operating revenue	\$ 1,414.9	\$ 1,927.3	\$ 1,715.5	\$ 2,095.9	\$ 7,153.6
Cost of merchandise sold and all expenses except for the undernoted items	1,284.0	1,729.6	1,537.0	1,866.3	6,416.9
Interest					
Long-term debt	19.9	19.1	18.8	18.2	76.0
Short-term debt	0.3	0.1	0.2	1.8	2.4
Depreciation and amortization	41.2	42.9	42.9	43.6	170.6
Employee profit sharing plan	3.4	8.3	7.0	8.1	26.8
Earnings before income taxes and minority interest	66.1	127.3	109.6	157.9	460.9
Income taxes	23.3	44.9	38.6	55.7	162.5
Minority interest	1.9	1.6	1.6	1.8	6.9
Net earnings	40.9	80.8	69.4	100.4	291.5
Basic earnings per share <sup>1</sup>	0.51	1.00	0.86	1.24	3.60
Diluted earnings per share <sup>2</sup>	0.50	0.98	0.84	1.22	3.53
<b>Canadian Tire Retail</b>					
Retail sales growth	5.0%	5.1%	3.9%	3.7%	4.4%
Comparable store sales growth	3.1%	2.2%	1.2%	1.1%	1.8%
Net shipments growth	10.0%	1.2%	5.3%	7.4%	5.6%
Number of new-format stores	312	319	321	327	
Number of traditional stores	141	136	134	130	
Cumulative number of Canadian Tire stores	453	455	455	457	
Number of PartSource stores	39	40	45	47	
<b>Canadian Tire Petroleum</b>					
Gasoline sales volume (millions of litres)	354.3	377.1	376.3	389.0	1,496.7
Number of gas bars	243	247	248	253	
Number of car washes	52	54	54	58	
Number of convenience stores	233	237	237	241	
<b>Mark's Work Wearhouse</b>					
Retail sales growth	11.3%	19.4%	26.5%	15.7%	17.8%
Same store sales growth	7.0%	14.7%	22.8%	11.3%	13.4%
Number of Mark's Work Wearhouse stores	322	320	325	333	
<b>Class A Non-Voting Shares</b>					
High	\$ 47.57	\$ 49.00	\$ 50.35	\$ 57.40	\$ 57.40
Low	39.00	42.37	43.66	49.36	39.00
Close	44.85	48.10	50.35	56.21	56.21
Volume (thousands of shares)	13,177	12,602	10,925	10,936	47,640
<b>Common Shares</b>					
High	\$ 61.00	\$ 61.00	\$ 59.20	\$ 75.50	\$ 75.50
Low	43.75	55.75	53.05	56.75	43.75
Close	58.00	58.50	59.20	71.50	71.50
Volume (thousands of shares)	78	35	29	66	208

<sup>1</sup> Quarterly basic earnings per share are calculated using the weighted average number of Common and Class A Non-Voting Shares outstanding for the quarter, while annual basic earnings per share are calculated using the weighted average number of Common and Class A Non-Voting Shares outstanding for the full year.

<sup>2</sup> Quarterly diluted earnings per share are calculated using the diluted weighted average number of Common and Class A Non-Voting Shares outstanding for the quarter, while annual diluted earnings per share are calculated using the average of the quarterly weighted average numbers of diluted Common and Class A Non-Voting Shares outstanding.

# Ten-Year Financial Review

(Dollars in millions except per share amounts)

	2005	2004	2003 <sup>1</sup>
<b>Consolidated Statements of Earnings</b>			
Gross operating revenue	\$ 7,774.6	\$ 7,153.6	\$ 6,552.8
Earnings before interest, income taxes, depreciation & amortization and minority interest	796.8	709.9	605.0
Earnings before income taxes and minority interest	527.7	460.9	365.9
Income taxes	190.0	162.5	116.0
Net earnings before minority interest	337.7	298.4	249.9
Minority interest	7.6	6.9	8.7
Net earnings	330.1	291.5	241.2
Cash generated from operations	721.2	630.4	534.5
Cash generated from operating activities	438.1	413.1	520.1
Earnings retained and reinvested	282.7	251.0	208.7
Capital expenditures	391.1	340.7	278.9
<b>Consolidated Balance Sheets</b>			
Current assets	\$ 2,981.0	\$ 2,434.6	\$ 2,291.5
Long-term receivables and other assets <sup>2</sup>	230.7	223.4	156.7
Property and equipment	2,743.9	2,585.2	2,444.9
Total assets	5,955.6	5,243.2	4,893.1
Current liabilities	1,821.0	1,487.4	1,612.0
Long-term debt (excludes current portion)	1,171.3	1,081.8	886.2
Other long-term liabilities	63.2	55.6	46.9
Future income taxes	89.0	67.2	30.9
Minority interest	300.0	300.0	300.0
Shareholders' equity	2,511.1	2,251.2	2,017.1
<b>Consolidated per share</b>			
Basic earnings per share	\$ 4.04	\$ 3.60	\$ 2.99
Diluted earnings per share <sup>3</sup>	3.98	3.53	2.95
Cash generated from operations	8.82	7.78	6.63
Cash generated from operating activities	5.36	5.10	6.45
Dividends declared	0.58	0.50	0.40
Shareholders' equity	30.83	27.75	24.98
<b>Statistics at Year End</b>			
Number of Canadian Tire stores	462	457	452
Number of PartSource stores	57 <sup>5</sup>	47	39
Number of gas bars	259	253	232
Number of car washes	67	58	47
Number of Mark's Work Wearhouse stores <sup>4</sup>	334	333	322

<sup>1</sup> 53-week period

<sup>2</sup> Includes goodwill and intangible assets

<sup>3</sup> Data required to calculate diluted earnings per share prior to 1998 is not available.

