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Building our future together
Annual Report

Canada Post · Postes Canada

From anywhere... to anyone

IF YOU CATCH SIGHT OF HUGUES BOIVIN, HE'S PROBABLY GOING BY YOU IN A FLASH. SNOWBOARDING, MOUNTAIN BIKING AND COMPETITIVE BOXING ARE JUST SOME OF THE FAST-PACED SPORTS HE ENJOYS, IN BETWEEN HIS BUSY JOB WITH A SPORTS MEDICINE COMPANY AND CARING FOR HIS BEAUTIFUL THREE-YEAR-OLD DAUGHTER.

And online shopping, Hugues finds, dovetails perfectly into that active lifestyle. "As a guy, especially, I don't enjoy going shopping to five stores to find what I want," he explains. "But you shop online and in ten minutes you're done. Fast! You don't even have to drive anywhere." Hugues adds that he'll also check out flyers and offers he receives in the mail and then order the items he wants online.

From his home, nestled in the woods near a river in picturesque Wakefield, Quebec, Hugues appreciates the freedom to shop the world through the Internet. "If you go to the big-box stores, you'll be able to buy what everybody else has," he says. "But online, you can find things that are unique and different."

In addition to finding a "princess" horse helmet and painting materials for his daughter, Hugues has purchased skeletal hand and wrist models for his job. "Canada Post delivers them and the process is easy. It's perfect!"

Canada Post's online shipping solutions help to bring a world of shopping experiences to Canadians on the go. A partnership with eBay.ca allows Canadians to choose Canada Post to deliver their purchases at the click of a mouse. And Canada Post's Borderfree™ service lets Canadians access a wide choice of retailers, where they can shop in Canadian dollars and receive a guaranteed price of what they can expect to pay in shipping, duties and taxes. No brokerage fees, no CODs and no surprises at the door.

WHEN ROGERS WANTED TO ENHANCE ITS ONLINE BILLING SERVICE, IT TURNED TO CANADA POST.

Rosie Serpa, Vice-president of Web Customer Experience and Operations at Rogers, explains: "We needed a user-friendly online billing application and Canada Post's SmartFlow was the most flexible. The team also shared our vision of putting our customer needs first."

The SmartFlow application was flexible, scalable and could be customized. But the most important factor? "Trust," says Rosie. "If the ebill experience isn't easy, secure and reliable, customers won't have any confidence in it. It's all about trust."

So Rogers and the Canada Post SmartfFlow team conducted customer-first usability testing and added functionality to meet customer needs. "We learned customers wanted to navigate their bill in many ways, to download call records and prioritize information. We made sure it was very easy to manage, and we added several enhanced features over paper bills."

As a result of the partnership, ebill usage by Rogers' customers has doubled. Customers can now access ebills through Rogers' website, epost.ca or online banking.

For Rosie, the partnership has been a match made in heaven. "We see this as a true partnership that benefits our customers and the environment."

Canada Post is offering choices in a world of paper and electronic communications. SmartFlow™ Document Management Services is a suite of services that helps businesses manage their communications process and enables them to meet the growing demand for a choice of communications channels from their own customers. Companies using SmartFlow services also can realize efficiencies and cost savings.

"I LIKE IT HERE!" SO SAYS LEA ABUBO ABOUT HER JOB WITH CANADA POST. THE CHANCE TO WORK OUTSIDE WAS WHAT FIRST ATTRACTED LEA TO BECOME A LETTER CARRIER IN THE CAPILANO AREA OF NORTH VANCOUVER.

A self-described athlete who's into scuba diving and running, walking 10 to 15 kilometres a day was right in step with Lea's training. While she now also drives a van to deliver the mail, she still likes the physically demanding aspects of her job.

Lea enjoys the chance to work with different people too, both inside and outside of her letter carrier depot. "I've made a lot of friends among my co-workers. The people here are very friendly and great to work with," she says. "When people ask me, I tell them Canada Post is a good place to work."

Lea also works hard to build a good relationship with her customers. "They call me Smiley," she grins, and it's easy to see why. "I think it's important to be friendly and say good morning. I try to give good customer service and I know they appreciate it. It means a lot to them, and it means a lot to me too. We're all in this for the customer."

Fostering employee engagement – a feeling of involvement, satisfaction and worth – is a key priority at Canada Post. When employees feel engaged, they tend to be more productive, happier in their jobs and provide better customer service – a win-win situation for everyone. Canada Post was named a Top 100 Employer in 2007, and launched a number of key initiatives to further its goal of becoming the employer of choice in Canada.

FIONA DAVID MAKES A LIVING BY FOLLOWING HER PASSIONS. HER FINE JEWELLERY IS INSPIRED BY TRAVEL, FINE ART AND NATURE. THE CHERRY TREE BLOSSOMS INSPIRED BY BRITISH COLUMBIA'S FRAGRANT TREES, THE SEA ROCKS NEAR HER HOME IN WHITE ROCK, AND MONET'S WATER LILIES HAVE ALL FOUND THEIR WAY ONTO HER ELEGANT FUSED-GLASS PENDANTS.

When Fiona decided to move her 20-year-old business online, she was excited by the possibilities of reaching a global audience.

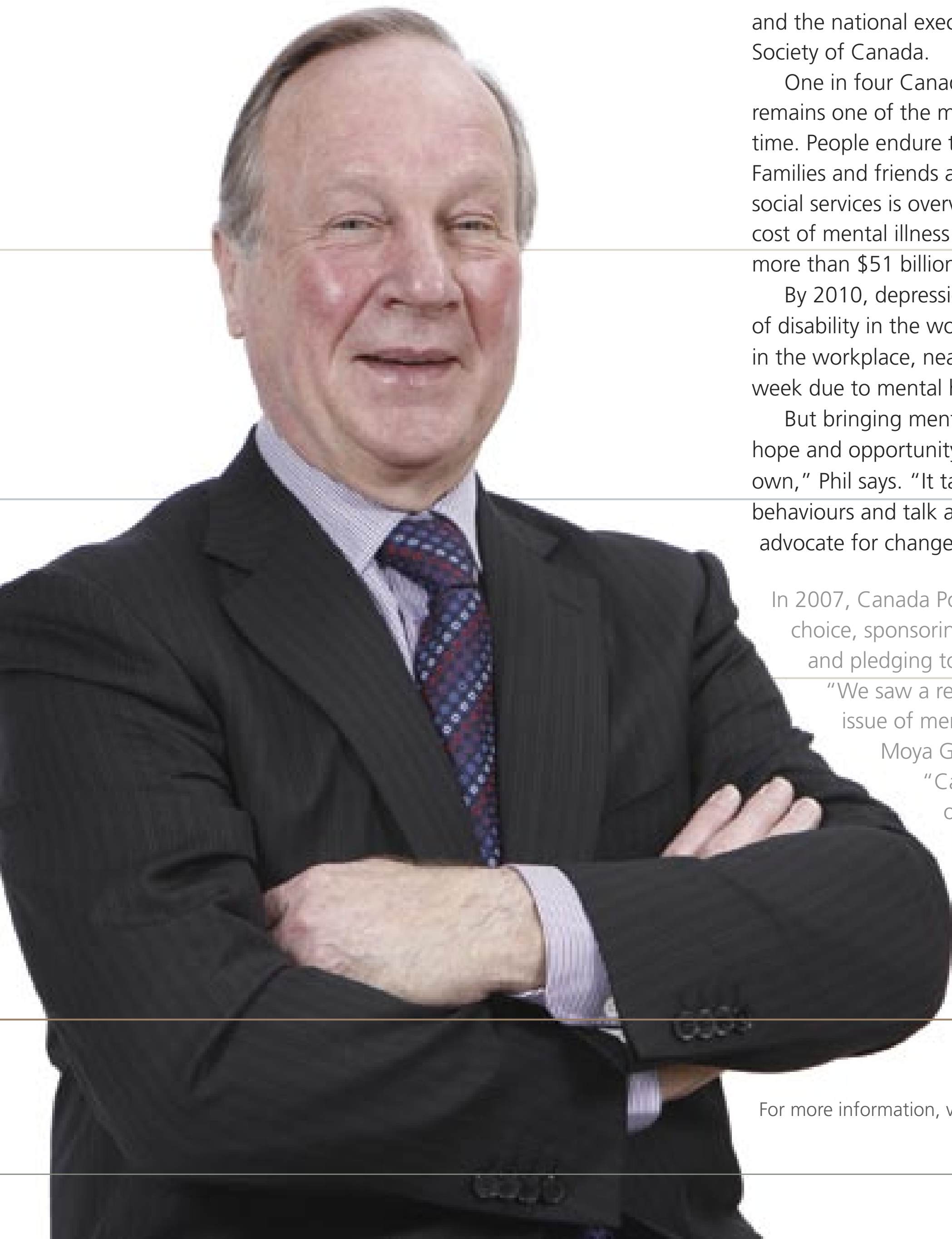
At first, selling to shows and shops, including the National Gallery of Canada, she later set up her eBay business and uses Canada Post to ship throughout Canada, the U.S., and as far away as Japan, Korea and Australia.

For Fiona, the entire business is a creative act. As she explains, "part one is creating the unique item, part two is the person receiving the jewellery at the other end and being delighted." So Fiona uses special gift boxes that fit through the lettermail slot, and each address is handwritten to personalize the experience for customers.

Twice a week she visits her post office and all her parcels have found their way safely to customers. "Right now, Canada Post is my partner in business," says Fiona, who is a VentureOne member. "And it's great to be able to rely on them."

Canada is a nation of entrepreneurs. More than half of Canada's labour force is employed by a company of less than 99 employees, and the nation's 2.3 million small businesses account for more than 96% of all businesses in the country. From eBay shipping discounts and online shipping labels to Small Packet™ service and VentureOne™ membership, Canada Post has created services to help every dream reach its full potential.

PHIL UPSHALL SUFFERED FROM AN UNDIAGNOSED MOOD DISORDER THAT WOULD DEVASTATE HIS LEGAL CAREER AND FAMILY LIFE. HE KNOWS THE STIGMA AND DISCRIMINATION FACED BY PEOPLE LIVING WITH MENTAL ILLNESS.



"It's an epidemic that in any other form would be at the top of everyone's health agenda," says Phil, who is a founding member of the Canadian Alliance on Mental Illness and Mental Health and the national executive director of the Mood Disorders Society of Canada.

One in four Canadians will suffer from mental illness, yet it remains one of the most neglected health care issues of our time. People endure the pain in silence, without treatment. Families and friends are shattered by loss, and the burden on social services is overwhelming. Including health services, the cost of mental illness to the Canadian economy is estimated at more than $51 billion per year.

By 2010, depression will become the second highest cause of disability in the world, following cardiovascular disease. And in the workplace, nearly 500,000 Canadians are absent each week due to mental health problems.

But bringing mental health out of the shadows provides hope and opportunity. "You can't change the world on your own," Phil says. "It takes real leaders to model anti-stigma behaviours and talk about mental illness. Together, we can advocate for change."

In 2007, Canada Post made mental illness its cause of choice, sponsoring Mental Illness Awareness Week (MIAW) and pledging to bring national awareness to the cause. "We saw a real need to lead the way in bringing the issue of mental illness out into the open," says Moya Greene, President and CEO of Canada Post. "Canada Post employees can be very proud of their leadership in this area."

For more information, visit www.mooddisorderscanada.ca and miaw.ca.

Photo: Canadian Forces

CELEBRATING YOUR DAUGHTER'S 12TH BIRTHDAY CAN BE A TOUGH EXPERIENCE WHEN YOU'RE MORE THAN 10,000 KILOMETRES AWAY.

But for Captain Steven Jefferys and other Canadian Forces members serving in Afghanistan, missing out on anniversaries and holidays, as well as the simple everyday pleasures of family life, is part of the sacrifice they're making for Canada's peacekeeping efforts.

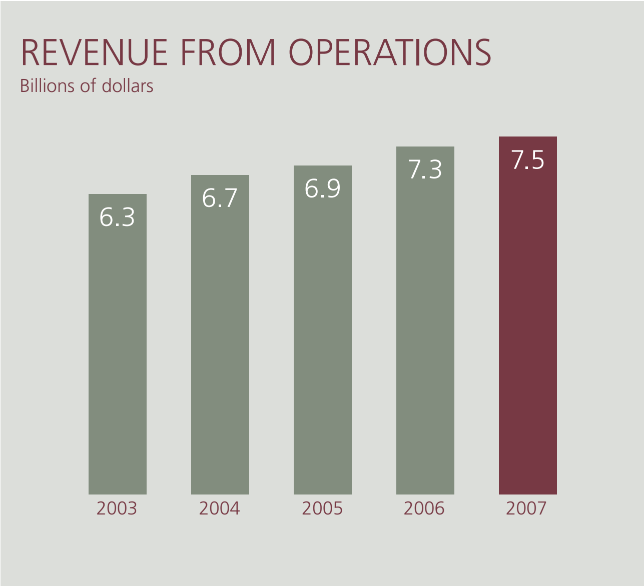
Growing up, Steven was fascinated by stories about his grandfather's military service in WWII. His grandfather also passed on his love of aircraft to his grandson. It was only natural that Steven went into Aerospace Engineering at Carleton University – where he met his future wife Tina – and joined the Forces soon after.

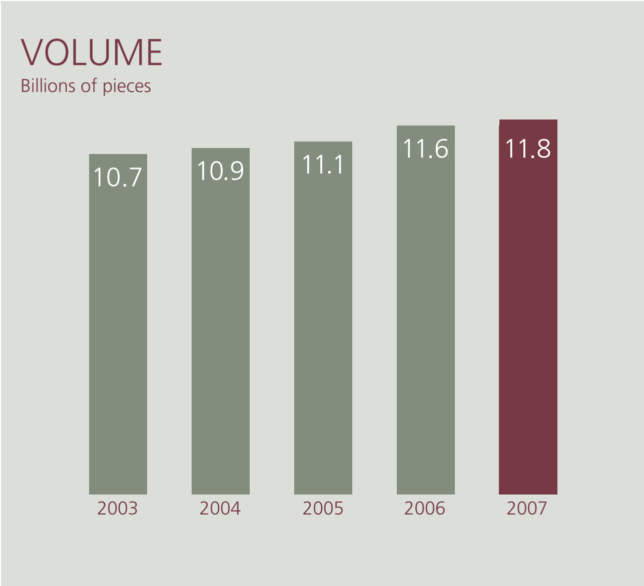
Now serving a nine-month tour in Afghanistan, Steven is known for the number of care packages he gets from friends and family back home. The packages always include something to share, like candy, peanuts and even a small decorated Christmas tree, as well as fan gear for Steven's beloved Toronto Maple Leafs.

But the best items, says Steven, are the cards and letters from Tina and their 12-year-old daughter, Amber. "Sometimes the biggest worry you have is whether everything is OK back home," says Steven. "Receiving the packages and reading the letters helps to put your mind at ease."

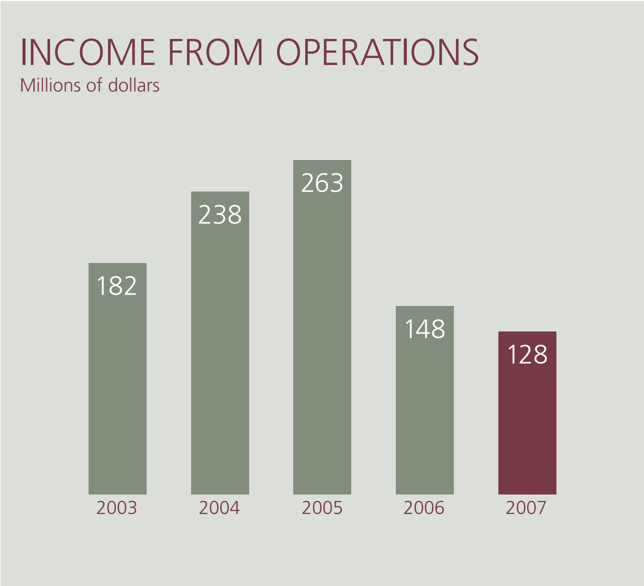
For the second year, Canada Post provided free delivery for parcels and letters sent from families and friends to deployed Canadian troops in Afghanistan. The program, which runs over the holiday season from October to January, delivered more than 10,000 letters and parcels to troops in 2007.

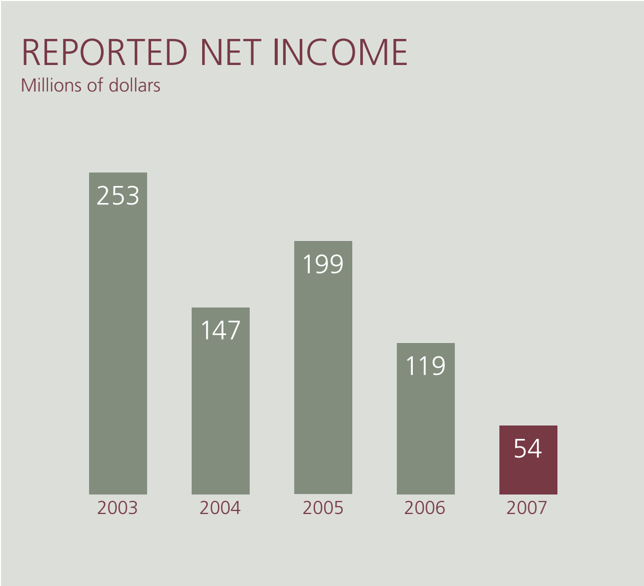
Highlights





On a consolidated basis, the Corporation processed 11.8 billion pieces during the 12-month period. Consolidated revenue from operations reached $7.5 billion and consolidated net income totalled $54 million.





Financial and Operating Highlights

(in millions of dollars)		2007	Annual Report 2006	% Change
Operations				
Revenue from operations	As reported	$ 7,474	$ 7,264	2.5%
Income from operations	Revenue from operations – cost of operations	128	148	(13.6%)
Operating profit margin (%)	Income from operations ÷ revenue from operations	1.7%	2.0%	–
Productivity (%)	Cost of operations as a percentage of revenue from operations	98.3%	98.0%	–
Income before income taxes	As reported	160	166	(4.1%)
Net income	As reported	54	119	(54.3%)
Return on equity (%)	Net income ÷ average equity	3.8%	8.4%	–
Dividend paid		47	80	(40.1%)
Dividend payout ratio (%)	Dividend paid as a percentage of prior year's net income	40%	40%	–
Cash from operations	As reported	342	267	27.8%
Capital expenditures	As reported	330	305	8.1%
Financial Position				
Cash		386	499	(22.7%)
Total assets		5,151	4,984	3.3%
Equity of Canada		1,439	1,433	0.4%

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President's Message

AS THE NEEDS OF CANADIAN BUSINESSES AND CITIZENS EVOLVE, CANADA POST HAS POSITIONED ITSELF TO BECOME A TRULY MODERN POST. WE ARE READY TO BUILD THE FUTURE TOGETHER.

When I first joined Canada Post three years ago, I set two important goals: to engage our employees and to make our customers the focus of all that we do. I'm proud to say that, during 2007, we have made real, measurable progress on both, thanks to the tremendous efforts of our people, Canada Post employees.

This progress was made even though 2007 was a challenging year. We saw a softening in revenues for our core product of domestic Lettermail™, where volumes decreased by 0.9 per cent compared to 2006. While we experienced solid revenue growth in our Parcels and Direct Marketing lines of business, they were not sufficient to help us meet our revenue objectives. As the year unfolded, there was growing uncertainty about whether we would meet our financial targets. Across the company, however, people rose to meet the challenge by applying stringent cost-cutting measures, which resulted in $93 million in savings, enabling us to reach our financial threshold. As a result, a team incentive was triggered to reward employees' extraordinary efforts and to encourage even greater engagement in our business.

Particularly gratifying was that 2007 marked the first year that the vast majority of employees were able to participate, as members of the Canadian Union of Postal Workers (CUPW) became eligible to share in the team incentive. This agreement was part of a negotiated, four-year settlement reached with the CUPW in the spring of 2007 – a milestone settlement that stands as testament to the improved relationship we have built with our largest union.

As a Modern Post, our people are the heart and soul of our company; their commitment to deliver the best products and services to Canadians is truly the foundation of our success. As such, we set out to meet, share with and learn from our employees in open, face-to-face exchanges. In 2007, we conducted 22 regional forums and more than 450 senior-executive visits, sharing the "big picture" and listening to the opinions and suggestions of thousands of employees.

The health and safety of our people continued to be a key priority for both me and my management team. Our employees suffered from more than 9,000 work-related accidents in 2007, with the vast majority of accidents, ranging from dog attacks to slips and falls, occurring in offsite locations over which we have little or no control. We

CHALLENGE: DELIVERING THE MAIL TO RURAL AREAS

Canada Post's 6,000 Rural and Suburban Mail Carriers (RSMCs) use vehicles to deliver the mail to more than 800,000 rural mailboxes. These employees pull their vehicles over at each rural mailbox, deposit the mail, and then merge back into traffic. The nature of roads (narrow or no shoulder), visual obstructions like curves and hills, and greatly increased traffic volumes are just some of the hazards during mail delivery.

Our RSMCs have been involved in more than 70 accidents since 2005, including three fatalities, and more than 1,400 workplace safety complaints have been received since 2004. As a responsible employer and respected service provider, Canada Post has a moral and legal obligation to address this issue. Under the direction of Human Resources and Social Development Canada, Canada Post has begun a Rural Mail Safety Review. The $500 million review will assess the safety of all rural mailboxes in Canada. Changing a customer's mode of delivery is only undertaken when the safety of our mail carrier is at risk and no other alternative is feasible.

take these issues very seriously. Reducing accidents requires a multi-part solution. During 2007, we laid important groundwork and have taken several steps to create more modern and ergonomic workspaces. We have hired health and safety professionals and have invested in new processes and tools to make our employees safer. In 2007, our front-line employees received safety training, and new anti-slip footwear was distributed to thousands of our delivery employees.

Our efforts have been recognized. For the second year in a row, Canada Post was named one of the Top 100 Employers in Canada in Maclean's magazine. Further evidence of our progress was seen in our annual independent Employee Engagement Survey, which showed a five percentage point overall increase in engagement compared with 2006. Conducted by International Survey Research (ISR), the survey revealed improvements across the board in almost every category; a remarkable achievement made in only one year. Still, more work needs to be done.

One area of continued concern is the safety of our rural and suburban mail carriers (RSMC). As part of our ongoing safety evaluation of Canada's rural mailboxes, we have assessed more than 69,000 mailboxes to date. This evaluation comes after Human Resources and Social Development Canada handed down to us more than 40 workplace safety decisions, which stem from the more than 1,400 workplace safety complaints from our rural and suburban mail carriers. The need for this review is critical; three people lost their lives delivering to rural mailboxes last year. RSMC vehicles have been equipped with lights and signs for better visibility, and when rural mailboxes are deemed unsafe, delivery is moved to other locations. We will continue to work to find the best solutions possible for all our stakeholders.

Addressing our health and safety challenges will be a major part of our postal transformation. We intend to replace obsolete buildings and upgrade mail-processing equipment and technology to meet modern competitive standards. The total amount of incremental capital spending over the next

CHALLENGE: PREVENTING INJURIES TO OUR EMPLOYEES

In 2007, Canada Post employees suffered more than 9,000 reportable, work-related accidents. Fifty-two per cent of these required external medical attention, with the employee returning to work the following day, while 48 per cent required at least one additional full day off work following the incident. Most of these injuries occur off of Canada Post property, when our employees are out in the community delivering the mail. Reducing accidents and ensuring the safety of our employees will require an increased public awareness regarding the importance of controlling dogs and keeping walkways clear of ice, snow and debris. The safety of our delivery personnel falls into the hands of many stakeholders.

Within our facilities, many employee injuries are musculoskeletal and can be attributed to poor ergonomics. Ergonomics are especially important for employees who spend much of their workday doing repetitive movements. Canada Post is investing in improvements for our equipment and processes, as well as new health and safety training for all CUPW employees, to minimize the risks associated with lifting, carrying, pulling and pushing the mail.

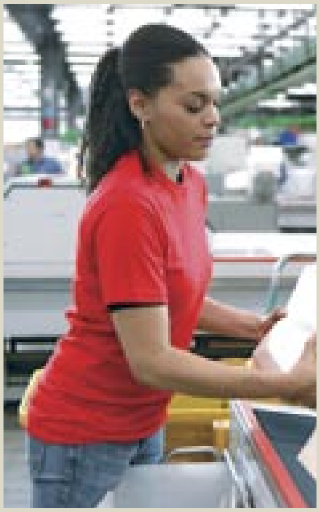
five years could reach $1.9 billion. We will prioritize our greatest needs and invest only what we can afford.

These initiatives not only make our workplaces more pleasant for employees, but also help increase productivity, lower costs, meet strict environmental standards, and provide faster, enhanced service to our customers. This investment in our infrastructure is timely. We're facing one of the most competitive marketplaces in our history. International competitors, including FedEx, DHL and UPS, as well as Posts from overseas countries, such as Deutsche Post, are all operating within Canada. All are supported by world-class equipment and the latest in technology. Transforming Canada Post's current equipment, some of which dates back to the 1970s, is essential to ensuring a competitive, cost-effective Canadian postal service, one that meets the growing demands of consumers, entrepreneurs and large enterprises.

AS A MODERN POST, OUR PEOPLE ARE THE HEART AND SOUL OF OUR COMPANY; THEIR COMMITMENT TO DELIVER THE BEST PRODUCTS AND SERVICES TO CANADIANS IS TRULY THE FOUNDATION OF OUR SUCCESS.

We have already made great progress by establishing a structure to better respond to those demands. Two years ago, we realigned Canada Post's operations into three lines of business: Transaction Mail, Parcels and Direct Marketing. Through these lines of business and our sales organization, we continue to listen to our customers so that our solutions respond to their specific business challenges. During 2007, these solutions ranged from addressing core needs, such as improving our on-time delivery of Admail™, making it easier to trace parcels and simplifying our products to innovative new products like SmartFlow, our new multi-channel electronic document management solution.

We recognize that, as Canadians increasingly operate through the Internet, their needs and expectations are changing. Consumers want more relevant, targeted offers as well as more choice in delivery options. Businesses want higher return on their mailing dollar investments. And, while 85 per cent of Canadians say they prefer to receive their bills by mail, a growing number of consumers and businesses want the freedom of both physical and secure electronic channels to communicate with each other. We continue to believe that we can play a relevant role in new markets. By building on and investing in the strong foundation we have established, we will seek to diversify our revenues and grow.



CHALLENGE: BUILDING THE MODERN WORKPLACE

To succeed, Canada Post requires an engaged workforce – employees who feel involved in the company, understand the Corporation's goals and are eager to give their best to our customers, every day. To attract and retain model employees, Canada Post must become a model workplace. We believe we can achieve this by fostering an environment based on respect and fairness, a dedication to health and safety and open communication with employees about business decisions that affect them, and a commitment to develop our employees.

By 2016, some 27,000 employees are expected to leave Canada Post, mostly due to retirement. Finding new leaders to replace these experienced employees, from both within the company and through external candidates, will require strategic planning and a sound knowledge of the skills and characteristics required to lead the Corporation into the future. Customers are recognizing our efforts to create positive change. We've seen proof in the results of our Customer Value Index (CVI). Out of 18 performance indicators in our CVI, we reached our targets in eight and improved in 10 during 2007.

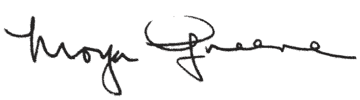
BY BUILDING ON AND INVESTING IN THE STRONG FOUNDATION WE HAVE ESTABLISHED, WE WILL SEEK TO DIVERSIFY OUR REVENUES AND GROW.

Of course, success in business means creating conditions today that also allow future generations to thrive. With 72,500 employees, The Canada Post Group has a presence in virtually every community across Canada. Our size and reach into Canadian households and Canadian companies means that we can help effect real change and influence everyday lives. In recognition of this, we made a commitment in 2007 to integrate sustainable practices companywide.

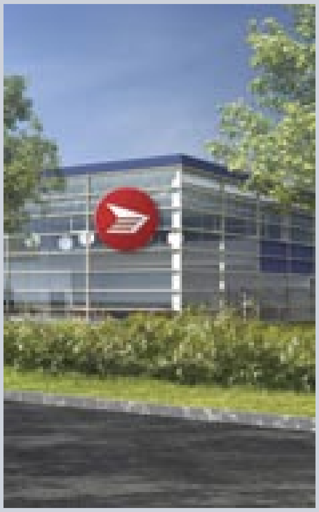
For many years, Canada Post employees have been actively involved in protecting the environment. Across the company, grassroots initiatives, ranging from composting to tree planting to green commuting challenges, have complemented corporate environmental programs. Our future investments will reflect this philosophy. A shining example will be our new Winnipeg plant that will be built to "green building" standards and equipped with environmentally friendly technologies. In 2007, we chose to address the stigma of mental illness and shine a light on the plight of millions of Canadians who often suffer in silence. With tremendous employee support, Canada Post has officially made mental health our corporate cause of choice. We are committed to raising funds to support awareness, research and local community treatment for this important cause.

We are also producing our first Corporate Social Responsibility Report, set for release in the spring of 2008. This report will not only be a benchmark for the Corporation's ongoing green initiatives and programs, but will serve as a valuable tool to enable even more positive change in the future.

Looking forward, we will continue to strive to create a successful, sustainable future for our employees, our customers and all Canadians. It is clear, however, that 2008 will be equally as challenging as 2007, if not more so. The threat of a recession in the United States is likely sufficient in itself to cause businesses to curb spending. This reduced spending will put pressure on Canada Post revenues. It is clear that we need to further reduce our cost base if we are to weather the inevitable revenue declines. I am certain that our people, once again, will rise to the challenge. As the needs of Canadian businesses and citizens evolve, Canada Post has positioned itself to become a truly Modern Post. We are ready to build the future together.



Moya Greene
President and Chief Executive Officer



CHALLENGE: FUNDING OUR TRANSFORMATION

To ensure Canadians continue to enjoy high-quality, cost-effective services, Canada Post needs to invest $1.9 billion of incremental capital and $0.6 billion in related program expenses to bring its aging plants, infrastructure and equipment up to modern standards. Canada Post will face challenges in making this funding available over the next five years. Costs such as fuel prices are increasing while the basic postage rate is restricted by a price-cap formula. An economic slowdown could affect our customers' bottom lines and, in turn, Canada Post's revenues.

Funding will also be derived from an employer-contribution holiday to the Canada Post Pension Plan. More than $750 million of supplementary contributions have created a healthy surplus, but financial markets also have an important impact on the valuation of our pension plan and related funding requirements.

To mitigate these risks, Canada Post is reviewing its cost structure and developing contingency plans to ensure our investment plans are prudent and flexible.

