



**SAPUTO INC.**

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**ANNUAL INFORMATION FORM**

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**June 1, 2001**

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## ITEM 1 - THE COMPANY

### 1.1 Incorporation

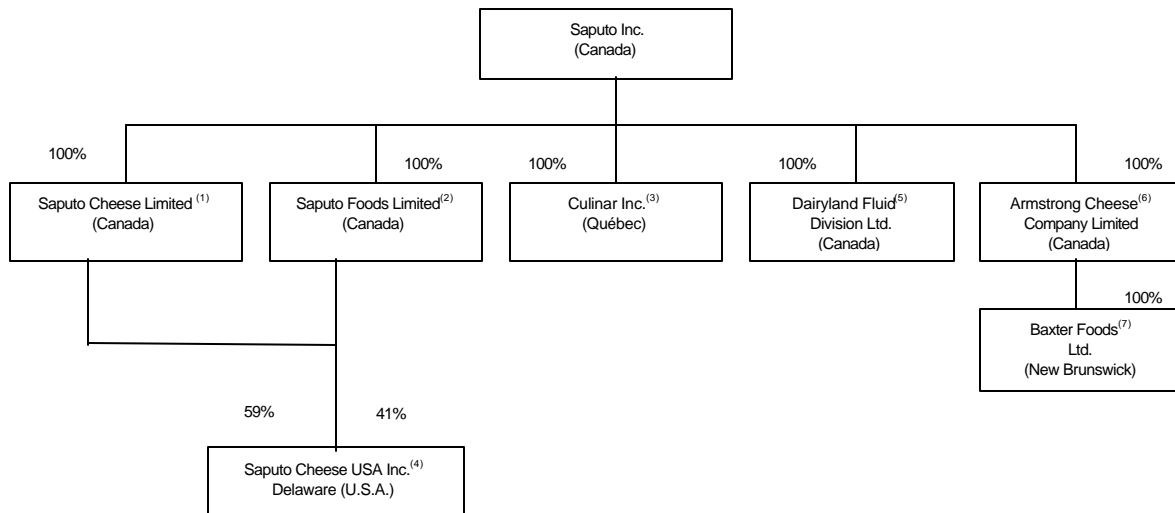
Saputo Inc. was constituted by a Certificate of Amalgamation issued pursuant to the provisions of the *Canada Business Corporations Act* on July 1, 1992, which was amended on August 25, 1997 in order to change the provisions attached to its authorized share capital. On August 2, 2000, the Certificate was further amended to enable the directors to appoint additional directors between shareholders' meetings. The head office and principal place of business of the Company is located at 6869 Metropolitan Boulevard East, Saint-Léonard, Québec, Canada, H1P 1X8.

In this Annual Information Form, unless the context otherwise requires or indicates, the terms "Saputo" and the "Company" mean Saputo Inc. itself or together with its subsidiaries, or any one or more of them.

In this Annual Information Form, all references to "\$" or "CDN \$" are to Canadian dollars and all references to "US \$" are to American dollars.

### 1.2 Corporate Structure

The following organizational chart illustrates the corporate structure of Saputo and its significant subsidiaries, and their respective jurisdictions of incorporation.



- (1) Production, sale and distribution of dairy and other food products in the Province of Québec.
- (2) Production, sale and distribution of dairy and other food products in Canadian provinces other than Québec.
- (3) Production, sale and distribution of snack cakes, cookies, fine breads and soups in Canada.
- (4) Production and sale of dairy products in the United States.
- (5) Production, sale and distribution of a wide range of fluid milk, cream products, sour cream, cottage cheese, yogurt and soft serve dairy mixes as well as juices and other beverages, and distribution of a variety of other dairy and related products in Western Canada and Ontario. Quebec fluid milk operations are conducted through Crémierie des Trois Rivières S.E.C.
- (6) Production and sale of dairy products including cheese, butter, powdered milk and evaporated milk throughout Canada.
- (7) Production, sale and distribution of dairy products including fluid milk, sour cream and juices and other beverages in the Maritime Provinces.

## ITEM 2 - GENERAL DEVELOPMENT OF THE BUSINESS

### 2.1 Overview

The Company operates its business through two sectors, the Dairy Products sector and the Grocery Products sector, which represented respectively 87.1% and 12.9% of total sales before the Dairyworld Acquisition (as defined below) on February 5, 2001.

With the Dairyworld Acquisition, the Dairy Products Sector of the Company has increased in size and represents approximately 92.4% of total sales on a pro forma basis. On such basis, 33.6% of the Company's total consolidated sales are made in the United States and 66.4% are made in Canada<sup>1</sup>. Through its two sectors, the Company operates 56 manufacturing facilities and employs over 7,800 employees.

#### *Dairy Products Sector*

The Dairy Products sector is comprised of the Cheese division and the Fluid Milk division. Through its Cheese division, Saputo produces and markets mozzarella, cheddar, as well as other specialty cheeses, butter, and value-added by-products such as lactose and whey protein. In Canada, Saputo also distributes fine imported cheeses to specialty delis and a large assortment of other non-dairy products that complement its cheese distribution to restaurants, especially pizzerias. On a pro forma basis, taking into account the sales by the businesses acquired in the Dairyworld Acquisition between February 5 and March 31, 2001 on an annualized basis, the Cheese division represented approximately 67.1% of the Company's total sales and 72.7% of the Dairy Products sector sales. Of the Company's total sales for the Cheese division in fiscal 2001, approximately 37.6% were made in Canada<sup>1</sup> and 62.4% were made in the United States. In the Cheese division, the Company operates 22 manufacturing facilities in Canada and 15 in the United States. On June 1, 2001, the Company had 3,751 full-time employees and 239 part-time employees working in the Cheese division.

Saputo has established itself as Canada's leading producer of cheese, with a share of approximately 35% of the Canadian cheese production, including the Dairyworld Acquisition, and also ranks as one of the leading natural cheese producers in the United States. In its Cheese division, Saputo services, through independent non-exclusive distributors and sales agents as well as through its own distribution network, three market segments: food service, retail and ingredient. With the Dairyworld Acquisition, the food service segment accounts for 36.1% of the Cheese division sales, the retail segment for 37.9%, and the ingredient segment for 26.0%.

Since the Dairyworld Acquisition, the Company also produces, markets and distributes fluid milk, cream products, sour cream, cottage cheese, yogurt, juices and other beverages which it sells mainly to the retail segment through its DSD (direct-store delivery) distribution network operated by Company-owned and independent distributors, as well as through an important home delivery network. The Fluid Milk division represents 25.3% of the Company's total sales on a pro forma basis, annualizing the revenues from the businesses acquired pursuant to the Dairyworld Acquisition between February 5 and March 31, 2001. In this division, the Company operates 14 manufacturing facilities, all of which are located in Canada. On June 1, 2001, the Company had 1,775 full-time employees and 185 part-time employees working in this division.

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<sup>1</sup> Including international sales made from Canada.

## *Grocery Products Sector*

The Company produces, markets and distributes snack cakes, cookies, fine breads and soups in Canada. These products are sold almost exclusively in the Canadian retail market through a DSD distribution network as well as independent non-exclusive distributors. Saputo is the largest manufacturer of snack cakes and fine breads, as well as one of the most important cookie manufacturers in Canada. In this sector, the Company operates four manufacturing facilities in the Province of Québec and one in the Province of Ontario and employed, as of June 1, 2001, 1,779 full-time employees and 125 part-time employees.

### **2.2 History**

Mr. Emanuele (Lino) Saputo, Chairman of the Board and Chief Executive Officer of Saputo, founded the Company with his parents in 1954, producing quality cheeses for the Italian community of Montréal. In the late 1950's, the Company's first major production facility was constructed in the Montréal Saint-Michel district. In the 1960's, Saputo grew significantly as demand for its products increased both in Montréal and in new markets, such as other regions of Québec, Ontario and the Maritimes.

In the 1970's, Saputo acquired several production operations and developed its national distribution network, positioning itself in Canada as the leading producer of mozzarella, primarily to the food service market segment. In 1981, the Company built a cheese plant in Mont-Laurier, Québec and acquired a cheese plant in Cookstown, Ontario. In 1984, Saputo acquired a plant in Saint-Hyacinthe, Québec which processes liquid whey, a by-product of its cheese production operations, into value-added products such as lactose and whey protein.

Since 1984, Saputo has continued its growth in Canada by acquiring small to medium-sized cheese manufacturers and food distributors located in various parts of Canada. In 1988, the Company entered the United States market by acquiring a cheese manufacturing plant located in Richmond, Vermont and the Jefferson cheese plant now located in Hancock, Maryland.

In 1996, Saputo acquired Fromages Caron Inc., a distributor of fine imported cheeses. On July 31, 1997, Saputo acquired Crémierie des Trois-Rivières, Limitée thereby entering the fluid milk and frozen novelties markets.

On October 15, 1997, the Company completed its initial public offering of 9,470,500 Common Shares at \$17.00 per share (the "**Initial Public Offering**"). In December of the same year, Saputo issued 9,000,000 special warrants at \$25.00 per warrant in order to finance, in part, the Stella Acquisition (as defined below).

On December 5, 1997, Saputo expanded its presence in the United States by acquiring Stella Holdings, Inc., a manufacturer of Italian and European cheeses (which, together with its then wholly-owned subsidiaries, are herein collectively referred to as "**Stella**") from Specialty Foods Corporation for a total consideration of approximately CDN \$580 million (US \$408 million) paid in cash (the "**Stella Acquisition**"). During its fiscal year ended December 31, 1996, Stella had revenues of approximately \$1 billion. With the Stella Acquisition, the Company tripled its revenues and established itself as one of the leading natural cheese producers in the United States.