<sup>4</sup> Mark's Work Wearhouse was acquired on February 1, 2002.

<sup>5</sup> Includes three acquired stores that will be re-branded to the PartSource banner in 2006.

	2002	2001	2000	1999	1998	1997 <sup>1</sup>	1996
\$	5,944.5	\$ 5,374.7	\$ 5,207.6	\$ 4,728.3	\$ 4,347.3	\$ 4,087.8	\$ 3,930.4
	553.0	496.6	457.8	447.3	410.2	350.6	323.7
	311.3	272.1	236.0	222.2	248.8	207.0	192.1
	103.0	98.0	90.9	79.4	82.4	60.2	62.8
	208.3	174.1	145.1	142.8	166.4	146.8	129.3
	7.4	0.6	—	—	—	—	—
	200.9	173.5	145.1	142.8	166.4	146.8	129.3
	460.1	362.4	350.0	323.6	315.6	306.8	271.7
	442.0	189.4	504.1	326.1	364.9	274.8	303.6
	169.3	142.0	113.8	112.0	135.1	113.5	94.4
	249.8	358.4	382.3	377.7	303.2	253.5	220.7
\$	2,303.1	\$ 1,985.0	\$ 1,519.6	\$ 1,896.1	\$ 1,504.9	\$ 1,433.8	\$ 1,334.5
	211.5	134.4	122.9	105.4	36.0	33.3	34.1
	2,351.1	2,245.0	2,098.4	1,865.5	1,619.7	1,404.6	1,231.4
	4,865.7	4,364.4	3,740.9	3,867.0	3,160.6	2,871.7	2,600.0
	1,577.0	1,106.5	1,119.6	1,434.0	1,042.0	1,155.6	848.4
	1,125.2	1,310.0	1,115.0	1,050.3	815.0	380.4	420.4
	43.7	38.6	34.2	15.9	6.3	5.9	5.7
	23.7	15.0	18.9	25.4	36.0	30.8	24.0
	300.0	300.0	—	—	—	—	—
	1,796.1	1,594.3	1,453.2	1,341.4	1,261.3	1,299.0	1,301.5
\$	2.54	\$ 2.21	\$ 1.85	\$ 1.85	\$ 2.09	\$ 1.77	\$ 1.49
	2.51	2.19	1.85	1.82	2.04	—	—
	5.82	4.61	4.47	4.19	3.96	3.69	3.12
	5.59	2.41	6.43	4.22	4.57	3.31	3.49
	0.40	0.40	0.40	0.40	0.40	0.40	0.40
	22.49	20.29	18.50	17.17	16.19	15.80	15.06
	451	450	441	432	430	430	426
	33	30	28	8	5	—	—
	212	203	206	202	195	193	197
	33	20	16	10	8	3	—
	306	—	—	—	—	—	—

# Corporate Reporting and Governance Information at a Glance

Canadian Tire is firmly committed to good disclosure practices and effective communication with our shareholders. This table summarizes where you can find important information about our Company.

Topic	Annual Report (including MD&A and Consolidated Financial Statements and Notes)		Annual Information Form		Management Information Circular		The information can be found within posted documents on:	
							Canadian Tire investor relations web site <sup>1</sup>	SEDAR <sup>2</sup>
2005-2009 Strategic Plan Overview	✓	Pages 14-19; 39					✓	✓
2005 Performance Scorecard	✓	Pages 4-7					✓	✓
Accounting Policies (Significant)	✓	Pages 85-88					✓	✓
Analyst Coverage/Earnings Estimates							✓	
Annual Meeting of Shareholders - Form of Proxy	✓	Page 112			✓	Inside front cover	✓	✓
Business Description	✓	Pages 2-3; 22-31; 36	✓	Pages 7-24			✓	✓
Board and Committees - Board Mandate - Audit Committee Mandate and Charter - Audit Committee Information			✓	Annex A Pages 34-36	✓	Pages 13-16 Annex A Annex B	✓	✓
Capital Structure	✓	Pages 66-72; 93-94	✓	Pages 25-28			✓	✓
CEO and CFO Certifications	✓	Page 33					✓	✓
Code of Business Conduct							✓	✓
Compensation	✓	Pages 94-96			✓	Pages 20-32	✓	✓
Corporate Responsibility	✓	Pages 107-109	✓	Pages 21-23	✓	Pages 16-19	✓	✓
Directors and Officers Information	✓	Pages 110-111	✓	Pages 30-33	✓	Pages 6-12	✓	✓
Dividend Policy and History			✓	Page 25			✓	✓
Dividend Reinvestment Program							✓	
Interim Financial Information	✓	Pages 42; 102-103					✓	✓
Investor Presentations and Webcasts							✓	
Non-GAAP Measures	✓	Pages 79-80					✓	✓
Risk Management	✓	Pages 40; 74-77; 108					✓	✓
Share Information and Price	✓	Pages 1; 102-103; 112	✓	Pages 28-29	✓	Pages 2; 29	✓	✓
Vision Statement	✓	Page 14					✓	✓