About Us

CANADA POST IS A FINANCIALLY SELF-SUSTAINING CROWN CORPORATION THAT'S A VITAL PART OF THE CANADIAN ECONOMY, EMPLOYS 72,500 CANADIANS WITHIN THE CANADA POST GROUP, AND CONNECTS MILLIONS OF INDIVIDUALS, COMMUNITIES AND COMPANIES TO EACH OTHER AND TO THE WORLD.

Canada Post and its affiliates spend more than $2.8 billion annually on goods and services, thereby creating an additional 30,000 jobs.

Every business day, Canada Post delivers some 40 million pieces of mail to approximately 14 million residential and business addresses; this delivery network expands by some 200,000 addresses every year. There are more than 20,000 delivery routes in Canada, and each day, 585 planned domestic flights, 100 national service delivery vehicles and 18 rail services are used to deliver the mail from coast to coast. Canada Post also has 6,600 post offices, giving it the largest retail network in Canada.

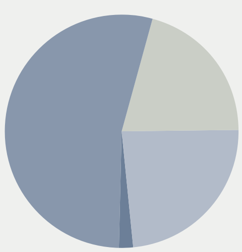
Canada Post and its employees are strong believers in giving back to the community. In 2007, we announced that mental health would be Canada Post's new cause of choice. Canada Post also supports literacy, the Canadian Freestyle Ski Team and the United Way. Each year, employees help Santa answer more than one million letters in 26 languages, a feat which earned Canada Post a spot in The Guinness World Records.

Canada Post's competitors range from niche players to large multinationals with revenues up to ten times higher than the Corporation's, including FedEx, UPS and DHL. Unlike its competitors, Canada Post has a mandated universal service obligation to deliver mail to every address in Canada, five days a week. Since 1982, Canada Post has also been restricted by a price-cap formula that holds rate increases on the basic letter rate to two-thirds the rate of inflation.

To compete more effectively, we operate as a group of companies called The Canada Post Group to deliver a full range of delivery, logistics and fulfillment services to customers. The Corporation holds an interest in Purolator Courier, Innovapost and SCI Logistics. The Canada Post segment represents approximately 80% of the Corporation's consolidated revenue.

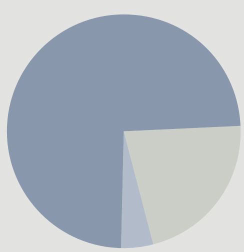
In 2006, Canada Post restructured into three lines of business – Transaction Mail (bills, invoices, notices and statements), Parcels and Direct Marketing – so that we could better focus on our customers. As our customers' needs evolve, Canada Post is changing too, developing new delivery and communication services so we can continue to offer real value to businesses and consumers alike.

PRODUCT VIEW



Transaction Mail **54.0%**
Parcels **20.6%**
Direct Marketing **23.6%**
Other **1.8%**

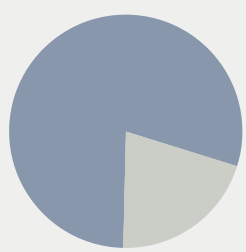
REVENUE SOURCES



Commercial **$4,418**
Retail **$1,292**
International Inbound **$250**
Other **($5)**

in millions of dollars

REVENUE
(Consolidated)

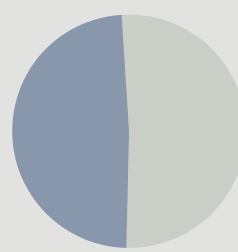


Canada Post **$5,955**
Subsidiaries/ Joint Venture* **$1,519**

* including consolidation entries

in millions of dollars

INCOME BEFORE TAXES
(Consolidated)



Canada Post **$78**
Subsidiaries/ Joint Venture* **$82**

* including consolidation entries

in millions of dollars

6,600

POST OFFICES ACROSS CANADA

96%

ON-TIME DELIVERY PERFORMANCE

A representative sample of fabricated short/long and oversized Lettermail test pieces is weighted according to origin-destination mail volumes.

14 million

ADDRESSES SERVED IN CANADA

TOP 100 EMPLOYER

Canada's Top 100 Employers 2008

For the second year in a row, Canada Post was recognized as one of the country's Top 100 Employers, chosen from more than 10,000 companies invited to apply. The 100 companies, selected by Mediacorp, were featured in a special edition of Maclean's magazine in October.

Companies were rated on their performance in several areas, including work atmosphere, community involvement, environmental leadership, benefits, training and development, vacation policy, and employee engagement.

Canadian $ equivalent (as of Feb. 2008)

AUSTRALIA	$0.40
UNITED STATES	$0.44
CANADA	**$0.52**
JAPAN	$0.69
SWEDEN	$0.70
UNITED KINGDOM	$0.73
FRANCE	$0.79
GERMANY	$0.81
ITALY	$0.88

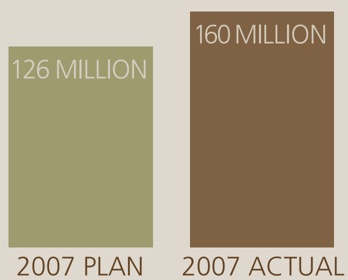
CANADA HAS ONE OF THE LOWEST BASIC LETTER RATES IN THE WORLD

Key Performance Indicators

FINANCIAL PERFORMANCE

CONSOLIDATED EARNINGS BEFORE TAX

TARGET: $126 MILLION
ACHIEVED: YES



Canada Post extended its record of profitability to 13 consecutive years. In spite of lower-than-expected revenues, Canada Post earned consolidated income before income taxes of $160 million, exceeding the plan by $34 million. Purolator and SCI Logistics had strong financial performance in 2007.

The Corporation paid a dividend of $47 million to its Shareholder, the Government of Canada. Total dividends paid over the last five years amounted to $267 million.

Although revenues at Canada Post were lower than plan, management implemented strong cost controls that resulted in earnings before taxes exceeding the financial targets. In 2008, the Corporation will remain vigilant in its goal to control costs.

Canada Post remains confident that our management focus on cost controls, developing new products and services, and business improvements from our investment in the Modern Post will position us well for the future.

DELIVERY SERVICE

LETTERMAIL™
ACHIEVED

EXPEDITED PARCEL
NOT ACHIEVED

XPRESSPOST ™
NOT ACHIEVED

PRIORITY COURIER™
NOT ACHIEVED

DIRECT MARKETING
SIGNIFICANTLY ENHANCED

Our delivery standards require that we deliver Lettermail consistently within two business days within the same metropolitan area or community; within three business days within the same province; and within four business days between provinces.

An independent professional services firm tests our Lettermail service by depositing mail through street letter boxes, post offices and community mailboxes, and tracking it to delivery points across the country. Our 2007 on-time service performance score, at 96.1%, topped our corporate target of 96%. However, this was slightly lower than our 2006 score of 96.4%. Diligent efforts by employees during the three last quarters of the year were not able to make up for a difficult start in the first quarter, and targets for Expedited Parcel, Xpresspost and Priority Courier were not achieved. Concerted efforts to improve the delivery of Direct Marketing products improved scores in this area.

Continuing on-time delivery is crucial to Canada Post's long-term success. We will continue to look for ways to further improve the quality of our delivery and earn our customers' loyalty and their business.

CUSTOMER VALUE INDEX

TRANSACTION MAIL
TARGET: +2 **ACHIEVED:** PARTIALLY

PARCELS
TARGET: +2 **ACHIEVED:** YES

DIRECT MARKETING
TARGET: +3 **ACHIEVED:** NO

Our Customer Value Management program identifies the drivers of customer value and loyalty through relationship surveys and transactional questionnaires. The relationship surveys explore our customers' mailing habits and practices, assess their loyalty to Canada Post, and capture feedback on our products and services, delivery, price, reputation and image, and service culture. The transactional questionnaires ask customers about their recent experience with Canada Post, including our sales and customer service representatives, post offices, delivery personnel and our website. These techniques offer insight about the quality of our service, our competitive advantage and areas needing improvement.

In 2007, our Parcels line of business achieved improvement targets in product offering, product delivery, price competitiveness, and reputation and image categories – in addition to meeting its overall 2007 CVI target, surpassing 2006 results by two percentage points. Transaction Mail maintained its 2006 score and achieved targets in product offering, price competitiveness, and reputation and image. Direct Marketing did not achieve its 2007 CVI target; however, it met its goal for improving service culture – an element critical to improving the overall customer experience.

EMPLOYEE ENGAGEMENT

ENGAGEMENT INDEX
TARGET: 54
ACHIEVED: PARTIALLY

ACCIDENT FREQUENCY
TARGET: 20% REDUCTION
ACHIEVED: NO

PAY DEFECTS
TARGET: 50% REDUCTION
ACHIEVED: YES

Employee engagement remains a top priority for Canada Post. It is our goal to become the best place to work in Canada, with every employee contributing to and sharing in our success. For the company to continue its transformation to the Modern Post, it is critical to focus on building the modern workplace characterized by high levels of employee engagement. Employees who are engaged serve customers well, providing positive service experiences that encourage customers to do more business with the company.

Our effort to increase employee engagement is making an impact. The results of our employee survey for 2007 show improvement across all categories and an increase of five percentage points in our Employee Engagement Index. Our efforts to improve health and safety in the workplace have been recognized by employees and there has been a significant increase in the number of employees who believe that the company acts with integrity in its dealings with them.

While we are encouraged by the results in 2007, much work remains to be done to drive higher levels of engagement and create a safer, modern workplace.

Changing our Culture

CANADA POST CONTINUES IN ITS EFFORT TO BUILD A MODERN WORKPLACE, ONE THAT IS CHARACTERIZED BY FAIRNESS AND RESPECT, A RENEWED FOCUS ON HEALTH AND SAFETY, AND ONGOING DIALOGUE WITH EMPLOYEES AT ALL LEVELS.

In keeping with our corporate values, three main principles have guided the effort.

Employees can't do their best at work unless they are treated with fairness and respect. Canada Post has put its values to work by insisting on respectful work habits throughout the company. Team leaders have been called upon to place greater emphasis on involving employees in decisions that affect their work and their workplace. As well, Canada Post is continuing to develop its employee recognition programs and is encouraging team leaders to acknowledge the contributions that employees make in serving our customers and improving the business operations.

The personal safety of employees must be protected. In 2007, Canada Post made improving the health and safety of its workplaces and work practices an overriding priority. Numerous measures have been introduced to help reduce accident rates, including a public awareness campaign asking our customers for help in keeping their premises safe for delivery employees.

Employees must be welcomed into an ongoing conversation about the business and its future. For the second year, 22 regional forums were held in eight cities with approximately 6,500 team leaders. The forums provided the executive with an opportunity to have a dialogue about the company's business challenges. As well, there were ongoing management visits and workplace discussions designed to engage front-line employees in dialogue about our business realities and strategic direction.

All these efforts produced measurable gains in 2007 – we saw improved results in our annual employee survey and Canada Post was included in Mediacorp's Top 100 Employers for the second year. While we are encouraged by these positive signs of progress, there is still much to accomplish if we are to meet our goal of becoming the best place to work in Canada with every employee contributing to and sharing in our success.

Increase in Employee Engagement score

OUR VALUES

We work to earn our customers' business.

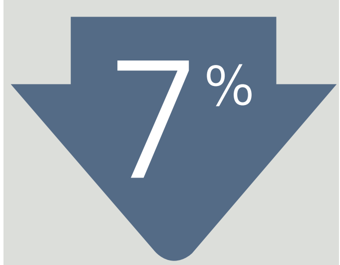
We succeed by working together.

We take responsibility for our actions.

We treat each other with fairness and respect.

We strive to continuously improve.

We act with integrity in all that we do.



2008 target: Reduce accident frequency rate by seven per cent.

AGILITY REQUIRED TO MEET CUSTOMER DEMANDS

As a letter carrier for 15 years, Matt Charlton has a front-line understanding of what Canada Post must do to succeed. "Canada Post has a long history of adapting to change, but as technology leads the way, we have to react with agility in order to remain relevant," he says. "This is no small feat for a company of our size. Add to that the demands of our federal mandate, the customers on both the receiving and sending ends of our business, and the people who do the work, and it becomes obvious the challenge is great."

Matt believes the corporate team incentive program works to help all employees feel like part of the solution. "With an incentive to become more efficient and profitable, we all stand to gain from our success and satisfying the customer."
Matt Charlton, Letter Carrier

CHANGE BEGINS WITH A CONVERSATION

Andrea Colley has gone from Christmas casual to letter carrier to courier supervisor at Canada Post in Halifax. You could say that change is part of her life.

"I always ask how do I change to make myself better?" she says, "and I think it's amazing how Canada Post is adapting in a world that's moving so quickly."

She's seen both the need and the impact of modernization first hand. "We're working with older machinery, a changing workforce. But our working conditions are getting better and better."

So how does she help keep her colleagues engaged? "Say hi and open up a conversation," she says. "When you listen and show respect, you realize that as a team, nothing is impossible."
Andrea Colley, Mail Service Courier Supervisor

TUNING INTO AWARD-WINNING RADIO FREQUENCY TECHNOLOGY

What happens when two organizations put their resources toward a common goal? Simply put: innovation.

When the Canada Revenue Agency (CRA) wanted to confirm delivery of sensitive intra-agency packages, it called on Canada Post to deliver.

As partners, the CRA joined a cross-functional team at Canada Post, including Byron Vienneau, Michael Rog and Steve Fulton, and set to work. They developed a pilot program using existing Radio Frequency Identification (RFID) technology. The RFID tag enables real-time, end-to-end tracking of packages. From the moment a package leaves the CRA office to the second it reaches the CRA receiving office, the shipment is fully visible.

The pilot project received a Silver Award for Innovation and Collaboration at the Canadian Government Technology Event (GTEC) awards. Phase 2 will include CRA's entire national coverage of 53 hubs and satellite offices.

From left to right: Michael Rog, Commercial Services Network; Byron Vienneau, Sales; and Steve Fulton, Product Innovation.

Connecting with Customers

Transaction Mail

OUR TRANSACTION MAIL LINE OF BUSINESS OFFERS A RANGE OF WAYS TO DELIVER DOCUMENTS, FROM PAPER TO ELECTRONIC DELIVERY – LETTERMAIL TO EPOST – WITHIN A SINGLE ORGANIZATION THAT CANADIANS HAVE TRUSTED FOR GENERATIONS.

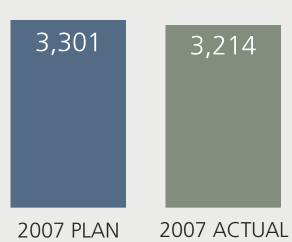
In 2007, we focused on helping our customers make better, more creative use of their investment in Lettermail, and introduced complementary services to raise the value to their mailings further. Our goal is to sustain Lettermail volumes, accounting for over half of Canada Post's annual revenues, and increase transactional mail business by constantly meeting our customers' changing needs.

This line of business includes transactions made through statements, invoices, payments and letters of all kinds, in both paper and electronic form. While many Canadians prefer to conduct these transactions on paper, Lettermail volumes are no longer growing. In 2007, physical mail volumes were lower than expected, at least in part because electronic alternatives are on the rise. Moving away from paper quickly, however, presents challenges to our business customers. Most consumers and businesses prefer communicating by mail, and most transactional communication systems are set up for paper.

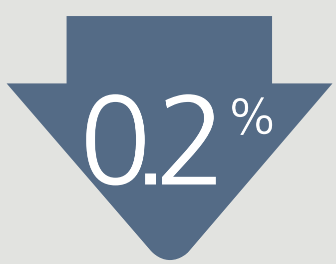
The price of domestic postage held constant in 2007, and customers heard more about mail's value as a marketing tool. Through our Great Statements program, Canada Post began working with business customers to design statements that deliver effective personalized messages, making transaction mail an even better, targeted customer communications conduit. With new customized postal indicia, businesses can use Lettermail to build brand awareness and communicate a message before the envelope is even opened. In the future, a foundation of new technology and processes will help businesses and customers continue to connect and build strong relationships.

Online tools, developed to support customers, and SmartFlow, introduced to help larger customers manage document processes and make the most of their mailing list data, will make transaction mail communications more effective. Our customers agree that transaction mail continues to have a definite place in this wired world, and we'll continue working to earn their business.

REVENUE (in millions of dollars)

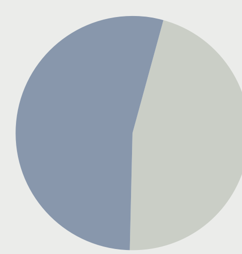


REVENUE



Decrease in revenue from Transaction Mail

% OF TOTAL REVENUE



Transaction Mail **54.0%**

MAKING A GOOD CALL ON OUTSOURCING

"Outsourcing crucial mailroom functions to Canada Post allows us to focus more on what we do best – providing communications solutions that contribute to the quality of life, infrastructure and economic health of the North. With Canada Post as our strategic partner, we've streamlined and accelerated our customer-statement mailings, transforming what used to be a three-day process into one. And that's not the only benefit. The solution has also allowed us to free up valuable space, redeploy resources into other core business areas, and eliminate the risks associated with having an in-house operation."

Gary Donadel, Finance Manager, TBayTel

Feature07

It sounds like a simple choice: paper or electronic? But for businesses with large mailings, it's much more complicated. Some customers prefer email while others expect an envelope, and many switch back and forth. For businesses, document management is a growing challenge.

In 2007, Canada Post introduced **SmartFlow**™ Document Management Services to offer secure, multi-channel communications and overcome that challenge. A business provides data and we deliver the finished communication to customers in their preferred medium. We even update mailing records from corrected returned mail and immediately capture responses – such as order forms – for prompt action.

It's another way customers benefit from Canada Post's innovation.

Looking forward08

For a business, every customer communication is an opportunity to start and keep a conversation going. Bills and statements carrying messages personalized for individual customers are especially valuable communications opportunities, because customers dedicate focused attention on them.

That's the message Canada Post began delivering to business customers with the **Great Statements** program. In 2008, customers will be hearing more about how to make the most of all their business communications, including both physical and electronic transactions. Already part of the commercial conversation for many Canadians, Canada Post will continue helping customers get more from their communications.

Connecting with Customers

Parcels

PARCELS AREN'T JUST FOR SENDING BIRTHDAY PRESENTS ANY MORE. IN RECENT YEARS, ONLINE SHOPPING HAS CHANGED THE CONSUMER LANDSCAPE, AS SHOPPERS MOVE FROM CROWDED SUBURBAN MALLS TO BUSY VIRTUAL ONES, WHERE THEY DEPEND ON DELIVERY AGENTS TO SHIP THEIR PURCHASES.

This market is growing – shipping and delivery has suddenly become a fast-paced and highly competitive business in Canada.

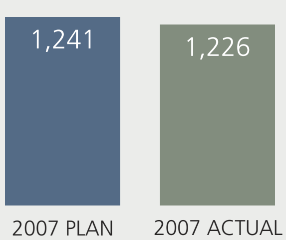
With our national network that reaches every household in the country, no one is better equipped to offer reliable shipping and delivery services than Canada Post. In 2007, revenues from our Parcels line of business totalled more than $1 billion, and together with our Purolator subsidiary we led the market. But our parcel volumes were lower than expected, and our competitors are multinational firms with higher marketing budgets and comparatively low operating costs. To maintain our lead in this competitive market, we must build business by providing the high-quality service customers are looking for.

Our business customers need to satisfy their own customers, and what they want above all is consistent, on-time delivery. In 2007, Canada Post introduced measures to improve operational efficiency in our key Toronto and Montréal parcel processing facilities, and to measure our service performance across all product lines. Because customers also want to track the progress of their deliveries, we improved our parcel scanning capabilities – among our core products, all parcels are now bar-coded, and delivery personnel carry hand-held scanners.

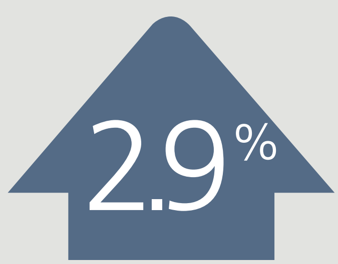
We launched several new products in 2007 as well, to ensure more customers can find a delivery option well suited to their specific needs. The new Light Packet™ product, for example, is attractively priced and just the right size for many eBay shippers. In addition, we introduced various measures to improve our customer service, including a simplified claims process and a billing adjustment process to give commercial customers their money back when they overestimate the weight of their parcel.

Our goal is to provide reliable service through a range of parcel products that are quick, easy and convenient to use. The response from customers has been positive – our research last year showed an increase in their loyalty to Canada Post. That's the measure that counts most, as we continue to grow with our customers in a fast-changing market.

REVENUE (in millions of dollars)

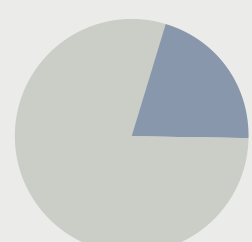


REVENUE



Increase in revenue from Parcels transactions

% OF TOTAL REVENUE



Parcels **20.6%**

DELIVERING MAGIC FOR AMAZON.CA

With a love for magic, wands and wizardry, thousands of people stood poised by their mailboxes on Saturday, July 21, 2007, to receive *Harry Potter and the Deathly Hallows*.

Canada Post delivered the seventh book in the best-selling series to customers of Amazon.ca. Orders placed at Amazon.ca are fulfilled and shipped from within Canada by Assured Logistics, part of The Canada Post Group.

Julie Todaro, director of Amazon.ca, says the delivery solution was impressive. "Canada Post offered Amazon.ca a customized delivery solution to ensure that the new Harry Potter release was in the hands of our customers on a Saturday. This solution also included a high-security network that kept the most anticipated book of the year under wraps."

Julie Todaro, Director, Amazon.ca

Feature07

If you're an online shopper, you're used to having information at your fingertips. So shouldn't a few quick keystrokes tell you when to expect your parcel delivery?

For Canada Post, tracking parcels depends on having the right tools in the right places. You can't track it unless you can scan it, so in 2007, we invested in **substantial improvements to our scanning capabilities**. All our core parcel products are now bar-coded, and incoming international parcels have a Canada Post label placed over the foreign bar code to ensure proper scanning. New scanning equipment was installed in three major urban centres, and 5,000 drivers across the country now carry hand-held scanners to scan parcels on pickup. Today, we offer customers delivery updates by email, putting the information they need right on their desktops.

Looking forward08

As technology improves and scanning equipment becomes more sophisticated, Canada Post plans to improve the visibility of its delivery processes and offer **more precise tracking information** for parcels. Today, Canada Post is working with key customer partners to research customer-specific tracking solutions using Radio Frequency Identity (RFID) technology. This technology could make it possible for our customers to access much more information about their parcel's location as it works its way through various checkpoints in the mail stream. Canada Post also continues to increase the number of times a parcel is scanned as it goes through the system, providing customers with more up-to-date information.

Connecting with Customers

Direct Marketing

BIG OR SMALL, EVERY BUSINESS HAS THE SAME PROBLEM. HOW DO YOU MOST EFFECTIVELY REACH YOUR CUSTOMERS, OR BETTER YET, PEOPLE WHO MAY BECOME YOUR CUSTOMERS?

Many types of advertising media claim to get results, but not many can prove it. Canada Post's business customers know that direct mail works – it's a measurable way of building business that offers a proven response rate. In 2007, Canada Post improved its direct mail products and began making the case for them more effectively. The Direct Marketing line of business is growing, because it offers the direct edge our business customers need in a competitive marketplace.

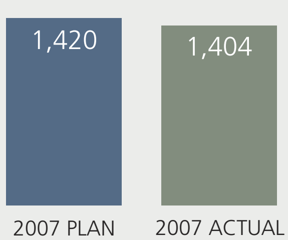
That's what many discovered last year, through Canada Post's efforts to educate the market. Seminars for small and medium-sized businesses and direct marketing advisors for large enterprises demonstrated just how well our Admail products work, in small- or large-scale mailings, on their own or in combination with other advertising media. Case studies and testimonials were compiled as well to offer real-life examples of success achieved through the mail.

Meanwhile, we continued to improve our product line and make direct mail easier to use. Today, customers can plan and execute an Admail campaign online. A simplified website offers easier access to Unaddressed Admail™ service, and items can now be mailed in a wider range of sizes. Improved targeting tools help customers reach the people who want to receive their advertising message.

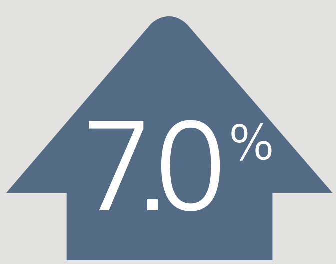
Our Admail products are now simpler, more flexible and more powerful, so they offer more value for customers. We're delivering the message – our research shows that customer perception of direct mail has improved, and that most perceive it as an effective direct marketing medium. In 2007, Canada Post saw increases in volumes and revenues for both Addressed Admail™ and Unaddressed Admail services.

The direct marketing business in Canada is booming, but unlike other media, direct mail is unique – it offers access to every household in Canada. By investing in ongoing improvements to our direct mail products, Canada Post aims to increase its share of this fast-growing market, and help more and more customers build their business through the mail.

REVENUE (in millions of dollars)

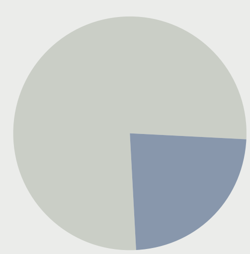


REVENUE



Increase in revenue from Direct Marketing

% OF TOTAL REVENUE



Direct Marketing **23.6%**

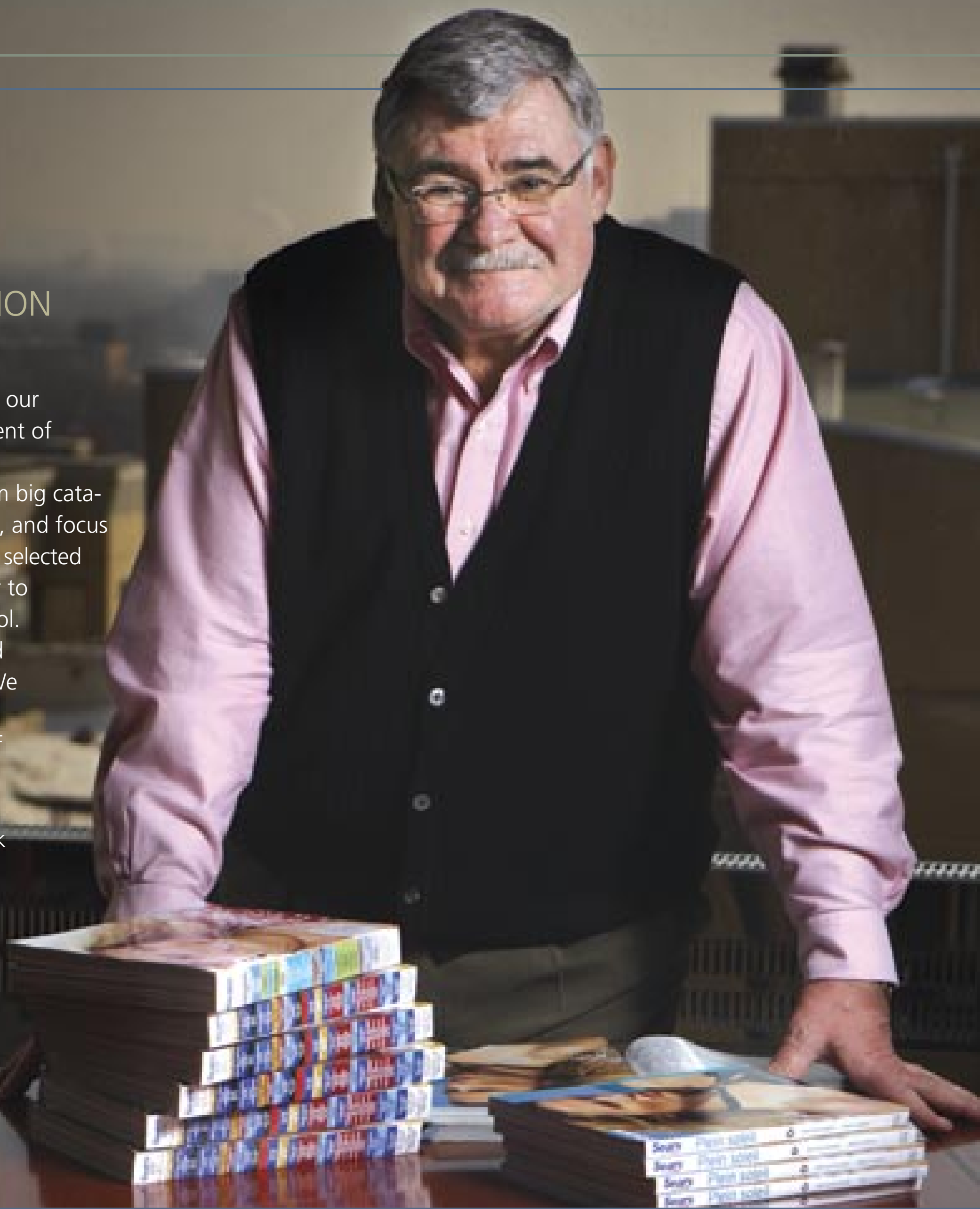
DISTRIBUTION WITH PRECISION

"With Canada Post, we can be laser-like in our distribution," says Rick Brown, Vice-president of Marketing for Sears Canada.

When Sears wanted to move away from big catalogues distributed to millions of Canadians, and focus on smaller catalogues mailed more often to selected markets, Canada Post provided the answer to better targeting with its GeoPost™ Plus tool.

Just as importantly, Canada Post helped enable Sears to better plan for its sales. "We found other delivery methods could only distribute our catalogues over a window of several days," says Rick. "Canada Post put rigour into our drop dates with surgical precision, so we could ensure we had stock and personnel on hand to work the sale."

Rick Brown, Vice-president of Marketing, Sears Canada



Feature07

The smart money in advertising is spent on sending a message to people who want to receive it. Canada Post's **GeoPost™ Plus** targeting tool helps businesses identify where potential customers live, so they can send Unaddressed Admail campaigns that get results.

Thanks to upgrades in 2007, GeoPost Plus is now even better at identifying target markets. Business customers can rely on improved behavioural and demographic data, including average household expenditures, to identify neighbourhoods best suited to their mailings. They can also import mapping files of their own, and precisely identify mailing areas by postal code and letter carrier route. It puts Unaddressed Admail items into the right mailboxes, and helps Canada Post hit the mark for its customers.

Looking forward08

As Canada Post continues to refine its GeoPost Plus tool and its targeting capabilities, our aim is getting better all the time. Today, we can identify particular streets where households share certain attributes such as interest in takeout pizza. In 2008, we'll add new data and capabilities, allowing us to offer a **"drive time analysis,"** which will identify all routes within a 10-minute drive to a location, for example, taking into consideration road patterns. We'll also be able to provide a "drive distance analysis" to identify all routes that are within a certain kilometre-distance from a location. With Unaddressed Admail service's increased targeting capability, Canada Post will continue to help customers build their business.

Social Responsibility

CANADA POST HAS THE UNIQUE PRIVILEGE OF BEING PRESENT IN EVERY COMMUNITY ACROSS CANADA – FROM THE LARGEST URBAN CENTRE TO THE SMALLEST RURAL AREA.