On May 1, 1998, Saputo acquired from Avonmore Waterford Group plc. all of the outstanding shares of Avonmore Cheese Inc. and Waterford Food Products, Inc., both located in the United States, mainly in Wisconsin (the "**AW Acquisition**") for CDN \$54.1 million (US \$37.8 million). These companies produced Italian specialty cheeses, sweetened condensed milk, Swiss cheese and value-added by-products such as whey protein concentrates, ingredient blends and cream. Of the six plants acquired, two were whey processing facilities.

On August 31, 1998, the Company acquired all of the outstanding shares of Riverside Cheese and Butter

Inc., a specialty cheese manufacturer located in Trenton, Ontario. Saputo also acquired, on September 16, 1998, substantially all of the assets and assumed certain liabilities of Bari Cheese Ltd., an Italian specialty cheese manufacturer based in Vancouver, British Columbia. The aggregate purchase price of \$11.4 million was paid through the private placement of 26,750 Common Shares of Saputo at a price of \$40.00 per share, with the balance paid in cash.

On September 15, 1999, the Company acquired all of the outstanding shares of Culinar Inc. (“**Culinar**”) from SGF Soquia Inc. and various minority shareholders for a price of \$283.5 million (the “**Culinar Acquisition**”). This transaction was paid by the issuance of 2,503,000 Common Shares of Saputo at a price of \$39.95 per share, with the balance paid in cash. Culinar produced, marketed and distributed snack cakes, cookies, fine breads and soups and had sales of approximately \$270 million. With this acquisition, Saputo became the largest manufacturer of snack cakes and fine breads as well as one of the most important cookie manufacturers in Canada.

On November 12, 1999, Saputo completed the private placement of US \$250 million Senior Notes to institutional investors in the United States. The term of the Notes ranges from seven to fifteen years with an average interest rate of 8.16%. The proceeds of the private placement were used to refinance part of the Company’s existing credit facilities.

On February 28, 2000, the Company acquired all of the outstanding shares of Groupe Cayer-JCB Inc., a manufacturer of European cheeses based in the Province of Québec, for a price of \$13.7 million paid in cash and \$6.7 million of indebtedness (the “**Cayer Acquisition**”). Cayer had sales of approximately \$55 million.

### **2.3 Significant Acquisition**

On February 5, 2001, Saputo completed the acquisition of the fluid milk and cheese operations of Agrifoods International Co-operative Limited (“**Agrifoods**”), one of the largest dairy processors in Canada, through the purchase of all of the outstanding shares of some of Agrifoods’ subsidiaries including Dairyland Fluid Division Limited (“**DFDL**”), Armstrong Cheese Company Limited (“**Armstrong**”) and Baxter Foods Ltd. (“**Baxter**”) for the price of \$407.3 million on a debt free basis, financed through bank indebtedness (the “**Dairyworld Acquisition**”). The acquired businesses generated net sales of approximately \$1.4 billion and EBITDA of \$61.4 million per annum. With the Dairyworld Acquisition, Saputo now holds an estimated 20% share of the Canadian market for fluid milk which ranks it among the top three fresh milk processors in Canada, and holds a share of approximately 35% of the Canadian cheese production.

## **ITEM 3 - INDUSTRY OVERVIEW**

### **3.1 Dairy Products Industry**

#### **3.1.1 The Canadian Dairy Industry**

##### *Regulatory Environment*

The regulation of the content, composition, labelling, packaging, marketing and distribution of all food products in Canada is a shared responsibility between the federal and the provincial governments. The dairy industry is further governed by a series of federal and provincial regulations specific to the production, processing and distribution of milk and milk-related products. All applicable statutes, whether provincial or federal, permit plant inspections, product testing and other regulatory scrutiny.

In Canada, all milk processing plants are subjected to regular inspections by federal authorities and are required to be registered under the Canada Agricultural Products Act. Provincial legislation also demands that milk processing plants be licensed, compelling them to comply with all provincial inspections and regulations.

### *Milk Supply*

The Canadian dairy industry operates within a highly regulated environment. The Canadian Dairy Commission (“**CDC**”), a crown corporation, has been mandated by the federal government to implement Canada’s national dairy policy which is predicated on shared jurisdictional powers between the federal and provincial governments. Fluid milk is regulated provincially, while industrial milk is regulated federally. “Fluid milk” refers to table milk or cream intended for consumption in fluid forms, whereas “industrial milk” is used for the manufacturing of all other dairy products, such as cheese, butter, ice cream and yogurt. According to CDC information, the fluid milk sector represents approximately 40% of raw milk delivered in Canada while the industrial milk sector represents approximately 60%.

The Canadian dairy industry operates within a supply management system. The key goal of supply management is to ensure stable revenues for dairy farmers while maintaining the production of sufficient volumes of industrial milk to satisfy the domestic Canadian consumer demand for dairy products as well as certain planned exports. This is essentially achieved by setting the support price that the dairy processors can receive for butter and skimmed milk powder and by controlling the supply of industrial milk.

Dairy farmers also receive a direct federal subsidy which is set to be phased out over the course of the five years commenced in February 1998. It is expected that the subsidy loss will be recovered through higher industrial milk prices.

Every dairy year, the CDC calculates the national industrial milk production quantum based on anticipated domestic demand and certain planned exports. This quantum is then allocated according to the terms of the National Milk Marketing Plan, a federal/provincial agreement. This agreement stipulates, among other things, that Québec’s and Ontario’s shares of the national industrial milk production quantum (the “**Market Sharing Quota**”) are approximately 47.3% and 31.3% respectively.

Once the industrial milk quantum is determined and allocated among the provinces, provincial marketing boards govern the production, pricing and marketing of milk within their own borders. Each provincial marketing board allocates the milk to dairy processors. Industrial milk is allocated according to a cascading system that classifies industrial milk into various classes of products to be manufactured. Priority of supply is given to the higher milk class, which also commands a higher milk price.

Although there may be some provincial variations, quantities of milk in each class other than fluid milk are generally restricted in their growth. As a result, operating in a supply managed system means that a dairy processor of industrial milk can only achieve significant growth through acquisitions. Any attempt to grow internally is stymied by the plant quota which limits a dairy processor of industrial milk to a specific guaranteed volume. Conversely, since the Market Sharing Quota is based on historical and anticipated demand for dairy products, the risk of a processor losing an important part of its market share is very low.

### *International Trade (Canada)*

*Imports.* The Department of Foreign Affairs and International Trade administers Canada’s cheese import quotas. These quotas are divided into European Union and non-European Union sources. This results from Canada’s obligation to the European Union to import 66.0% of the approximately 20.4 million kilograms of cheese that Canada is committed to import annually under the World Trade Organization (“**WTO**”) Agreement on

Agriculture. Imports within this minimum access commitment of 20.4 million kilograms of cheese are subject to low rates of duty while imports over this commitment are subject to significantly higher tariffs. Over-access tariffs for cheese currently stand at 245.5% of invoiced value.

*Exports.* In 1997, the United States and New Zealand challenged the legality of Canada's dairy supply management system under the terms of the 1994 GATT Agreement alleging that Canada's dairy exports benefit from subsidies. In March 1999, the WTO panel ruled in favour of the United States and New Zealand and determined that the structure of Canada's dairy export system provides for the grant of subsidies as a result of the intervention of the governments and their agencies. Canada appealed this decision and, in October 1999, an appellate body of the WTO confirmed most of the original decision. Until the end of February 2000, all cheese export activities had to be submitted for consideration by the CDC. With the WTO decision, the CDC is no longer involved in the issuance of permits to export cheese over and above Canada's export subsidy commitment to the WTO. The federal and provincial governments have since worked with industry stakeholders to devise a system that is WTO compatible, while attempting to protect the integrity of Canada's supply management system and Canada claims to have modified its dairy system accordingly. On March 1, 2001, the United States and New Zealand formally asked the WTO for the permission to impose on Canada economic sanctions of US\$35 million per year for each country as compensation for alleged damages to their dairy industry due to Canadian dairy exports. The United States and New Zealand officially requested that the WTO establish a special committee to examine the issue of compliance in light of Canada's new system. The WTO agreed and the Committee has until January 2002 to decide whether Canada's new system complies with the WTO's regulations. The federal government has undertaken to defend the interest of the Canadian dairy industry before the WTO.

#### *Canadian Market*

The dairy processing industry makes a major contribution to the Canadian economy with shipments valued at over \$9.8 billion in 2000. Second only to meat processing, the dairy processing sector accounted for approximately 14% of the estimated value of all food and beverage processing sales during the same year. Significant rationalization is occurring in the processing sector as plants strive to achieve the greater efficiencies and economies of scale required to remain competitive in increasingly global markets.

In 1999-2000, there were 20,576 dairy farms in Canada. This represents a decrease of 985 farms from the previous dairy year. Approximately 81% of Canada's dairy farms are located in the Provinces of Québec and Ontario. The Western provinces and the Atlantic provinces account for 14% and 5% respectively.



The following table indicates the production volumes of selected dairy products manufactured in Canada in 2000.