<sup>1</sup> Canadian Tire investor relations web site (<http://investor.relations.canadiantire.ca>)

<sup>2</sup> System for Electronic Document Analysis and Retrieval (<http://www.sedar.com>)

## **Responding to our stakeholders' needs**

Canadian Tire is one of Canada's largest and most successful retailers because of the relationships we have fostered with our stakeholders. We embrace the belief that, in order to achieve our vision of being Canada's most trusted company, we must effectively meet our responsibilities to all of our stakeholders.

We broadly define corporate responsibility to include responsible practices and behaviours related to governance and corporate reporting; business practices; risk management; stewardship of the environment, health and safety; the workplace; and community involvement. On an ongoing basis, we review and augment our policies, business practices and initiatives to ensure that we are meeting high standards of corporate responsibility.

## **Corporate Governance**

Our Board of Directors ensure that we meet our mandated, regulatory governance obligations to shareholders and that we also act in a manner befitting our role as one of Canada's most recognized and trusted companies. We regularly review our corporate governance policies and practices to ensure they remain comprehensive, relevant and effective, and that our disclosures are transparent and full. Canadian Tire has achieved award-winning standards for proactive, comprehensive disclosure, recognized externally by organizations such as the Canadian Institute of Chartered Accountants.

Highlights of our key governance policies and practices include:

- > The separation of the roles of Chairman and Chief Executive Officer;
- > The Chairman of the Board is independent, as are the majority of the Directors;
- > The Board regularly assesses its effectiveness and the effectiveness of our Directors;
- > The Board is actively engaged with Management in the development of strategic plans and reviews and approves the Company's strategic, business and financial plans;
- > Directors are provided with orientation and education programs and may attend conferences, courses or other educational experiences at the Company's expense;
- > The CEO's and individual Officer's performance and objectives are evaluated annually by the Board;
- > Organizational and succession planning reviews are conducted; and
- > The Board approves disclosure and insider trading policies.

For a full statement of our corporate governance practices, and how we are meeting the guidelines adopted by the Canadian Securities Administrators, refer to Canadian Tire's 2005 Management Information Circular. Please also refer to Corporate Reporting and Governance Information at a Glance on Page 106 of this Annual Report, for a listing of places to obtain more comprehensive governance and disclosure information.

## **Responsible Business Practices**

In 2005, Canadian Tire adopted a Code of Business Conduct for all employees and Directors to ensure a clear understanding of our standards for ethical business practices. Employees and Directors are required to sign the Code on an annual basis. Canadian Tire also implemented a Supplier Code of Business Conduct, which sets out specific expectations regarding supplier workplace standards and business practices including unlawful payments, working hours, human rights, discrimination and forced labour, safe and healthy work environments and environmental protection.

In conjunction with the adoption of our Codes, Canadian Tire established a Business Conduct Compliance Program. The Business Conduct Compliance Office oversees compliance with our Code of Business Conduct and provides methods to enable any stakeholder to voice concerns or issues anonymously or confidentially, if needed, through:

- > Business Conduct Compliance Office;
- > Business Conduct Hotline or Web Reporting (third party); and
- > Direct contact to the Chairman of the Board, Audit Committee and Social Responsibility and Risk Governance Committee.

### **Reporting Tools:**

*Business Conduct Compliance Office  
2180 Yonge Street  
Toronto, Ontario M4P 2V8  
Attention: Director, Compliance*

*Business Conduct Hotline  
From Canada and the USA,  
call toll free 1-800-620-6943  
From other countries,  
call collect 678-250-7521*

*Business Conduct Web Reporting  
<https://www.twinco.com/webreport>*



## **Risk Management**

Canadian Tire employs an enterprise risk management (ERM) framework that sets out principles, processes and tools for evaluating, prioritizing and managing risk effectively and consistently across the organization. The Board of Directors has oversight of the ERM process and has delegated to the Social Responsibility and Risk Governance Committee – and in certain instances, the Audit Committee – the task of gaining and maintaining reasonable assurance that we appropriately identify, assess, monitor and manage risks – including our most significant, or principal risks – and develop, implement and maintain a policy which accurately sets out our risk philosophy and tolerance and the related expectations and accountabilities.

For more information on our approach to ERM and the risks that have the most potential to impact our business, please refer to section 9 in Management's Discussion and Analysis of this Annual Report.