This national presence enables us to have a positive effect on Canadian communities from coast to coast. For this reason, we feel a particular sense of obligation to ensure that our organization thinks, operates and acts responsibly and ethically.

At a corporate level, Canada Post is committed to dedicating one per cent of its pre-tax profits to non-profit and registered charitable organizations across the country. This donation total incorporates cash and in-kind contributions.

In 2007, we donated more than $500,000 to 300 different registered charities and not-for-profit organizations – for the benefit of all Canadians and on behalf of all employees. In addition to this one-per-cent donation in 2008, we are aiming to use the efforts of our people and the scale of our business to fund a national strategy that supports our new cause of choice: mental health.

Making charitable donations is just one way in which we show our commitment to being a socially responsible corporation; investing in community programs is another.

Investing in community programs is also a priority for our employees, with 92 per cent of those surveyed in 2007 saying they feel it is important for Canada Post to be involved at the community level. We are proud of the charitable efforts of our employees, and recognize that they can contribute significantly to positive social change at national and local levels. We support their contributions in many ways, including with the Coaching and Community Involvement Program (CCIP). Through CCIP, we offer employees donations to support them in their personal community activities outside of the workplace. In 2007, we donated more than $50,000 through the program for employees' involvement in various community organizations.

Our company and our employees have also been long-time supporters of the United Way. In 2007, we raised more than $2.5 million through employee and corporate donations, and were delighted to become the country's first-ever donor to receive a 16th consecutive "Thanks A Million" award. This award recognizes organizations that raise $1 million or more. Additionally, in 2007, for the seventh consecutive year, we made a donation of $25,000 to The Salvation Army. In line with our new cause of choice, mental health, the money was allocated to The Salvation Army's Suicide Prevention Ministry.

Photo: Mike Ridewood

CANADIAN FREESTYLE IN STYLE

Canada Post has been proud to be a major sponsor of the Canadian Freestyle Ski Association (CFSA) for the past six years. In 2006, we announced a six-year partnership agreement with the CFSA that made Canada Post the title sponsor of Canada's freestyle ski team. After a successful 2006/2007 season, the Canada Post Freestyle Team is ready once again to impress the world with its athleticism, strength and agility as it works toward the 2010 Vancouver Olympic Games.

As well as supporting Canada's freestyle ski team, the CFSA and Canada Post are creating a bursary program that will recognize athletic excellence and encourage the development of athletes at all levels.

We are also delighted that many of our employees continue with their good works even after they have retired. The Heritage Club, which is made up of 25,000 long-service and retired employees, has 28 chapters across the country and makes many important contributions to community and charitable causes and events. Over the past decade, Heritage Club members have volunteered close to half-a-million hours organizing and supporting events, such as food-hamper drives at Christmas and Easter, and contributing to worthwhile causes. Club members are also the driving force behind the National Heritage Literacy Project and help with the Santa Letter-writing Program.

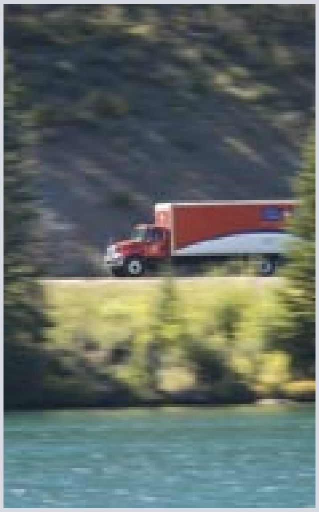
Every Christmas season, thanks to the efforts of more than 11,000 Canada Post volunteers and Heritage Club members, more than one million letters and 44,000 emails to Santa, from children across Canada and around the world, are replied to. This accomplishment was recognized in 2007 – the program's 26th year – by The Guinness World Records. Employees manage the Santa Letter-writing Program, donating some 170,000 hours of their collective time every year, and Canada Post provides all associated materials. We also host a website with games, activities and a "Write to Santa" email feature.

The Santa Letter-writing Program is only one way in which we support literacy – a long-time area of importance and involvement for us. In 2007, we were, for the first time,

CANADA POST'S FIRST "GREEN" BUILDING

In 2007, Canada Post announced that it is building a new mail-processing plant in Winnipeg. The building will be a model for future plants across the country and will reflect the Modern Post by being equipped with new technology and ergonomically sound equipment. The building will also be environmentally friendly, incorporating green technologies and conforming to recognized green building standards.

We appreciate the enormous impact buildings can have on the environment and the opportunities for savings that come with more sustainable design. Beginning in 2008, we will ensure that all new Canada Post buildings are compliant with or registered for certification under the Leadership in Energy and Environmental Design (LEED) Green Building Rating System administered by the Canada Green Building Council.



PROTECTING THE ENVIRONMENT

Climate change presents enormous challenges; it also offers tremendous opportunities for Canada Post to innovate technologically, create economic and environmental benefits, and ultimately improve quality of life for all Canadians.

In 2002, we set a goal to reduce direct GHG emissions from our buildings and vehicles. We have a number of programs, projects and initiatives in place to help ensure we meet this target, including the anti-idling campaign, which encourages our drivers to reduce vehicle idling time and turn off engines whenever possible, and the commuting challenge, which was in its 12th year in 2007 and promotes "active commuting" by encouraging employees to walk, cycle, run or inline skate to work. We are also working with manufacturers and after-market outfitters to find a viable fuel-efficient vehicle that is suitable for our delivery operations.

As well, we recognize the need to reduce the pressure on Canada's landfills. Our environment policy details waste-management and prevention plans, as well as local recycling practices, and we have launched an aggressive national recycling program at all of our facilities for 2008.

the presenting sponsor of the CanWest CanSpell National Spelling Bee. This one-year partnership with CanWest is one more way in which we strive to celebrate excellence in academic achievement and encourage positive study habits. Additionally, we also support La Dictée Paul Gérin-Lajoie, which aims to improve the quality of written French.

Our commitment to helping people learn and continue with their education also includes the Canada Post Aboriginal Education Incentive Award, which celebrates and rewards the hard work and determination of Aboriginal and Métis people who have overcome personal, economic or social adversity to return to high school, trade school, college or university. Canada Post is a committed participant in the Progressive Aboriginal Relations (PAR) program developed by the Canadian Council for Aboriginal Business (CCAB) and the National Quality Institute. The employment category within PAR promotes employee development and advancement.

Our advocacy for learning among young people is important to us, and we provide direct educational support to the children of full- and part-time employees through our Scholarship Program.

For the second year in a row, we're also helping our troops serving overseas feel a little closer to family and loved ones here at home. From October 26, 2007, to January 11, 2008, we again instituted free delivery of parcels and letters from family and friends to Canadian troops deployed in Afghanistan and elsewhere overseas.

Additionally, we believe that social responsibility includes doing our share on behalf of the environment. While the battle against climate change presents enormous challenges, it is also a tremendous opportunity for us to innovate technologically and economically, and ultimately improve quality of life for all Canadians. We are committed to taking steps to conserve energy, reduce greenhouse-gas emissions and improve the performance of our vehicles and facilities. Our overarching goal is to ensure the sustainability of our operations today and into the future.

MAKING CHARITABLE DONATIONS IS JUST ONE WAY IN WHICH WE SHOW OUR COMMITMENT TO BEING A SOCIALLY RESPONSIBLE CORPORATION; INVESTING IN COMMUNITY PROGRAMS IS ANOTHER.

CANADA POST'S CORPORATE SOCIAL RESPONSIBILITY REPORT

In 2007, Canada Post initiated its first Corporate Social Responsibility (CSR) Report, which established clear objectives around employee health and safety, environmental impact, business practices and community support. These objectives, and the mechanisms for measuring them, will be refined in future years as we work toward establishing a CSR framework that is fully transparent and accountable.

No CSR initiative can succeed without the full engagement and support of employees. Publication of our first CSR Report in 2008 will open up a conversation about our social responsibility to all employees, as well as to our partners and stakeholders.

For more information about Canada Post's 2007 Corporate Social Responsibility Report or to download a copy, please visit www.canadapost.ca/socialresponsibility.

Our commitment to mental health
OUT OF THE DARKNESS AND INTO THE LIGHT

"My postpartum depression evolved into psychosis. I wasn't just tired anymore, I barely wanted to live. I had no choice but to be admitted into hospital and treated. For the sake of my son, I'm so glad I got the help I needed, but I was one of the lucky ones. I was really embarrassed when friends and co-workers came to visit me in the hospital. I didn't know how they would react. To my great surprise they were all so supportive and were in fact a big part of my recovery. I'm happy to talk about my success story whenever I can – talking about mental illness is the key to overcoming it. "

Patty McGuire, Officer, Employee Relations

It is estimated that 20 per cent of Canadians will suffer from a mental illness at some time in their lives, and the remaining 80 per cent will be affected by the mental illness of a family member, friend or colleague. In 2007, Canada Post was proud to announce that it was adopting mental health as its cause of choice.

With our more than 60,000 employees, we have an opportunity to really make a difference by raising awareness about mental health issues and, in turn, breaking down barriers for sufferers. In 2008, we will implement a national strategy that supports mental health, and will also urge businesses and governments to do more to help. As well, we're supporting our mental-health agenda through a variety of activities, including sponsorship of Mental Illness Awareness Week and a national "Address your Stress" campaign.

Mental Illness Awareness Week

Mental Illness Awareness Week (MIAW) is the annual national public education campaign of the Canadian Alliance on Mental Illness and Mental Health (CAMIMH). This annual national public education campaign, which takes place from October 5 to October 11 in 2008, helps Canadians to appreciate the human cost of mental illness and delivers the message that mental illness can be treated. We are proud to have chosen to become the Platinum Plus sponsor of MIAW for 2008.

A national strategy to support mental health

We hope to set an example that other companies will follow by implementing a national strategy in support of mental health. This strategy involves promoting awareness of mental-health issues through a variety of activities, as well as raising funds to support mental-health organizations. We will raise funds through the collective efforts of our people and the scale of our business.

Corporate Governance

The Role and Composition of the Board

The role of the Board is explicitly supported by the statutory framework within which Canada Post operates (the *Canada Post Corporation Act* and the *Financial Administration Act*), the Corporation's bylaws, and its Statement of Board Values and Board Charter.

The Board is responsible for overall guidance on the strategy, business plans and related affairs of the Corporation. It is responsible for overseeing Canada Post on behalf of the Shareholder. In carrying out its oversight role, it is the Board that holds management accountable for business performance and achievement of the Corporation's other objectives. To fulfill these responsibilities, the Board is called upon to exercise judgment in the following general areas:

- Canada Post's strategic direction and Corporate Plans;
- major contracts;
- safeguarding Canada Post's resources;
- establishing and implementing processes for the recruitment of senior officers and Board members;
- monitoring corporate performance; and
- providing timely reports to the Shareholder.

Canada Post's Board of Directors is comprised of 11 members, including the Corporation's President and Chief Executive Officer. Two directorships were vacant during part of 2007. However, in October, the vacancies were filled to constitute a full Board. The Chairman and the President and Chief Executive Officer are Governor-in-Council appointees. As overseer of a $7-billion commercial and self-sufficient enterprise, the Board must bring strong business judgment, and valuable experience and insight in other fields, to the stewardship of the Corporation. The Board meets on both pre-arranged meeting dates and at such other times as deemed necessary by the Chairman. In order to provide strong oversight for such a large, complex and important company, the Board must devote approximately 35 days per year to its deliberations. In 2007, the Board held seven meetings and its committees met 22 times.

Independence of the Board

Traditionally, the position of the Chairman and that of the Chief Executive Officer are separate, although both are Governor-in-Council appointments. In addition, the Board normally holds its meetings with the President and Chief Executive Officer as a member and the Chief Operating Officer as an invitee. Otherwise, the Board meets without the presence of management unless its presence is required for presentations or reports and, at each meeting, the Board holds an in camera session. The Audit Committee regularly meets in camera individually with the Corporation's external and internal auditors. Furthermore, the Board, its committees and individual directors may engage independent counsel and advisors upon request and at the discretion of the Board.

Committees of the Board

The Board has formed the following committees to assist it in fulfilling its oversight responsibilities:

- The Audit Committee reviews financial information, which will be provided to Parliament and other stakeholders, the systems of corporate controls, which management and the Board have established, the audit process, the risk management framework, and assesses the Corporation's financial performance against its Corporate Plan.

- The Corporate Governance and Nominating Committee provides a focus on corporate governance, assesses corporate values and the elements which facilitate Board effectiveness, such as Board self-assessment, Committee structure and Terms of Reference, assists the Board in determining the composition and structure of the Board, and recommends candidates for Board membership, Chairman and President and Chief Executive Officer.
- The Human Resources and Compensation Committee reviews human resources and compensation matters, including the compensation of the President and Chief Executive Officer, recruitment, compensation and development, retention, and significant human resource policies and labour relations issues.
- The Pension Committee oversees the $14-billion Canada Post Pension Plan, pension plan matters and policies, including pension plan liabilities, pension plan strategies, the Corporation's responsibilities as pension plan sponsor, the Corporation's fiduciary responsibilities as pension plan administrator, makes investment decisions in accordance with the Statement of Investment Policies and Procedures, and oversees investment managers.
- The Corporate Social Responsibility (CSR), Environment, Health and Safety Committee oversees the Corporation's policies, programs, practices, procedures and performance with respect to CSR, including the environment and occupational health and safety.

Board Effectiveness

The Board regularly assesses its effectiveness and functioning through a self-assessment survey. The Board has created membership criteria that set out the skills and personal qualities expected of its members for the use of the Government in appointing Board members. The compensation of the Board complies with the Remuneration Guidelines for Part-time Governor in Council Appointees in Crown Corporations issued by the Privy Council Office, and an orientation process is established for new directors. As well, a process is in place to assess the ongoing development requirements of directors, and training opportunities are provided to continue to enhance the effectiveness of existing directors.

Fraud and Error

Pursuant to recommendations issued by the Canadian Institute of Chartered Accountants in 2004, the Audit Committee assumed enhanced responsibility to consider fraud and error in financial statements. Accordingly, the Audit Committee reports that it has reviewed and accepts the company's financial statements, the attached notes, the auditor's opinion and their assertions on independence.

Subsidiaries

A Governance Model for Canada Post's subsidiaries ensures consistent governance practices where the Corporation holds a majority interest.

The Board and management of Canada Post hold the view that sound governance practices that are dynamic in nature are the bedrock of a quality organization that builds value and is dedicated to its employees and customers. Corporate governance is an essential component to the fulfillment of Canada Post's public policy and commercial mandates, and will contribute to ensuring that all Canadians continue to receive a universal and affordable national postal service.

Board of Directors

Marc A. Courtois ▲❇✖★●

Westmount, Quebec
Chairman of the Board
Canada Post Corporation

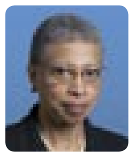
Moya Greene

Ottawa, Ontario
President and CEO
Canada Post Corporation

Ernest J. Brennan ▲❇
F.C.A.
Winsloe, Prince Edward Island

Denyse Chicoyne ◗▲●
CFA, MBA
Outremont, Quebec
Corporate Director

Thomas Cryer ■★
F.C.A.
Etobicoke, Ontario



Dr. Daurene Lewis ❖❇
C.M., MBA
Bedford, Nova Scotia

Siân M. Matthews ✖●

Calgary, Alberta

Robert Pletch ▲❇
Q.C.
Regina, Saskatchewan

William H. Sheffield ✿▲★

Toronto, Ontario
Corporate Director

Jean Turmel ★

Outremont, Quebec
President
Perseus Capital Inc.

Donald Woodley ♦✖●

Orangeville, Ontario

■ Chairperson of the Audit Committee
♦ Chairperson of the Corporate Governance and Nominating Committee
❖ Chairperson of the Corporate Social Responsibility, Environment and Health and Safety Committee
✿ Chairperson of the Human Resources and Compensation Committee
◗ Chairperson of the Pension Committee

▲ Member of the Audit Committee
❇ Member of the Corporate Governance and Nominating Committee
✖ Member of the Corporate Social Responsibility, Environment and Health and Safety Committee
● Member of the Human Resources and Compensation Committee
★ Member of the Pension Committee

Annual Public Meeting:
June 18, 2008
Hamilton, Ontario

Officers of the Corporation

Moya Greene
President and CEO

Jacques Côté
Chief Operating Officer

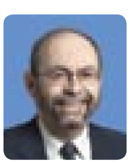
Stewart Bacon
Senior Vice-President
Marketing, Sales and Service

Wayne Cheeseman
Chief Financial Officer

Laurene Cihosky
Senior Vice-President
Direct Marketing, Advertising and Publishing Business

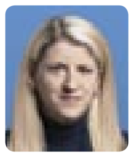
Cal Hart
Senior Vice-President
Postal Transformation

Peter Melanson
Senior Vice-President
Transaction Mail



Louis F. O'Brien
Senior Vice-President
Parcels

John Smith
Senior Vice-President and Chief Information Officer

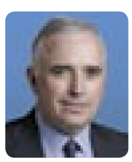


Mary Traversy
Senior Vice-President
Operations

Phil Ventura
Senior Vice-President
Strategy

Robert Waite
Senior Vice-President
Corporate Social Responsibility

Bonnie Boretsky
Vice-President
Compliance



John Duncan
Vice-President
Human Resources

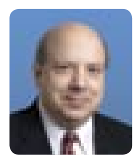
Stephen Edmondson
Vice-President
Customer Service

Douglas Greaves
Vice-President
Pension Fund and Chief Investment Officer

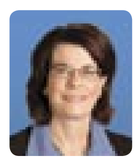
Kathy Haley
Vice-President
Marketing

Douglas Jones
Vice-President
Field Operations

Susan Margles
Vice-President
Government Relations and Policy Framework

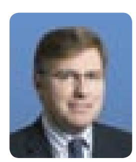


Clary Ottman
Vice-President
Finance and Comptroller

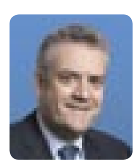


Cheryl A. Persad
Vice-President
Enterprise Sales

Serge Pitre
Vice-President
Business Sales



Gerard Power
Vice-President, General Counsel and Corporate Secretary



Anthony Wilson-Smith
Vice-President
Communications

Mike Garvey Corporate Auditor

As of March 31, 2008

Chairman's Message

IN A CHALLENGING BUSINESS ENVIRONMENT, THE SUCCESS OF EACH OF OUR LINES OF BUSINESS AND THE CORPORATION WILL RELY ON A CONTINUING FOCUS TO IMPLEMENT POSTAL TRANSFORMATION.

On behalf of the Board and Shareholder, I am pleased with the results of the Corporation during 2007. The integrity and determination of our organization and its employees were key in meeting the health and safety needs of our people, while facing the market volatility experienced in some sectors in 2007. That integrity and determination is also reflected in the financial results for the 12-month fiscal period ending December 31, 2007. The Corporation ended the period with net income of $54 million. Income before taxes was $160 million, a good performance against a plan of $126 million. This extends the Corporation's record of profitability to 13 consecutive years, a sustained period of success in achieving or exceeding financial targets. The Corporation paid a dividend of $47 million to its Shareholder, the Government of Canada; total dividends paid over the last five fiscal periods amount to $267 million. The return on equity, however, reached only 3.8 per cent reflecting the difficult market conditions.

To remain successful, the Board recognizes that the company must be transformed to improve delivery services across all media and to continue to deliver real value to all its customers – businesses and consumers alike. To meet customer needs in the future – and build a strong and profitable Canada Post – both the Board and management agree that we must be prepared to make significant investments in renewing the network and equipment, as well as in our employees. During 2007, the Board approved management's strategy to make these investments and continue on its journey toward the Modern Post.

As a result, in early 2008, the company announced that a state-of-the-art, environmentally friendly mail-processing plant will be built in Winnipeg. This plant, which represents an investment of $50 million, is expected to be up and running in 2010. A model for the Modern Post and future plants across the country, the building will be equipped with new technology and ergonomically sound, new-generation mail-processing equipment. The plant will give Canada Post's customers the best possible service and its employees a new and efficient working environment with more safety features. Management and the Board will continue to work closely together to ensure that these important investments are made prudently and that the ensuing benefits to employees, customers and Canadians are realized.

TO MEET CUSTOMER NEEDS IN THE FUTURE – AND BUILD A STRONG AND PROFITABLE CANADA POST – BOTH THE BOARD AND MANAGEMENT AGREE THAT WE MUST BE PREPARED TO MAKE SIGNIFICANT INVESTMENTS IN RENEWING THE NETWORK AND EQUIPMENT, AS WELL AS IN OUR EMPLOYEES.

As the second-largest Crown corporation in Canada, with a workforce of more than 60,000 and a presence in every city and town across the country, Canada Post's dealings can have far-reaching effects on communities, the environment and the economy. As such, the Board recognizes that the company must take a serious approach to its corporate social responsibility and, as a result, is pleased to play a key oversight role in these vital activities.

It's clear that 2008 will be equally as challenging as 2007, if not more so. The threat of recession could exacerbate the declining Lettermail volumes experienced in 2007. It is clear that continued cost control is needed if the company is to overcome the inevitable revenue declines a recession would bring. We must continue the evolution into a dynamic, forward-thinking organization if we are to prevail over the new and ongoing challenges that 2008 will bring.

As Canada Post's new Chairman of the Board, I'm aware that I joined the Corporation at a challenging time. On behalf of the Board of Directors, however, I would like to say that I am convinced that we have the committed management team and dedicated employees needed to continue to operate successfully. Together, you have built the solid foundation needed. The Board is committed to working with you to transform Canada Post into a Modern Post that's prepared and able to meet the needs of Canada and all Canadians – today and tomorrow.

Marc A. Courtois
Chairman of the Board of Directors

Ombudsman's Message

IN ACCORDANCE WITH MY *MISSION STATEMENT*, I INDEPENDENTLY REVIEW CUSTOMER CONCERNS UNRESOLVED BY ALL OTHER AVENUES OFFERED BY CANADA POST IN A FAIR, UNBIASED AND TIMELY MANNER TO IMPROVE POSTAL SERVICE FOR ALL CANADIANS.

I act as an impartial mediator committed to maintaining confidentiality on issues that are brought to my attention and I recommend actions that are equitable to all parties.

In 2007, my office processed 6,921 requests for assistance, representing a decrease of 5% from last year. We examined 6,572 complaints and processed 349 requests for information. Of the complaints examined, we processed 1,718 complaints at intake, resolved 1,847 complaints at the initial stages of the investigative process, and conducted 3,007 in-depth investigations. These investigations resulted in 1,242 recommendations where Canada Post modified its original decision and 601 recommendations where I concluded that Canada Post's original decision should be maintained as I found no cause or justification to recommend a different resolution.

The complaint resolution process ensures that Canada Post has every opportunity to resolve customer complaints. As such, customers may only appeal to my office once Canada Post has completed its review of their complaint and they are not satisfied with the proposed solutions. With this in mind, in late 2006, we incorporated this process into our integrated voice response system. Given that my office receives in excess of 10,000 calls per year, this initiative has had a positive impact on intake staff, as our statistics revealed a 53% decrease in the number of premature calls processed over the previous year.

My office operates at arms-length from Canada Post and does not have access to Canada Post files. Therefore, before customer complaints can be assessed, we ask that customers provide us with the details pertaining to their complaint, including copies of all relevant documentation. As we noted an increasing number of customers who did not provide all the necessary information, we encountered delays in initiating the investigative process. To minimize these delays, our Request for Review form was modified to include a number of prompting questions aimed at drawing more product/service specific information from customers.

We also undertook a two-phased approach to reviewing our website. Phase one involved redesigning and amending its contents to provide concise information to customers, and phase two consists of introducing an On-line Request for Review form, which is currently being developed.

Again this year, Canada Post played a fundamental role to the success of my office, as it continued to be receptive to settling customer complaints. Also, I am very pleased with the ongoing dedication of my staff as they have consistently demonstrated a firm commitment to the values described in my *Mission Statement*. Their sustained effort undoubtedly contributed to the success of the office.

Michel Tremblay

Effective March 31, 2008, Michel Tremblay is retiring from his position as Ombudsman for Canada Post. The Corporation wishes to acknowledge his ten years of excellent service and dedication.

Financial Performance

CONTENTS

MANAGEMENT'S DISCUSSION AND ANALYSIS

This Management's Discussion and Analysis (MD&A) comments on the operations and financial condition of Canada Post Corporation (the "Corporation" or "Canada Post") for the year ended December 31, 2007. This discussion should be read together with the consolidated financial statements and accompanying notes, which have been prepared in accordance with Canadian generally accepted accounting principles and are reported in Canadian dollars. The information in this MD&A is current to March 28, 2008, unless otherwise noted.

Management is responsible for the information presented in the Annual Report, including the MD&A. All references to "our" or "we" are references to management of Canada Post.

Forward-looking statements

This Annual Report, including this MD&A, contains forward-looking statements that reflect management's expectations regarding the Corporation's objectives, plans, goals, strategies, future growth, results of operations, performance, and business prospects and opportunities. Forward-looking statements are typically identified by words or phrases such as "anticipates," "expects," "believes," "estimates," "intends," and other similar expressions. These forward-looking statements are not facts, but only estimates regarding future results. These estimates are based on certain factors or assumptions regarding expected growth, results of operations, performance, business prospects and opportunities (collectively, the "Assumptions"). While we consider these Assumptions to be reasonable, based on information currently available to us, they may prove to be incorrect. These estimates of future results are subject to a number of risks, uncertainties and other factors that could cause actual results to differ materially from what the Corporation currently expects. These risks, uncertainties and other factors include, but are not limited to, those risks and uncertainties set forth in *Section 5 – Risk Management on page 54* of this MD&A (collectively the "Risks").

To the extent the Corporation provides forward-looking information that is future-oriented financial information or financial outlooks, i.e., future growth and results of operations, the Corporation is providing this information for the purposes of describing its future expectations, and readers are cautioned that this information may not be appropriate for any other purpose. Further, future-oriented financial information and financial outlooks, as with forward-looking information generally, are based on the Assumptions and subject to the Risks.

Readers are urged to consider these factors carefully when evaluating these forward-looking statements. In light of these Assumptions and Risks, the events predicted in these forward-looking statements may not occur. The Corporation cannot assure that projected results or events will be achieved. Accordingly, readers are cautioned not to place undue reliance on the forward-looking statements.

The forward-looking statements included in this Annual Report, including this MD&A, are made only as of the date of this Annual Report, and the Corporation does not undertake to publicly update these statements to reflect new information, future events or changes in circumstances or any other reason after this date.

1 Introduction and Financial Highlights

An overview of The Canada Post Group and a summary of the 2007 financial results

1.1 Materiality

In assessing what information is to be provided in the MD&A, management applies the materiality principle as guidance for disclosure. Management determines if the information is material if, under current circumstances, it is considered probable that its omission or misstatement would influence or change the decisions of our Shareholder or others with a reasonable knowledge of the business and economic activities of the Corporation.

1.2 The Canada Post Group

The Canada Post Group provides a variety of traditional and innovative services to connect Canadians and meet our customers' needs. We are one of the largest employers in Canada as well as one of Canada's top recognized brands and a substantial enabler of the Canadian economy. With a dedicated workforce of 72,500 employees, we process over 11 billion pieces of mail each year, and deliver them to over 14 million addresses in urban, rural and remote locations across Canada.

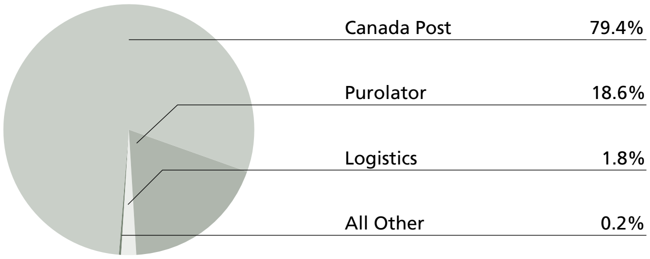
Our organizational model includes a number of subsidiaries that have allowed us to increase the diversity of the products and services we offer, as well as our capability and reach and our ability to access new sources of revenue. Today we hold, directly or indirectly, an interest in Purolator Courier Ltd. (Purolator), SCI Logistics Inc. (SCI Logistics), Innovapost Inc. (Innovapost), and Canada Post International Limited (CPIL).

We periodically evaluate our corporate holdings to assess their strategic fit and whether business objectives continue to be met. Changes over the last two years include:

- In 2006, we fully integrated the epost™ service into our Transaction Mail line of business, to provide a more strategic alignment of physical and electronic services.
- In January 2007, we sold our 50% interest in Intelcom Courier Inc., following an assessment of market dynamics in relation to our strategic priorities.
- In March 2007, as part of a reorganization, SCI Logistics was established as the parent organization of Progistix-Solutions Inc. and Assured Logistics Inc. As described in *note 5 to the consolidated financial statements on page 99*, SCI Logistics acquired AMG Logistics Inc., First Team Transport Inc. and Partnership Inc. (The AMG Group) to diversify its services and competencies.

The chart below illustrates the distribution of our revenue by segment, as a percentage of total revenue.

Revenues by segment – 2007



Revenues by Segment	2007	2006	2005
Canada Post	79.4%	80.0%	80.2%
Purolator	18.6%	18.0%	17.6%
Logistics	1.8%	1.7%	1.9%
All Other	0.2%	0.3%	0.3%

1.3 Consolidated highlights

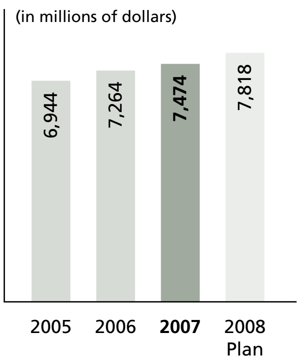
In 2007, The Canada Post Group recorded its 13th consecutive year of profitability, earning consolidated net income of $54 million on consolidated revenue from operations of $7,474 million. With narrow margins and lower-than-expected revenues, the Corporation focused on controlling discretionary costs and finding operational efficiencies.