**Canadian Production Volumes of Selected Dairy Products in 2000 <sup>(1)</sup>**  
(in thousands)

|  |                |                         |                  |
|--|----------------|-------------------------|------------------|
| Cheddar.....                                 | 134,829 kg     | Yogurt.....             | 149,851 kg       |
| Specialty cheeses <sup>(2)</sup> .....       | 193,596 kg     | Milk powder.....        | 75,386 kg        |
| Cottage cheese.....                          | 22,723 kg      | Concentrated milk ..... | 102,450 kg       |
| Butter.....                                  | 76,852 kg      | Fluid milk .....        | 2,706,964 litres |
| Ice cream and other ice cream products ..... | 497,599 litres | Cream .....             | 170,351 litres   |

(1) Source: Canadian Dairy Commission.

(2) Includes mozzarella (114,594 kg).

### 3.1.2 The United States Dairy Industry

#### *Regulatory Environment*

In the United States, the production of all food products is subject to extensive federal, state and local government regulations regarding the advertising, quality, packaging, labelling and safety.

All food plants are subject to regulation and inspection by agencies such as the Food and Drug Administration (“**FDA**”) and the United States Department of Agriculture (“**USDA**”). Individual states may also enforce more stringent regulations regarding the manufacturing of food products. State and local government agencies work with the federal government to ensure the safety of food produced within their jurisdictions. Violations of federal, state and local regulations may result in seizure and condemnation of products, cease and desist orders, injunctions and monetary penalties. State and local government agencies also enforce environmental compliance.

#### *Milk Supply*

In the United States, there are two grades of milk: Grade A and Grade B. Grade A milk is produced under specific sanitary requirements and dairy producers must hold a Grade A shipping permit. Grade A milk accounts for 98% of the United States milk supply and is used for fluid as well as manufacturing purposes. Grade B milk represents 2% of the United States milk production, and it is used exclusively to manufacture butter, cheese and skim milk powder.

The following table presents the utilization of the United States milk production in 2000:

**Utilization of United States Milk Production in 2000 <sup>(1)</sup>**

|   |       |
|---|-------|
| Utilized as fluid milk and cream.....                 | 33.1% |
| Manufactured into cheese .....                        | 37.1% |
| Manufactured into creamery butter.....                | 13.6% |
| Manufactured into frozen dairy products.....          | 8.6%  |
| Manufactured into evaporated and condensed milk ..... | 1.3%  |
| Used on farms where produced.....                     | 0.8%  |
| Other uses .....                                      | 5.5%  |

(1) Source: USDA, Dairy Products 2000 Annual Report, published April 2001.

In most cases, milk marketed within the United States is priced according to its use. Milk prices are set monthly based on product price formulas. Price data used in the formulas is collected through surveys conducted by the USDA's National Agriculture Statistics Service. Milk used in fluid products is placed in Class I, the highest priced class. Milk used to produce ice cream, yogurt and other soft products is Class II. Milk used to manufacture cheese is Class III, and milk used to produce butter and milk powders is Class IV.

Wholesale pricing for the bulk of the United States cheese production is established by daily cash cheddar cheese trading on the Chicago Mercantile Exchange (CME). The last trade of the day establishes the market price for the day. If no trades occur, the market price is determined based on the bid and offer prices. Processors usually charge a premium over the CME price.

A dairy processing plant is not limited in terms of the quantity of milk it can receive and is free to negotiate its milk supply with whomever it chooses. Independent processors usually negotiate with local cooperatives or may procure milk directly from individual farms. Processors are charged a price which reflects the current month's milk price plus a negotiated handling charge.

United States dairy programs influence the production and marketing of milk and milk products through the operation of the Commodity Credit Corporation ("CCC"), a federal agency. CCC buys butter, non-fat dry milk and cheese at the following support prices:

- Butter @ US \$0.8548 per pound;
- Cheddar Cheese 40 pound blocks @ US \$1.1314 per pound;
- Nonfat dry milk powder @ US \$0.9000 per pound.

Such products are sold or used either domestically or internationally in specific government programs. However, the CCC does not directly support dairy farmers, nor does it establish a target return for farmers.

### *International Trade (United States)*

*Imports.* Another key component of the United States dairy program is import restrictions. Most United States cheese import quotas are country and product specific. Under the terms of the WTO Agreement on Agriculture, the United States agreed to import, at a lower tariff rate, approximately 141,991 metric tons of cheese in 2001. Tariffs for cheese in excess of the quota are prohibitive.

Entry for dairy products made with sheep, goat and buffalo milk do not require a license nor are they subject to a United States duty. The same is true for a few other products including Brie cheese.

*Exports.* The United States is not a significant exporter of dairy products. Its export activity accounted for US \$987.8 million in 2000 and US \$911.6 million in 1999.

Most export activity is conducted through the Dairy Export Incentive Program which allocates subsidized export volumes to specific countries thereby enabling exporters to bid for export assistance for dairy products destined to these countries.

### *United States Market*

The USDA states that there were 395 cheese manufacturing plants in the United States in 2000, which produced 3.8 billion kilograms of cheese. Cheddar accounted for 34.3% of this amount, or 1.3 billion kg, while Italian cheeses totalled 1.5 billion kg, or 40.1%. Mozzarella alone added up to 1.2 billion kg, representing 79.6% of Italian cheeses and 31.9% of all cheeses produced in 2000.

### **3.1.3 Future Trends**

The consolidation trend which began several years ago in both the American and Canadian dairy industries is, in the Company's opinion, set to continue. This evolving competitive environment will necessarily force regional processors to either adapt, sell or merge with other industry participants. Well-capitalized industry consolidators should take advantage of this consolidation trend to make strategic acquisitions.

Despite the failure, in December 1999, of the Seattle conference where the next round of WTO negotiations regarding agriculture were supposed to be held, representatives of the various governments met on March 23, 2000 to initiate discussions that should lead to new tariff and subsidy reductions in agricultural products during the coming years.

In light of the WTO's decision on Canada's dairy exports in 1999, the federal and provincial governments worked with industry stakeholders to devise a system that they claim is WTO compatible. Following the request by the United States and New Zealand to examine Canada's new system, the WTO established a committee which has until January 2002 to decide whether Canada's new system complies with the WTO's regulations. The outcome may not be determined at this time.

As long as Canada's supply management system remains in place, no significant growth can be achieved by Canadian dairy processors other than through acquisitions.

In the United States, plant quotas are non-existent. Accordingly, dairy processing companies are not limited to their existing milk reception volumes, but rather their expansion is a function of the market place's acceptance of their products.

### 3.2 Grocery Products Industry

#### *Regulatory Environment*

The regulation of the content, composition, labelling, packaging, marketing and distribution of all food products in Canada is a shared responsibility between the federal and the provincial governments. The grocery products industry is subject to stringent quality and labelling standards, including those of the *Food and Drugs Act* and of the *Consumer Packaging and Labelling Act*.

#### *Canadian Retail Market*

Over the recent years, Canada's retail market has changed with the increasing importance of non-supermarket channels of distribution such as mass merchandisers and warehouse clubs. This trend has resulted in significant consolidation within the supermarket channel where five national chains controlled more than 82% of all retail sales made through the supermarket channel in 2000.

The snack cake industry generates sales of approximately \$525 million per year in Canada. This industry segment comprises among others, snack cakes, muffins, granola, cereal and fruit bars, fresh baked deserts business as well as marshmallow squares. Prepackaged snack cake products enjoy a 24.4% market share of all snack cake products sold in Canada. Of the prepackaged snack cake products total sales in Canada, approximately 62.6% and 26.5% are made in the provinces of Québec and Ontario, respectively.

## ITEM 4 - DESCRIPTION OF THE BUSINESS

The Company operates its business through two sectors, the Dairy Products sector (which includes the Cheese division and the Fluid Milk division) and the Grocery Products sector. Through its two sectors, the Company operates 56 manufacturing facilities and employs over 7,800 employees.

The following table presents the relative importance of the Company's two sectors during fiscal 2001 as well as on a pro forma basis to better reflect the impact of the Dairyworld Acquisition:

|                         | Sales by Sector                                       |                     |                              |                     |
|-------------------------|---|---------------------|------------------------------|---------------------|
|                         | Pro forma year ended<br>March 31, 2001 <sup>(1)</sup> |                     | Year ended<br>March 31, 2001 |                     |
|                         | Sales<br>(\$000)                                      | % of<br>total sales | Sales<br>(\$000)             | % of<br>total sales |
| Dairy Products sector   |   |                     |                              |                     |
| Cheese division         | 2,209,042   | 67.1                | 1,772,125                    | 82.0                |
| Fluid Milk division     | <u>831,014</u>  | <u>25.3</u>         | <u>137,884</u>               | <u>6.4</u>          |
|                         | 3,040,056   | 92.4                | 1,910,009                    | 88.4                |
| Grocery Products sector | 251,662   | 7.6                 | 251,662                      | 11.6                |
| Total                   | <u>3,291,718</u>                                      | <u>100.0</u>        | <u>2,161,671</u>             | <u>100.0</u>        |

- (1) Takes into account the impact of sales by the businesses acquired pursuant to the Dairyworld Acquisition between February 5 and March 31, 2001 on an annualized basis.