## **Environment, Health and Safety Stewardship**

Responsible management of environment, health and safety (EHS) matters is a fundamental obligation to the health and well-being of our employees and other stakeholders. We have an established EHS policy in place and have undertaken a broad range of activities to support that policy.

### **Environment**

In 2005, our environmental programs focussed on waste diversion, energy conservation and recycling. Our distribution centres diverted a variety of waste materials from landfill including over 2,700 tonnes of cardboard and over 21 million pounds of scrap lead acid batteries from Associate Dealer stores that were recycled. We retrofitted lights in our distribution centres, reducing greenhouse gas emissions and lowering energy consumption by approximately 5.2 million kilowatt-hours per year.

Our Petroleum group continued its program of replacing underground steel storage tanks with fiberglass tanks in order to reduce the risk of tank leaks, and their comprehensive program to control gasoline inventory losses has resulted in performance that exceeds government standards.

### **Health and Safety**

Our workplace health and safety performance substantially exceeds that of comparable firms, according to data from the Ontario's Workers' Safety Insurance Board on the frequency of lost-time injuries. In 2005, we instituted improvements in workplace safety through training and hazard identification; developed an ergonomic program that prevents the development of musculo-skeletal disorders; and opened new health/wellness facilities within our head office and at the A.J. Billes Distribution Centre.

We provided hazardous chemical product safety information to employees and customers through access to Material Safety Data Sheets (MSDS) posted on the Canadian Tire web site. In 2005, over 33,000 MSDS files were accessed.

Mark's implemented a store compliance audit program which includes EHS elements and compliance scorecards, and PartSource trained nine new franchisees and store managers on their EHS responsibilities as part of the franchisee training program.

## Workplace

A unique culture permeates Canadian Tire and is reflected in the “Canadian Tire Way” – a framework that establishes the vision for the organization, our statement of purpose, team values and leadership expectations. We are a pioneer of profit-sharing programs in Canada, remaining firmly committed to the principle of aligning employees’ interests as owners. Our culture fosters innovation, accountability and balanced risk-taking.

It has become a business imperative in today’s work environment to focus on providing employees with opportunities to learn and develop new skills. Knowledge is essential to business success and personal performance. Some of the initiatives we have developed include:

- > eLearning – a tool to help employees learn about the products they sell and how to help customers. There are currently 340 courses available in English and French and over 1.8 million lessons have been completed, leading to an overall improvement in product knowledge and customer satisfaction ratings in our stores
- > Canadian Tire operates two universities. Canadian Tire University, launched in 2005, is an award-winning program recognized for its progressive approach to meeting the specific learning needs of Canadian Tire Retail’s front and back-line team members. Canadian Tire University-Niagara, launched in 1996, supports Financial Services’ focus on increasing organizational capability and developing skills, leadership competencies and relationships.

Canadian Tire continues to be widely recognized in external studies and employee surveys for the exceptional pride and loyalty of our workforce and for the inspiring work environment we have created.

## Involvement in the Community



Good corporate citizenship through community support is core to the culture of Canadian Tire. Enhancing the communities within which our employees work and live is in keeping with our long-term corporate objectives. We give to a variety of social causes, but the largest single beneficiary is the Canadian Tire Foundation for Families. In 2005, Canadian Tire gave nearly \$5.5 million to the Foundation and other community organizations.

Launched in 1999, the Canadian Tire Foundation for Families strengthens communities through three programs: Canadian Tire JumpStart helps kids in financial need participate in organized sports and recreation, while the Foundation’s other two programs – Community Programs and Regional Disaster Recovery – lend a helping hand to families when they need it most.

The Canadian Tire JumpStart program, launched in February 2005, has delivered significant benefits for kids in terms of health, confidence and social development. Canadian Tire JumpStart’s 225 community chapters across Canada gave more than 24,000 kids in financial need the chance to play in its first year of operation. Together with Canadian Tire Associate Dealers, Petroleum Agents and community partners, the local chapters identify children who might benefit from the program and ensure successful delivery. The goal for 2006 is to give 35,000 kids in need a sporting chance.

Community Programs provide financial support to people facing difficult circumstances by ensuring life’s basic needs are met – food, shelter, clothing and essential goods. Last year, we were able to help families across the country with over 189,000 warm meals and 23,000 nights of shelter.

With an emergency response network prepared for times of crisis, the Foundation was able to donate over \$98,000 last year through the Regional Disaster Recovery program to help with relief efforts when flooding affected Stephenville, Newfoundland and Brandon, Manitoba and water was contaminated in Stratford, Ontario.

Through the generosity of our employees, vendors, customers and partners in the community, the Foundation for Families has donated more than \$23 million in the last six years.