Consolidated highlights

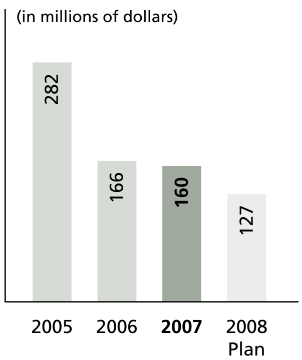
(in millions of dollars)

Year ended December 31	2007	2006	Change	Explanation of change
Consolidated income statement				*Highlights, as discussed in Section 8 – Results from Operations on page 65*
Revenue from operations	7,474	7,264	2.5%	Up 2.5% from 2006, driven primarily by a strong performance in Admail™ products and Purolator courier services
Cost of operations	7,346	7,116	3.2%	Up 3.2% from 2006, due to wage increases, growth in points of call, and higher transportation and rural delivery costs. Increases were partially offset by lower pension expense and tight control over discretionary expenditures
Income before income taxes	160	166	(4.1%)	Down 4.1% from 2006, as cost increases outpaced revenue growth
Net income	54	119	(54.3%)	Down 54.3% from 2006. Income tax expense increased $58 million due to reductions in statutory income tax rates on future tax benefits recorded
Return on equity	3.8%	8.4%	(4.6%)	Down 4.6% from 2006, due to lower net income
Dividends paid	47	80	(40.1%)	Based on 40% of previous year's net income
Dividends declared subsequent to year-end	22	47	(54.3%)	Based on 40% of 2007 net income
Consolidated cash flow statement				*Highlights, as discussed in Section 6 – Liquidity and Capital Resources on page 59*
Cash and cash equivalents	386	499	(22.7%)	Down 22.7% from 2006, reflecting lower net income and transfer of financial investments to short-term investments
Cash provided by operating activities	342	267	27.8%	Up 27.8% from 2006, primarily due to lower payments to the Canada Post Pension Plan, offset by reduced net income and changes in non-cash working capital
Cash used in investing activities	511	278	83.0%	Up 83.0% from 2006, primarily a higher net increase in short-term investments. Also reflects increased capital spending and the acquisition of The AMG Group by SCI Logistics, partially offset by proceeds from the sale of two Canada Post properties
Capital expenditures	330	305	8.1%	Up 8.1% from 2006, due to replacement of obsolete and aging equipment and facilities
Cash provided by financing activities	56	36	56.3%	Up 56.3% from 2006, primarily due to lower dividends paid, partially offset by a decline in transitional funding from the Government of Canada related to pension contributions

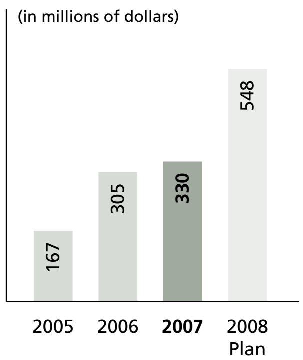
Revenue



Income before income taxes (EBT)



Capital expenditures



1.4 Consolidated performance to plan

In spite of lower-than-expected revenues, The Canada Post Group exceeded its earnings plan by $34 million, earning income before income taxes of $160 million.

The following table presents the Corporation's consolidated performance for the 2007 fiscal year compared to the 2007 Corporate Plan and the 2008 plan forecast.

Year ended December 31 (in millions of dollars)	2007 Results	2007 Plan		Explanation	2008 Plan
Consolidated				*For further information, see Section 2 – Our Business, Vision and Strategy on page 34 and Section 8 – Results from Operations on page 65*	
Revenue from operations	7,474	7,583	(109)	Fell short of expectations by $109 million, primarily due to: • Lower volume growth of Canada Post products, including domestic Lettermail™, international outbound lettermail and Addressed Admail™ • Lower-than-expected revenue per piece for domestic Lettermail This was partially offset by: • Acquisition of The AMG Group by SCI Logistics	7,818
Cost of operations	7,346	7,471	125	Exceeded expectations by $125 million, primarily due to: • Tight control over administration and discretionary costs and initiatives at Canada Post and Purolator • Lower Canada Post pension expense • Rural mail directive costs lower than planned This was partially offset by: • Acquisition of The AMG Group by SCI Logistics • Canada Post net productivity and absenteeism • Higher transportation costs and use of contractors to cover rural routes, especially in Alberta • One-time expenses relating to write-down of asset-backed commercial paper, epost impairment losses, and CPIL settlement with the Government of the Netherlands Antilles	7,714
Non-operating income (expense)	32	14	18	Exceeded expectations by $18 million, primarily due to: • Sale of two Canada Post properties • Higher than expected net interest	23
Income before income taxes	160	126	34	Exceeded expectations by $34 million	127

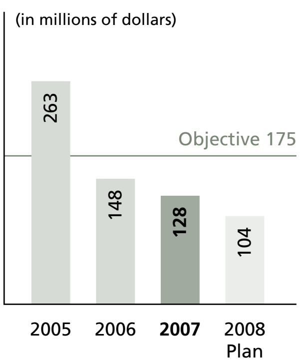
1.5 Consolidated performance to Policy Framework objectives

In December 1998, the Government of Canada approved a multi-year Policy Framework for Canada Post. This framework includes long-term financial and service objectives, as well as a price-cap formula for the basic letter rate. The long-term financial objectives for The Canada Post Group are annual earnings before interest and taxes (EBIT[1]) of $175 million, return on equity[2] of 11%, and a productivity ratio[3] of 97%.

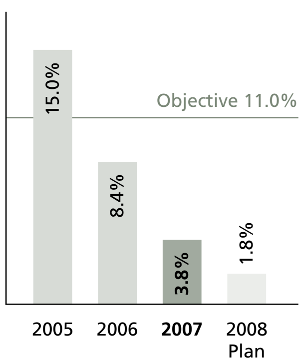
Each year, we review our prospects and priorities, and submit our five-year Corporate Plan to our Shareholder. At the date of this report, the 2007 Corporate Plan and the 2008 Corporate Plan had not been approved by the Shareholder. However, the Corporation is able to operate based on the *Financial Administration Act*.

The charts below set out the Policy Framework objectives, and our progress and plan forecast towards achieving them.

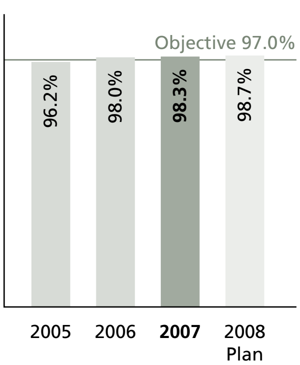
EBIT



Return on equity



Productivity ratio



Of particular note, if one-time transactions, primarily transitional support from the Government of Canada related to pension and certain ancillary benefits, were removed from 2006 and 2007 results, the Canada Post segment would have incurred losses in these years. This transitional support ends in 2010, therefore putting more pressure on our earnings going forward.

2 Our Business, Vision and Strategy

A discussion of the business, vision and strategy of our core businesses

2.1 Trends, opportunities and threats

Global trends

Canada Post and other postal operators (Posts) worldwide operate under a different legal framework than private-sector companies and, as a result, face different challenges.

Traditionally, postal operators' exclusive privilege, combined with the right to engage in related competitive activities, such as parcel and courier services, financed the costs of the Posts' universal service obligations (USO) during a time of sustained volumes of lettermail. However, technology, globalization and other factors have greatly changed the nature of the postal market.

For several years, the Internet, email and other technological advances in communications have reduced lettermail volumes and as a consequence considerably eroded the economic value of the exclusive privilege. Globalization has increased the level of competition in the parcel and courier business. Companies, such as UPS and FedEx for example, offer one-stop international services and operate without the public policy obligations that Canada Post must meet.

As the postal market has evolved, most governments have responded by commercializing their postal operators. Some governments have also updated postal legislation, allowing operators to manage their operations in a clear regulatory environment and with a minimum of interference. A number of countries, such as the United Kingdom, Sweden, Finland and New Zealand, have opened their postal markets to full competition. Many Posts have taken advantage of these changes to their regulatory framework to expand into direct marketing, logistics, document management and financial services. Some have expanded their geographic presence regionally and even into other countries, including Canada.

To date, however, no government has removed or substantially diminished their Post's USO – all postal operators in the developed world retain responsibility for some minimum level of public service. Thus, as lettermail volumes continue to stagnate or decline and as competition increases, the challenge remains how best to provide and finance public obligations and how best to ensure the long-term sustainability of the postal market and the incumbent national postal operator.

[1] EBIT equates with income from operations as reported in the consolidated financial statements
[2] Return on equity = net income ÷ average equity
[3] Productivity ratio = cost of operations ÷ revenue from operations

The evolution has been most evident in the European Union (EU), which has been progressing in stages since 1997 towards a completely open postal market, now scheduled for January 1, 2011. The United States (U.S.) has also had a domestic postal debate, and in December 2006 enacted new postal legislation for the first time since 1970.

Compared to the EU or the U.S., there has been less debate on the postal market in Canada, and the postal regulatory framework has remained largely unchanged since the creation of Canada Post in 1981 and the establishment of the Policy Framework in 1998. However, implementation of proposed legislation (Bill C-14) to amend section 15 of the *Canada Post Corporation Act* would liberalize the outbound international portion of Canada Post's business.

Canada

Although The Canada Post Group has enjoyed many successes, we face many of the same challenges as other Posts. Increased competition both within Canada and internationally, along with rapid technological changes, are forcing our business to change. Customers have more and more options. Canadian businesses, which account for close to 90% of our revenues, have electronic substitutes for letters, a cornerstone of Canada Post's business. In the international segment, re-mailers can offer lower-cost service to Canadian businesses and organizations, but they do not have the variety of public policy obligations that we must meet.

Canada Post remains committed to being financially self-sufficient. However, we face cost pressures that our competitors do not. Canada Post is required to deliver mail to all Canadians regardless of where they live, five days a week, and to meet specific service standards at a reasonable cost. At the same time as our delivery network has been increasing by approximately 200,000 points of delivery a year, the volumes of our most profitable product, Lettermail, are decreasing. Many of our products and services are price regulated and pricing on other products is under strong competitive pressure. We have high fixed costs, due largely to labour costs resulting from the USO and collective agreements. The limited profitability of the Corporation is further hampered by the financial pressures of Shareholder directives and public policy commitments, which, in total, amounted to almost $40 million in 2007, and is expected to grow to approximately $75 million in 2008, and continue to grow to approximately $100 million per year by 2012.

As a result of these challenges, we continue to explore various alternatives to the means we have at our disposal to fund our increasing universal service and public policy obligations, with our Shareholder, the Government of Canada, in consideration of our need to remain financially self-sufficient.

2.2 Strategic vision – Building the Modern Post

In order for the Corporation to remain relevant in the future, we are committed to continuing our transformation into an efficient and modern postal service that we refer to as the "Modern Post."

We have continued to make strong progress in our journey toward the Modern Post. In 2005, we aligned the Corporation along three lines of business – Transaction Mail, Parcels and Direct Marketing – to further shift our mindset toward the customer. In 2006, we advanced our employee engagement initiative, with objectives to reduce absenteeism, increase job commitment and satisfaction, and improve productivity. In 2007, we intensified our efforts to engage our employees and improve health and safety, and clarified our long-term strategies for the Modern Post.

Building the Modern Post

With this foundation in place, we are better positioned to make the necessary investments to modernize our core infrastructure, thus becoming more competitive and delivering a new value proposition to our customers and our customers' customers. A number of strategic initiatives, as illustrated at the bottom of page 35, are now underway toward building the Modern Post.

Investment in Canada Post's core infrastructure has been inadequate in recent years, and our network is in need of renewal. Our aging infrastructure stands in the way of our priorities for modern, efficient operations. It is expected that new infrastructure will also provide the capabilities to enhance our product and service offerings, enabling us to defend and grow our core businesses.

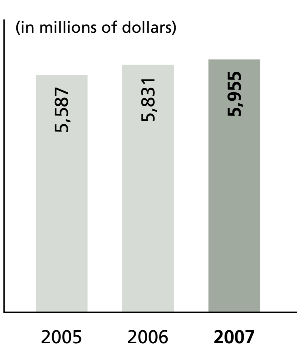
Over the next five years, we could invest up to $1.9 billion of capital to support these major improvements. This is in addition to the $1.1 billion of capital investment that is needed to support ongoing operations. We will prioritize our investments based on the greatest need and spend only what we can afford. See *Section 6.5 – Liquidity and capital resources on page 60.* By acting now, we plan to put these improvements in place and make the necessary process changes, taking advantage of a window of natural attrition, while respecting all provisions in our collective agreements, including the commitments relating to job and income security. Additionally, as part of our overall commitment to corporate social responsibility, it is our intent to ensure that our investments and strategies meet sustainable criteria in terms of the environment as well as the health and safety of our employees.

2.3 Canada Post segment

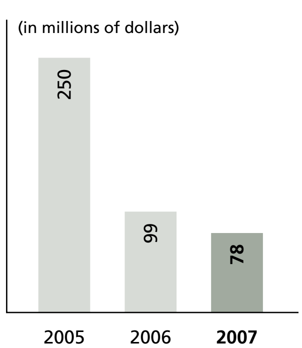
Canada Post Corporation is an important public institution and fulfills a critical role within the Canadian economy. Canadians have ranked Canada Post as the most trusted federal institution.

The Canada Post segment generates approximately 80% of our consolidated revenue.

Revenue

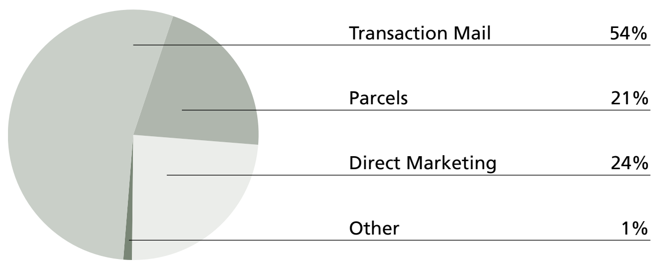


EBT



The following chart illustrates the distribution of our operating revenues by line of business, as percentages of the segment's total.

Operating revenues by line of business – 2007



Operating revenues by line of business	2007	2006	2005
Transaction Mail	54%	55%	56%
Parcels	21%	20%	21%
Direct Marketing	24%	23%	21%
Other	1%	2%	2%

2.4 Canada Post – Transaction Mail

Our business

Transaction Mail is Canada Post's most profitable line of business, representing approximately 54% of Canada Post's revenue in 2007. Transaction mail includes bills, statements, invoices, payments and other letters, in either paper or electronic form. We offer three primary delivery services: Lettermail for correspondence within Canada, International Letter-Post, and our electronic product, epost.

In 2007, we launched the SmartFlow™ Document Management Services suite (SmartFlow). SmartFlow transforms data to help manage mailers' communication processes from end to end. The services include:

- SmartFlow Send, in which Canada Post takes raw or print-ready data provided by large mailers, transforms it into a form appropriate for any given medium, prepares it for delivery, and then delivers it in the medium chosen by the recipient;
- SmartFlow Recover, in which Canada Post captures the data from mailers' undeliverable mail and then provides back formatted address information to help them keep their customer mailing information up to date; and
- SmartFlow Respond, in which Canada Post collects all the information from reply cards, application forms, questionnaires and other mailed response vehicles, then transforms the information into electronic data for the customer.

Business environment

Transaction Mail competes in the larger Canadian communications market, which includes telephones, instant messaging, email and other means of communication.

Advances in technology, such as the Internet and email, have created substitutes for letters, reducing Lettermail volumes and threatening the business. Large commercial mailers are consolidating their mailings to reduce costs. The global nature of business has encouraged new entrants into the Canadian market to set up re-mail operations, eroding our International Letter-Post volumes. In 2007, Transaction Mail volumes decreased by 1.6%, at the same time as points of delivery increased by approximately 200,000.

Vision

Our vision is to *provide a unique multi-channel offering that combines the physical mail stream and the electronic channel with security and certainty to increase the value of mail services to our customers and their customers.*

Strategy

Our vision is consistent with the ambitions of postal operators around the world, supporting our evolution into the Modern Post. In 2008, we intend to focus on three strategic priorities to guide our actions:

- refine products and services to meet the evolving needs of our customers;
- develop markets; and
- invest in capabilities to improve productivity.

Adding value to our current services and customizing services to satisfy specific user needs will assist in strengthening our Transaction Mail services. For example, we intend to broaden SmartFlow to satisfy those needs that the market has indicated it values most. We plan to make epost easier to use and more inviting as well as integrate epost's website into the Canada Post website. One of our goals is to make value-added features, such as communication activity data analytics, feasible and available for all delivery services, including Lettermail.

We will seek to expand our customer base by targeting small to medium-sized businesses and by focusing on service application niches. The expansion would be supported by increased market investment involving traditional promotional programs and that would promote these novel services.

Increasing our connection with all Canadians is crucial to maintaining relevance with Canadian businesses. We intend to introduce new online access services to present a more modern version of Canada Post to our customers. Based on market acceptance, we will continue to expand electronic services, giving Canadians the choice of how they receive their mail, either through printed material or secure, easy-to-use electronic services offered by Canada Post.

Our experience in 2007 continued to expose the Corporation's vulnerability to any reduction or shift in Lettermail volumes. Improved productivity is essential to the health of the Transaction Mail line of business and to the Corporation's viability. Over the next several years, Canada Post intends to invest strategically in new letter sorting equipment and mail processing plants to improve the speed and reliability of service delivery and reduce physical handling and processing time. *For further discussion, refer to Section 6.5 – Liquidity and capital resources on page 60.*

2007 objectives and achievements

We set out an ambitious strategy of defense and growth for Transaction Mail. The following outlines the progress we have made against our objectives.

Defend the Lettermail business

In 2007, revenue for Transaction Mail was flat, when compared with 2006.

- We continued to meet our Lettermail service performance target of 96% as measured by an independent firm.
- The PERMANENT™ stamp, which is always valued at the current basic domestic lettermail rate, was expanded in 2007 to include seasonal and special releases.
- We engaged in more meaningful discussions with our customers, ranging from resolving customer issues to collectively contemplating future development and offering services that provide greater customer value.

Strengthen the Transaction Mail business

In 2007, we significantly rationalized services and improved infrastructures for more efficient delivery.

- We rationalized the print and epost operations with the Multi Channel Mail Presentment Solutions (SWITCH), and packaged them as SmartFlow, which was launched successfully.

Grow the Transaction Mail business

While we made progress growing the Transaction Mail business in 2007, the strategic services of epost and SmartFlow did not fulfill our 2007 goals due to slower-than-forecast sales. However:

- SmartFlow acquired a significant number of new customers during the year.
- We identified epost shortcomings in usability and low market awareness. The intention is to address these shortcomings in 2008 by upgrading the way in which epost is presented to consumers, and by integrating epost into the canadapost.ca website.
- We intend to work with several large mailers on joint promotional campaigns to increase consumer awareness of epost.

Financial highlights

Transaction Mail revenue remained relatively flat at $3,214 million in 2007, when compared with 2006. This represents a decrease of 0.2%, when adjusted for trading days. Volumes declined 1.6%, but were offset by an increase of 1.3% in the average revenue per piece. *For further discussion of year over year results, see Section 8.4 – Results from Operations – Canada Post segment on page 66.*

2.5 Canada Post – Parcels

Our business

Canada Post's Parcels line of business serves domestic destinations through Xpresspost™, Priority Courier™ Expedited Parcel and Regular Parcel services. Our Xpresspost service is an economical alternative to next morning courier services. Priority Courier is a next morning before noon courier service. Expedited Parcel provides ground service to commercial customers, while Regular Parcel is a low-price delivery service for consumers. Internationally, Canada Post provides a similar diversity of services to both consumers and commercial customers, including Xpresspost-USA, Xpresspost-International and Expedited Parcel-USA.

Business environment

Canada Post and its subsidiary, Purolator, are leading players in the highly competitive and growing Canadian shipping and delivery market. By revenue, Purolator continues to be a market leader at $1.4 billion, followed closely by Canada Post with revenue of $1.2 billion, and global players FedEx, UPS and DHL, respectively. In terms of volume share, the Parcels line of business is a leader in the domestic market.

Our strength lies in the fast-growing business-to-consumer home delivery segment of the market, which is greatly influenced by the growth of online retail e-commerce. Within this segment, Canada Post has a competitive advantage in that we deliver to every address in Canada.

With our 6,600 post offices, Canada Post has the largest retail network in Canada, more than six times larger than that of our competitors combined. Due to the strong Canadian dollar, these post offices are seeing decreased shipping volumes from small business retailers who compete in the North American market.

The Canadian shipping and delivery market will remain fiercely competitive as customer expectations continue to rise. The industry is an early adopter of new technology and is increasingly characterized by abilities to serve the globalizing economy.

Vision

Our vision is to *use our competitive advantage of a national network to become the standard for efficient delivery of parcel items, offering clear end-to-end tracking and delivery flexibility to our customers.*

Strategy

The key to our customer-driven Parcels strategy is "ease and convenience," which, in our view, helps us provide value-based parcel delivery services to Canadian shippers. Improved parcel tracking and our drive to enhance operational efficiencies are balanced with a focus on providing quality customer and consumer offerings. We expect that this approach will continue to drive growth and increase profitability. We intend to focus on four strategic priorities to guide our actions.

Improve the visibility of our products to meet customer expectations

- Tracking of items is the competitive norm within the parcels market, and our ability to provide timely and accurate scans is crucial for long-term success.

Provide a high-quality offering to the customer (shipper) with superior integration of products and services

- We plan to focus on the business-to-consumer segment, using our core competency in home delivery.
  - Online access to our services on customers' retail Internet sites will be improved by enhancing "plug-and-play" applications that provide rates, labels, addressing information and more. This will allow us to enhance services on existing partner platforms, such as eBay™, while allowing broader access to other retailers.
- Focusing on our core competency in retail access and reach, we plan to focus on the small and medium-sized business segment.
  - Our current On Demand Pickup service will be expanded to include all products and reduce restrictions.
  - We expect to increase retail access for small business customers through strategic partnerships with independent full-service dealerships such as PostNet™.

Provide high-quality offerings to the consumer (receiver) with integration of valued features and preferences

- We plan to further leverage our leadership in home delivery by giving receivers the ability to exercise choice in alternate delivery services.
- Where charges are due, such as collection on delivery (COD) or customs fees, flexible online prepayment options will be made available.

Increase operational efficiency to improve service and reduce costs

- By continuing to apply modern processing methodologies in our facilities, we expect to realize further cost efficiencies and maintain a viable service and performance standard.
- Over the next several years, as part of the postal transformation initiative, major investments are planned to replace outdated parcel-processing equipment and facilities. Winnipeg is scheduled to see a new, environmentally friendly, ergonomic and efficient plant in 2010. *See Section 4.5 – Infrastructure on page 51 and Section 6.5 – Liquidity and capital resources on page 60.*

2007 objectives and achievements

In 2007, the Parcels line of business maintained its drive to increase profitable revenue and improve service performance, thus increasing financial contribution.

Improve our tracing capability

To ensure that our customers are able to trace their parcels throughout our delivery process, we undertook several activities to enhance our parcel tracking capability.

- Every core Parcels product now has a bar code, making scanning and item visibility more consistent.
- Visibility of international items has been enhanced with an overlabelling process, which allows our employees to easily scan the appropriate bar code label quickly and accurately.
- We expanded our program to improve in-process scanning by installing sophisticated equipment in Montréal, St. John's and Regina.
- Customers can get automatic updates on their shipped items when they use our new free service, "Delivery updates by email."
- We equipped our drivers with 7,000 new hand-held scanners to capture parcel items as soon as they are picked up. This improves the visibility of shipments and our billing accuracy by matching the parcel to the submitted manifest.

Improve service quality and create a responsive customer-centred service culture

The results of our customer-focused actions have been positively received by our customers as measured by the Customer Value Index, an independent measure of loyalty. We achieved our target of 26 in terms of customer loyalty. Many enhancements and improvements influenced our customers in their evaluation.

- We redesigned our delivery claims process to provide a quick and easy experience for the customer. Our claims agents are now able to provide immediate refunds for valid claims.
- We introduced a program to automatically adjust billings for commercial customers where the customer-declared parcel weight exceeds the actual weight. These adjustments reduced customer billing by approximately $1.4 million in 2007.
- Our Commercial Expedited Parcel-USA service was improved to include more features and faster delivery. Delivery time has been reduced by two business days to major urban centres in the U.S. Electronic commercial customs clearance and prepaid duty and taxes make shipping more convenient, while enhanced tracking provides more timely updates throughout the delivery process.
- We strengthened our leadership in the consumer and small business segments by completing an agreement with PostNet, a full-service business centre franchise operation that complements our vast retail network, as well as through Purolator stores, and our Staples™ partnership.

Implement focused programs to effectively target and communicate to growth segments

We introduced new and enhanced services to adapt to the changing shopping and shipping needs of consumers.

- The Xpresspost Gift Card Envelope, a small, customized prepaid Xpresspost envelope with a pocket for a gift card and space for a written message, was created for the holiday season.
- We have maintained our strong partnership with eBay. With the addition of a French version of PayPal™ and a shipping calculator on the eBay website, the eBay online shopping and shipping experience was further improved. We also enhanced the eBay shipper's options by introducing a new product called Light Packet™, which bridges the price gap between Lettermail and USA and International Small Packet™.
- Our marketing efforts were highlighted with the high-profile *Harry Potter and the Deathly Hallows* release, which saw customized delivery service for key customers.

Increase operational efficiency

- We redesigned business processes in our key Toronto and Montréal facilities, improving our delivery capability and operational efficiency. As a result, costs were reduced while maintaining delivery commitments.
- Our service performance is now measured across all product lines, using a new combined target of on-time and scanned delivery. Although we did not meet our expectations in the early part of 2007, we did improve throughout the three remaining quarters of the year.

Improve Parcels margins

- As a result of the actions listed above, and many other smaller initiatives, the Parcels line of business margins improved by 1% during the year.

Financial highlights

Parcels revenue was $1,226 million in 2007, an increase of $39 million, or 2.9%, when compared with 2006. The revenue growth resulted from an increase of 3.8% in the average revenue per piece, which was partially offset by a volume decrease of 0.7%. *For further discussion of year over year results, see Section 8.4 – Results from Operations – Canada Post segment on page 66.*

2.6 Canada Post – Direct Marketing, Advertising and Publishing

Our business

Addressed Admail™ and Unaddressed Admail™ (collectively "Admail" or "Admail products") are the primary products of the Direct Marketing, Advertising and Publishing (Direct Marketing) line of business. The Addressed Admail product targets promotional messages to specific individuals or businesses, and the Unaddressed Admail product enables our customers to reach specific neighbourhoods or regions across Canada.

We also distribute periodicals, including newspapers, magazines and newsletters, putting more single copies into the hands of readers than newsstands or other distributors in Canada. As discussed in *note 20 to the consolidated financial statements on page 118*, Canada Post has been supporting Canadian Heritage's Publications Assistance Program and will continue to do so, as directed by the Government of Canada, until March 2009.

Business environment

Our direct-mail products compete in the annual $17 billion Canadian advertising industry[4] with other advertising media that range from traditional television and newspaper channels to email and text messaging. Technology has had a major impact on the advertising world, providing marketers with numerous new media options and the potential to effectively target and personalize their messages. The Internet is the fastest-growing marketing channel, and while it still represents a small percentage of overall marketing spending, its continued growth creates a challenge requiring monitoring of the evolution and development of appropriate commercial responses and countermeasures.

Overall, the advertising industry in Canada is growing and current forecasts are for continued growth. The specific niche of direct marketing is predicted to outpace overall industry growth. With annual revenue of $1.4 billion in 2007, Canada Post is one of the largest players in the Canadian direct-marketing business.

Direct mail permits our customers to deliver targeted messages and offerings to highly defined target groups. Direct mail provides an attractive alternative to mass media because it allows marketers to measure response rates. Marketers can justify direct-mail investments and overcome the challenges that audience fragmentation poses for mass-media advertising. Direct mail has high consumer acceptance and earns a strong return on investment (ROI) for customers compared to other media.

We anticipate marketers to pursue a multi-channel approach, combining direct marketing with other marketing communications techniques in step with the advance of new media. This trend is expected to demand a greater analytical capability and enable more personalization, attention to consumer preferences and sophisticated assessments of direct marketing's contribution to customers' profits.

Vision

Our vision is to *be recognized as a foremost driver of effective, results-proven direct marketing in Canada, helping companies grow their business while serving as an industry leader in consumer knowledge, consumer protection and privacy, and multi-channel direct marketing delivery.*

[4] Canadian Marketing Association, Marketing's Contribution to the Canadian Economy, 2007

Strategy

Our strategy continues to focus on the development of our products and services, knowledge, and capabilities, so we can help marketers meet their challenges. We intend to fuel growth by concentrating on four key strategic goals:

- customer-driven growth;
- product-driven growth;
- improving the customer experience; and
- building for our future.

We aim to capture a greater share of the rising direct-marketing expenditure. We will continue to demonstrate the impact and effectiveness of direct mail, through trial programs of existing products to our large enterprise and retail customers. We will also continue making direct marketing more accessible to small and medium-sized businesses to drive growth in this segment.

We intend to offer new products and services with more options that improve the effectiveness and ROI of direct-mail campaigns. We are proposing a number of initiatives to improve response rates, cost-effectiveness and measurability of results of our core products and services. We also intend to continue to work with our operations to improve delivery performance of our Addressed Admail and Unaddressed Admail products. To ensure the growth, sustainability and viability of the publication mail business, we plan to examine areas where costs can be reduced.

Improving customers' perceptions of Canada Post is an important component of our growth strategy. We will continue to review trends and talk with consumers to develop a better understanding of the future and needs. We will apply these insights to develop products and services that will serve our customers and, in turn, their customers.

2007 objectives and achievements

Educate customers to demonstrate that our products meet their needs

- To serve larger enterprises, our team of direct-marketing advisors continued to build relationships with sophisticated direct marketers in Canada and delivered insights to help them achieve their marketing objectives. We conducted a series of pilot projects demonstrating that targeted data and direct mail, combined with other media, can accelerate sales above traditional growth rates.
- We created a series of case studies and testimonials by industry segment to further demonstrate and promote the value of the direct-mail media. Our approach built a new level of trust with many businesses, demonstrating we can support them in developing and implementing marketing strategy.
- We produced a spring and fall version of the lookbook™ catalogue to help traditional retailers test the interest of consumers in cataloguing. This cost-effective approach is proving to be successful, confirming that opportunities exist for catalogue retailing in Canada, a market that is very underdeveloped compared to the U.S.
- We delivered training seminars to inform small and medium-sized businesses about direct marketing.

Introduce new direct marketing and advertising solutions

- We worked with small and medium-sized businesses to simplify the direct marketing experience through turnkey products and enhancements to our web channel.
- We improved the Canada Post website to simplify access to our Unaddressed Admail products.
- Our Direct Marketing Online™ web-based tool was launched to help small businesses plan, create and distribute direct mail from their computer desktop.
- We increased the size flexibility allowable for Unaddressed Admail items to support customer needs.
- We authorized mailers to place repositionable notes on products to highlight specific messages and improve direct-mail response rates.

Enhance business processes to improve delivery performance

- In 2006, we introduced measures to improve the performance of our Admail products. Specific plans were developed and implemented over the past two years, which continue to improve the predictability of delivery.
- We have defined measures to relieve operational challenges in some key areas across the country with high volumes. This has resulted in improved delivery predictability for our customers.

Financial highlights

In 2007, Direct Marketing revenue was $1,404 million, an increase of $97 million, or 7.0%, when compared with 2006. The revenue growth was primarily attributable to an overall volume increase of 4.4%, an increase of 1.7% in the average revenue per piece, and non volume-related product growth. *For further discussion of year over year results, see Section 8.4 – Results from Operations – Canada Post segment on page 66.*

2.7 Purolator segment

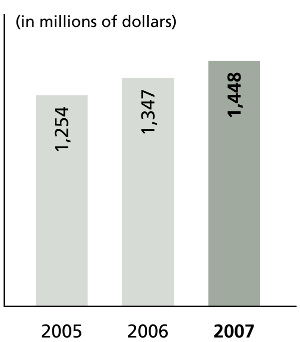
The business

Canada Post owns 90.99% of the common shares of Purolator.