### *Dairy Products Sector – Cheese division*

Through its Cheese division, Saputo produces and markets mozzarella, cheddar as well as other specialty cheeses, butter and value-added by-products such as lactose and whey protein. In Canada, Saputo also distributes fine imported cheeses to specialty delis and a large assortment of other non-dairy products that complement its cheese distribution to restaurants, especially pizzerias. In fiscal 2001, the Cheese division represented approximately 67.1% of the Company's total sales (taking into account the impact of sales by the businesses acquired pursuant to the Dairyland Acquisition between February 5 and March 31, 2001, on an annualized basis) and 72.7% of the Dairy Products sector sales. Of the Company's total sales for the Cheese division in fiscal 2001, approximately 37.6% were made in Canada<sup>2</sup> and 62.4% were made in the United States. In the Cheese division, the Company operates 22 manufacturing facilities in Canada and 15 in the United States. On June 1, 2001, the Company had 3,751 full-time employees and 239 part-time employees working in the Cheese division.

Saputo has established itself as Canada's leading producer of cheese, with a share of approximately 35% of the Canadian cheese production, including the Dairyworld Acquisition, and also ranks as one of the leading natural cheese producers in the United States. In its Cheese division, Saputo services, through independent non-exclusive distributors and sales agents as well as through its own distribution network, three market segments: food service, retail and ingredient. With the Dairyworld Acquisition, the food service segment accounts for 36.1% of the Cheese division sales, the retail segment for 37.9% and the ingredient segment for 26.0%.

### *Dairy Products Sector – Fluid Milk division*

Since the Dairyworld Acquisition, the Company also produces, markets and distributes fluid milk, cream products, sour cream, cottage cheese, yogurt, juices and other beverages which it sells mainly to the retail segment through its DSD (direct-store delivery) distribution network operated by Company-owned and independent distributors, as well as through an important home delivery network. The Fluid Milk division represents 25.3% of the Company's total pro forma sales. In this division, the Company operates 14 manufacturing facilities, all of which are located in Canada. On June 1, 2001, the Company had 1,775 full-time employees and 185 part-time employees working in the Fluid Milk division.

### *Grocery Products Sector*

The Company produces, markets and distributes snack cakes, cookies, fine breads and soups in Canada. These products are sold almost exclusively in the Canadian retail market through a DSD distribution network as well as independent non-exclusive distributors. Saputo is the largest manufacturer of snack cakes and fine breads, as well as one of the most important cookie manufacturers in Canada. In this sector, the Company operates four manufacturing facilities in the Province of Québec and one in the Province of Ontario and employed, as of June 1, 2001, 1,779 full-time employees and 125 part-time employees.

### *Overall Profile*

The Dairyworld Acquisition changed the Company's overall profile by increasing the level of sales made in Canada and in the different market segments. The following tables present the segmentation of total Company sales by region and by market segment for the last two fiscal years and on a pro forma basis, to better reflect the impact of the Dairyworld Acquisition on the Company's sales segmentation:

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<sup>2</sup> Including international sales made from Canada.

Total Company Sales – Geographic Segmentation

|                             | Pro forma year ended<br>March 31, 2001 <sup>(1)</sup> |                     | Year ended<br>March 31, 2001 |                     | Year ended<br>March 31, 2000 |                     |
|-----------------------------|---|---------------------|------------------------------|---------------------|------------------------------|---------------------|
|                             | Sales<br>(\$000)                                      | % of<br>total sales | Sales<br>(\$000)             | % of<br>total sales | Sales<br>(\$000)             | % of<br>total sales |
| United States .....         | 1,106,039   | 33.6                | 1,106,039                    | 51.2                | 1,186,136                    | 63.7                |
| Canada <sup>(2)</sup> ..... | 2,185,679   | 66.4                | 1,055,632                    | 48.8                | 674,742                      | 36.3                |
| Total.....                  | <u>3,291,718</u>                                      | <u>100.0</u>        | <u>2,161,671</u>             | <u>100.0</u>        | <u>1,860,878</u>             | <u>100.0</u>        |

(1) Takes into account the impact of sales by the businesses acquired pursuant to the Dairyworld Acquisition from February 5 to March 31, 2001, on an annualized basis.

(2) Includes international sales made from Canada.

Total Company Sales – Market Segmentation

|  | Pro forma year ended<br>March 31, 2001 <sup>(1)</sup> |                     | Year ended<br>March 31, 2001 |                     | Year ended<br>March 31, 2000 <sup>(2)</sup> |                     |
|--|---|---------------------|------------------------------|---------------------|---|---------------------|
|  | Sales<br>(\$000)                                      | % of<br>total sales | Sales<br>(\$000)             | % of<br>total sales | Sales<br>(\$000)                            | % of<br>total sales |
| <b>Dairy Products Sector</b>                     |   |                     |                              |                     |   |                     |
| Cheese Division                                  |   |                     |                              |                     |   |                     |
| Food Service .....                               | 796,956   | 24.2                | 694,206                      | 32.1                | 759,821                                     | 40.8                |
| Retail.....                                      | 838,035   | 25.5                | 568,966                      | 26.3                | 452,798                                     | 24.3                |
| Ingredient .....                                 | 574,051   | 17.4                | 508,953                      | 23.6                | 501,983                                     | 27.0                |
| Sub-Total .....                                  | 2,209,042   | 67.1                | 1,772,125                    | 82.0                | 1,714,602                                   | 92.1                |
| Fluid Milk<br>Division <sup>(3)</sup>            | 831,014   | 25.3                | 137,884                      | 6.4                 | --  | --                  |
| <b>Grocery Products<br/>Sector<sup>(3)</sup></b> | 251,662   | 7.6                 | 251,662                      | 11.6                | 146,276                                     | 7.9                 |
| Total.....                                       | <u>3,291,718</u>                                      | <u>100.0</u>        | <u>2,161,671</u>             | <u>100.0</u>        | <u>1,860,878</u>                            | <u>100.0</u>        |

(1) Takes into account the impact of sales by the businesses acquired pursuant to the Dairyworld Acquisition from February 5 to March 31, 2001, on an annualized basis.

(2) Fluid milk sales of a nominal amount are included in the Cheese division sales for the March 31, 2000 year end.

(3) The Fluid Milk division products and the grocery products are mainly sold in the retail market segment.

As the Company's sectors are completely different, the description of the Company's business will be divided in two sections, (i) the Dairy Products sector, segregated into the Cheese division and the Fluid Milk division, and (ii) the Grocery Products sector.

## 4.1 Dairy products sector

The following table shows, for the Dairy Products sector, the segmentation of sales by product category for the last two fiscal years as well as on a pro forma basis to better reflect the impact of the Dairyworld Acquisition:

|   | Pro forma year ended<br>March 31, 2001 <sup>(1)</sup> |                     | Year ended<br>March 31, 2001 |                     | Year ended<br>March 31, 2000 <sup>(2)</sup> |                     |
|---|---|---------------------|------------------------------|---------------------|---|---------------------|
|   | Sales<br>(\$ 000)                                     | % of total<br>sales | Sales<br>(\$,000)            | % of<br>total sales | Sales<br>(\$,000)                           | % of<br>total sales |
| Cheese.....   | 1,922,886   | 63.3                | 1,568,058                    | 82.1                | 1,536,070                                   | 89.6                |
| Fluid milk, cream,<br>cottage cheese,<br>yogurt, dairy mixes,<br>juices, and frozen<br>novelties .....                  | 831,014   | 27.3                | 137,884                      | 7.2                 | --  | --                  |
| By-products,<br>sweetened condensed<br>milk, powdered and<br>evaporated milk, butter<br>and non-dairy<br>products ..... | 286,156   | 9.4                 | 204,067                      | 10.7                | 178,532                                     | 10.4                |
| <b>Total .....</b>  | <b><u>3,040,056</u></b>                               | <b><u>100.0</u></b> | <b><u>1,910,009</u></b>      | <b><u>100.0</u></b> | <b><u>1,714,602</u></b>                     | <b><u>100.0</u></b> |

- (1) Takes into account the impact of sales by the businesses acquired pursuant to the Dairyworld Acquisition from February 5 to March 31, 2001, on an annualized basis.
- (2) Fluid milk sales of a nominal amount are included in the Cheese division sales for the March 31, 2000 year end.

### 4.1.1 Products

#### 4.1.1.1 Cheese division

In Canada, Saputo produces and markets nationally a wide variety of quality cheeses including mozzarella and cheddar, speciality cheeses such as ricotta, provolone, parmesan and feta, European cheeses such as havarti, brie and camembert, other firm cheeses including brick, colby, farmer, munster and monterey jack, as well as process cheeses. Saputo's cheese products are sold under various brand names, such as *Saputo*, *Stella*, *Bari*, *Caron*, *Cayer*, *Armstrong*, *Dari-Fresh* and *Faith Farms*. Saputo also sells its cheese products under private labels and produces butter, powdered milk and evaporated milk as well as a number of by-products derived from its cheese production, including lactose and whey protein. The Company's distribution network distributes fine imported cheeses to specialty delis and a large assortment of third party manufactured non-dairy products that complement its cheese distribution to the pizzerias in the food service industry.

In the United States, Saputo produces a broad line of mozzarella, specialty cheese and imitation cheese products which are sold under various brand names such as *Stella*, *Frigo*, *Cheese Heads*, *Dragone* and *Lorraine*,



as well as under private label. The Company also produces sweetened condensed milk as well as whey protein concentrates and ingredient blends which are derived from its cheese production.

#### **4.1.1.2 Fluid Milk division**

With the Dairyworld Acquisition, Saputo has become one of the three largest fresh milk processors in Canada, with an estimated 20% share of the Canadian market. Fluid milk is sold under the *Dairyland* brand in Western Canada, the *Baxter* brand in Eastern Canada and the *Regal* brand in Quebec (through its interest in Cr merie des Trois-Rivi res). Saputo also produces and markets cream, sour cream and cottage cheese under the *Dairyland* and *Baxter* brands and specialty milk under the brand names *Pure'n Fresh Microfiltered Milk*, *Pure'n Fresh Calcium Extra*, *Milk 2 Go*, *Acidophilus Bifidus Milk* and *Lactaid*. In addition to its dairy products line, Saputo also produces and distributes other refrigerated products, including its own brand of juices as well as other products under license from third parties.