## Directors

### **Gilbert S. Bennett**

Chairman of the Board  
Canadian Tire Corporation, Limited,  
Consultant and Corporate Director

### **Martha G. Billes**<sup>3,4</sup>

President, Albikin Management Inc.,  
an investment holding company

### **Owen G. Billes**<sup>3</sup>

Manager, New Business Development,  
Canadian Tire Corporation, Limited

### **Gordon F. Cheesbrough**<sup>2,3</sup>

Managing Partner,  
Blair Franklin Capital Partners Inc.,  
an investment bank and asset management  
company and Corporate Director

### **Austin E. Curtin**<sup>3</sup>

President, Austin Curtin  
Sales Ltd., which operates  
two Canadian Tire Associate stores and a  
Petroleum outlet

### **James D. Fisher**<sup>1,2</sup>

Associate Dean, Rotman School  
of Management, University of Toronto

### **Keith E. Gostlin**<sup>3</sup> \*Appointed February 9, 2006

President, K.E. Gostlin Enterprises Ltd.  
which operates a Canadian Tire Associate store

### **Rémi Marcoux**<sup>2,4</sup>

Founder, controlling shareholder and  
Executive Chairman, Transcontinental Inc.,  
a public company holding interests in printing  
and publishing companies

### **Suzanne R. Perles**<sup>3,4</sup> \*Appointed November 10, 2005

Managing Director, The Corporate Development  
Company, a corporate advisory firm

### **Frank Potter**<sup>1,3</sup>

Chairman, Emerging Market Advisors Inc.,  
a consulting firm dealing with international  
direct investment

### **Maureen J. Sabia**<sup>1,2</sup>

President, Maureen Sabia International,  
a consulting firm, and Corporate Director

### **Wayne C. Sales**

President and Chief Executive Officer  
Canadian Tire Corporation, Limited

### **Graham W. Savage**<sup>2,4</sup>

Chairman, Callisto Capital LP,  
a merchant banking partnership,  
and Corporate Director

### **Stephen G. Wetmore**<sup>1,2</sup>

Group President, National Markets  
and Performance Management, Bell Canada  
and Executive Vice-President, BCE Inc.,  
a communications company

## Board Committees

### <sup>1</sup> **Management Resources and Compensation Committee**

Chairman, James D. Fisher

### <sup>2</sup> **Audit Committee**

Chairman, Maureen J. Sabia

### <sup>3</sup> **Social Responsibility and Risk Governance Committee**

Chairman, Frank Potter

### <sup>4</sup> **Governance Committee**

Chairman, Martha G. Billes

Additional disclosure on Canadian Tire's  
corporate governance is provided in the  
Company's Management Information  
Circular, which is available on the Canadian  
Securities Administrators' SEDAR web site  
at [www.sedar.com](http://www.sedar.com), or in the investor  
relations section of Canadian Tire's web site  
at <http://investor.relations.canadiantire.ca>

Note: Numbering indicates committee membership.

## Officers

### **Gilbert S. Bennett**

Chairman of the Board

### **Wayne C. Sales**

President and Chief Executive Officer

### **J. Huw Thomas**

Executive Vice-President, Finance and Administration and Chief Financial Officer

### **A. Mark Foote**

President, Canadian Tire Retail

### **Michael R. Lambert**

President, Mark's Work Wearhouse and Executive Vice-President, Canadian Tire Corporation, Limited

### **Marco Marrone** \*Appointed February 9, 2006

President, Canadian Tire Financial Services

### **Michael B. Medline**

Executive Vice-President, New Business Development

### **Laura J. Dunne**

Senior Vice-President, Human Resources

### **Stanley W. Pasternak**

Senior Vice-President and Treasurer

### **Susan J.E. Rogers**

Senior Vice-President, Corporate Affairs

### **Kenneth Silver**

Senior Vice-President, Real Estate and Construction

### **Patrick R. Sinnott**

Senior Vice-President, Supply Chain

### **Cameron D. Stewart**

Senior Vice-President, Secretary and General Counsel

### **Andrew T. Wnek**

Senior Vice-President, Information Technology and Chief Information Officer

### **Robyn Collver**

Vice-President, Regulatory Affairs and General Counsel, Canadian Tire Financial Services and Assistant Secretary, Canadian Tire Corporation, Limited

### **Candace A. MacLean**

Vice-President and Assistant Treasurer

## Home Office

### Canadian Tire Corporation, Limited

2180 Yonge Street  
P.O. Box 770, Station K  
Toronto, Ontario M4P 2V8  
Telephone (416) 480-3000  
Fax (416) 544-7715  
Web site: [www.canadiantire.ca](http://www.canadiantire.ca)

## Shareholder and Corporate Information

### Susan J.E. Rogers

Senior Vice-President, Corporate Affairs

### Scott Bonikowsky

Divisional Vice-President  
Corporate Communication & Investor Relations

### Michelle J. Dodokin

Director, Investor Relations

## Annual Meeting of Shareholders

The Carlu  
Concert Hall  
444 Yonge Street, 7th Floor  
Toronto, Ontario M5B 2H4  
Thursday May 11, 2006  
10:00 a.m. (E.S.T.)

## Exchange Listings

The Toronto Stock Exchange:  
Common Shares (CTR)  
Class A Non-Voting Shares (CTR.NV)

## Share Symbols

Canadian Tire Corporation, Limited intends to change its share symbols on the Toronto Stock Exchange (TSX) from CTR to CTC for its Common Shares and from CTR.NV to CTC.a for its Class A Non-Voting Shares. The changes will coincide with the TSX's planned discontinuation of symbol extensions, which are currently scheduled to be implemented on May 8, 2006 for Canadian Tire's shares.