As Canada’s leading overnight courier company, Purolator delivers innovative products and dependable service. Purolator has approximately 11,000 employees, a fleet of more than 3,000 vehicles, and makes 275 million deliveries and pickups annually.

Purolator is very proud to be named one of Canada’s 10 Most Admired Corporate Cultures in the 2007 Corporate Culture Study conducted by Waterstone Human Capital.

Revenue



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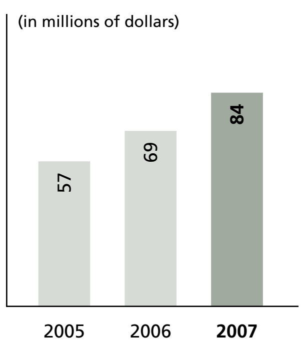
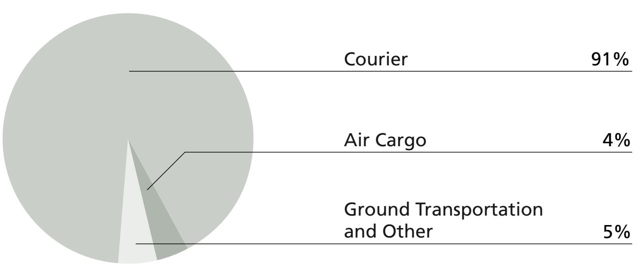


Operating revenues by market – 2007



Operating revenues by market	2007	2006	2005
Courier	91%	93%	95%
Air Cargo	4%	3%	2%
Ground Transportation and Other	5%	4%	3%

Business environment

Purolator is a leading provider of courier services in Canada, with the largest market share (by revenue). Leveraging this strong domestic position, Purolator continues to put a focus on growing its northbound/southbound market share.

The courier and transportation market continues to change rapidly. Industry consolidations and horizontal integrations are prevalent, with competitors becoming larger and stronger. In addition, a number of freight companies are seeing courier products as an attractive market to enter. Overall, the distinction between the various sectors of the industry has lessened.

Customer needs are evolving, partly driven by globalization and industry consolidation. Customers are looking to outsource more of their supply chain and transportation needs to reduce costs and focus on their core business. The ability of the provider to bring creative solutions and a wider array of services has become an important criterion in supplier selection. Customers also require shipment visibility from start to finish and stronger integration of shipping systems with their information systems.

Innovation in information technology has dramatically changed how business is being conducted and how transportation and distribution processes are being managed. Information technology has shifted the balance of power from the traditional transportation providers to customers and created a new class of competitors – logistics service providers. The technology bar is continually being raised and is forever changing customers’ expectations.

Vision

Purolator Courier aims to *be the leading provider of integrated distribution solutions to, from and within Canada.*

Strategy

Through its core strategy and the “Purolator 2010” initiative, Purolator intends to transform the company and enable its employees to deliver improved service and enhance the customer experience.

The four elements of Purolator’s long-standing strategy are to create:

- competitive advantage through investment in employees;
- sustainable market advantage through superior service and brand leadership;
- profitable growth through innovation in products and services; and
- continuous unit cost improvement through process innovation and technology.

Last year, Purolator embarked on a five-year business transformation initiative, “Purolator 2010.” This initiative involves the replacement of technology with new systems intended to make Purolator more customer-responsive and efficient. It also includes designs for new terminals to improve package sorting and delivery, and an accelerated pace to process improvements to better Purolator’s capability and effectiveness.

This transformation requires significant investment in technology, infrastructure and internal coordination. Over the next three years, Purolator intends to invest in its sorting plants and equipment, make significant investment in its new freight business, and further improve its cross-border capabilities to reduce operational costs and improve service. It also intends to invest significantly in its employees, ensuring they have the knowledge, skills and abilities to maintain Purolator’s leading market share.

The next few years will see significant change in the way Purolator runs its business. It plans to introduce and migrate to new customer-facing systems, introduce new products and services, expand coverage of premium products, implement a new pricing structure and service directory, automate facilities, and invest in automated reweigh and cube equipment.

2007 objectives and achievements

Purolator achieved some key milestones in 2007 against its core strategy and the “Purolator 2010” initiative.

- Purolator’s first automated hub opened in Montréal as planned in the summer of 2007. Equipped with the latest package sorting capabilities and scanning technologies to serve the Quebec market, the 160,000-square-foot facility is Purolator’s most efficient and technologically advanced hub. The hub is designed to accommodate growth for the next several years.
- September saw the launch of the new Purolator E-Ship Online (ESO) solution, replacing Online Shipping (OLS). All customers shipping at www.purolator.com now see the new look and feel of ESO. Online customers, including consumers and small to medium-sized firms, are now experiencing Purolator’s new and improved products, services and pricing in our new service directory. ESO was the culmination of a huge undertaking that involved converting all customer records to a new SAP system platform, resulting in more timely and accurate customer information. This initiative will continue in 2008 with the migration of information for Purolator’s larger regional and national customers to the new environment in a controlled, phased-in approach.
- Purolator continued its strategy to increase profits through new products and services. Purolator Freight™ , its premium less-than-truckload (LTL) service, continued to expand capability and tripled its revenues.
- Purolator strengthened its relationship with its international service provider to improve its U.S. and international service for Canadian clients. In the fourth quarter of 2007, Purolator began offering enhanced tracking capabilities for shipments destined for the U.S. – increasing the number of scans from five to twelve. In addition to the enhanced-visibility scans, customers can view electronic delivery signatures as part of the shipment tracking details.
- Awareness of Purolator’s premium service and brand leadership continues through its national advertising campaign. Demonstrating Purolator’s unique ability to provide solutions to out of the ordinary shipping challenges, the 2007 campaign emphasizes Purolator’s reliability, flexibility and ability to provide solutions.

Financial highlights

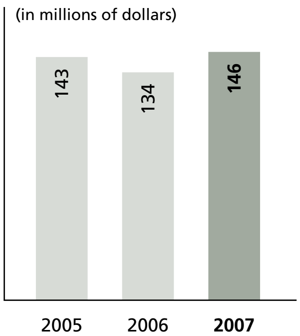
Purolator contributed $84 million to Canada Post consolidated income before income taxes. Revenue totalled $1,448 million, an increase of 7.1% over the previous year. *For further details, see Section 8.5 – Results from Operations – Purolator segment on page 69.*

2.8 Logistics segment

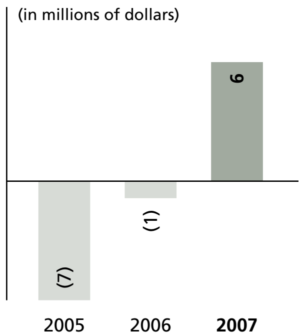
The business

The Logistics segment consists of SCI Logistics, a subsidiary of Canada Post (98.74%). SCI Logistics expanded in March 2007 when it acquired The AMG Group. Canada Post's previous investment in Intelcom was sold in January 2007.

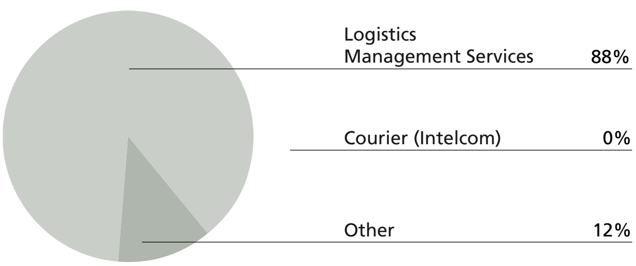
Revenue



EBT



Operating revenues by market – 2007



Operating revenues by market	2007	2006	2005
Logistics Management Services	88%	85%	88%
Courier (Intelcom)	0%	8%	7%
Other	12%	7%	5%

SCI Logistics

Through its subsidiaries, SCI Logistics offers order-management and inventory-management services, including order processing, inventory control, order fulfillment, reverse logistics, delivery and transportation. Each subsidiary has a specific market focus, allowing entrenchment of its logistics outsourcing services within its clients' organizations, enabling Canada Post to offer Canadian businesses more comprehensive and end-to-end supply chain services.

Business environment

SCI Logistics has gained recognition across North America as a well-run logistics provider. It is the largest Canadian-owned logistics company, although small when compared to global competitors such as UPS and DHL. While positioned in a strong and growing logistics outsourcing market, SCI Logistics must grow faster to keep up with the high growth rates achieved by its major competitors, who are consolidating globally to gain market share and scale in technology, back office and transport buying power. SCI Logistics' singular focus on the Canadian market makes it difficult to attract new large, global clients in its market space.

SCI Logistics' long-term growth and sustainability depends on its ability to provide services in markets outside Canada. Consequently, it is planning to access the U.S. market to attract and enhance its client base.

Vision

SCI Logistics aims to *be a leading source for global, worry-free supply chain services with local solutions, and to be differentiated by world-class solutions that make clients' complex problems simply disappear.*

Strategies

The strategic direction for 2008 and beyond is to continue to expand SCI Logistics' presence in the Canadian market and build a presence in the U.S. In order to deliver its commitments, profitability and value to all stakeholders, SCI Logistics plans to focus on the following specific strategic goals:

- grow by securing new clients and new markets;
- promote the growth and development of team members;
- strengthen relationships with clients and business partners;
- continue to build a culture of quality and innovation that responds to changing market needs; and
- leverage the capabilities of its operating companies.

2007 objectives and achievements

In 2007, in support of its strategic goals, SCI Logistics expanded and strengthened its presence in the Canadian market. SCI Logistics acquired AMG Logistics Inc. and First Team Transport Inc., with the intent of diversifying its logistics services and competencies.

Through its subsidiaries, SCI Logistics opened four new facilities and significantly expanded a fifth facility in Canada to serve its clients. It is expected that these new facilities will significantly improve the performance of SCI Logistics and provide greater capability for business growth.

Financial highlights

The Logistics segment recorded income before taxes of $6 million, an increase of $7 million over the prior year.

SCI Logistics contributed $8 million to this result, an improvement of $9 million, when compared with 2006. The Board of Directors of SCI Logistics declared a dividend of $5 million for 2007 that was paid in January 2008. In 2006, SCI Logistics paid a dividend of $8 million.

For further details, see Section 8.6 – Results from Operations – Logistics segment on page 70.

2.9 All Other segment

The All Other segment includes Innovapost (a joint venture between Canada Post [51%] and CGI Information Systems and Management Consultants Inc. [CGI] [49%]) and CPIL, a wholly-owned subsidiary of Canada Post.

Innovapost

Innovapost is the information technology service provider to The Canada Post Group. Within its operations, infrastructure services are subcontracted to CGI, and Innovapost provides application-development and maintenance services. Innovapost brings value to the Group by reducing costs, improving service levels, and providing technology consulting services.

Innovapost uses its relationship with strategic partners, such as CGI, to add value to its customer solutions. The key agreements with The Canada Post Group provide for an option to renew.

The Innovapost strategy involves improving its internal systems, processes and capabilities and transforming its application-management and development services to world-class levels through industry standard tools, processes and methodologies.

In 2007, Innovapost continued to reduce base operating costs for its clients, passing on price efficiencies gained in application-management and architecture services, and keeping its prices for Canada Post application-development services at 2006 levels. Innovapost achieved all of its expected service levels and key corporate metrics, such as customer satisfaction, employee satisfaction and service quality, with the exception of one major project that affected service quality and financial performance in the fourth quarter.

Revenues are dependent upon the level of information technology activity at Canada Post and Purolator. In 2008, revenue is expected to increase, as Canada Post continues to invest aggressively. It is also expected that Innovapost will continue to play a key role in assisting with the "Purolator 2010" technology modernization program.

Canada Post International Limited

CPIL, originally set up in 1990 to market Canada Post's technology and management expertise primarily to other postal administrations, has withdrawn from seeking new opportunities. The company has focused on managing existing contracts, the most significant of which is a postal concession in the Netherlands Antilles.

CPIL owns 100% of Nieuwe Post Nederlandse Antillen N.V. (NPNA), the entity that operates the postal concession in the Netherlands Antilles. Compliance with certain terms of the agreement for the concession has been in dispute, with each party alleging defaults by the other. A number of meetings were held in 2007 with the Government of the Netherlands Antilles with the objective of reaching an amicable settlement. In December 2007, the parties signed a Memorandum of Understanding, the terms of which provide, among other things, for a transfer of all the shares of NPNA to the Government of the Netherlands Antilles. The transfer of all the shares of NPNA was authorized by the Governor in Council under the *Financial Administration Act* on February 28, 2008.

The shares in NPNA are substantially all the assets of CPIL. Following the transfer of NPNA's shares to the Government of the Netherlands Antilles, Canada Post expects to dissolve CPIL in 2008. Procuring the dissolution of CPIL was also authorized by the Governor in Council under the *Financial Administration Act* on February 28, 2008.

CPIL has recorded a provision of $7.4 million in 2007 to reflect the settlement with the Government of the Netherlands Antilles for terminating the concession 15 years early.

3 Key Performance Drivers

A discussion of the key drivers of our performance, our progress against 2007 objectives and 2008 priorities

3.1 Key performance drivers

Canada Post uses a balanced scorecard management system to measure the company's progress relative to its vision and strategies, and to provide management with a comprehensive view of the performance of the business. By applying this approach, Canada Post ensures that there is a balance between financial results, customer value, delivery performance and employee engagement when establishing its key performance drivers and corporate priorities each year.

Customer value

Canada Post employs a customer value management process that uses relationship surveys and transactional questionnaires to identify the drivers of customer value and loyalty. These techniques provide insight about our quality of service, competitive advantage and areas requiring improvement.

The 2007 customer value target for the Parcels line of business was reached. Although Transaction Mail did not meet its full target, it did reach the interim threshold. Despite efforts to simplify Admail specifications and the launch of new value-added services, the Direct Marketing target was not attained.

Employee engagement

The Corporation measures employee engagement through our employees' perception of Canada Post and their working environment via periodic formal employee surveys managed by an independent professional services firm. *See Section 4.2 – Capability to Deliver Results – Employee engagement on page 49.*

In 2007, employee engagement increased by 5 percentage points over the prior year's index. This significant improvement reflects the company-wide focus on ensuring that our employees are committed to Canada Post's continued success.

The Corporation also focuses on the health and safety of employees, and measures the severity and frequency of accidents. In 2007, this target was not met.

Delivery performance

Our delivery standards require us to deliver Lettermail consistently within two business days within the same metropolitan area or community; within three business days within the same province; and within four business days between provinces.

An independent professional services firm tests our Lettermail service by depositing mail through mailboxes and post offices, and tracking it to delivery points across the country. Our 2007 on-time service performance score of 96.1% once again exceeded our corporate target of 96%.

Financial performance

Financial performance is monitored through the line of business revenues, corporate earnings and financial ratios. *For further information, see Section 1 – Introduction and Financial Highlights on page 31 and Section 8 – Results from Operations on page 65.*

3.2 Progress against 2007 objectives and 2008 priorities

In 2007, a corporate performance dashboard was implemented to track and manage progress against our corporate priorities. Results are reported on a monthly basis to senior management. Here, we summarize our progress toward meeting our 2007 objectives and provide an overview of our priorities for 2008.

Progress against 2007 objectives and 2008 priorities

Legend

- ●●● Achieved
- ●● Partially achieved
- ● Not achieved

Customer Value			
2007 Objectives		**2007 Results**	**2008 Priorities**
Establish long-term corporate vision and strategy to support Canada Post's transformation to the Modern Post	●●●	Canada Post's network-modernization plan was completed and externally validated	Commence implementation of Canada Post's physical delivery network modernization plans, one example being the new mail processing plant in Winnipeg
Launch Direct Marketing Online to make direct marketing easier for customers	●●	Direct Marketing Online was successfully launched, however customer acquisition lagged expectations for the year	Improve visibility of parcel tracking throughout the delivery network to increase the Parcels product value proposition and enhance customer satisfaction
Building on momentum from 2006, grow Returns/Response Mail and Multi-Channel Mail Presentment Solutions service	●●	Customer acquisition levels for Returns/Response Mail and Multi-Channel Mail Presentment Solutions was in line with expectations for the year, however revenues fell short of plan	Launch next generation Parcels delivery confirmation solution to enhance delivery notification for our customers
Upgrade parcel process quality to competitive levels to further enhance customer service levels	●●●	Process quality enhancements were implemented in 2007 with planned efficiencies realized. Process quality enhancements will continue in 2008	Implement Canada Post's online strategy to enhance the customer interface experience and support the growth of the online business channel
Complete digital meter conversion to provide visibility on the products used by meter customers and enhance revenue verification	●●●	Digital meter conversion completed on schedule, increasing customer convenience, and providing enhanced revenue verification and customer usage insight for Canada Post	

Progress against 2007 objectives and 2008 priorities (continued)

Employee Engagement

2007 Objectives		2007 Results	2008 Priorities
Create a healthy and safe workplace by delivering programs to increase employee safety and reduce accident frequency	●	Canada Post continued to raise safety awareness and provide safety training programs. While some progress was made in certain areas, the number of accidents remains at an unacceptably high level	Reduce accident frequency, and create a healthy and safe workplace by delivering programs focused on raising safety awareness, accident prevention and adherence to safe operating practices
Continue to improve work environment through investments in plants and depots	●●●	Invested $17 million in visible improvements to enhance the workplace environment and increase employee satisfaction	Implement a new system to manage and report on accidents
Introduce "best-in-class" recognition programs	●●●	Recognition program developed for launch in 2008 to recognize operational performance excellence	Deliver technical and leadership development programs to increase productivity and enhance employee engagement
Improve productivity through technical training	●●●	Technical training requirements prioritized. Programs to address highest priority issues developed and deployed	Provide more targeted and timely employee communications to ensure goal congruence across all employees
Implement face-to-face communication plans to improve internal communication	●●●	Executive presentations conducted across Canada, in conjunction with regional and management forums, to improve internal communication	Develop an approach for corporate social responsibility and begin to integrate environmental sustainability actions into Canada Post operations
Reach collective agreement with the Canadian Union of Postal Workers (CUPW)	●●●	Four-year collective agreement reached with the CUPW on schedule. This new collective agreement will remain in effect until January 31, 2011	
Achieve Employee Engagement Index	●●	The Employee Engagement Index fell short of target, however it increased by 5 percentage points over the prior year's index	
Reduce pay defects by 50%	●●●	The number of pay defects was reduced by more than 50%	

Delivery Performance

2007 Objectives		2007 Results	2008 Priorities
Achieve delivery service targets	●●	Lettermail delivery service target achieved	Achieve delivery services targets
		Direct Marketing service was significantly improved for Unaddressed Admail product, however Addressed Admail product did not meet established objectives	Improve Admail delivery process to further enhance on-time delivery performance and reduce cost of delivery
		Parcels service fell short of expected improvement targets	Implement strategy to increase Admail capacity to support this growing business
Complete bar-coding of core parcel products to enhance tracking performance and visibility for our customers	●●●	Bar-coding of core Parcels products completed on schedule allowing improved product tracking and operational efficiencies	Ensure compliance with International "Pay for Performance" delivery requirements
Enhance customer service experience – improve problem-resolution response rates	●●	Problem-resolution objectives for Lettermail and Admail products achieved, however Parcels products fell short of planned improvement target	
Consult communities, ensuring widespread knowledge and understanding of The Canada Post Group's existing and emerging issues	●●●	Through Canada Post's community outreach program, communities, as well as local MPs and the Minister's office, were kept apprised of the status of key issues on a timely basis	

Progress against 2007 objectives and 2008 priorities (continued)

Financial Performance			
2007 Objectives		**2007 Results**	**2008 Priorities**
Deliver The Canada Post Group earnings commitment of consolidated income before income taxes of $126 million	●●●	Consolidated income before income taxes of $160 million exceeded plan by $34 million	Deliver The Canada Post Group earnings commitment of $127 million
Deliver Canada Post earnings commitment of income before income taxes of $56 million	●●●	Canada Post income before income taxes of $78 million exceeded plan by $22 million	Deliver Canada Post earnings commitment of $25 million
Leverage new product and service offerings to drive profitable revenue growth across all lines of business	●●	New product and service revenues fell short of plan for the year, however customer acquisition levels were in line with expectations	Develop options for long-term strategic revenue growth
Deliver Lettermail and parcel process enhancements and information technology efficiencies to achieve cost of operations objectives	●●	While significant operational efficiencies were realized during the year, actual savings fell short of expected levels	Deliver operational efficiencies without affecting the creation of customer value and service quality

4 Capability to Deliver Results

A discussion of the issues that affect our ability to execute strategies, manage key performance drivers and deliver results

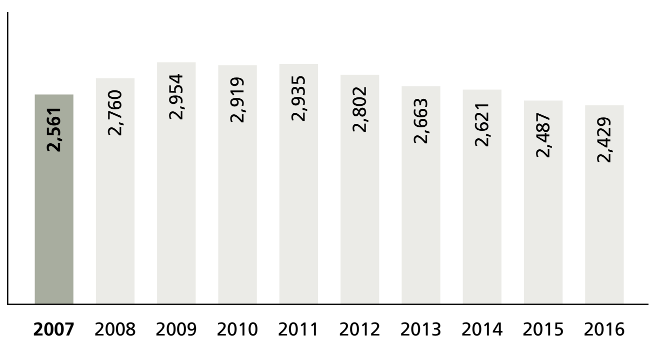
4.1 Employees

The Canada Post Group is one of the largest employers among businesses in Canada, with 72,500[5] employees. Canada Post employs approximately 60,600 people, and our subsidiaries employ an additional 11,900.

The labour-intensive nature of our business means our customer value derives directly from the performance of our employees. Both Canada Post and Purolator have undertaken ambitious reinvestment plans to modernize their operations. The transformation to the Modern Post and the "Purolator 2010" initiative require open dialogue with bargaining groups as well as continued engagement with employees.

Over the 10-year period from 2007 to 2016, we expect that 27,000 full-time employees will leave Canada Post, mostly due to retirement, but also through normal, voluntary turnover. Attrition provides an opportunity to improve processes, but poses a risk with respect to competing for skilled resources. *See Section 5.5 – Risk Management – Human resources on page 56.*

Full-time attrition retirements and other departures



Note: 27,131 departures are expected by 2016 (including 22,541 retirements and 4,590 other departures). Forecast is based on retirement rates covering the five-year period 1996-2000 and the five-year period 2002-2006, and an average number of other departures from 2003 to 2006.

[5] Employment figures include full-time and part-time paid employees; excludes temporary, casual and term employees

4.2 Employee engagement

Canada Post

We are very proud that, for the second year in a row, Canada Post has been named one of the Top 100 Employers in Canada in Maclean's magazine.

Employee engagement remains a top priority for Canada Post. It is our goal to become the best place to work in Canada, with every employee contributing to and sharing in our success. For the Corporation to continue its evolution to the Modern Post, it is critical to focus on building a modern workplace characterized by high employee engagement.

In 2007, Canada Post's strategic framework for achieving higher levels of employee engagement focused on respect and fairness in the workplace, dedication to employee health and safety, and commitment to create a dialogue with our employees.

In pursuing this strategy, we continued to place an emphasis on face-to-face communications with front-line employees and their team leaders. For the second year, the president and several senior executives held Regional Forums with team leaders across the country. In an effort to reach a broader audience, the number of Forums was increased from 16 in 2006 to 22 in 2007, with participation increasing from approximately 2,500 to 6,500 team leaders. Vice-presidents and general managers led more than 450 employee discussion groups with approximately 4,000 front-line employees. The Forums and discussion groups were held to connect our employees to the Corporation by sharing the "big picture." More importantly, they are intended to create dialogue with employees, where members of the senior team can listen and respond to what employees have to say about the Corporation, its future, its products and services, and its processes.

Another critical component of the employee engagement strategy in 2007 was the successful negotiation of the CUPW Collective Agreement. Under the new agreement, employees represented by the CUPW became eligible for the first time for a Corporate Team Incentive, which is based directly on company performance against predetermined business targets. Through this historic achievement, Canada Post has been able to create an environment where the vast majority of our employees have a financial incentive to help improve performance. We believe that giving employees such an incentive is one of the most effective tools available to change our relationship with them. It provides a tangible means of demonstrating to employees that their efforts affect the results of the Corporation and that we value their contribution.

Our employee engagement efforts in 2007 included a high degree of focus on the health and safety of our employees. We have strengthened our Health and Safety Management System, and have rolled out an extensive safety training program. A comprehensive communication strategy has been developed to bring health and safety to the forefront. Canada Post is firmly committed to protecting its employees from hazardous situations.

Leadership excellence is a critical dimension of any engagement strategy. We continued our endeavour to develop our front-line team leaders by providing supervisory training. A training program for middle management was also developed and initiated in 2007.

Our efforts to increase employee engagement have had a positive effect and suggest that we are on the right track, as the results of the 2007 employee survey show improvement across all categories. While the results are very encouraging, much work remains to be done to achieve higher levels of engagement.

In terms of our employee engagement strategy for 2008, Canada Post intends to stay the course. Our plan is to remain focused on building a workplace characterized by fairness and respect, an overarching concern for the health and safety of all employees, and leadership that encourages dialogue with employees.

Our goal is to continue to reach out to our employees and team leaders through a broad face-to-face communication effort. It is intended that Regional Forums for our front-line team leaders will continue in 2008 and that the audience at each session will extend to include some employees represented by the CUPW. Members of the senior executive will continue to conduct front-line employee discussion groups to encourage dialogue and to ensure that our employees understand and are aligned with the Corporation's strategic goals.

Our goal is to expand our efforts to build a culture of health and safety through employee safety training and a leadership focus on safety management. The objective is to have team leaders put greater emphasis on involving employees in decisions that affect their work and their workplace. As well, our goal is to continue to develop employee recognition and actively acknowledge the contributions that employees make in serving our customers and improving our business operations. We also intend to move forward with improvements to the physical work environment by upgrading facilities and equipment.

Purolator

Purolator continued to invest in its employees by ensuring that they have a safe place to work with the proper tools to do their job well. The results of an anonymous internal effectiveness survey indicated a high level of employee engagement and commitment to Purolator.

Sustained investment in employee training continues to be a foundation of Purolator's success. The second cohort graduated from the "Leader's Edge" initiative, a program that aims to retain and develop key talent, grow leadership skills, and improve business skills. The second phase of the Internal Capability initiative, aimed at accelerating process improvements within front-line operations, was rolled out to Western Canada. Key to the success of this initiative is an investment in employees, involving a new comprehensive front-line supervisory training initiative.

4.3 Collective bargaining

Workplace stability is essential in being able to continuously improve the value provided to our customers. The Canada Post Group must be able to provide uninterrupted service to customers and implement change on a timely basis to meet their needs.

Within each company of The Canada Post Group, a governance model is in place to ensure that the financial and operating impacts of any terms of settlement with a collective bargaining group are analyzed and determined to be aligned with the strategic direction of the company.

The following discussion summarizes our collective agreements and our progress toward achieving a stable workplace.

Canada Post

Bargaining Unit	# of Represented Employees*	Collective Agreement Expiry Date
CUPW (1)	42,090	January 31, 2011
CUPW-RSMC (2)	6,034	December 31, 2011
CPAA (3)	6,386	December 31, 2009
APOC (4)	3,859	March 31, 2009
PSAC/UPCE (5)	2,117	August 31, 2008
Total	60,486	

* Includes all full-time and part-time employees who are represented by a bargaining group as at December 31, 2007; excludes temporary, casual and term employees
(1) CUPW = Canadian Union of Postal Workers
(2) CUPW-RSMC = Canadian Union of Postal Workers – Rural and Suburban Mail Carriers
(3) CPAA = Canadian Postmasters and Assistants Association
(4) APOC = Association of Postal Officials of Canada
(5) PSAC/UPCE = Public Service Alliance of Canada / Union of Postal Communications Employees

Canadian Union of Postal Workers (CUPW) – Urban Postal Operations
We are proud that in the spring of 2007 we achieved a negotiated, four-year collective agreement with the Urban Postal Operations of the CUPW that will expire on January 31, 2011. In addition to a number of other changes, the Corporation was successful in introducing the Corporate Team Incentive to its largest group of employees and controlling its benefits costs in the new agreement.

Canadian Union of Postal Workers – Rural and Suburban Mail Carriers (CUPW-RSMC)
Canada Post and the CUPW-RSMC, currently in the fourth year of an eight-year collective agreement, were unable to reach agreement on a number of outstanding issues brought forward in the second of three contractual re-openers. The parties will refer these unresolved matters to an arbitrator for final resolution as per the provisions of the collective agreement. The results of the negotiation process and the time delay until the process concludes poses limited risk to Canada Post as these employees do not have the right to strike and monies allocated for this group of employees originate from a predetermined (and negotiated) financial cap.

The Association of Postal Officials of Canada (APOC)
The current collective agreement between Canada Post and APOC, which represents supervisory and sales employees, expires on March 31, 2009. Bargaining is expected to begin in December 2008.

Union of Postal Communications Employees (UPCE)
The current collective agreement between Canada Post and the UPCE expires on August 31, 2008. The UPCE represents employees who perform clerical and administrative work, including call centres, administration, finance and engineering. Canada Post plans to open negotiations in the spring of 2008.

Purolator

Bargaining Unit	# of Represented Employees*	Collective Agreement Expiry Date
Teamsters	8,917	December 31, 2007
Other (1)	1,075	December 31, 2008 December 31, 2009 February 1, 2010
Total	9,992	

* Includes all full-time and part-time employees who are represented by a bargaining group as at December 31, 2007; excludes temporary, casual and term employees
(1) Other = Clerical and administrative

Teamsters

In 2007, Purolator and the Teamsters union, which represents operations personnel, entered into negotiations to replace the collective agreement that expired on December 31, 2007. Negotiations continue to progress and a new collective bargaining agreement is expected to be finalized before the end of the second quarter in 2008. Purolator's strong partnership with its employees will help facilitate a mutually acceptable agreement.

SCI Logistics

Bargaining Unit	# of Represented Employees*	Collective Agreement Expiry Date
CEP (1)	399	December 31, 2009 December 31, 2010 December 31, 2011

* Includes all full-time and part-time employees who are represented by a bargaining group as at December 31, 2007; excludes temporary, casual and term employees
(1) CEP = Communications, Energy and Paperworkers Union of Canada

4.4 Workplace health and safety

Fostering a safe and healthy workplace where employees are treated with fairness and respect is a corporate priority. In the last year, we have strengthened our Health and Safety Management System and front-line safety leadership capabilities through a number of initiatives, training of our local joint management and union committees, comprehensive accident prevention plans, and regulatory compliance audits. We have added 40 professionals to our team to augment in-house expertise in health and safety, and have also brought in outside expertise for traffic and ergonomic safety.