#### **4.1.2 Production**

##### *Milk Sourcing*

Due to the regulated nature of the Canadian dairy industry, Saputo sources its milk in Canada from the F d ration des producteurs de lait du Qu bec, the Dairy Farmers of Ontario, the Manitoba Milk Producers, and from Agrifoods in the three Western Canadian provinces. In the Maritimes, milk is purchased from the Milk Marketing Board in New Brunswick and from contracted farmers in Nova Scotia. In the United States, Saputo sources its milk primarily from cooperatives pursuant to contracts.

##### *Facilities*

In the Dairy Products sector, the Company operates a total of 51 manufacturing facilities, 36 of which are located in Canada and 15 in the United States. All of the manufacturing facilities operated in the United States relate to the Cheese division while in Canada, 22 facilities relate to the Cheese division and 14 to the Fluid Milk division. In Canada, the Company owns all of its plants with the exception of the facilities located in Edmonton, Alberta, and Annacis Island, British Columbia. The Company has entered into an agreement to acquire by July 15, 2001 the Edmonton facility, which is presently leased. In the United States, except for the facility located on Rolling Meadows Drive in Fond du Lac, Wisconsin, all of the facilities are owned by the Company.

*Canada.* The Company operates twenty facilities in Western Canada, of which eleven operate in the Cheese division and nine in the Fluid Milk division. These facilities have the overall weekly capacity to process approximately 36 million litres of milk into cheese, fluid milk and other related dairy products and to produce processed cheese.

In Ontario, the Company operates six facilities, with an overall weekly capacity to process approximately 9.5 million litres of milk into cheese or fluid milk. Five of these facilities are used in the Cheese division while the other operates in the Fluid Milk division.

Of the Company's ten facilities in Quebec and Eastern Canada, six form part of the Cheese division and the remaining four are in the Fluid Milk division. The Company has an overall weekly capacity to process approximately 16 million litres of milk into cheese, fluid milk and other related dairy products as well as liquid whey in these facilities.

*United States.* In the American Northeast, the Company operates two plants with an overall weekly capacity to process approximately 5.2 million litres of milk into cheese. The Company also operates eleven facilities in the Midwest, with a total overall weekly capacity to process approximately 33.5 million litres of milk

into cheese and related dairy products and to produce 630,000 lbs of canned milk powders. Finally, the Company operates two facilities in the Western United States, which have a combined weekly capacity to process approximately 9.6 million litres of milk into cheese. All of the U.S. facilities operate in the Cheese division.

### *Net Capital Expenditures*

Management believes that the Company has adequate dairy manufacturing capacity to meet current and near term demand for its products. It is Saputo's intention to continue to expand and modernize its plants, with investments being focused on equipment and processes designed to increase output per litre of milk. More specifically, during the last five fiscal years, Saputo incurred \$179.7 million in net capital expenditures. In fiscal 2001, the Company spent \$9.8 million on its Canadian dairy operations and \$30.9 million on its United States operations. During the last five fiscal years, the previous owners have spent \$144.3 million in net capital expenditure on the Dairyworld operations. In fiscal 2002, Saputo intends to incur net capital expenditures of approximately \$26.3 million for its Canadian dairy operations and \$21.3 million for its United States dairy operations to enhance the efficiency of its plants. The foregoing amounts do not take into account additional expenditures which may become required following the establishment of the integration plans relating to the operations recently acquired through the Dairyworld Acquisition.

### *Environment*

The Company's operations are subject to various federal, provincial, state and local government laws and regulations relating to the protection of the environment. Compliance with these laws and regulations requires the Company to incur expenses and to monitor its operations on an ongoing basis. The Company believes that its operations are in compliance in all material respects with currently applicable environmental laws and regulations except for the issues discussed below. It is the Company's intention to comply with all applicable environmental laws and regulations.

On February 21, 2001, the municipal authority sent a notice to the Grocery Products facility located in Montreal requesting the Company to complete its application for a wastewater discharge permit by July 1, 2001. The Company expects to complete the application within the required delay and does not anticipate any problems in obtaining same.

None of the Grocery Products facilities located in Saint-Lambert, Sainte-Marie and Sainte-Martine has the required environmental certificates of authorization to operate. The Company is presently establishing an action plan with respect to these facilities and expects to file all requests to obtain such permits and authorizations in the course of this fiscal year. Saputo does not anticipate any problems in obtaining same.

The Saint-Raymond facility does not have the required certificate of authorization for its current operations. The Company has filed with the authority a request to obtain a certificate of authorization and does not anticipate any problems in obtaining same.

Certain of the recently acquired Dairyworld facilities have minor contamination issues. At the Calgary dairy plant, the Company, with the concurrence of provincial authorities, is undertaking remediation activities in respect of petroleum contaminated groundwater. At the Harrowsmith, Bashaw and Yorkton facilities, discrete areas of minor petroleum contamination in the soil and/or groundwater have been identified and the Company is considering its options and plans to take appropriate measures in this regard.

Effluent from the Winkler facility is not in compliance with the Town of Winkler's current sewer use by-law. The Company has been paying fines and penalties to the Town to allow the facility to discharge overstrength effluent into the Town's wastewater treatment system. In May 2001, the Town notified the Company that it will

no longer accept overstrength effluent from the facility. The Company is currently negotiating with the Town to resolve this issue and has proposed to fund a portion of the costs (capital and operating) required by the Town to upgrade its treatment system.

Some groundwater quality monitoring wells at the Almena and Lena facilities have shown levels of chloride exceeding the permitted concentration which are the result of past historical practices. The Company continues to monitor the groundwater situation to assess the natural attenuation process.

The Tulare facility has been exceeding its effluent discharge permit limits issued by the City of Tulare and is considered to be in violation with municipal wastewater discharge by-law. During fiscal 2002, the Company will be implementing reduction at source initiatives and expects to improve wastewater quality.

One of the six groundwater quality monitoring wells located at the Kent facility shows levels of chloride in excess of the level permitted in the State of Illinois. The Company closed this facility on April 1, 1999 and is discussing with authorities means to close out the monitoring wells permanently.

On October 20, 1999, the Peru facility received a notice of violation relating to the quality of its wastewater effluent discharge. The Company responded to the authority and has since been implementing various actions, including reduction at source, to improve its wastewater quality. An evaluation of different treatment equipment has been completed and the installation of a pre-treatment system will be done within the next fiscal year.

During fiscal 2001, approximately \$3 million were spent to comply with existing environmental laws and regulations and improve plant efficiency to reduce wastewater loadings, to update or remove underground storage tanks, and to improve wastewater systems at a number of its facilities in Canada and the United States. Management estimates that similar expenditures will amount to \$5 million during fiscal 2002.

Management believes that compliance with currently applicable environmental protection requirements will not have a material effect on the Company's earnings or competitive position during fiscal 2002. Any new environmental laws or regulations could have a material adverse effect on the financial position of the Company and could require significant additional expenditures to achieve or maintain compliance.

### 4.1.3 Markets

#### *Geographic Segmentation*

The Company sells its products in Canada and the United States. The following table presents, for the Dairy Products sector, the geographic segmentation of sales during the last two fiscal years and on a pro forma basis to better reflect the impact of the Dairyworld Acquisition:

Dairy Products Sector – Sales – Geographic Segmentation

|                             | Pro Forma Year ended<br>March 31, 2001 <sup>(1)</sup> |                     | Year ended<br>March 31, 2001 |                     | Year ended<br>March 31, 2000 |                     |
|-----------------------------|---|---------------------|------------------------------|---------------------|------------------------------|---------------------|
|                             | Sales<br>(\$000)                                      | % of<br>total sales | Sales<br>(\$000)             | % of<br>total sales | Sales<br>(\$000)             | % of<br>total sales |
| United States .....         | 1,106,039   | 36.4                | 1,106,039                    | 57.9                | 1,186,136                    | 69.2                |
| Canada <sup>(2)</sup> ..... | 1,934,017   | 63.6                | 803,970                      | 42.1                | 528,466                      | 30.8                |
| Total.....                  | <u>3,040,056</u>                                      | <u>100.0</u>        | <u>1,910,009</u>             | <u>100.0</u>        | <u>1,714,602</u>             | <u>100.0</u>        |

- (1) Takes into account the impact of sales by the businesses acquired pursuant to the Dairyworld Acquisition from February 5 to March 31, 2001, on an annualized basis.
- (2) Includes international sales made from Canada.

*Canada.* Saputo is Canada's leading producer of cheese with a share of approximately 35% of the Canadian cheese production. Saputo sells its products to the food service, retail and ingredient market segments. In Canada, the Company also distributes fine imported cheeses to specialty delis and provides independent pizzerias with numerous food and non-food products sourced from third-party manufacturers that are complementary to the sale of its cheeses to such clients. Since the Dairyworld Acquisition, the Company has become one of the three largest fresh milk processors in Canada with an estimated 20% share of the Canadian market. Saputo also sells, through its Canadian operations, cheese, lactose and whey protein to a vast array of clients in Europe, South America, Asia and Africa.

*United States.* The Company competes in the United States natural cheese industry, by selling branded and private label products to retail, ingredient and food service customers.