The decision to change symbols reflects the availability of the CTC root symbol which had previously been unavailable to Canadian Tire and its more appropriate reflection of the breadth of Canadian Tire's business.

## Auditors

Deloitte & Touche LLP  
Chartered Accountants

## Bankers

Canadian Imperial Bank of Commerce  
Bank of Montreal  
Royal Bank of Canada  
The Bank of Nova Scotia  
TD Canada Trust  
Citibank Canada  
National Bank Financial

## Registrar and Transfer Agent

### Computershare Trust Company of Canada

100 University Avenue  
Toronto, Ontario M5J 2Y1  
Telephone 1-800-564-6253  
(toll free in Canada and the United States)  
1-514-982-7555  
Fax 1-866-249-7775  
(toll free in Canada and the United States)  
1-416-263-9524  
Email: [service@computershare.com](mailto:service@computershare.com)

To change your address, eliminate multiple mailings, transfer Canadian Tire shares, inquire about our Dividend Reinvestment Program or for other shareholder account inquiries, please contact the principal offices of Computershare Trust Company of Canada in Halifax, Montreal, Toronto, Winnipeg, Calgary or Vancouver.

## Disclosure Documents

Corporate governance disclosure and other investor information is available online from the investor relations pages of the Company's web site at <http://investor.relations.canadiantire.ca>. Additional copies of this Annual Report and other disclosure documents such as the Company's Management Information Circular, the Annual Information Form and quarterly reports can be downloaded or requested in print form from the same web site.

## Recycling

This report has been printed on recyclable acid-free paper.

## Version française du rapport

Pour obtenir la version française du rapport annuel de Canadian Tire, veuillez vous adresser au Service des relations extérieures en composant le 1-800-564-6253 ou écrire à :

La Société Canadian Tire  
C.P. 770, succursale K  
Toronto (Ontario) M4P 2V8

# Glossary of Terms

## **Bank card**

A credit card offered by, or with, Visa or MasterCard.

## **Bankers' acceptance**

A short-term credit investment created by a non-financial firm and guaranteed by a bank as to payment.

## **Basis point**

One hundredth of a percentage point.

## **Black-Scholes model**

A complex model used to calculate the value of an option by considering the share's price, the option's strike price and expiration date, risk-free return and the standard deviation of the share's return.

## **Comparable store sales**

Sales from stores that have been open for more than 53 weeks and that have not been expanded by more than 25 percent in the last year.

## **Counterpart**

In the context of stock-based compensation plans, an offsetting entry to stock option expense.

## **Credit risk**

The potential for loss due to the failure of a borrower to meet their financial obligation.

## **Current ratio**

Current assets divided by current liabilities.

## **Debentures**

Long-term corporate debt that is not secured by the pledge of specific assets.

## **Debt covenants**

Restrictions on the activities of a debtor written into bank loan agreements or bond indenture agreements that prohibit the debtor from taking actions that might hurt the interests of the lenders or bondholders.

## **Debt discount**

The amount by which the price for a security is less than its par or face value. The discount or difference between such a reduced value purchase price and the redemption (par) value comprises all or part of the investor's compensation for owning the security.

## **Derivative**

A financial instrument whose value depends upon the values of underlying assets, interest rates, currency exchange rates, or indices.

## **Derivative equity contract**

A financial instrument used to hedge the anticipated exposure relating to certain stock-based compensation plans.

## **Diluted earnings per share**

The amount of earnings for the period available to each share outstanding during the period including the potential impact of dilutive stock options using the Treasury Stock Method.

## **Discount rate**

An interest rate applied to a single cash flow that will not be paid or received until a future date in order to calculate the present value of that future cash flow.

## **Documentary letter of credit**

A financial instrument issued by a bank on behalf of a customer whereby the issuing bank has guaranteed payment of a financial obligation to a third party upon presentation of specified documents. The customer in turn reimburses the bank.

## **Fair value**

The amount of the consideration that would be agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act.

## **Fair-value based method**

A method of accounting for stock options whereby compensation expense is recorded for the fair value of the stock options issued.

## **Foreign exchange contract**

An agreement between parties to exchange stipulated amounts of one currency for another currency at one or more future dates.

## **Hedge**

A risk management technique used to manage interest rate, foreign currency exchange or other exposures arising from regular business transactions.

## **Interest coverage**

Earnings before interest and income taxes divided by interest expense.

## **Interest rate risk**

The potential impact on the Company's earnings and economic value due to changes in interest rates.

## **Interest rate swap**

A contractual agreement between two parties to exchange fixed and floating rate interest payments based on a notional value in a single currency.

## **Interest-only strip**

Represents the present value of the Company's share of the spread to be earned over the collection period on the loan receivables sold.

## **Inventory turnover**

Cost of goods sold divided by average inventory for the main CTR distribution centres.

## **Liquidation rate**

The rate at which receivables held by the lender are paid down by the debtor.