Although we did not meet our target for reduction of accidents in the workplace, the 2007 employee survey results show a marked improvement in the area of health and safety over the 2006 survey.

In 2007, Canada Post increased its resources in the area of occupational health and safety. We are assessing our current health and safety program and organization, and developing a health and safety model for Canada Post that will be aligned with our business processes and all levels of the organization. To support this model, our plan is to continue to focus on our Health and Safety Management System in 2008, improving our Workers' Compensation Board claims management process.

We plan to implement an integrated and sustainable Health and Safety Management System. Our first focus will be on leadership, communication, and emergency preparedness and response to build a foundation and culture that supports a safe and healthy workplace. Other elements will follow once the foundation is solidly developed and implemented.

Ongoing health and safety initiatives, such as training for new and existing employees, front-line safety leadership training for supervisors, and comprehensive and focused accident prevention plans, are all activities that support our strategic objectives. In January 2008, we launched our front-line supervisory and management employees training program in general safety management.

Our local joint health and safety committees are being restructured under direction from Human Resources and Social Development Canada, which dissolved our existing umbrella committee structure. This restructuring is expected to create approximately 300 local joint health and safety committees and several hundred health and safety representatives. It is intended that these additional committees and representatives will support an active health and safety program on many fronts in our workplaces, especially hazard identification and workplace inspections.

With respect to compliance and due diligence, the Corporation plans to develop a comprehensive Occupational Health and Safety Audit program with help from external auditing expertise. We expect the 2008 program will build on our compliance audit activities, and ensure due diligence in health and safety.

4.5 Infrastructure

Up-to-date physical assets, including processing facilities and delivery and retail networks, are required to enable us to meet our service commitments and customer requirements. Investment in basic infrastructure has lagged and significant capital expenditures are required to rejuvenate the asset base, modernize it, and leverage new technologies.

This section should be read in conjunction with Section 6.3 – Investing activities on page 59 and Section 6.5 – Liquidity and capital resources on page 60.

Canada Post

In 2007, Canada Post invested $237 million in capital assets focused mainly on buildings, systems and equipment.

In 2008, we expect our capital investment to rise to $460 million in order to maintain and replenish equipment and facilities, support business growth in key areas, and maintain service delivery to rural mailboxes affected by traffic-safety risks.

Our postal transformation plan to renew our processing, delivery and technology infrastructure was approved by Canada Post's Board of Directors in October 2007.

Over the next five years, we could spend up to $1.9 billion to transform the Corporation into the Modern Post that will serve the needs of Canadians today and into the future. We will prioritize our spending on the areas of greatest need and invest only what we can afford. In the short term, we plan to replace aging equipment and essential items, standardize our operations, and implement a robust productivity-management system. This is intended to enable us to defend our core businesses by providing more value to customers and lay the foundation for future growth.

Work will begin in 2008 to build a new mail processing plant in Winnipeg that will be a model for future plants across the country. The new plant will reflect the Modern Post and be equipped with upgraded technology and ergonomically sound, new-generation equipment. It will also be more environmentally friendly, incorporating green technologies and conforming to recognized green building standards. This investment is expected to be in excess of $50 million.

Purolator

In 2007, Purolator continued the implementation of its business transformation strategy "Purolator 2010," which includes increased investment in technology, infrastructure, processes and employees. In 2007, Purolator invested $83 million in capital infrastructure to support key milestones in the transformation, including the roll-out of the automated Montréal hub facility, the launch of ESO and a new SAP automated time-capture system for its employees.

In 2008, Purolator expects to continue the expansion and automation of its Richmond, B.C., hub.

In coming years, the next phases of the "Purolator 2010" initiative are expected to bring new strengths, increased reach and scope of network, making it easier to find distribution solutions that fit customer requirements and ensure Purolator continues to provide the customer experience that has made it Canada's largest courier.

4.6 Delivery

Canada Post delivers to more than 14 million addresses every day, an expansive reach that sets us apart from any other delivery company in the country. At the same time, the actual number of pieces of mail delivered to each household has decreased. To meet the challenge of increasing costs, we are striving to become more productive by enhancing our delivery methods, practices and information tools in both urban and rural Canada.

In urban areas, we are increasing the efficiency of ongoing restructuring of letter carrier routes with the introduction of a Route Optimizer tool, which automates many of the tasks involved in designing routes. This tool maximizes delivery efficiency, while ensuring consistent standards to create fair and equitable delivery routes for our employees. We are also continuing the implementation of more efficient and ergonomically designed workstations for letter carriers to help improve sorting efficiency, while providing a safer and healthier work environment for employees.

We further improved delivery quality by increasing the address data in the address management system. This year, we decentralized the update and maintenance of the system to our delivery facilities to provide more timely and accurate address information and service. We also successfully completed the implementation of the Parcel Delivery Model, which creates dedicated, centralized parcel delivery hubs. Software designed specifically for optimizing parcel delivery route workloads has enabled an increased delivery window to serve our customers better. This improved parcel delivery capability is now installed in 17 cities across Canada. As described in *Section 2.5 – Our Business, Vision and Strategy – Canada Post – Parcels on page 38*, we also completed bar-coding of core parcel products to enhance tracking performance and visibility for our customers.

Moving towards the Modern Post in 2008, we intend to enhance the Route Optimizer to increase the benefits and speed at which we can modify the delivery structures and processes without affecting the job security of our current regular employees. We also plan to pursue the use of technology for delivery-route sequencing of mail and strategies to maximize real-estate use.

4.7 Rural mail delivery

Rural and suburban mail carrier health and safety

Approximately 6% of our 14 million residential and business addresses receive their mail through rural mailboxes (RMBs). Continued urbanization throughout Canada has changed the traffic flow and volumes on previously quiet rural roads, resulting in potential safety hazards to employees delivering the mail to these boxes. Rural and suburban addresses are served by Rural and Suburban Mail Carriers (RSMCs), who have expressed more than 1,400 workplace health and safety concerns since September 2005.

The two main areas of concern centre on traffic safety and ergonomics. These concerns have been reviewed by safety experts from Human Resources and Social Development Canada (HRSDC). As a result of rulings by HRSDC and in order to ensure the safety of our employees and compliance with the relevant laws, we moved approximately 10,000 customers whose RMBs did not meet safety criteria from RMB delivery to a centralized delivery alternative such as a community mailbox (CMB).

In December 2006, the Government of Canada directed Canada Post to develop and implement an operational plan to restore and maintain RMB delivery within 18 months, while respecting safety laws. We responded quickly with an accelerated plan to restore and maintain delivery to affected RMB customers. Within the first six months of 2007, we attempted to restore delivery to approximately 5,000 customers. In some instances, customers favoured the centralized mode of delivery and declined the reinstatement of an RMB. Only 1,500 customers chose to reinstate their RMB delivery.

We also have undertaken a comprehensive safety review of all rural delivery routes and RMBs. To date, we have assessed more than 69,000 RMBs, and intend to complete a review of all RMBs. Nationally, less than 30% have been deemed hazardous and required a change to the mode of delivery. To assess the safety risk of the RMBs, we use the Traffic Safety Assessment Tool (TSAT), designed by third-party experts in the field of traffic engineering. It is the first of its kind in North America and can be used to assess any RMB in any geographical setting. The TSAT considers various factors such as road conditions, visibility and traffic volume.

In order to avoid potential repetitive stress injuries, we have hired contractors to assist RSMC drivers with delivery to RMBs through the passenger-side window of their vehicles. Also, we are conducting a pilot project whereby RSMCs drive right-handed vehicles to deliver the mail. If successful, these vehicles may be one of the long-term solutions to address these ergonomic concerns.

The Rural Mail Safety Review follows an elaborate community outreach process along with the assessments. We inform Members of Parliament about assessments in their respective ridings and let them know the results and final solution. We also keep municipal officials abreast of the information and consult them when choosing CMB sites. Finally, we engage our customers throughout the process. Customers' input and co-operation are vital to the success of this project.

Over the next five years, the costs for assessing and resolving health and safety risks for the RMBs are estimated to be $450 million in operating costs and $75 million in capital investment.

4.8 Retail

Canada Post's 6,600 post offices form the largest retail network in Canada. The urban and rural networks have different functions and dynamics.

The urban network mainly consists of private-sector dealers who are contracted to provide postal services. Operating inside a host business, such as a drug or grocery store, their primary purpose is to serve consumers and small businesses. Urban private-sector dealers are responsible for just over 50% of $1.3 billion of total retail sales and are the recipients of more than 20 million call-for items annually. Call-for items are deliveries requiring pickup by customers at the post office. We continue to work with our national dealers (Shoppers Drug Mart, Katz Group [Rexall], Sobeys, Jean Coutu and Uniprix) and to develop other national accounts. Corporately staffed post offices are also key in our urban network. Many are located with letter carrier depots and support commercial induction and mail pickup, either via a large postal box lobby or bag service.

The rural network's focus is to be the hub of mail delivery in a community. Any change in our rural Canada network is managed by our well-developed community outreach program. The cornerstone of this process is community involvement through local elected officials. This process has proven very successful in managing change in these communities.

In 2007, Canada Post continued to invest in the Retail Automation project, which is intended to deliver a more flexible and cost-effective point of service application, hardware platform and communications network. Through 2008 and 2009, we plan to automate the majority of post offices. Urban locations will also receive new hardware with high-speed network access, providing counter personnel with better tools to serve our customers.

4.9 Internal controls and procedures

In 2007, Canada Post continued with its commitment to enhance the accountability and transparency of financial reporting. Using the framework developed by the Committee of Sponsoring Organizations (COSO), we continued the assessment of the effectiveness of internal controls over financial reporting. Although this assessment revealed a generally good state of internal controls, we have identified some opportunities for improvement. Remediation plans have been prioritized and are being implemented.

5 Risk Management

A discussion of the key risks and uncertainties inherent in our business and our approach to managing these risks

There has been a shift in the corporate risk landscape in Canada over the last few years. The pace of globalization and technology has broadened the risks that companies need to consider. Companies are increasing their focus on risk management, and Canada Post is following suit. Our competition is more prevalent than ever, and our slim margins make it even more important to understand and mitigate risks to ensure that we maintain and grow our profitability, particularly in light of the major investment program we have initiated in 2007. As a result, we have begun to examine Enterprise Risk Management (ERM) best practices to enhance our ability to proactively identify and mitigate significant risks facing Canada Post.

Management at all levels of the organization already considers risks and opportunities in the course of its ongoing business decisions. However, a more systematic, cohesive and rigorous approach is required to manage business risks in the future. In 2007, we examined and enhanced our business practices with respect to risk management. Best practices suggest that risk assessment should be part of the strategic and business planning process. Consequently, we conducted risk-assessment workshops with senior executives in each of the Corporation's functional areas, to provide the Audit Committee of Canada Post's Board of Directors with an assessment of the areas of greatest risk and potential mitigation plans. These workshops were imbedded in the annual business planning process for the first time in 2007, and their outcome was a key input to the internal audit plan.

We will continue to further evolve and improve our ERM processes in 2008 to better align risk assessments with industry best practices.

5.1 Definition of risk

Canada Post defines risk as any event or condition that could impact the Corporation's ability to meet its key strategic, financial and organizational objectives.

The following is a summary of the principle sources of risk and uncertainty facing the Corporation and the associated risk mitigation activities.

5.2 Economic conditions

Canada Post will be undergoing its important transition to the Modern Post at a time when economic performance forecasts are increasingly pessimistic. All Canadian businesses, including Canada Post, its subsidiaries and customers, will be affected by shifting market expectations and conditions. In addition to their potential negative effect on revenue growth, financial markets also have an important impact on the valuation and expenses pertaining to the Canada Post Pension Plan. Of particular note are the risks associated with the fluctuation of interest rates affecting the value of both the Pension Plan's assets and the obligations thereby impacting the planned level of funding based on the expected continuation of the Pension Plan's surplus position. In addition, Canada Post is assessing its options relating to the Modern Post renewal. The total amount of incremental capital spending will be based on what we can afford.

Risk mitigation

Canada Post has developed stress-test scenarios for its business plans, including recovery options for the short term. We will continue to monitor the general economic environment, and escalate those recovery actions as appropriate. Longer-term adjustments will be evolved further and incorporated into upcoming business plans.

5.3 Competition

Competition

The Canada Post Group continues to face aggressive competition in its market segments. These trends and pressures will continue to put pressure on market shares, volumes and pricing.

Globalization has introduced our competitive products, especially parcels and express/courier, to intense and increasing competition from well-resourced multinational corporations. The rise of the Internet as a marketing channel has created a new competitive challenge to direct mail.

Risk mitigation

The Canada Post Group strives to improve its ability to compete in the marketplace through the implementation of segment strategies as described in *Section 2 – Our Business, Vision and Strategy on page 34*.

Lettermail volume erosion

Lettermail volumes are declining as consumers and businesses migrate to the electronic channel and corporations consolidate their mailings to reduce costs. In the international segment, the activities of re-mailers and the anticipated opening of this segment of the market are expected to further erode the international outbound mail volumes. The pressure on revenue from physical mail is further exacerbated by other factors. Price increases to the basic domestic letter rate are limited to less than the rate of inflation. The number of addresses in Canada increases each year, while mail volumes remain steady or decline, hence a decreasing number of pieces of mail per point of delivery.

Risk mitigation
In an effort to combat revenue loss, Canada Post plans to continue the expansion of its service offerings beyond the areas of vulnerability as well as aggressively providing multi-channel offerings that link the physical mail stream with the electronic channel.

Shifting market expectations

The speed of technological advances and the resulting customer demands pose an additional risk if we are not able to respond to market expectations in a timely manner.

Risk mitigation
As we begin our investment in our infrastructure, the need to be flexible in light of changing market conditions will be integral to successful implementation of our plan. Market research, including customer focus groups, will provide additional third-party validation to help in identifying and planning to mitigate this risk.

5.4 Regulatory

Public policy

As a Crown corporation, Canada Post's ability to plan and execute business strategy is influenced by public-policy considerations. Canada Post's legal framework requires the Corporation to provide a universal service, while operating on a self-sustaining financial basis. Often public-policy objectives are established to take priority over commercial considerations, one example being the moratorium on rural post office closures.

Under the *Canada Post Corporation Act* and the *Financial Administration Act*, the government may issue directives governing any aspect of the Corporation's operation. Depending on their nature and scope, directives can add significant financial exposure to the Corporation. In 2006, the Government of Canada issued two directives to Canada Post, one to maintain traditional rural mail delivery and the other to continue funding the Publications Assistance Program for $15 million per year for two years.

Under the *Canada Post Corporation Act* and the associated regulations, a share of our business is protected from direct competition by means of our statutory exclusive privilege in the collection, transportation and delivery of letters. The exclusive privilege exists as a matter of public policy. It is meant to allow us a reasonable means to fund universal services to all Canadians. However, within our exclusive privilege market, costs are rising, volumes are relatively flat, and price growth is constrained. Across our business, we face increased competitive pressure.

While until now Canada Post has retained an exclusive privilege on domestic and international Lettermail, Posts in the European Union and Asia are seeing their exclusive privilege being reduced or eliminated. In October 2007, Bill C-14 was introduced in Canada, which, if implemented, would amend the *Canada Post Corporation Act* by specifically excluding outbound international letters from Canada Post's exclusive privilege. Liberalizing the outbound international portion of our business would pose additional challenges for Canada Post in the form of increased competition, loss of revenue and pressure to reduce costs.

At the time of this report, Canada Post is not aware of any further intention to change its legal framework. Any changes in this domain could affect the nature of competition in markets where Canada Post operates, the cost of the provision of universal services, and the Corporation's ability to finance its operations.

Risk mitigation
As a result of these challenges, we continue to explore various alternatives to the means we have at our disposal to fund our increasing universal-service and public-policy obligations, with our Shareholder, the Government of Canada, in consideration of our statutory obligation to remain financially self-sufficient and provide continuing service to Canadians.

Privacy

Increasing privacy legislation will provide a continual risk to Canada Post. The national "Do Not Call" list being launched in Canada on September 30, 2008, could provide an opportunity to the Corporation, but could also pose a risk, as it will raise awareness on "Do Not Contact" issues across all channels.

Risk mitigation
Increasing our ability to target customers' preferences may allow us to combat the negative perception surrounding unsolicited advertising mail and thus mitigate this risk.

5.5 Human resources

Attrition

Most companies will be facing risks from attrition in the coming years. For The Canada Post Group, approximately one in every three employees will retire over the next 10 years. This provides an impetus to improve processes, coinciding with attrition rates. However, it also poses an additional risk around competing for skilled resources to meet the needs of the Modern Post.

A major challenge will be to attract, develop and retain new employees. We will need to recruit across a broad array of skills and experiences, and ensure critical knowledge is transferred from departing employees. We will need to train and develop those who remain for current and emerging roles. We recognize that we will be recruiting in a highly competitive labour market – a key reason we must maintain a strong focus on becoming an employer of choice.

Risk mitigation

Succession planning, as well as striving to become an employer of choice through improved working conditions, stronger internal communications and greater recognition of employees' efforts, are prime plans to mitigate this risk.

The Corporation is working on plans to address knowledge management, knowledge transfer and recruitment. In 2007, we invested in e-recruitment technology that we are currently testing, and we plan to roll out this solution nationally in 2008. In addition, we are assigning our resources and working with suppliers to help us meet the recruiting and training demands associated with such high levels of attrition. This will involve standardization, process improvement and alignment, and learning tools to maximize the training benefits.

We also view employee attrition as a significant opportunity to align the workforce with corporate objectives, as we seek to acquire the skills we will need to support our long-term business goals, especially as our company increasingly relies on technology and analytical capability for business success.

5.6 Health and safety

Safety and health concerns are a major risk for Canada Post. These concerns can be divided between accidents or injuries due to unsafe working conditions or human error and ergonomic issues. Reducing the level of accidents for all employees continues to be a main focus for Canada Post.

Risk mitigation

Extensive work continues on assessing rural routes and implementing safe alternatives for our employees and customers, as well as training to address awareness and prevention, the creation of a national safety business council, and stronger controls and accountability. *For further information, see Section 4.4 – Workplace health and safety on page 51.*

5.7 Process risk

Capacity

A continuing concern when implementing a new strategy is the ability to deliver on new projects, while maintaining the core business. Misalignment of resources and expectations could lead to unrealistic capacity requirements when objectives are set.

Risk mitigation

Senior management is assessing the ability to absorb change by employees and customers alike, and ensure plans are in place to deliver on both the strategic initiatives as well as our core business. Ongoing prioritization of initiatives enables continuous assessment of resource availability. Change management plans are an integral component of Canada Post's endeavours.

5.8 Environmental sustainability

An increased awareness of environmental concerns from government, customers and the population at large imposes changes to the way Canada Post does business.

Risk mitigation – Canada Post

As part of its overall corporate social responsibility strategy, Canada Post is responding to these ever-pressing issues by putting a series of concrete measures in place that will demonstrate its leadership role towards sustainable development. One of our key commitments is to reduce our overall direct greenhouse gas emissions by 14% by 2012, based on our 2002 baseline of 205 kilotonnes.

Green buildings: To achieve this goal and to minimize our energy consumption, we have committed to make all our new buildings LEED (Leadership in Energy and Environmental Design) compliant. LEED is a widely recognized standard for green building design. In the long term, this measure, along with a series of other energy-reduction initiatives, will help us significantly reduce our environmental footprint. A little-known fact is that our buildings count for more than half of our direct greenhouse gas emissions. Moreover, we aim to achieve a landfill waste diversion rate of over 75% throughout our network by December 2008.

Green fleet: Canada Post has been engaged in the search for environmentally friendly vehicles for more than 10 years. In 1998, Canada Post partnered with a third party to convert two letter carrier trucks to electric power, and the testing of a variety of fuel-efficient options has been ongoing ever since. These tests have included solutions such as hybrid technology, alternate fuels (e.g., propane, natural gas, bio-diesel, ethanol), on-board computerized engine monitoring, fuel atomizers, engine idling limiters and smaller engines. Although some of these solutions have limited application in our fleet, none are ready for widespread use. Currently, there are 18 hybrid vehicles in use in the corporate (non-delivery) fleet and Canada Post continues to explore numerous upcoming solutions being proposed by manufacturers.

We believe the best potential for saving fuel and cutting greenhouse gases in the near term lies in two key strategies. The first is focused on finding smaller vehicles with smaller engines that are suitable for our delivery operation. The plan is to have these vehicles replace larger, less efficient step vans in the 2010 to 2015 timeframe. The second strategy will focus on finding a viable hybrid vehicle by working with manufacturers or after-market outfitters. Hybrid technology is already proven in the consumer marketplace and is being applied in limited applications for commercial vehicles. This holds the most promise for the medium term and is particularly suited to urban delivery where the stop-and-go driving takes maximum advantage of the hybrid technology.

Green products and services: Finally, for our various products and services, we intend to launch two key initiatives in 2008. First, we are in the process of redesigning the paper, board and polyethylene prepaid envelopes sold under the brand names of Priority Courier and Xpresspost to meet new environmental and social criteria. Also, we plan to introduce new innovative ways for our Direct Marketing and Transaction Mail customers to reduce the environmental impact of their mailings.

Risk mitigation – Purolator

Purolator is the only national courier company in Canada to use hybrid electric vehicles (HEVs) in its curb-side delivery fleet. After analyzing the environmental effects of its operations, Purolator identified fleet fuel usage and vehicle air emissions as the best way to reduce its environmental footprint. Since introducing HEVs to its fleet of curb-side delivery vehicles in 2005, Purolator has logged more than 333,000 kilometres, saving almost 60,000 litres of fuel and preventing the emission of over 150 tonnes of greenhouse gas emissions, in carbon dioxide equivalents, as well as associated smog-causing emissions (as of June 2007).

In addition, in the fourth quarter of 2007, Purolator introduced the Quicksider prototype, a battery-operated electric delivery vehicle. The first of its kind in Canada to be used within the courier industry, the Purolator Quicksider is a zero emission vehicle while in operation. The emissions associated with charging its battery are expected to be less than 20% of those produced by a conventional diesel-powered curb-side delivery vehicle. The Quicksider will be tested and evaluated for performance on urban streets.

5.9 Pension

The Canada Post Pension Plan's primary risk exposure is to a decline in long-term real interest rates combined with weak returns on the Pension Plan's assets that could result in higher contributions required to meet pension obligations. During calendar years 2003 through 2006, the Canada Post Pension Plan's assets earned competitive double-digit returns, however, 2007 was a challenging year earning 2.1%. As well, an increase in long-term benchmark interest rates during the year reduced the present value of the pension obligations at the end of 2007. In aggregate, these factors improved the funded status of the Canada Post Pension Plan during 2007, allowing the Plan to maintain its fully funded status.

At the end of 2007, the Canada Post Pension Plan's most significant concentration of credit risk was with the Government of Canada and the Provinces of Ontario and Quebec. This concentration is related primarily to the holding of $2.1 billion of securities issued by the Government of Canada, $444 million issued by the Province of Ontario and $338 million issued by the Province of Quebec. Each investment portfolio within the total pension fund has a limit regarding exposure to any single corporate entity. No such entity represents more than $129 million or 0.9% of total Plan assets. The Pension Plan's $27 million of non-bank asset-backed commercial paper will not have a material impact on the Plan.

Liquidity risk for a pension plan is the risk that more illiquid assets will need to be sold at inopportune times to meet benefit payments. The Plan has more than sufficient short-term assets to offset this risk.

Risk mitigation

Canada Post ensures that investment decisions are made in accordance with the Canada Post Pension Plan Statement of Investment Policies and Procedures. The Pension Committee of Canada Post's Board of Directors provides oversight of pension investments. An asset-liability study will be conducted in 2008 and the Pension Plan risk-management framework will be reviewed as part of this study.

5.10 Legal risk

Pay equity – PSAC

The Public Service Alliance of Canada (PSAC) has filed a complaint against Canada Post that office clerks did not receive equal pay for work of equal value compared to postal clerks and letter carriers. The Human Rights Tribunal found Canada Post liable and ordered payment for lost wages, discounted by 50% because of poor quality of evidence. Canada Post and PSAC appealed to the Federal Court Trial Division.

The appeals were heard during November 2007 and January 2008. In February 2008, the Federal Court Trial Division allowed Canada Post's application for judicial review to set aside the decision of the Canadian Human Rights Tribunal, and has referred the complaint back to the Tribunal with the direction that the complaint be dismissed as not substantiated according to the legal standard of proof. PSAC and the Canadian Human Rights Commission have appealed this decision to the Federal Court of Appeal.

Canada Post vs. Spring

Canada Post has sought an injunction against Spring, a consortium of the Royal Mail, Netherlands Post and Singapore Post, for collecting mail in Canada, shipping it abroad and inducting it into foreign postal streams for delivery. The Corporation contends the activity violated our exclusive privilege over international outbound mail. The Ontario Superior Court of Justice granted a permanent injunction in May 2006, which was stayed until the Court of Appeal unanimously rejected Spring's appeal in May 2007. Spring filed an application for leave to appeal to the Supreme Court of Canada, which was dismissed in November 2007.

However, in October 2007, the Government of Canada introduced Bill C-14 to amend the *Canada Post Corporation Act* to allow other parties to deliver mail addressed to recipients located outside of Canada. Spring sought a stay of injunction unopposed, and remains free to operate until June 2008, or until Bill C-14 is enacted.

Spring counterclaim

Spring commenced an action in February 2005, claiming that Canada Post had interfered in Spring's economic relations and had engaged in defamation. This action was brought in response to Canada Post's attempts to regain business taken by Spring in contravention of Canada Post's exclusive privilege, and was clearly intended as a defensive strategy. It was not advanced while the main acion proceeded through the courts, and was finally dismissed on October 30, 2007, for failing to be set down for trial.

Volumetric process – Canada Post

A class-action suit was filed in August 2006 in the Superior Court of Ontario alleging that Canada Post's volumetric weighing practices contravene the *Weights and Measures Act*. This action was certified as a class action pursuant to the *Class Proceedings Act* in December 2007. The certification order was not appealed.

The parties will now proceed to assemble the plan of proceeding, including notification of members of the class, followed by documentary and examinations for discovery.

UPS – NAFTA

On May 24, 2007, an international trade tribunal, convened pursuant to the provisions of the North American Free Trade Agreement, ruled on a complaint by United Parcel Service (UPS) alleging discriminatory conduct by Canada and anti-competitive conduct by Canada Post resulting in unfair business disadvantage to UPS. Although Canada Post was not a defendant, it participated in the Government of Canada's defense.

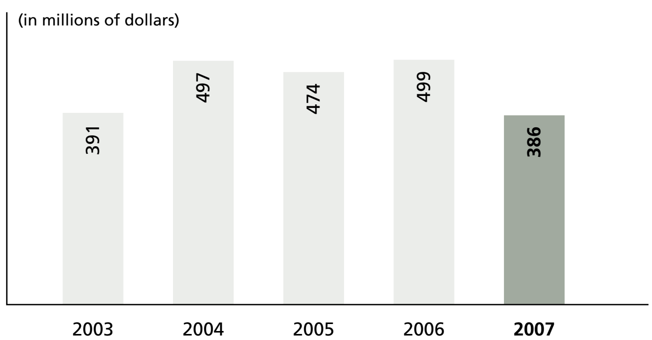
The tribunal found against UPS on each of the claims that were advanced. No appeal has been filed by UPS.

Canada Post has made no provision for these claims. Should the ultimate resolution of these actions differ from management's assessments and assumptions, a material adjustment to the company's financial position and results of its operations could result.

6 Liquidity and Capital Resources

A discussion of our cash flow, liquidity and capital resources

6.1 Cash and cash equivalents



Cash and cash equivalents at the end of 2007 totalled $386 million, a decrease of $113 million from $499 million at the end of 2006. The majority of the difference reflects the conversion of $82 million in short-term commercial paper to marketable securities by Canada Post.

6.2 Operating activities

(in millions of dollars)	2007	2006	Change
Cash provided by operating activities	342	267	75

Cash provided by operating activities was $342 million in 2007, an increase of $75 million, when compared with 2006. Cash was provided primarily by Canada Post ($291 million) and Purolator ($49 million).

The increase in cash from operating activities of $75 million was primarily due to the following:

- Payments for pension, other retirement and post-employment benefits decreased by $414 million, when compared to 2006. This was primarily due to the elimination of solvency deficiency payments to the Canada Post Registered Pension Plan in 2007 ($240 million in 2006) and the cessation of employer contributions in July 2007 that otherwise would have been in the amount of $135 million, due to the Pension Plan's surplus position.

The increase was partially offset by the following:

- Net income decreased by $65 million, *as described in Section 8 – Results from Operations on page 65.*
- Changes in non-cash operating working capital decreased by $236 million, when compared to 2006.

6.3 Investing activities

(in millions of dollars)	2007	2006	Change
Cash used in investing activities	(511)	(278)	(233)

Cash used for investing activities increased by $233 million in 2007, when compared with 2006, primarily due to:

- Canada Post's net position in short-term investments from normal cash management transactions increased by $230 million, compared with a reduction of $24 million in 2006;
- Investment in capital assets increased by $25 million; offset by the sale of two properties in 2007. Proceeds from the sales amounted to $56 million; and
- SCI Logistics acquired The AMG Group for $13 million, which was paid in cash.

Capital expenditures

(in millions of dollars)	2007	2006	Change
Canada Post	237	227	10
Purolator	83	73	10
Logistics	13	5	8
All Other and intersegment	(3)	0	(3)
The Canada Post Group	**330**	**305**	**25**

Capital acquisitions for The Canada Post Group increased by $25 million in 2007, when compared with 2006.

- Canada Post segment capital expenditures increased by $10 million in 2007, when compared with 2006.
  - Real estate capital expenditures increased by $15 million, primarily as a result of increased spending to maintain national facilities and buildings;
  - Asset maintenance/replenishment programs decreased capital spending by $21 million, primarily street furniture expenditures and vehicle replacements;
  - Information technology expenditures increased by $14 million, primarily for improvements to the canadapost.ca website and disaster recovery capability; and
  - Spending on other infrastructure and strategic projects increased by $3 million, primarily to support the lines of business and implement the RSMC health and safety delivery strategy.

- Purolator segment capital expenditures totalled $83 million in 2007, $10 million higher than 2006, as it continued its multi-year initiative to replace and automate its major hubs and transform its technology. Purolator's investment focused on investments in facilities, new technology, and health and safety. Purolator began work to replace most of its customer-facing technology platform with systems that allow it to be more responsive to customer needs, help set standards within the industry and improve efficiency. This will include additional capability within the SAP software application system. Similarly, from an infrastructure perspective, Purolator began replacing some of its older facilities with newly designed terminals to improve the flow of packages, while maintaining a healthy and safe work environment. It also plans to build or upgrade existing facilities to support growth in key markets.
- Logistics segment capital expenditures increased by $8 million in 2007, when compared to 2006, primarily due to a restructuring program related to the contract renewal with SCI Logistics' largest customer.