#### *Clientele*

Within the Cheese division, the Company services three market segments: food service, retail and ingredient. Within the Fluid Milk division, the Company operates in Canada and sells its products mostly in the retail market segment.

The following table illustrates, for the Dairy Products sector, the segmentation of sales by market segment for each of the last two fiscal years and on a pro forma basis to better reflect the impact of the Dairyworld Acquisition:

Dairy Products Sector – Sales – Market Segmentation

|                                    | Pro Forma Year ended<br>March 31, 2001 <sup>(1)</sup> |                     | Year ended<br>March 31, 2001 |                     | Year ended<br>March 31, 2000 <sup>(2)</sup> |                     |
|------------------------------------|---|---------------------|------------------------------|---------------------|---|---------------------|
|                                    | Sales<br>(\$000)                                      | % of<br>total sales | Sales<br>(\$000)             | % of<br>total sales | Sales<br>(\$000)                            | % of<br>total sales |
| Cheese Division                    |   |                     |                              |                     |   |                     |
| Food Service .....                 | 796,956   | 26.2                | 694,206                      | 36.3                | 759,821                                     | 44.3                |
| Retail.....                        | 838,035   | 27.6                | 568,966                      | 29.8                | 452,798                                     | 26.4                |
| Ingredient .....                   | 574,051   | 18.9                | 508,953                      | 26.7                | 501,983                                     | 29.3                |
| Sub-Total .....                    | 2,209,042   | 72.7                | 1,772,125                    | 92.8                | 1,714,602                                   | 100.0               |
| Fluid Milk Division <sup>(3)</sup> | 831,014   | 27.3                | 137,884                      | 7.2                 | --  | --                  |
| Total.....                         | <u>3,040,056</u>                                      | <u>100.0</u>        | <u>1,910,009</u>             | <u>100.0</u>        | <u>1,714,602</u>                            | <u>100.0</u>        |

(1) Takes into account the impact of sales by the businesses acquired pursuant to the Dairyworld Acquisition from February 5 to March 31, 2001, on an annualized basis.

(2) Fluid milk sales of a nominal amount are included in the Cheese division sales for the March 31, 2000 year end.

(3) The fluid milk products are mainly sold in the retail market segment.

*Cheese Division*

*Food service.* Food service customers principally include distributors, restaurants (corporate restaurant chains, franchisees and individually-owned) and hotels. Saputo provides its food service customers with branded and private label dairy products. In the case of independent pizzerias in Canada, Saputo also provides these clients with non-dairy products manufactured by third parties through its own distribution network. With the Dairyworld Acquisition, Saputo also produces soft-serve dairy mixes for quick service restaurant chains and holds an important market share of volume processed in this category in Canada. No food service customer represented more than five percent of total consolidated sales during each of fiscal 2001 and 2000.

*Retail.* Saputo sells both branded and private label products to its retail customers which include supermarket chains, independent retailers, warehouse clubs and specialty cheese boutiques. In fiscal 2001, approximately 80% of Saputo's retail sales were in branded products with the remainder being private label. Saputo's retail grocery products are sold in the dairy case and deli cheese counter sections of stores. In Canada, Saputo also provides its retail customers with European cheeses and imported cheeses. The acquisition of Fromages Caron Inc. in 1996, of Groupe Cayer-JCB Inc. in February 2000, and the Dairyworld Acquisition in 2001, have enhanced the Company's presence in the retail market segment. No retail customer represented more than five percent of total consolidated sales during each of fiscal 2001 and 2000.

*Ingredient.* Ingredient clients include processors who use the Company's products as an ingredient in the preparation of other food items. The Company supplies cheese to a majority of Canadian frozen pizza manufacturers as well as to processors of frozen entrées and supplies many important food manufacturers in the United States. Consistent with the trend of increased home-meal replacements, Saputo continues to seek opportunities in this market segment. To support this effort, Saputo's technical experts work with customers to

develop new products customized to their needs. No ingredient customer represented more than five percent of total consolidated sales during each of fiscal 2001 and 2000.

### *Fluid Milk Division*

Saputo's fluid milk products are mainly sold in the retail market segment. Through the Dairyworld Acquisition, Saputo has inherited strong relationships with the majority of the large national and regional grocery retailers in Canada for its Fluid Milk division. The Canadian retail segment is mainly comprised of the grocery channel, which represents approximately 75% of fluid milk and related products sold to consumers. The top ten customers in the Fluid Milk division account for approximately 62% of the sales of this division.

## **4.1.4 Distribution**

### **4.1.4.1 Cheese division**

In Canada, sales are made through direct shipments to certain large food service, retail and ingredient customers as well as to national and regional third party distributors. Saputo has also developed a nation-wide distribution network for its cheese operations which is targeted at serving a clientele comprised of independent pizzerias and retail deli customers. This network is comprised of 15 distribution centers located across Canada. Saputo believes that its distribution network is the cornerstone of its market penetration in these markets as its weekly personalized service constitutes an advantage against competing cheese manufacturers.

In the United States, sales are made through direct shipments to certain large food service, retail and ingredient customers as well as to national and regional third party distributors.

### **4.1.4.2 Fluid Milk division**

With respect to its fluid milk operations, Saputo inherited from the Dairyworld Acquisition a comprehensive DSD network in all Canadian provinces other than Quebec and Newfoundland. The DSD network covers major retailers, mass merchandisers, convenience store chains, food service organizations and individual retailers. Saputo also operates one of the largest home delivery networks for milk and other food products in Canada, with over 60,000 accounts.

The Company's Canadian distribution network for the Fluid Milk division is comprised of 545 distribution routes and 14 warehouses.

## **4.1.5 Competition**

### **4.1.5.1 Cheese division**

*Canada.* In the Cheese division in Canada, the Company competes mainly with Agropur coopérative agro-alimentaire (“**Agropur**”), Parmalat Canada Inc. (“**Parmalat**”), Kraft General Foods Canada Inc. (through the production volumes of Agropur) and National Cheese Co. Ltd. Saputo has established itself as Canada's leading producer of cheese with a share of approximately 35% of the Canadian cheese production, including the Dairyworld Acquisition.

*United States.* In the United States, the Company competes on a national basis with regional and national competitors including Belgioioso Cheese Inc., Con Agra Dairy Foods (formerly known as Beatrice), Dairy Farmers of America, Kraft Foods, Inc., Lactalis USA, Inc. (Sorrento), Land O'Lakes, Inc. and LePrino Foods Company.

#### **4.1.5.2 Fluid Milk division**

Saputo holds an estimated 20% share of the Canadian market for fluid milk which ranks it among the top three largest fresh milk processors, all of which hold similar market shares. The Company faces very broad competition in most product categories, with specific competitors varying widely by region. Among the Company's largest competitors are Agropur and Parmalat. Other competitors include co-operatives in British Columbia and Atlantic Canada.

#### **4.1.6 Employee Relations**

As at June 1, 2001, the Company's Dairy Products sector had 3,752 full-time employees and 378 part-time employees in Canada and 1,774 full-time and 46 part-time employees in the United States.

Before the Dairyworld Acquisition, all of the Company's Canadian plants and distribution centres were non-unionized, except for the Trois-Rivières facility. Since the Dairyworld Acquisition, approximately 35% of the Canadian Dairy Products sector work force is unionized. In the United States, approximately 36% of the Dairy Products sector work force is unionized.

The Company presently does not foresee any labour unrest in connection with the renewal of the agreements expiring in fiscal 2002. All agreements that expired in fiscal 2001 were either renewed upon satisfactory terms or continue to govern during ongoing negotiations, which are expected to result in satisfactory renewals. The Company has good employee relations both in Canada and in the United States. The loyalty and dedication of its employees are key elements in the Company's performance. In Management's opinion, this is the direct result of the family culture that has permeated the entire Company.

### **4.2 Grocery Products Sector**

The Company operates this sector since the Culinar Acquisition, which was completed on September 15, 1999. The following provides an overview of the products, production facilities, markets, competition and employee relations for the Grocery Products sector.

#### **4.2.1 Products**

The Company produces and markets four categories of products, being snack cakes, cookies, fine breads and soups. These products are sold almost exclusively in the Canadian retail market. Within this sector, the Company manufactures snack cakes, muffin bars, flakies and tarts. Saputo occupies a predominant position in the snack cake market in Canada and its products are sold under the *Vachon* and *Hostess* umbrella brands which carry recognized brand names such as *Ah Caramel!*, *Hop & Go*, *Jos Louis*, *May West*, *Passion Flakie* and others. The Company also manufactures a variety of cookies which are sold under the *Viau-McCormick* umbrella brand which carries recognized brand names such as *Normandie*, *Viva Puffs*, *Wagon Wheels*, *Whippet*, *Imagine* and others; as well as rusks, croutons, melba toasts, bread sticks, crisp breads and snack breads that are sold under recognized brand names such as *Grissol* and *Li'l Craving*; and a variety of soups and stock mixes which are sold under the *Loney's* brand.

## **4.2.2 Production**

### *Facilities*

Saputo operates four manufacturing facilities in Quebec within the Grocery Products sector, all of which are owned by the Company, and one in Ontario which is leased. These facilities have a combined total weekly capacity of 1,951,000 kg.

### *Net Capital Expenditures*

During fiscal 2001 and 2000, the Company incurred \$2.2 million and \$3.1 million in capital expenditures, respectively. During the four years prior to the acquisition, the prior owners had spent an aggregate of approximately \$43.8 million in net capital expenditures on existing facilities. In fiscal 2002, the Company expects to incur net capital expenditures of approximately \$4.3 million to enhance the efficiency of its Grocery Products sector.