## **Loans receivable**

The aggregate amount of outstanding balances owed to the Company by Canadian Tire credit cardholders and personal loan customers.

## **Long-term debt to total capitalization**

Long-term debt divided by the sum of short-term debt, long-term debt, future income taxes, other long-term liabilities, minority interest and shareholders' equity.

## **Marked to market**

The valuation of financial instruments using prevailing market prices or fair value as of the balance sheet date.

## **Medium term notes**

Debt instruments with maturities ranging from nine months to 30 years that are offered on a continuous basis, which means that they are issued and sold as buyers request them rather than on a single issue date.

## **Minority interest**

A reference to shareholders – individuals, corporations or partnerships – that own less than 50 percent of a subsidiary's outstanding voting common stock. The minority shareholders hold an interest in the subsidiary's net assets and share earnings with the majority shareholder.

## **Net managed portfolio**

The total value, after allowances, of the loans receivable portfolio which includes both credit card receivables and personal loans. A significant portion of the managed loan portfolio has been securitized.



**New-format store**

A Canadian Tire store that has opened since 1993 in one of the Company's newer store formats, and incorporating, among other features, a larger, more convenient layout and expanded merchandising offering.

**Notional amount**

The amount considered as principal when calculating interest and other payments for derivative contracts.

**Off-balance sheet financial instrument**

An asset or liability that is not recorded on the balance sheet, but has the potential to produce positive or negative cash flows in the future.

**Projected benefit method**

An actuarial valuation method whereby a distinct unit of future benefit is attributed to each year of credited service with equal portions of the total estimated future benefit attributed to each year of service in the attribution period. The actuarial present value of that unit of benefit is computed separately for the period during which it is presumed to have accrued.

**Re-branding**

In the context of Canadian Tire Petroleum's strategy, re-branding is the conversion of a competitor's gas bar and kiosk (in most cases) to the Canadian Tire brand. Generally, Petroleum incurs relatively low costs to convert the site. In exchange for the conversion, the re-branding partner participates in the profits of the converted site or is paid a fixed rent depending upon the agreement.

**Retail method**

An inventory valuation method used primarily by retailers under which the inventory is carried at the lower of the estimated cost and anticipated selling price, less an expected average gross margin.

**Retained interest**

A beneficial interest in the assets transferred over which a seller has not relinquished control, including servicing assets, residual interest, cash or securitization reserve accounts and securities backed by the transferred assets.

**Return on equity**

Net earnings divided by average shareholders' equity.

**Return on invested capital**

After-tax earnings before interest, income taxes and minority interest divided by average invested capital. Invested capital is the sum of current assets, current portion of long-term debt, property and equipment, goodwill, intangible assets, long-term receivables and certain other assets less current liabilities.

**Same store sales**

Sales from stores that have been open for more than a year, including stores that have been expanded by more than 25 percent in the last year.

**Securitization of receivables**

Securitization is a term that refers to the process by which financial assets are sold to a third party. At Financial Services, both credit card and personal loan receivables are routinely financed by selling an interest in the assets to trusts involved in the business of handling receivables portfolios. In the case of credit card receivables, a co-ownership interest is sold to Glacier Credit Card Trust. For personal loans, the loans are sold to a third party trust for consideration that includes cash and a retained interest in the assets. We record these transactions as a sale, and as a result, these assets are not included on our Consolidated Balance Sheets.

**Self-sustaining foreign operation**

A foreign operation which is financially and operationally independent of the reporting enterprise such that the exposure to exchange rate changes is limited to the reporting enterprise's net investment in the foreign operation.

**Servicing**

The collection of principal and interest from borrowers, accounting for the cash flows due and the cash flows received, and remitting the cash flows to the entitled recipients.

**Servicing liability**

A contract to service receivables under which the estimated future revenues from contractually specified servicing fees, late charges, and other ancillary revenues are not expected to adequately compensate the company that is servicing the receivables.

**Standby letter of credit**

A financial instrument issued by a bank on behalf of a customer whereby the issuing bank has guaranteed payment of a financial obligation to a third party should the customer fail to meet its obligation to the third party.

**Superbranding**

A Mark's Work Wearhouse initiative to expand the presence and strength of the brand across Canada.

**Total managed portfolio**

The total value, before allowances, of the loans receivable portfolio which includes both credit card receivables and personal loans. A significant portion of the managed loan portfolio has been securitized.

**Traditional store**

A Canadian Tire store that has not been replaced by a new-format store or expanded to incorporate new-format store features.

**Treasury stock method**

A method of recognizing the use of proceeds that could be obtained upon exercise of stock options when computing the diluted earnings per share. This method assumes that the proceeds are used to repurchase shares at the average market price in the period.