6.4 Financing activities

(in millions of dollars)	2007	2006	Change
Cash provided by financing activities	56	36	20

Cash flows provided by financing activities increased by $20 million in 2007, when compared with 2006, primarily due to the following:

- Dividends paid to our Shareholder decreased by $33 million, due to the decline in 2006 net income from 2005;
- An obligation of $10 million under a capital lease held by Innovapost expired and was discharged in December 2006; offset by
- Transitional support, received from the Government of Canada to assist with incremental costs incurred as a result of establishing the Canada Post Pension Plan, decreased $25 million in 2007. The declining transition funding will end in 2010.

Dividends

In accordance with the Policy Framework, the Corporation's objective is to pay an annual dividend to our Shareholder, the Government of Canada, equal to 40% of the prior year's consolidated net income. Dividends paid over the past five years total $267 million.

(in millions of dollars)	2007	2006	2005	2004	2003
Consolidated net income	54	119	199	147	253
Dividend paid	47	80	59	63	18
Dividend payout ratio	40%	40%	40%	40%	25%

Based on 2007 consolidated net income of $54 million, we expect to pay a dividend of $22 million in 2008, subject to approval by Canada Post's Board of Directors.

6.5 Liquidity and capital resources

In developing its financial management plan, Canada Post considers the following significant factors:

- current and planned financial performance of the Corporation;
- financial performance of the Canada Post Pension Plan;
- amount of liquidity and working capital the Corporation needs;
- sources of capital available to the Corporation;
- degree of financial leverage planned by the Corporation; and
- corporate tax management strategies.

Canada Post requires sufficient working capital to fund its ongoing operations. The Corporation's objective is to maintain a cash balance of at least $200 million to maintain operations. Ongoing initiatives, as referenced throughout this document, are included in the operating plans of each segment and funded as a part of ongoing operations.

The postal transformation plan to renew the processing, delivery and technology infrastructure, i.e., the Modern Post, could require capital investment of up to $1.9 billion over the next five years. This is in addition to the ongoing capital investment requirements of the Corporation, which total $1.1 billion over the same period.

In July 2007, due to the surplus position of the Canada Post Registered Pension Plan, the Corporation stopped making current service contributions to the Pension Plan that otherwise would have been in the amount of $135 million. It is expected that current service contributions will not be required for at least the next 18 months. *See Section 6.6 – Canada Post Pension Plan below.*

Based on the assessment of these factors, it is expected that the Corporation will have sufficient liquidity and will not need to borrow in 2008 or 2009 to meet planned commitments and investments.

However, the Corporation's financial performance has weakened in 2007 and this trend is expected to continue for at least the next two fiscal years. As a result of this expectation and the significant increase in planned capital expenditures, the Corporation will require additional sources of capital to complete the financing of the expenditures in later years of its transformation to the Modern Post.

Canada Post has authority to borrow both short-term and long-term debt to a maximum of $300 million from sources other than the Crown. The Corporation maintains a line of credit with a Canadian chartered bank of up to $50 million, but this has not been used for several years. A commercial paper program is also available. If additional funds are required, the sources will be developed to minimize the cost and maximize the flexibility of those borrowings.

Although the Policy Framework includes an objective of a 40% debt-equity ratio, it is expected that this degree of leverage will not be required in 2008 or over the next five years.

6.6 Canada Post Pension Plan

The Canada Post Pension Plan is required to file periodic actuarial valuations with the Office of the Superintendent of Financial Institutions. These actuarial valuations are required to set out the funded status of the Canada Post Pension Plan on a going-concern and a solvency basis. If the actuarial valuation reveals a shortfall of assets to liabilities on a going-concern basis, *the Pension Benefits Standards Act*, 1985 requires us to make special payments into the Canada Post Pension Plan to eliminate this shortfall over 15 years. Where the actuarial valuation reveals a shortfall of assets to liabilities on a solvency basis, then *the Pension Benefits Standards Act*, 1985 requires us to make special payments into the Pension Plan to eliminate this shortfall over five years.

The actuarial valuation for the Canada Post Pension Plan as at December 31, 2006, disclosed a going-concern surplus of $993 million and a solvency surplus of $283 million, as compared to a going-concern surplus of $351 million and a solvency deficit of $1,201 million as at December 31, 2005. The solvency deficit was eliminated in 2006 as a result of strong investment returns, higher bond yields and additional contributions from Canada Post. With the elimination of the solvency deficit, no further solvency payments are required. In June 2007, the Board of Directors of Canada Post authorized us to recover special payments previously made to the Canada Post Pension Plan as provided in the Canada Post Pension Plan document. As a result, in July we stopped making current service contributions to the Canada Post Pension Plan. Our total contributions to the Canada Post Pension Plan in 2007 were $100 million; special payments recovered were $161 million. Funds that are not contributed to the Canada Post Pension Plan will be used to fund future capital expenditures that are required to modernize Canada Post or for required regulatory contributions to the Corporation's Pension Plan in the event of either a solvency or going-concern shortfall.

The current estimate of the financial position of the Canada Post Pension Plan as at December 31, 2007, is a going-concern surplus of $1,329 million and a solvency surplus of approximately $400 million. As the Canada Post Pension Plan is expected to continue to be in a surplus position on all actuarial measures, it is expected that employer current service contributions will not be made to the Canada Post Pension Plan in 2008. The estimated amount of the 2008 special payment recovery is $280 million. The Corporation is required, at a minimum, to file the next actuarial valuation for the Canada Post Pension Plan as at December 31, 2009, or at an earlier date if required under the *Pension Benefits Standards Act*, 1985. However, as small changes in discount rates can significantly affect the results of actuarial valuations prepared on a solvency basis, the Corporation will continue to monitor carefully the impact of changes in discount rates, the return on plan assets, and changes in legislation on the financial position of the Canada Post Pension Plan on both a solvency and a going-concern basis. *See Section 9.1 – Critical accounting estimates on page 71.*

6.7 Contractual obligations and commitments

A summary of the Corporation's total contractual obligations and commitments to make future payments is presented below. *For further details, see notes 13 and 16 to the consolidated financial statements on pages 113 and 115 respectively.*

Summary of total contractual obligations and commitments

(in millions of dollars)	< 1 year	1-3 years	3-5 years	> 5 years
Long-term debt*	3	–	–	55
Interest on long-term debt	6	11	11	19
Operating leases**	138	234	189	315
Total	147	245	200	389

* Long-term debt includes $55 million of long-term bonds maturing March 2016. Interest at 10.35% is paid semi-annually.

** Operating leases include the future minimum payment obligations associated with facilities, transportation equipment and other operating leases with terms in excess of one year.

6.8 Related party transactions

As described in *note 19 to the consolidated financial statements on page 118,* the Corporation has a variety of transactions with related parties, both in the normal course of business and in supporting the Government of Canada's public policies.

6.9 Liquidity risks associated with financial instruments

Canada Post Corporation addresses a variety of risks associated with financial instruments. The Corporation has taken a series of steps to strengthen its processes and procedures over investments in marketable securities.

Price risk

The Corporation's investment policy for cash and segregated financial assets carries a low probability of default. Therefore, the value and timing of cash flows (interest- and principal-related) can be determined and are not subject to significant risk.

The market for non-bank-sponsored asset-backed commercial paper (ABCP) in Canada ceased to operate in August 2007. A total of $38 million was invested in these securities at the time of the market disruption. As a result, the Corporation's ABCP was adjusted to a fair value of $30 million. The Investors' Committee, on which Canada Post has a representative, will recommend a restructuring proposal for the ABCP in early 2008. *See note 7 to the consolidated financial statements on page 100.*

Canada Post does not explicitly hedge any of its existing financial instruments.

The value and timing of cash flows associated with debt can be determined with certainty.

Credit risk

The Corporation does not believe that it is subject to any significant concentration of credit risk.

The Corporation is exposed to normal credit risk with respect to accounts receivable. As described in *note 21 to the consolidated financial statements on page 119*, credit risk associated with accounts receivable is minimized by the company's large customer base, which covers substantially all business sectors in Canada.

The investments of cash and segregated financial assets in financial institutions and corporations must have a minimum rating of R1 low, depending upon the term to maturity of the assets. As a result, the credit risk with respect to investments is minimized.

6.10 Off balance sheet arrangements

In the normal course of operations, we provide indemnifications that are often standard contractual terms in favour of third parties in transactions such as purchase and sale contracts, service agreements and leasing transactions. In addition, Canada Post has entered into indemnity agreements with each of its directors and officers. These agreements do not contain specified limits on our liability for compensation to a third party incurred as a result of certain events. Therefore, it is not possible to estimate our potential future liability under these agreements. Historically, we have not made any significant payments under such indemnifications and no amounts have been accrued in our financial statements with respect to these indemnities.

Upon termination or expiration of certain agreements with Innovapost, Canada Post and Purolator have agreed to purchase the assets being used on a dedicated basis and assume the obligations related to the purchase of those assets. Currently, we do not possess sufficient information to estimate the maximum potential future liability related to these agreements. Therefore, no amounts have been accrued in the financial statements. The terms of the agreements provide for no limitation to the maximum potential future payments.

There are no other off balance sheet arrangements that would have a material adverse effect on our liquidity, financial position or results of operations.

7 Financial Condition

A discussion of significant changes in our assets and liabilities between December 31, 2007, and December 31, 2006.

(in millions of dollars)

ASSETS	2007	2006	Change	%	Explanation of Change
Cash and cash equivalents (note 7)	386	499	(113)	(22.7%)	*Refer to Section 6 – Liquidity and Capital Resources on page 59*
Marketable securities (note 7)	309	231	78	34.0%	Primarily increased investments in Government of Canada T-bills rather than shorter-term corporate paper, partially offset by a reclassification of ABCP ($7 million) as long-term securities
Accounts receivable	592	582	10	1.7%	Primarily increased trade receivables related to Purolator revenue growth and SCI Logistics business acquisition, offset by receipt of 2006 international settlements receivable
Income tax recoverable	10	4	6	173.3%	Primarily a shift from current to future taxes for Purolator
Prepaid expenses	68	69	(1)	(1.2%)	Primarily a reduction in retail products inventory
Current portion of segregated securities (note 7)	–	21	(21)	(100.0%)	Employee termination benefits segregated assets portfolio liquidated through settlements in 2007
Current portion of future income tax assets (note 8)	20	63	(43)	(69.0%)	Primarily a reduction related to the use of non-capital losses recognized upon wind-up of epost in 2006 combined with the impact of a reduction in the statutory tax rate for 2008
Total Current Assets	1,385	1,469	(84)	(5.7%)	
Segregated securities (note 7)	632	469	163	34.9%	Primarily segregation of funds ($135 million) made available when Canada Post stopped making employer current service contributions to the Canada Post Registered Pension Plan in July 2007. Also includes income earned on the portfolio and transitional support received from the Government of Canada relating to the establishment of the Canada Post post-retirement dental, term life and death benefit plans, partially offset by employee termination benefit and other payments
Capital assets (note 9)	1,847	1,722	125	7.2%	Primarily capital acquisitions in excess of amortization and impairment – *see Section 6.3 – Investing activities – Capital expenditures on page 59 and Section 8 – Results from operations on page 65*
Accrued pension benefit asset (note 10)	944	1,010	(66)	(6.5%)	Primarily attributable to the cessation of employer contributions to the Canada Post Registered Pension Plan
Future income tax assets (note 8)	203	135	68	49.7%	Primarily temporary differences on the Canada Post Registered Pension Plan offset by the impact of a reduction in the statutory tax rate for future years
Goodwill (note 11)	124	123	1	0.5%	Primarily an increase of $3 million related to goodwill from the acquisition of The AMG Group by SCI Logistics, offset by impairment of epost goodwill
Other assets (note 12)	16	56	(40)	(70.6%)	Primarily a decrease of $48 million from the sale of two properties, partially offset by the classification of $7 million of ABCP as illiquid securities.
Total Assets	5,151	4,984	167	3.3%	

Financial Condition (continued)

(in millions of dollars)

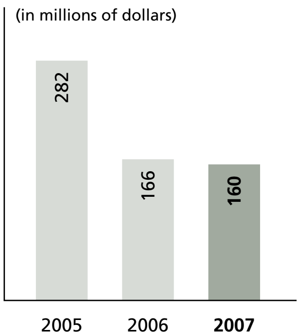
LIABILITIES AND EQUITY	2007	2006	Change	%	Explanation of Change
Accounts payable and accrued liabilities	446	453	(7)	(1.6%)	Several offsetting components – Decreased supplier payables, an Innovapost payable settled in 2007, partially offset by the settlement with the Government of the Netherlands Antilles for termination of the postal concession
Salaries and benefits payable	374	385	(11)	(2.8%)	Primarily due to the decrease in employer contributions to the Canada Post Registered Pension Plan partially offset by increased Purolator accrued salaries and benefits
Income tax payable	34	68	(34)	(50.2%)	Primarily Canada Post income taxes owing due to the Canada Post Pension Plan funding status, more than offset by the use of non-capital losses available from the wind-up of epost in 2006
Deferred revenue	153	177	(24)	(13.9%)	Primarily decreased deferrals for stamp and meter sales and fewer customer prepayments of services for 2008
Outstanding money orders	47	52	(5)	(8.5%)	Primarily reduction in exchange provision for U.S. dollar money orders
Current portion of long-term debt (note 13)	3	3	–	0.6%	
Current portion of accrued post-employment benefit liability (note 10)	–	32	(32)	(100.0%)	Settlement of employee termination benefits for CPAA members
Total Current Liabilities	1,057	1,170	(113)	(9.7%)	
Long-term debt (note 13)	55	58	(3)	(4.9%)	Payments due to a third party due in December 2008 reclassified as current
Accrued pension, other retirement and post-employment benefit liability (note 10)	2,513	2,247	266	11.8%	Primarily attributable to the Canada Post post-retirement health care plan current year expense, partially offset by employee termination benefit settlements for CPAA members
Future income tax liabilities (note 8)	24	19	5	29.1%	Primarily relates to Purolator current year capital cost allowance in excess of amortization
Other long-term liabilities	41	38	3	6.4%	Primarily Purolator obligation to repurchase employee shares
Total Liabilities	3,690	3,532	158	4.5%	
Non-controlling interest	22	19	3	19.8%	Minority interest on net income of Purolator.
Equity of Canada	1,439	1,433	6	0.4%	Primarily consolidated net income of $54 million, offset by the dividend of $47 million paid to the Government of Canada
Total Liabilities and Equity of Canada	5,151	4,984	167	3.3%	

8 Results from Operations

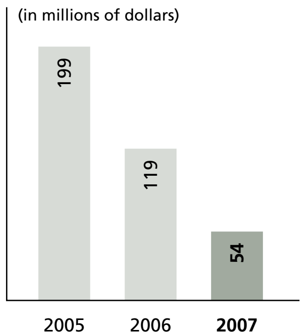
A detailed discussion of our financial performance in 2007

8.1 Consolidated trends

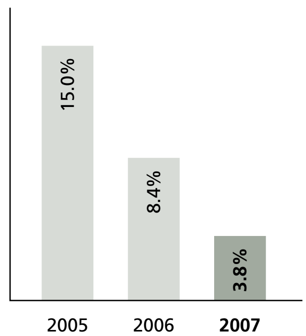
Consolidated income before income taxes



Consolidated net income



Return on equity



8.2 Consolidated results from operations

Consolidated income statement

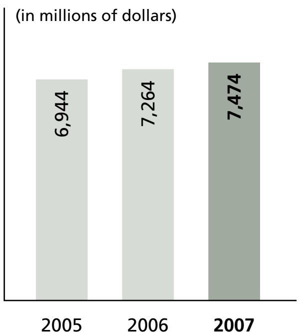
Increase (decrease)

(in millions of dollars)	2007	2006	Change	%
Revenue from operations	7,474	7,264	210	2.5%
Cost of operations	7,346	7,116	230	3.2%
Income from operations	128	148	(20)	(13.6%)
Non-operating income (expense)	32	18	14	72.9%
Income before income taxes	160	166	(6)	(4.1%)
Income tax expense	102	44	58	128.4%
Non-controlling interest	4	3	1	23.9%
Net income	54	119	(65)	(54.3%)
Return on equity	3.8%	8.4%	(4.6%)	

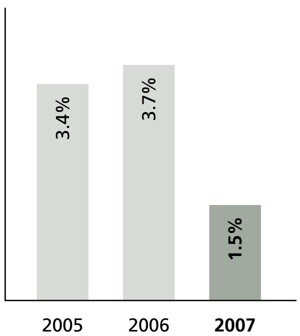
The Canada Post Group earned consolidated net income of $54 million in 2007, a decrease of $65 million, when compared with 2006. Cost increases outpaced revenue growth but the differential was kept to a minimum through ongoing monitoring and control of costs. As a result, the decline in consolidated income before income taxes was held to $6 million. Income tax expense increased by $58 million in 2007.

Consolidated revenue from operations

Revenue from operations



Volume growth



Revenue from operations increased 2.5% or $210 million in 2007, when compared with 2006, driven primarily by a strong performance by Canada Post's Admail and Xpresspost products and Purolator's courier revenue. A detailed discussion of revenue by segment follows.

Consolidated cost of operations

A strong focus on cost control and operational efficiencies kept cost increases in 2007 to 3.2%, when compared with 2006. A detailed discussion of cost of operations by segment follows.

Consolidated non-operating income (expense)

Investment and other income increased by $13 million in 2007, when compared to 2006.

Gains on the sale of property, plant and equipment increased by $10 million. Two properties held for sale at the end of 2006 were sold during 2007 as anticipated. A gain of $8 million was recorded on the dispositions.

Interest revenue increased by $1 million, due to higher rates of return on the short-term portfolio. Average cash balances were lower ($574 million in 2007 vs. $604 million in 2006) but were more than offset by higher rates of return (4.15% in 2007 vs. 3.80% in 2006). As a result of liquidity issues in the non-bank-sponsored asset-backed commercial paper (ABCP) market, the investment in ABCP was reduced by $2 million and classified as illiquid securities.

Consolidated income tax expense

Consolidated income tax expense increased by $58 million, when compared with 2006, due primarily to the impact of reductions in statutory income tax rates on future tax benefits recorded.

8.3 Operating results by segment

In 2007, performance improved in all segments when compared to 2006, except the Canada Post segment where income before income taxes fell by $21 million.

Segmented results – Income before income taxes

(in millions of dollars)	2007	2006	Change
Canada Post	78	99	(21)
Purolator	84	69	15
Logistics	6	(1)	7
All Other	8	2	6
Intersegment and unallocated	(16)	(3)	(13)
The Canada Post Group	160	166	(6)

8.4 Canada Post segment

The Canada Post segment contributed $78 million of income before taxes to the 2007 consolidated results, a decrease of $21 million, when compared with 2006. Decreasing Lettermail volumes, and cost pressures from wages, transportation and rural mail delivery contributed to the decline. The results of epost are included from October 31, 2006, when its operations were integrated into the Transaction Mail line of business.

Canada Post summary

Increase (decrease)

(in millions of dollars)	2007	2006	Change	%
Revenue from operations	5,955	5,831	124	1.7%
Cost of operations	5,928	5,761	167	2.9%
Income from operations	27	70	(43)	(62.1%)
Non-operating income (expense)	51	29	22	74.8%
Income before income taxes	78	99	(21)	(21.9%)

Revenue from operations

Canada Post generated revenue from operations of $5,955 million in 2007, an increase of $124 million or 1.7%, when compared to 2006. The revenue growth was attributable primarily to increases in revenue per piece across all lines of business and a 4.4% volume growth in Direct Marketing. Transaction Mail volumes declined 1.6% and Parcels volumes decreased by 0.7% in 2007.

The $124-million revenue increase was comprised of an $8-million increase of revenue in Transaction Mail, a $39-million increase of revenue in Parcels, and a $97-million increase of revenue in Direct Marketing. The increases were partially offset by a decrease in revenue from other services of $20 million.

Revenue and volumes by line of business

	Revenue (in millions of dollars / trading day adjusted per cent)				Volume (in millions of pieces / trading day adjusted per cent)			
	2007	2006	Change	%	2007	2006	Change	%
Transaction Mail								
Domestic/Outbound	3,100	3,092	8	(0.2%)	5,116	5,161	(45)	(1.3%)
Inbound	114	114	0	0.1%	290	310	(20)	(6.8%)
Total Transaction Mail	3,214	3,206	8	(0.2%)	5,406	5,471	(65)	(1.6%)
Parcels								
Domestic/Outbound	1,092	1,053	39	3.3%	123	123	0	(0.2%)
Inbound	134	134	0	(0.6%)	51	51	0	(2.2%)
Total Parcels	1,226	1,187	39	2.9%	174	174	0	(0.7%)
Direct Marketing								
Addressed Admail	621	583	38	6.1%	1,525	1,470	55	3.3%
Unaddressed Admail	376	339	37	10.3%	3,940	3,722	218	5.4%
Publications Mail™	285	275	10	3.2%	535	536	(1)	(0.4%)
Other	122	110	12	11.1%	66	60	6	9.5%
Total Direct Marketing	1,404	1307	97	7.0%	6,066	5,788	278	4.4%
Other revenue	111	131	(20)	(16.1%)	–	–	–	–
Total	5,955	5,831	124	1.7%	11,646	11,433	213	1.5%

Transaction Mail

Overall, Transaction Mail revenue in 2007 remained relatively flat compared to 2006, at $3,214 million. The small revenue decline of 0.2% was driven by reduced volumes of 1.6%, partially offset by an increase in the average rate per piece of 1.3%.

Domestic Lettermail revenue increase by $26 million, or 0.5% in 2007, when compared with 2006. Volumes declined 0.9% but were offset by price increases that included a basic letter rate increase of one cent. Volume drivers included the migration of a major customer to a Direct Marketing product and reduced demand in the public sector as government programs were not implemented at the same level as 2006.

Other Transaction Mail service revenue grew by $3 million, including $5 million from epost, which was brought in-house in November 2006. This was partially offset by large, one-time prior year activities, such as the Canadian census, not being replaced.

International outbound mail revenue decreased by $21 million, or 11.5%, when compared with 2006. Volumes declined partially due to the strength of the Canadian dollar, which made U.S. direct entry more attractive to Canadian commercial customers than using Canada Post for mailing.

International inbound mail revenue (postage revenue collected by other postal administrations and shared with Canada Post for delivering their mail in Canada) of $114 million was equal to that of last year. Volume declines were seen primarily with countries other than the U.S. Mail from the U.S. increased, as the high Canadian dollar made sending mail to Canada through the United States Postal Service (USPS) more attractive to commercial customers than cross-border shipping and using only Canada Post for mailing. An overall price increase negotiated in the USPS-CPC bilateral agreement also contributed to revenue stability.

Parcels
Parcels revenue totalled $1,226 million in 2007, increasing by $39 million, or 2.9%, when compared with 2006.

Domestic parcel revenue increased by $41 million, or 4.6%, over the previous year. Overall volumes in 2007 remained stable, when compared to 2006, reversing the trend of declining domestic volumes experienced over the last number of years. Revenue growth was primarily driven by price increases. Xpresspost volumes grew 8.7% in 2007, contributing $33.5 million of the year-over-year revenue increase. This was mainly attributable to a number of high-growth customers, particularly in the area of online sales. Regular Parcel volumes declined, partly attributable to continued migration to Expedited Parcel, which experienced some volume increase.

International outbound revenue decreased by $2 million, even though there was a slight volume increase of 0.1% over 2006. The strong Canadian dollar negatively affected Canadian retail outbound shipments, including online pharmacies, which experienced continued erosion.

International inbound revenue remained the same as 2006 at $134 million, with a decrease in volume of 2.2%.

Direct Marketing
Direct Marketing revenue increased by $97 million, or 7.0%, over the prior year. Overall volumes increased by 4.4%. The health of the economy in Canada, the value of the direct-mail media, and strong performance from the telecommunications and retail sectors, both from large enterprises and medium-size businesses, contributed to this performance.

Our Admail products grew by $75 million, or 7.6%, generating approximately 80% of the growth for this business segment. Addressed Admail revenue grew by $38 million, or 6.1%, with year-over-year volume growth of 3.3%. Growth for Addressed Admail was strong within the highly competitive telecommunications sector, the retail sector and with Canadian business in general. We saw a softening in the year-over-year growth within the financial sector, when compared with the record growths of the prior year. Unaddressed Admail performed very well for a second consecutive year, generating an additional $37 million in revenue, or 10.3%, over the prior year, which represents volume growth of 5.4%. This product continues to outperform a traditionally flat unaddressed print advertising market. All key sectors performed well in 2007, including retail, telecommunications and the financial sector, across all customer segments.

Revenue from our Publications Mail service grew by $10 million, or 3.2%, over the prior year. Business from new publications in the telecommunication sector contributed to this growth. Canada Post continued to support the publishing industry through cost-reduction initiatives, business build and participation in the Canadian Heritage Publications Assistance Program.

Other revenue
Other revenue decreased by $20 million, or 16.1%, in 2007, when compared with 2006. The strengthening of the Canadian dollar and other currency fluctuations resulted in exchange losses of $8 million from settlements with foreign postal administrations (compared to exchange gains of $6 million in 2006). Philatelic revenue for collector stamp items also declined with fewer philatelic stamp releases.

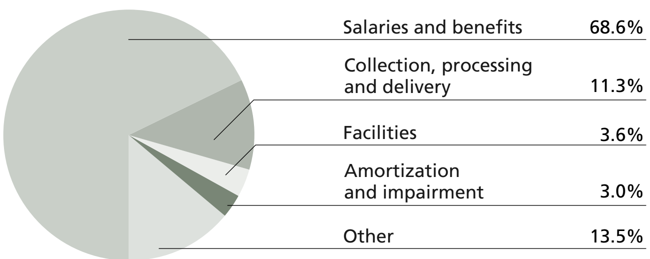
Cost of operations

In 2007, the Canada Post segment's cost of operations totalled $5,928 million, an increase of $167 million, or 2.9%, over the prior year.

(in millions of dollars)	2007	2006	Change	%
			Increase (decrease)	
Salaries	3,221	3,089	132	4.3%
Benefits	843	885	(42)	(4.7%)
Total salaries and benefits	4,064	3,974	90	2.3%
Collection, processing and delivery	671	597	74	12.4%
Facilities	213	206	7	3.2%
Amortization and impairment	180	183	(3)	(1.6%)
Other	800	801	(1)	(0.1%)
Total	5,928	5,761	167	2.9%

The chart below shows the breakdown of costs as a percentage of total cost of operations. Salaries and benefit costs comprise 68.6% of the total cost, demonstrating the labour-intensive nature of the business.

Cost of operations – 2007



Cost of Operations	2007	2006	2005
Salaries and benefits	68.6%	68.9%	68.1%
Collection, processing and delivery	11.3%	10.4%	10.4%
Facilities	3.6%	3.6%	4.0%
Amortization and impairment	3.0%	3.2%	3.5%
Other	13.5%	13.9%	14.0%

Salaries

The cost of salaries increased by $132 million or 4.3%, when compared with 2006. The most significant portion of this increase was due to employee wage increases. The addition of 200,000 new points of call, further requirements for letter carrier route support, and a 5.4% growth in our Unaddressed Admail product added further pressure on our delivery network costs. Salaries for new supervisors hired in 2006, higher absenteeism levels, and additional labour costs relating to the rural mail directive also contributed to the cost increase. These rising costs were partially offset by productivity improvements in operations.

Employee benefits

Increase (decrease)

(in millions of dollars)	2007	2006	Change	%
Active employee benefits	415	395	20	5.0%
Retirement health benefits	258	253	5	2.0%
Pension expense	186	310	(124)	(39.9%)
Transitional funding	(106)	(162)	56	34.2%
Interest on segregated assets	(17)	(20)	3	17.1%
Other	107	109	(2)	(1.5%)
Net benefit costs	843	885	(42)	(4.7%)

Employee benefit costs decreased by $42 million or 4.7%, when compared with 2006.

Pension expense declined by $124 million, primarily due to an increase in the discount rate from 5.1% in 2005 to 5.3% in 2006 and an increased return on pension assets, which put our Pension Plan in a position where no amortization of actuarial loss was required in 2007. This decrease was partially offset by a reduction of $56 million in transitional funding from the Government of Canada. As described further in *note 2 to the consolidated financial statements on page 92,* declining transitional support is provided to assist the Corporation with the incremental costs incurred as a result of establishing the Canada Post Corporation Pension Plan and the associated ancillary benefits.

Income earned on the segregated securities portfolios, which is recorded against benefits expense, decreased by $3 million in 2007, when compared to 2006. Higher rates of return (4.6% in 2007 vs. 3.7% in 2006) and higher portfolio values, primarily due to transitional funding, resulted in an increase of $3 million in income. However, as a result of liquidity issues in the non-bank-sponsored asset-backed commercial paper (ABCP) market, the value of our investment in ABCP was reduced by $6 million. The rate of return after the adjustment was 3.5%.

Collection, processing and delivery

Contracted collection, processing and delivery costs increased by $74 million in 2007, when compared with 2006. Transportation costs increased by $44 million, primarily due to additional mail volumes transported by air, and inflationary pressures on contractual rates and fuel costs. Points of call growth, paid assistants hired to accompany CUPW/RSMC-represented employees on their routes, and pay for economic conditions in Alberta contributed to an increase of $23 million in rural mail contracted costs.

Facilities

Facilities costs increased by $7 million to $213 million, primarily due to increases in contract rent and cost of utilities.

Amortization and impairment

Amortization and impairment expense decreased by $3 million, or 1.6%, when compared with 2006. Amortization of property, plant and equipment declined $12 million as a result of the SAP software asset, which was fully amortized in 2006. This was partially offset by impairment charges related to epost customer contracts ($5 million), epost goodwill ($3 million), and amortization of other customer contracts and relationships ($1 million).

Other expense

Total other expense, which includes information technology, administration, settlements with foreign postal administrations, retail and other costs, remained flat in 2007, when compared to 2006.

8.5 Purolator segment

The Purolator segment contributed $84 million to 2007 consolidated income before income taxes, an increase of $15 million, when compared with 2006.

Purolator summary

Increase (decrease)

(in millions of dollars)	2007	2006	Change	%
Revenue from operations	1,448	1,347	101	7.1%
Cost of operations	1,360	1,275	85	6.7%
Income from operations	88	72	16	22.2%
Non-operating income (expense)	(4)	(3)	(1)	(46.6%)
Income before income taxes	84	69	15	21.0%

Revenue from operations

Purolator revenue from operations increased by $101 million or 7.1% in 2007, when compared with 2006.

This growth was primarily attributed to increases in revenue per shipment across the various lines of business. The expanding Purolator Freight and Purolator-USA™ divisions have continued to drive volume growth at double digit growth rates. Purolator's strong service levels continue to attract air cargo volumes and these revenues have also seen double-digit growth rates.

The strong revenue performance of 2007 reflects the premium service that the Purolator brand represents. Overall volumes grew 1.5%. With continuing service level improvements on air and ground delivery times, satisfied customers continue to support Purolator's growth.