### *Environment*

For a discussion of environmental matters relating to the Grocery Products sector, reference is made to the section entitled “**Dairy Products Sector – Production – Environment**”.

## **4.2.3 Markets and distribution**

The Company is the largest manufacturer of snack cakes and fine breads as well as one of the most important cookie manufacturers in Canada. Saputo sells its products almost exclusively in the Canadian retail market, including a significant portion through the supermarket channel. In fiscal 2001, 95.2% of the Company's sales for this sector were in branded products, with the remainder being private label and ingredient. The Company's products are distributed mainly through its DSD grocery distribution network.

## **4.2.4 Competition**

In the snack cakes category, the Company competes with regional manufacturers which enjoy significantly smaller market shares than Saputo. In the Province of Québec, the Company's main competitors are Pâtisserie Chevalier Inc. and Pâtisserie Jean-Claude Fortin Inc. In Ontario and Western Canada, the principal competitors are Oakrun Farm Bakery Ltd. and McSweeney's Plus Distribution Ltd., respectively.

## **4.2.5 Employee Relations**

As at June 1, 2001, the Grocery Products sector had 1,779 full time employees and 125 part time employees, approximately 75% of which were unionized. None of the collective agreements relating to the employees in this sector expires in fiscal 2002.



## ITEM 5 - SELECTED CONSOLIDATED FINANCIAL INFORMATION

### 5.1 Selected Consolidated Financial Information for the Last Five Fiscal Years

|   | Years ended March 31   |                  |                  |                     |                     |
|---|--|------------------|------------------|---------------------|---------------------|
|   | 2001 <sup>(1)</sup>  | 2000             | 1999             | 1998 <sup>(2)</sup> | 1997 <sup>(3)</sup> |
|   | (audited)<br>(in thousands of dollars, except per share amounts) |                  |                  |                     |                     |
| <b>Statement of earnings data</b>                               |  |                  |                  |                     |                     |
| Revenue .....   | 2,161,671  | 1,860,878        | 1,915,637        | 817,255             | 450,512             |
| Cost of sales, selling and administrative expenses .....        |  |                  |                  |                     |                     |
|   | <u>1,890,697</u>   | <u>1,623,933</u> | <u>1,724,550</u> | <u>721,828</u>      | <u>378,845</u>      |
| EBITDA <sup>(4)</sup> .....                                     | 270,974  | 236,945          | 191,087          | 95,427              | 71,667              |
| EBITDA margin .....   | 12.5%  | 12.7%            | 10.0%            | 11.7%               | 15.9%               |
| Depreciation of fixed assets .....                              | 51,763   | 37,785           | 27,051           | 13,068              | 7,383               |
| Operating income .....  | 219,211  | 199,160          | 164,036          | 82,359              | 64,284              |
| Interest on long-term debt .....                                | 40,703   | 34,184           | 28,589           | 8,435               | --                  |
| Other interest, net of interest income .....                    | <u>(1,184)</u>   | <u>3,397</u>     | <u>5,307</u>     | <u>491</u>          | <u>231</u>          |
| Earnings before income taxes and amortization of goodwill ..... | 179,692  | 161,579          | 130,140          | 73,433              | 64,053              |
| Income taxes .....  | <u>55,607</u>  | <u>51,386</u>    | <u>43,170</u>    | <u>25,053</u>       | <u>22,642</u>       |
| Earnings before amortization of goodwill .....                  | 124,085  | 110,193          | 86,970           | 48,380              | 41,411              |
| Amortization of goodwill .....                                  | <u>13,844</u>  | <u>10,125</u>    | <u>7,877</u>     | <u>2,635</u>        | <u>413</u>          |
| Net earnings .....  | <u>110,241</u>   | <u>100,068</u>   | <u>79,093</u>    | <u>45,745</u>       | <u>40,998</u>       |
| Net margin .....  | 5.1%   | 5.4%             | 4.1%             | 5.6%                | 9.1%                |
| Earnings per share <sup>(5)</sup> .....                         | 2.15   | 2.00             | 1.63             | 1.23                | 1.37                |
| Diluted earnings per share <sup>(6)</sup> .....                 | 2.14   | 1.99             | 1.62             | 1.22                |                     |
| <b>Balance sheet data</b>                                       |  |                  |                  |                     |                     |
| Total assets .....  | 2,012,979  | 1,411,002        | 1,072,049        | 896,662             | 175,767             |
| Long-term debt (excluding current portion) .....                | 700,821  | 461,353          | 328,639          | 330,271             | --                  |
| Dividends per share <sup>(7)</sup> .....                        | 0.36   | 0.24             | 0.24             | 0.05 <sup>(8)</sup> |                     |
| Shareholders' equity .....                                      | 747,901  | 628,894          | 449,993          | 369,893             | 114,190             |
| <b>Statement of cash flow data</b>                              |  |                  |                  |                     |                     |
| Cash generated by operations <sup>(9)</sup> .....               | 190,090  | 176,047          | 128,334          | 63,972              | 49,114              |
| Net additions to fixed assets .....                             | 42,934   | 53,115           | 62,624           | 22,107              | 4,242               |

(1) Includes the results of Dairyworld from February 5, 2001 to March 31, 2001.

(2) Includes the results of Stella from December 6, 1997 to March 31, 1998.

(3) Certain amounts for periods prior to the Company's Initial Public Offering are omitted as such information would be based upon assumptions that would make it irrelevant.

(4) Earnings before interest, income taxes, depreciation and amortization.

(5) Earnings per share have been calculated using the weighted average number of Common Shares outstanding during the year.

(6) Diluted earnings per share have been calculated using the sum of the weighted average number of outstanding Common Shares during the year ended March 31 as well as the number of potentially dilutive shares under options granted pursuant to the Company's Stock Option Plan.

(7) The amounts of dividends per share for the year ended March 31, 1997 have been omitted as they are not indicative of future dividends as a result of the amount of dividends paid and the number of shares then outstanding.

(8) The amount of \$0.05 per share represents the quarterly dividend declared and paid on March 6, 1998 for the period from October 15, 1997 to December 31, 1997 in accordance with the Company's dividend policy. See "Dividend Policy".

(9) Before changes in non-cash operating working capital items.

(10) For information on each of the Dairy Products sector and the Grocery Products sector, reference is made to page 42 and page 43 of the 2001 Annual Report of Saputo, which information is incorporated herein by reference.

## 5.2 Selected Consolidated Quarterly Financial Information

Three-month periods ended

|  | Fiscal 2001  |                |                 |                | Fiscal 2000    |                |                 |                |
|--|--|----------------|-----------------|----------------|----------------|----------------|-----------------|----------------|
|  | March<br>31 <sup>(1)</sup>   | December<br>31 | September<br>30 | June<br>30     | March<br>31    | December<br>31 | September<br>30 | June<br>30     |
|  | (unaudited)<br>(in thousands of dollars, except per share amounts) |                |                 |                |                |                |                 |                |
| Revenue .....  | 688,079  | 490,135        | 503,508         | 479,949        | 453,525        | 497,391        | 495,031         | 414,931        |
| Cost of sales, selling and<br>administrative expenses .....          | <u>608,495</u>   | <u>432,534</u> | <u>436,478</u>  | <u>413,190</u> | <u>387,917</u> | <u>431,824</u> | <u>439,428</u>  | <u>364,764</u> |
| EBITDA <sup>(2)</sup> .....  | 79,584   | 57,601         | 67,030          | 66,759         | 65,608         | 65,567         | 55,603          | 50,167         |
| <i>EBITDA margin</i> .....   | 11.6%  | 11.8%          | 13.3%           | 13.9%          | 14.5%          | 13.2%          | 11.2%           | 12.1%          |
| Depreciation of fixed assets<br>.....                                | 15,359   | 11,960         | 12,052          | 12,392         | 10,229         | 10,777         | 8,779           | 8,000          |
| Operating income .....   | 64,225   | 45,641         | 54,978          | 54,367         | 55,379         | 54,790         | 46,824          | 42,167         |
| Interest on long-term debt.  | 12,117   | 9,233          | 9,446           | 9,907          | 11,411         | 9,800          | 6,655           | 6,318          |
| Other interest, net of interest<br>income .....                      | <u>(173)</u>   | <u>(680)</u>   | <u>(274)</u>    | <u>(57)</u>    | <u>(565)</u>   | <u>861</u>     | <u>1,584</u>    | <u>1,517</u>   |
| Earnings before income<br>taxes and amortization of<br>goodwill..... | 52,281   | 37,088         | 45,806          | 44,517         | 44,533         | 44,129         | 38,585          | 34,332         |
| Income taxes .....   | <u>15,571</u>  | <u>11,480</u>  | <u>14,529</u>   | <u>14,027</u>  | <u>12,549</u>  | <u>14,695</u>  | <u>12,766</u>   | <u>11,376</u>  |
| Earnings before amortization<br>of goodwill.....                     | 36,710   | 25,608         | 31,277          | 30,490         | 31,984         | 29,434         | 25,819          | 22,956         |
| Amortization of goodwill...  | <u>4,252</u>   | <u>3,235</u>   | <u>3,177</u>    | <u>3,180</u>   | <u>3,049</u>   | <u>3,137</u>   | <u>2,109</u>    | <u>1,830</u>   |
| Net earnings .....   | <u>32,458</u>  | <u>22,373</u>  | <u>28,100</u>   | <u>27,310</u>  | <u>28,935</u>  | <u>26,297</u>  | <u>23,710</u>   | <u>21,126</u>  |
| <i>Net margin</i> .....  | 4.7%   | 4.6%           | 5.6%            | 5.7%           | 6.4%           | 5.3%           | 4.8%            | 5.1%           |
| Earnings per share <sup>(3)</sup> .....                              | 0.63   | 0.44           | 0.55            | 0.53           | 0.57           | 0.51           | 0.49            | 0.43           |

(1) Includes the results of Dairyworld from February 5, 2001 to March 31, 2001.