**Undivided co-ownership interest**

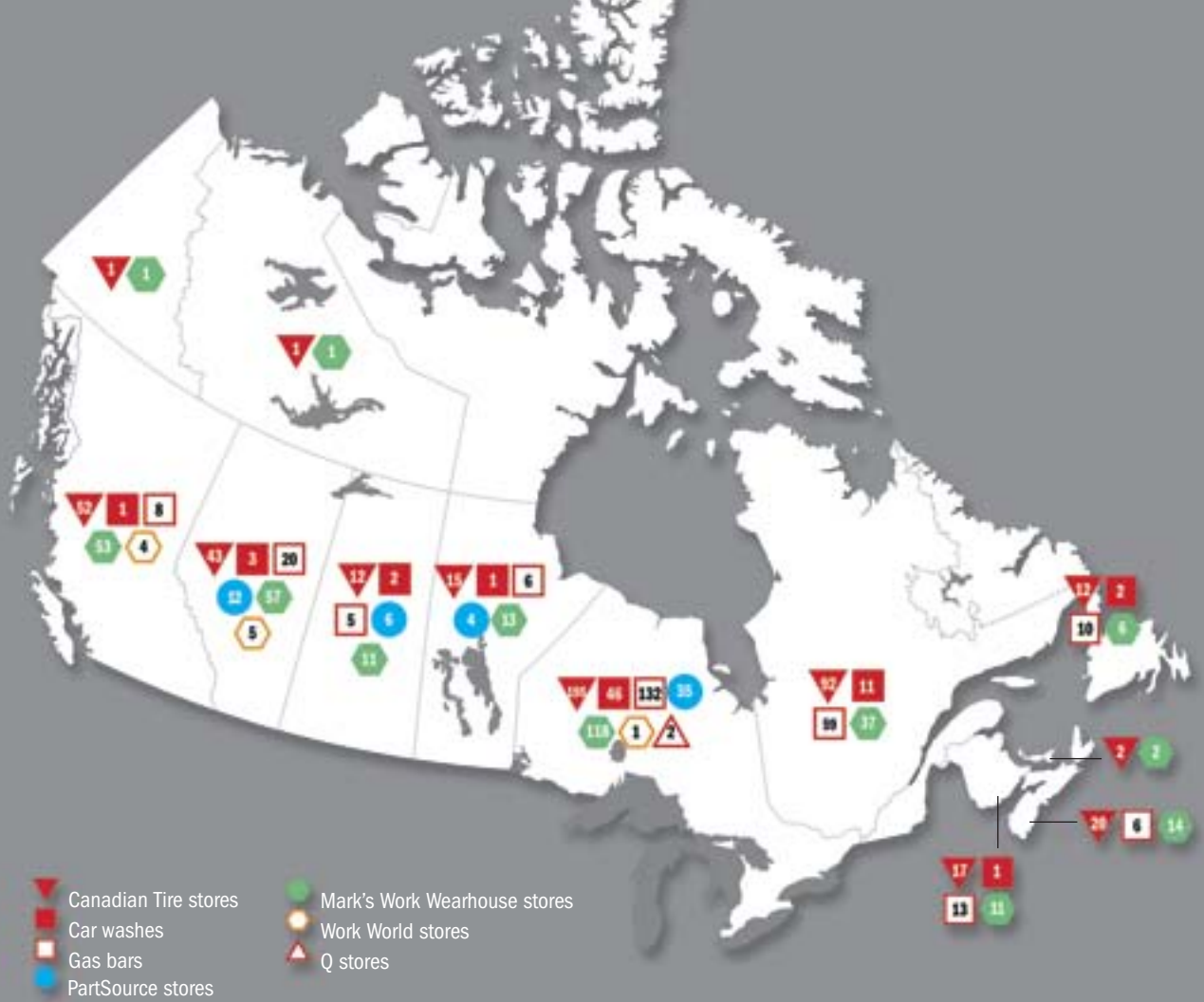
A partial legal or beneficial ownership of account assets.

**Variable interest entity (VIE)**

An entity that by design does not have sufficient equity at risk to permit it to finance its activities without additional subordinated financial support, or in which equity investors do not have the characteristics of a controlling financial interest.

**Weighted average number of shares**

The number of shares determined by relating the portion of time within the reporting period the shares have been outstanding to the total time in that period.



## Canadian Tire Network at a Glance

As at December 31, 2005

Province	Canadian Tire Stores	Car Washes	Gas Bars	PartSource Stores	Mark's stores	Work World Stores	Q Stores	Total
Alberta	43	3	20	12	57	5	-	140
British Columbia	52	1	8	-	53	4	-	118
Manitoba	15	1	6	4	13	-	-	39
New Brunswick	17	1	13	-	11	-	-	42
Newfoundland	12	2	10	-	6	-	-	30
Northwest Territories	1	-	-	-	1	-	-	2
Nova Scotia	20	-	6	-	14	-	-	40
Ontario	195	46	132	35*	118	1	2	529
Prince Edward Island	2	-	-	-	2	-	-	4
Quebec	92	11	59	-	37	-	-	199
Saskatchewan	12	2	5	6	11	-	-	36
Yukon	1	-	-	-	1	-	-	2
<b>Total</b>	<b>462</b>	<b>67</b>	<b>259</b>	<b>57*</b>	<b>324</b>	<b>10</b>	<b>2</b>	<b>1,181</b>

\* Includes three acquired stores that will be re-branded to the PartSource banner in 2006.

**Working to be Canada's most trusted company**