(2) Earnings before interest, income taxes, depreciation and amortization.

(3) Earnings per share for each quarter have been calculated using the weighted average number of Common Shares outstanding during the quarter.

## **ITEM 6 - DIVIDEND POLICY**

Saputo has a policy of declaring quarterly cash dividends on the Common Shares. In fiscal 2001, the Company's dividend policy was reviewed by the Board of Directors and the dividend of \$0.06 per share, representing a yearly dividend of \$0.24 per share, was increased on August 2, 2000 to \$0.09 per share, representing a yearly dividend of \$0.36 per share. The balance of the Company's earnings are reinvested to finance the growth of its business. The Company's dividend policy will be reviewed from time to time by the Board of Directors and will depend on Saputo's financial condition, results of operations, capital requirements and such other factors as the Board of Directors, in its sole discretion, deems relevant.

## **ITEM 7 - MANAGEMENT'S DISCUSSION AND ANALYSIS**

A discussion and analysis by management of the financial condition and results of operations of the Company for the fiscal year ended March 31, 2001 is presented under the section "Management's Discussion and Analysis" on pages 21 to 26 of the 2001 Annual Report of Saputo, which section is incorporated herein by reference. To complete Management's discussion and analysis, reference is made to the Consolidated Financial Statements of Saputo for the fiscal year ended March 31, 2001, and the Notes thereto appearing on pages 28 to 43 of the 2001 Annual Report of Saputo, which Consolidated Financial Statements and Notes are also incorporated herein by reference.

## **ITEM 8 - MARKET FOR SECURITIES**

The Common Shares of Saputo are listed on The Toronto Stock Exchange under the stock market symbol "SAP".

## **ITEM 9 - DIRECTORS AND OFFICERS**

### **9.1 Directors**

The following table sets forth, for each director, his name and municipality of residence, the year in which he first became a director, the principal occupation of each director and the number of Common Shares beneficially owned, directly or indirectly, or over which control or direction was exercised as at June 1, 2001. Directors are elected until the next annual meeting of shareholders or, in the case of a vacancy or resignation, until a successor is elected or appointed.

| Name and municipality<br>of residence                       | Director<br>since | Principal occupation   | Common Shares<br>beneficially owned<br>or over which<br>control or<br>direction was<br>exercised |
|---|-------------------|--|--|
| EMANUELE (LINO) SAPUTO <sup>(2)</sup><br>Senneville, Québec | 1992              | Chairman of the Board and<br>Chief Executive Officer of the<br>Company   | 33,800,037 <sup>(1)</sup>  |
| ANDRÉ BÉRARD <sup>(2)</sup><br>Verdun, Québec               | 1997              | Chairman of the Board and<br>Chief Executive Officer of a<br>Canadian Chartered Bank                               | 2,500  |
| CLAUDE BLANCHET <sup>(3)</sup><br>Île Bizard, Québec        | 2000              | Chairman of the Board,<br>President and Chief Executive<br>Officer of Société générale de<br>financement du Québec | --   |
| PIERRE BOURGIE <sup>(2)</sup><br>Outremont, Québec          | 1997              | President and Chief Executive<br>Officer of Société Financière<br>Bourgie Inc. (a holding<br>company)              | 230,000  |
| CATERINA MONTICCIOLO, CA <sup>(3)</sup><br>Laval, Québec    | 1997              | Controller of Placements<br>Vigica Inc. (a holding<br>company)   | 59,500   |
| LINO A. SAPUTO, JR.<br>Westmount, Québec                    | 2001              | Executive Vice-President,<br>Operations of the Company   | 16,588   |
| PATRICIA SAPUTO, CA, FP <sup>(3)</sup><br>Laval, Québec     | 1999              | President of Pasa Holdings<br>Inc. (a holding company)   | 8,600  |
| LOUIS A. TANGUAY <sup>(3)</sup><br>Laval, Québec            | 1997              | President and Chief Executive<br>Officer of Bell Canada<br>International   | 2,000  |

(1) The shares are held by Jolina Capital Inc. and Gestion Jolina Inc., both of which are holding companies controlled by Mr. Emanuele (Lino) Saputo, and by other holding companies owned and controlled by his brothers and sisters and their families, which have granted to Gestion Jolina Inc. a power of attorney to vote all of the Common Shares held by them at the time of the Company's Initial Public Offering.

(2) Members of the Corporate Governance and Human Resources Committee.

(3) Members of the Audit Committee.

During the last five years, all of the above directors have been engaged in their present principal occupations or in other executive capacities with the companies indicated opposite their name or with related or affiliated companies, except for: Mr. Claude Blanchet, who, prior to April 1997, was President – General Manager of Fonds de solidarité des travailleurs du Québec (FTQ); Mr. Pierre Bourgie who, prior to January 1997, was President and Chief Executive Officer of Urgel Bourgie Inc. (funeral services); Ms. Caterina Monticciolo who, from January 1995 to October 1996, was a financial analyst with the Company and prior thereto was an accountant with Deloitte & Touche (an accounting firm); Mr. Lino A. Saputo, Jr. who, from January 1, 2000 to

January 15, 2001, was Assistant to the President of Uniforêt Inc. (a lumber company); and Ms. Patricia Saputo who, prior to July 1998, was a Senior Tax Manager with Deloitte & Touche.

Information as to shares beneficially owned by each director, or over which each exercised control or direction, as at June 1, 2001, has been furnished by the directors individually as such information is not within the knowledge of the Company.

## 9.2 Executive Officers

The following table sets forth the name, municipality of residence and position with the Company of each person who is an executive officer of the Company as of the date hereof:

| <b>Name and municipality of residence</b>       | <b>Position</b>  |
|---|--|
| Emanuele (Lino) Saputo<br>Senneville, Québec    | Chairman of the Board and<br>Chief Executive Officer                   |
| Louis-Philippe Carrière, CA<br>Lorraine, Québec | Executive Vice-President,<br>Finance and Administration and Secretary  |
| Dino Dello Sbarba<br>Rosemère, Québec           | Executive Vice-President,<br>Sales, Marketing and Logistics            |
| Pierre Leroux<br>Boucherville, Québec           | Executive Vice-President,<br>Human Resources and Quality Assurance     |
| Lino A. Saputo, Jr.<br>Westmount, Québec        | Executive Vice-President, Operations                                   |
| Randy Williamson<br>Surrey, British Columbia    | Executive Vice-President and<br>Chief Operating Officer, Milk Division |

During the last five years, all of the above executive officers have held the principal occupation indicated above or other executive capacities with the Company, except for Lino A. Saputo, Jr. who, from January 1, 2000 to January 15, 2001, was Assistant to the President of Uniforêt Inc. (a lumber company) and Randy Williamson who, between 1998 and the completion of the Dairyworld Acquisition, was Chief Operating Officer of Dairyworld, and prior to 1998 was Senior Vice-President, Operations of Dairyworld.

As at June 1, 2001, the directors and executive officers of Saputo, as a group, beneficially owned, directly or indirectly, or exercised control or direction over, an aggregate of 34,130,215 Common Shares, representing approximately 66.5% of the outstanding Common Shares of the Company. Additional information concerning the share holdings of directors is contained in the section entitled "Election of Directors" appearing on page 3 of the Company's Management Proxy Circular dated June 5, 2001, which information is incorporated herein by reference.

## ITEM 10 – ADDITIONAL INFORMATION

Additional information, including directors' and officers' remuneration and indebtedness, principal holders of Saputo's securities, options to purchase securities and interests of insiders in material transactions, where applicable, is contained in Saputo's Information Circular for Solicitation of Proxies dated June 5, 2001. Additional financial information is included in the Consolidated Financial Statements of Saputo and Notes thereto for the fiscal year ended March 31, 2001. Copies of these documents may be obtained upon request from the Secretary of Saputo, at its head office, 6869 Metropolitan Boulevard East, Saint-Léonard, Québec, H1P 1X8, Telephone: (514) 328-6662.

In addition, when the securities of Saputo are in the course of a distribution pursuant to a short form prospectus or when a preliminary short form prospectus has been filed, the following documents may be obtained free of charge from the Secretary of the Company:

- (i) one copy of the Annual Information Form, together with one copy of any documents or portion thereof incorporated by reference therein;
- (ii) one copy of the comparative financial statements of Saputo for its most recently completed fiscal year together with the report of the auditors thereon and one copy of any interim financial statements of Saputo subsequent to the financial statements for its most recently completed fiscal year;
- (iii) one copy of Saputo's Information Circular for Solicitation of Proxies for its most recent annual meeting of shareholders which involved the election of directors; and
- (iv) one copy of any other documents that are incorporated by reference in the preliminary short form prospectus or the short form prospectus.

At any other time, one copy of the documents referred to in subparagraphs (i) (ii) and (iii) above will be provided free of charge upon request to the Secretary.

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