Cost of operations

In 2007, the cost of operations increased by $85 million, or 6.7%, when compared to 2006. Cost pressures were significant. Salary and benefit costs increased 5.0% and variable operating costs rose 10.1%. Fuel prices continued to increase, and the ripple effect of the booming western Canadian economy on local staffing and network equilibrium continued to be a challenge that required considerable management focus. As the expanding Purolator Freight and Purolator-USA divisions continue to grow at double-digit rates, costs have increased correspondingly as the infrastructure and network is solidified. The significant capital investment of the "Purolator 2010" initiative over the last few years in infrastructure, systems and people has enabled Purolator's strong growth but has also caused increases in amortization, information technology and training costs. These increases were partially offset by a 7.8% reduction in administration and discretionary costs.

8.6 Logistics segment

The Logistics segment includes the consolidated financial results of SCI Logistics. The results of Intelcom are included up to January 9, 2007, the effective date of disposal of the joint venture.

Logistics summary

Increase (decrease)

(in millions of dollars)	2007	2006	Change	%
Revenue from operations	146	134	12	8.3%
Cost of operations	140	136	4	2.6%
Income from operations	6	(2)	8	392.7%
Non-operating income (expense)	0	1	(1)	(35.2%)
Income (loss) before income taxes	6	(1)	7	992.6%

Income by entity

Increase (decrease)

Income before income taxes by entity (in millions of dollars)	2007	2006	Change
SCI Logistics	8	(1)	9
Other	(2)	0	(2)
Total segment	6	(1)	7

SCI Logistics

SCI Logistics' financial performance improved significantly in 2007, with net income before income taxes of $8 million, an increase of $9 million, when compared with 2006.

Revenue from operations increased by $23 million, primarily due to the addition of revenue from The AMG Group, which was acquired in March 2007. In 2007, 47% of SCI Logistics' revenue was derived from its largest customer, a decrease of 18%, when compared to 2006.

Cost of operations increased by $14 million in 2007, when compared with 2006. This increase was primarily due to the addition of costs relating to The AMG Group, which was partially offset by lower restructuring costs.

During 2006, SCI Logistics renewed its logistics services agreement with its largest customer that will extend until 2010. In conjunction with the contract renewal, the customer sought significant price reductions. In response, SCI Logistics agreed to both service and margin reductions, including service level changes, rationalized facilities and reduced corporate support services. In 2006, the company commenced a restructuring program, which continued in 2007. The total cost of the restructuring program was $3 million in 2007, compared to $10 million in 2006. The customer agreed to pay for these costs in exchange for reduced ongoing costs and a capped margin. Due to revenue recognition guidelines, the payment is amortized over the contract renewal period to 2010, while the costs are expensed as incurred.

Intelcom

The 2006 results include revenue from operations of $11 million and cost of operations of $11 million.

8.7 All Other segment

The All Other segment includes the financial results of Innovapost and CPIL. The results of epost are included in this segment until October 31, 2006, when its operations were integrated into the Canada Post segment and Innovapost.

All Other summary Increase (decrease)

(in millions of dollars)	2007	2006	Change	%
Revenue from operations	175	177	(2)	(1.4%)
Cost of operations	168	173	(5)	(3.0%)
Income from operations	7	4	3	85.4%
Non-operating income (expense)	1	(2)	3	142.1%
Income (loss) before income taxes	8	2	6	427.9%

Income by entity Increase (decrease)

Income before income taxes by entity (in millions of dollars)	2007	2006	Change
Innovapost (at 51%)	17	18	(1)
CPIL	(9)	0	(9)
epost	0	(16)	16
Total segment	8	2	6

CPIL

The 2007 results of CPIL include a provision of $7.4 million to reflect the settlement with the Government of the Netherlands Antilles for terminating the postal concession in 2008. It is expected that CPIL will be dissolved in 2008, following the transfer of NPNA shares to the Government of the Netherlands Antilles. *See Section 2.9 – All Other segment – Canada Post International Limited on page 45.*

epost

The results of epost are included in the Canada Post segment and Innovapost after October 31, 2006.

9 Critical Accounting Estimates and Accounting Policy Developments

A review of critical accounting estimates and changes in accounting policies in 2007 and future years

9.1 Critical accounting estimates

Our significant accounting policies are described in *note 2 to the consolidated financial statements on page 92.* The preparation of financial statements in accordance with Canadian generally accepted accounting principles (GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses, and the disclosure of contingent assets and liabilities. Actual results could differ from those estimates.

The critical accounting estimates described here require us to make particularly complex or subjective judgments about matters that are inherently uncertain or where it is likely that materially different amounts could be reported under different conditions or using different assumptions. The Audit Committee of Canada Post's Board of Directors has reviewed the disclosures described in this section.

Capital assets

Capital assets, comprising property, plant and equipment and intangible assets with finite useful lives, are amortized over their useful lives. Useful lives are based on management's estimates of the periods of service provided by the assets, and are provided in *note 2 to the consolidated financial statements on page 92.* The useful lives of these assets are periodically reviewed for continued appropriateness. Due to the long lives of many of the assets, changes to the estimates used would cause significant variations in the carrying values that could result in a material impact on the consolidated financial statements.

A change in the remaining useful lives will affect the amortization expense as reported in the Corporation's results of operations. A change of one year in the composite useful life of the Corporation's capital asset base would impact annual amortization expense by approximately $9 million.

Long-lived assets are tested for impairment when events or circumstances indicate that the carrying value is not recoverable from future cash flows. If future conditions were to adversely differ from management's best estimate of key economic assumptions and associated cash flows were to materially decrease, the Corporation could potentially experience future material impairment charges in respect of its capital assets.

Goodwill

Goodwill is not amortized but is tested at least annually for impairment at the reporting unit level. Goodwill is tested by comparing the fair value of the reporting unit to its carrying value. The Purolator segment represents the significant portion of goodwill in the consolidated financial position. The estimated fair value of this reporting unit is based on a discounted cash flow analysis, which includes making assumptions and estimates in a number of areas, including future cash flows, cash flow periods, terminal values and discount rates.

In estimating future cash flows of the Purolator segment, the Corporation uses its approved plans. These plans reflect management's best estimates; however, they are subject to change as they involve inherent uncertainties that management may not be able to control. In addition, growth and profitability levels are compared to other competition in the industry, and general economic conditions prevailing at the valuation date. The discount rate applied to the future cash flows of the Purolator segment is equal to the estimated weighted average cost of capital. In addition, the range of terminal value multiples is determined by adjusting the weighted average cost of capital by an amount reflecting a sustainable real growth rate for the reporting unit beyond the forecast period. A change in the weighted average cost of capital could have a significant impact on the estimate of the fair value of goodwill, and related impairment charge, if any.

Contingencies

Contingencies are recorded as liabilities when it is probable that a liability has been incurred and the amount of the loss is reasonably estimable. Disclosure is required when the amount of the loss is not estimable, or if there is a reasonable possibility that the ultimate loss will exceed the recorded provision. Contingent liabilities are often resolved over long time periods. Further information on the Corporation's contingencies is provided in *note 16 to the consolidated financial statements on page 115.*

An estimate of the liability for grievance claims is recorded based on the estimated likelihood of making a payment on settlement of the grievance and an estimation of the settlement amount. Changes to the likelihood of settlement and the estimated payment amounts of certain grievance claims may have a material impact on the financial statements in future years.

Pension and other retirement and post-employment benefits

The Canada Post Group sponsors plans that provide pensions and other retirement benefits for most of its employees. The Corporation believes the accounting estimates related to its employee benefit plan costs are critical accounting estimates because: (1) the amounts are based on complex actuarial calculations using several assumptions; and (2) given the magnitude of the estimated costs, differences in actual results or changes in assumptions could materially affect the consolidated financial statements.

Due to the long-term nature of these benefit plans, the calculation of expenses and obligations depends on various assumptions such as discount rates, expected long-term rate of return on plan assets, health care cost trend rates, projected salary increases, retirement age, mortality rates, and termination rates. These assumptions bear the risk of change as they require significant judgment and have inherent uncertainties that management may not be able to control. Other than the discount rate, the assumptions are determined by management and are reviewed annually by The Canada Post Group's actuaries.

The Group's discount rate assumptions, which are set annually at the measurement date, are used to determine the present value of the projected benefit obligation at the end of the year and the net periodic benefit cost for the following year. The discount rate is used to measure the single amount that, if invested at the measurement date in a portfolio of high-quality debt instruments with a rating of AA or better, would provide the necessary cash flows to pay for the benefit plans as they become due. The actuary determines the discount rate using a yield curve approach, which is based on pricing and yield information for high quality AA-rated corporate bonds. The selected discount rate will have a cash flow pattern that resembles that of the plan being valued. The actuary determines the future benefit payments based on assumptions, which include the respective plans, demographics, retirees' profile and medical trend.

The expected rate of return on plan assets assumption is based on the statement of investment policies and procedures. It is a long-term assumption for which the accuracy can only be measured over a long period based on past experience. The investment strategy for the assets in the pension plans is to maintain a diversified portfolio of assets, invested in a prudent manner to maintain the security of funds while maximizing returns within the guidelines provided in the investment policy.

The rate of compensation increase is another significant assumption in the measurement of the accrued benefit obligation for pension benefit plans and some of the other non-pension benefit plans. The short-term assumptions for projected salary increases are as reflected in the current active collective agreements, otherwise an assumption of 3% is used. The long-term salary increases assumption is also 3%.

The Corporate Team Incentive, which is included in the pensionable earnings of the Group's major pension plan, is assumed to be paid at 100% payout level.

The demographic assumptions are used to project the future number of retirees and dependants from year to year who will be eligible for benefits under the benefit plans. These assumptions include expected mortality, termination and retirement experience.

Other assumptions are based on actual experience and management's best estimates. Actual results that differ from the assumptions result in actuarial gains or losses, which, in accordance with the recommendations of the Canadian Institute of Chartered Accountants (CICA), are accumulated and amortized over future periods, and therefore, generally affect recognized expense and the recorded liability in future periods. The amortization of all employee future benefits other than post-employment benefits are amortized over the expected average remaining service life of the active employee group covered by the plans only to the extent that the unrecognized net actuarial gains and losses are in excess of 10% of the greater of the accrued benefit obligation and the market-related value of plan assets as at the beginning of the year. Gains or losses arising at the measurement date of post-employment benefit plans are amortized over the average duration of the respective obligations without the use of the 10% limit.

In *note 10 to the consolidated financial statements on page 106,* a table has been included that quantifies the impact of these differences in each of the last two years. These differences relate primarily to: (1) actual versus expected return on plan assets; (2) actual actuarial gains/losses incurred on the benefit obligation versus those expected and recognized in the consolidated financial statements; and (3) actual past service costs incurred as a result of plan amendments versus those expected and recognized in the consolidated financial statements.

The benefit obligations and associated expense are very sensitive to actuarial assumptions, namely changes in the discount rate, expected long-term return on plan assets, rate of compensation increase, and medical trend rate assumptions. A lower discount rate results in a higher benefit obligation and a lower funded status. Similarly, poor fund performance results in a lower fair value of plan assets and a lower funded status. In either situation, the cash contributions to the funded benefit plans are affected.

Sensitivity to changes in key assumptions for our principal pension plan follows:

	Change in assumption	
(in millions of dollars)	Increase	Decrease
Change in discount rate of 10 basis points		
Increase (decrease) in annual pension expense	(12)	21
Increase (decrease) accrued pension obligation	(210)	215
Change in expected return on plan assets of 25 basis points		
Increase (decrease) in annual pension expense	(33)	33

Our principal health care plan is very sensitive to the following assumptions:

	Change in assumption	
(in millions of dollars)	Increase	Decrease
Change in discount rate of 10 basis points		
Increase (decrease) in annual health care expense	(6)	7
Increase (decrease) accrued health care obligation	(44)	45
Change in health care cost trend rates of 100 basis points		
Increase (decrease) in annual health care expense	102	(77)
Increase (decrease) accrued health care obligation	532	(408)

For further details on our annual expense and obligation, see *note 10 to the consolidated financial statements on page 106.*

Income taxes

The Corporation is subject to income tax in numerous jurisdictions and significant judgment is required in determining the provision for tax. There are many transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business. The Corporation recognizes liabilities for anticipated tax issues based on estimates of the additional taxes that are likely to become due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income tax and future tax provisions in the period in which such determination is made.

Future income tax assets and liabilities are comprised of temporary differences between the carrying amount and tax basis of assets and liabilities as well as tax losses carried forward. The timing of the reversal of the temporary differences is estimated, and the tax rate substantively enacted for the period of reversal is applied to the temporary difference. The carrying amounts of assets and liabilities are based upon the amounts recorded in the financial statements and are therefore subject to accounting estimates that are inherent in those balances. The Corporation has significant deductible temporary differences, however, future tax assets have only been recorded to the extent that they are more likely than not to be realized. The deductible temporary differences that are not expected to reverse relate mainly to the accrued other retirement and post-employment benefit liability. *See note 8 to the consolidated financial statements on page 103.*

The tax basis of assets and liabilities as well as tax losses carried forward are based upon the applicable income tax legislation, regulations and interpretations, all of which in turn are subject to interpretation. Assumptions underlying the composition of future income tax assets and future income tax liabilities include expectations about future results of operations and the timing of reversal of deductible temporary differences and taxable temporary differences. These assumptions also affect classification between income taxes recoverable and future income tax assets. The composition of future income tax assets and future income tax liabilities is reasonably likely to change from period to period because of the significance of these uncertainties.

If future outcomes were to adversely differ from management's best estimate of future results of operations and the timing of reversal of deductible temporary differences and taxable temporary differences, the Corporation could experience material future income tax adjustments. Such future income tax adjustments do not result in immediate cash outflows and, of themselves, would not affect the company's immediate liquidity.

9.2 Accounting policy developments

The consolidated financial statements are prepared in accordance with Canadian GAAP as set out in the CICA *Handbook of Standards and Guidance Collection.* The impact of current year and future changes in Canadian GAAP is described below.

Current year accounting changes

Financial instruments – Recognition and measurement, hedges and comprehensive income

The Corporation has adopted the new accounting standards related to financial instruments: (i) "Financial Instruments – Recognition and Measurement," (ii) "Hedges," and (iii) "Comprehensive Income," effective January 1, 2007.

Under the new standards, all financial instruments, including derivatives, are to be included on a company's balance sheet and measured either at their fair values or, in limited circumstances when fair value may not be considered most relevant, at cost or amortized cost.

The standards also specify when gains and losses, as a result of changes in fair values, are to be recognized in the income statement (other comprehensive income provides a new financial statement location for temporarily recording such gains and losses).

Hedge accounting is optional, and certain financial instruments may be designated as hedges under specific circumstances.

The Corporation has identified the appropriate accounting treatment for its financial instruments according to these standards and determined the impact on opening balances as at January 1, 2007. Cash equivalents, marketable securities and segregated securities have been designated as held-for-trading as at January 1, 2007. Future purchases of such investments will be designated as held-for-trading, unless specified otherwise on initial recognition.

The adjustment to reflect the opening carrying amount of held-for-trading financial instruments at fair value did not materially impact the consolidated financial statements. The application of the effective interest method to calculate the amortized cost of other financial assets, including loans and receivables, and financial liabilities also did not result in a significant impact on the consolidated financial statements. As a result of a review of significant contracts, no derivative financial instruments, nor financial instruments containing embedded derivatives requiring bifurcation, were identified.

Amounts recorded in other comprehensive income in these consolidated financial statements comprise foreign currency translation adjustments.

Accounting changes

The Corporation has adopted the revised recommendations in Section 1506 "Accounting Changes," effective January 1, 2007. Under the revised recommendations, voluntary changes in accounting policy are only permitted if they result in the financial statements providing reliable and more relevant information. Changes in accounting policy are to be applied retrospectively unless doing so is impracticable, or where the change in accounting policy is made on initial application of a primary source of GAAP, in accordance with the specific transitional provisions under the new requirement. New disclosures are also required in respect of changes in accounting policies, changes in accounting estimates and correction of errors.

Future year accounting changes

Implementation in 2008

Capital disclosures

In December 2006, the CICA issued a new accounting standard, Section 1535 "Capital Disclosures," to converge with recent amendments to International Financial Reporting Standard IAS 1 "Presentation of Financial Statements." This new standard will be effective for fiscal years beginning on or after October 1, 2007, although earlier adoption is permitted. Section 1535 requires an entity to disclose information about its objectives, policies and processes for managing capital, quantitative data about what the entity regards as capital, as well as its compliance with any externally imposed capital requirements.

Financial instruments disclosures and presentation

In December 2006, the CICA issued a new accounting standard on disclosures about financial instruments. Section 3862 "Financial Instruments – Disclosures," improves upon the disclosure requirements in existing Section 3861 "Financial Instruments – Disclosure and Presentation," and converges with International Financial Reporting Standard IFRS 7 "Financial Instruments: Disclosures." Section 3862 must be implemented in the first fiscal year beginning on or after October 1, 2007, although earlier adoption is permitted.

Section 3862, like Section 3861, is based on the fundamental principle that entities should provide disclosures in their financial statements that enable users to evaluate the significance of financial instruments for the entity's financial position and performance. However, Section 3862 places an increased emphasis on disclosures about the risks associated with both recognized and unrecognized financial instruments and how those risks are managed.

Concurrent with the release of Section 3862, the Accounting Standards Board (AcSB) of the CICA also issued Section 3863, "Financial Instruments – Presentation," which carries forward unchanged the presentation requirements of Section 3861 and must be applied at the same time that Section 3862 is adopted.

Convergence with international reporting standards

In early 2006, the AcSB ratified a strategic plan that will result in Canadian GAAP used by publicly accountable enterprises being converged with International Financial Reporting Standards. The Accounting Standards Board remains on target for the changeover date of January 1, 2011. The Canada Post Group has commenced its initial scoping exercise for the conversion, however, as of the date of these consolidated financial statements, it would be premature to assess the impact of the initiative, if any, on the Corporation at the present time.

10 Outlook for 2008

Our prospects for 2008

10.1 Current operating context

The economic climate is uncertain and the risk of a downturn in our economy could have a negative effect on our revenues. As inflation remains moderate, there will be no basic letter rate increase in 2008. This is combined with the continued growth of more than 200,000 new addresses each year. We have increased investment spending as we enter the early stage of our modernization journey. With narrow margins, the Corporation needs to be very vigilant in controlling its discretionary costs and finding innovative operational efficiencies. Canada Post remains confident that our management focus on cost controls, developing new products and services, and business improvements from our investment in the Modern Post will position us well for the future.

10.2 Economic outlook

The demand for our services has traditionally been derived largely from the overall condition of the Canadian economy. The weakening U.S. economy and the high Canadian dollar are expected to have an adverse effect on Canada's economy in 2008. Real GDP growth is expected to increase by a weak 1.8% and average about 2.7% annually over the next few years. Inflation will moderate to just below 2% in 2008 and average just over 2% for the next four years. Energy prices are expected to remain high and unstable, leading to the imposition of fuel surcharges, where possible, in order to offset the impact of high fuel costs.

Household formation growth is expected to remain relatively strong in the next few years, but it is forecast to start moderating after 2010, as population growth slows. This, in turn, will slow down the growth in points of delivery (POD), since households account for more than 90% of POD.

The appreciation of the Canadian dollar has had an adverse effect on Canada Post's overall international revenues and these impacts may be more severe in 2008, if the Canadian dollar remains, as expected, near parity with the U.S. currency. The Canadian logistics industry is also feeling the negative effects of the high dollar, as manufacturing shipments to the U.S. stall and cheaper imports replace some locally produced goods. One positive impact of the appreciation of the Canadian dollar has been the increase of online purchases from U.S. suppliers. Canada Post has experienced an increase in parcel deliveries from the U.S. to Canada, as Canadian consumers try to take advantage of lower U.S. prices.

Canada has also been affected by the sub-prime financial crisis, and these developments have also had a negative impact on some of the Corporation's short-term investments. The short-term liquidity problems have also increased the risk associated with corporate bonds, and the spread between government bonds and corporate bonds has widened. This is beneficial to Canada Post, as higher corporate bond yields enhance the solvency of the Corporation's Pension Plan. Nevertheless, there is a risk that a recession in the U.S. could lead to a reduction in long-term interest rates.

Economic outlook

	2008	2009	2010	2011	2012
Economic (% change)					
Real Gross Domestic Product	1.8	2.7	2.8	2.8	2.7
Real Final Domestic Demand	3.2	3.0	3.1	3.2	2.9
Inflation (Consumer Price Index)	1.8	2.2	2.1	2.0	2.2
Prime Lending Rate (%)	5.6	6.0	6.3	6.3	6.3
Demographic (% change)					
Total Population	0.9	0.8	0.8	0.8	0.8
Households	1.5	1.5	1.4	1.3	1.3

Sources:
The economic outlook is based on Statistics Canada data, the December 2007 Canadian Outlook of The Conference Board of Canada, and the December 2007 Global Insight Macro Economic forecast. Forecasts from the major banks were also used for the first two years of the forecast.
The demographic indicators are based on actual data from Statistics Canada and projections from Global Insight and Canada Post.

10.3 Canada Post segment

In addition to general economic factors, our outlook takes into account that competition, already powerful, will intensify across all our businesses as we and our competitors harness the forces of technology, globalization and customer empowerment.

Transaction Mail

Competition in the Transaction Mail line of business was more obvious in 2007, as evidenced by the decrease in physical mail volume. Ongoing modest decline is anticipated in 2008, as mailers continue to adopt electronic alternatives and businesses look for ways to reduce costs through mail consolidation.

Lettermail remains an important element in the suite of options available to the communications market and industry. As organizations provide a more complex range of communication solutions to their own customers, Canada Post's service complement of Lettermail plus epost and other electronic delivery services, along with the SmartFlow Document Management Services suite, becomes more relevant and valuable.

Increasing our connection with Canadians is central to our ability to serve Canadian businesses. In the coming years, we plan to continue expanding our electronic services, giving Canadians the choice of how they receive their mail.

Parcels

We expect to maintain our strategic focus to enhance the customer experience and improve profitability through our attention to modernizing our infrastructure, continued cost efficiencies, and strengthening our integration with customers and consumers.

"Near real time" tracking is the staple of visibility in this marketplace. Plans are in place to improve the timeliness of our scan events, which would match our competitors and fulfill our customers' expectations when using our products and services. We plan to test modern, lightweight, wireless portable data terminals for our vast letter carrier network, which would provide delivery confirmation of small packets in near real time.

The key to our volume and profitable revenue growth is our leadership in the fast-growing business-to-consumer segment. Focused attention on developing solutions to maintain and grow our share with these segments will seed our successful future. Plans are in place to integrate with not only the shipper, but also with the receiver. The development of tools, products and enhanced services to solidify our relationship with both ends of the logistics market is expected to be supported by key marketing activities and modern work methods.

Improved interfaces for data communication and options, such as delivery preferences, expanded pickup options and prepayment of COD and customs fees, among others, will provide a value-added experience with Canada Post. In conjunction with the Canadian Borders Services Agency, our international parcel services aim to improve the visibility of items by enhancing scan events and instituting faster customs clearance processes. With the expected continuation of the strong Canadian dollar and our relatively low share, our strategy is to use The Canada Post Group to provide an easy, reliable and complete end-to-end service through integration with Borderfree™, a service facilitating online shopping from U.S.-based retailers, Purolator and SCI Logistics.

Direct Marketing

We anticipate continued growth for the Direct Marketing line of business in 2008. We believe our core Admail products are well positioned for growth in a context where marketers expect measurability, high return on investment and more personalized communications with their customer base. In 2007, a strong economy, a gradual shift in media mix favouring direct marketing, and the implementation of our plans "to be recognized as the foremost driver of effective, results-proven direct marketing in Canada," all contributed to strong overall revenue growth of 7.0%. This growth, achieved within the overall advertising market which grew approximately 4%, is a strong indication of the growth potential.

In 2008, we will strive to continue generating industry-leading growth by demonstrating to our key customers the impact and effectiveness of direct mail through trial programs inside the customer's marketing mix. We also plan to improve and expand our product offerings to improve marketing effectiveness and marketing return on investment.

10.4 Purolator segment

In 2008, Purolator expects to continue to improve revenues, achieve productivity gains, and increase the diversity of services that have enabled it to be a leading player in the domestic market for shipping and delivery.

Purolator has undertaken a major change in its business with the "Purolator 2010" vision, and continues to make progress in this transformation initiative. These investments in technology and processing capability are expected to help Purolator achieve improved capacity to handle its growing volumes. As well, Purolator Freight is well positioned to manage growth in this important segment of the market.

As Purolator's customers become increasingly sophisticated, Purolator plans to develop a global supply chain services offering to help customers deal with globalization and the gradual disappearance of geographical boundaries.

10.5 Logistics segment

While positioned in a strong and growing logistics outsourcing market, SCI Logistics must grow faster to keep up with the high growth rates achieved by its major competitors that operate in global markets. Management has introduced new measures to increase growth, and the short-term outlook is more positive.

SCI Logistics' long-term growth and sustainability depend on its ability to provide services in markets outside Canada.

10.6 All Other segment

Innovapost will continue to drive improvements to information technology and management across The Canada Post Group. Along with improving its internal capabilities, processes and controls, Innovapost also intends to concentrate on its ability to develop effective, world-leading applications within a process that increasingly meets industry standards for best practices.

HISTORICAL FINANCIAL INFORMATION

(unaudited, in millions of dollars)	**2007**	2006	2005	2004	2003
OPERATIONS					
Revenue from operations	**7,474**	7,264	6,944	6,651	6,344
Cost of operations	**7,346**	7,116	6,681	6,413	6,162
Income from operations	**128**	148	263	238	182
Per cent of revenue from operations	**1.7 %**	2.0 %	3.8 %	3.6 %	2.9 %
Non-operating income	**32**	18	19	3	2
Income before income taxes	**160**	166	282	241	184
Income tax expense (benefit)	**102**	44	80	93	(69)
Net income before non-controlling interest	**58**	122	202	148	253
Non-controlling interest in net income of subsidiaries	**4**	3	3	1	–
Net income	**54**	119	199	147	253
Return on equity of Canada *	**3.8 %**	8.4 %	15.0 %	12.1 %	10.5 %
BALANCE SHEET					
Assets					
Current	**1,385**	1,469	1,466	1,287	1,742
Segregated securities	**632**	469	446	505	443
Capital assets	**1,847**	1,722	1,684	1,743	1,747
Accrued pension benefit asset	**944**	1,010	784	497	374
Other	**343**	314	224	282	252
Total assets	**5,151**	4,984	4,604	4,314	4,558
Liabilities and equity of Canada					
Current	**1,057**	1,170	1,102	1,092	1,596
Accrued pension, other retirement and post-employment benefit liability	**2,513**	2,247	1,973	1,818	1,637
Other liabilities	**120**	115	119	137	143
Non-controlling interest	**22**	19	16	13	12
Equity of Canada	**1,439**	1,433	1,394	1,254	1,170
Total liabilities and equity of Canada	**5,151**	4,984	4,604	4,314	4,558
ACQUISITION OF CAPITAL ASSETS					
Land and buildings	**110**	65	42	48	71
Other capital assets	**220**	240	125	174	180
	330	305	167	222	251

* For 2003, the return on equity of Canada has been adjusted to take into consideration the income tax benefit of $142 million resulting from the curtailment of the employee termination benefit plan.

HISTORICAL FINANCIAL INFORMATION

	2007	% Change	2006	% Change	2005*	% Change	2004	% Change	2003
LINE OF BUSINESS DIMENSIONS									
REVENUE FROM OPERATIONS (unaudited, in millions of dollars/ trading day adjusted per cent)									
Transaction mail									
Domestic mail/mail to foreign postal administrations	**3,100**	**(0.2) %**	3,092	3.5 %	2,987	3.2 %	2,919	2.7 %	2,830
Mail from foreign postal administrations**	**114**	**0.1 %**	114	(4.1) %	119	(9.2) %	132	(9.8) %	146
Canada Post segment	**3,214**	**(0.2) %**	3,206	3.2 %	3,106	2.6 %	3,051	2.1 %	2,976
All other segments	**–**	**(100.0) %**	4	(1.9) %	4	73.6 %	3	9.3 %	2
Elimination of intersegment	**(5)**		(6)		(5)		(7)		(7)
The Canada Post Group	**3,209**	**(0.3) %**	3,204	3.2 %	3,105	2.8 %	3,047	2.1 %	2,971
Parcels									
Domestic mail/mail to foreign postal administrations	**1,092**	**3.3 %**	1,053	(1.0) %	1,063	7.8 %	994	6.7 %	929
Mail from foreign postal administrations**	**134**	**(0.6) %**	134	33.0 %	101	45.7 %	70	11.7 %	62
Canada Post segment	**1,226**	**2.9 %**	1,187	1.9 %	1,164	10.3 %	1,064	7.0 %	991
Purolator segment	**1,448**	**7.1 %**	1,347	7.4 %	1,254	9.3 %	1,156	6.7 %	1,079
Logistics segment	**146**	**8.3 %**	134	(6.1) %	143	5.0 %	137	10.6 %	124
Elimination of intersegment	**(84)**		(61)		(56)		(42)		(37)
The Canada Post Group	**2,736**	**4.6 %**	2,607	4.0 %	2,505	9.1 %	2,315	7.0 %	2,157
Direct marketing									
Addressed Admail™	**621**	**6.1 %**	583	9.9 %	530	4.1 %	513	3.9 %	492
Unaddressed Admail™	**376**	**10.3 %**	339	14.4 %	297	11.4 %	269	9.2 %	245
Publications Mail™	**285**	**3.2 %**	275	4.3 %	263	5.3 %	252	6.7 %	235
Other	**122**	**11.1 %**	110	11.3 %	99	10.6 %	90	4.5 %	86
Canada Post segment	**1,404**	**7.0 %**	1,307	9.9 %	1,189	6.6 %	1,124	5.8 %	1,058
All other segments	**–**	**(100.0) %**	–	(100.0) %	2	(64.6) %	5	857.2 %	1
The Canada Post Group	**1,404**	**7.0 %**	1,307	9.8 %	1,191	6.3 %	1,129	6.2 %	1,059
Other revenue									
Canada Post segment	**111**	**(16.1) %**	131	2.8 %	128	(9.8) %	143	1.3 %	140
All other segments	**175**	**1.2 %**	173	(1.4) %	175	(4.5) %	184	(11.4) %	207
Elimination of intersegment	**(161)**		(158)		(160)		(167)		(190)
The Canada Post Group	**125**	**(14.7) %**	146	2.4 %	143	(9.9) %	160	1.0 %	157
Revenue from operations									
Canada Post segment	**5,955**	**1.7 %**	5,831	4.4 %	5,587	4.7 %	5,382	3.8 %	5,165
Purolator segment	**1,448**	**7.1 %**	1,347	7.4 %	1,254	9.3 %	1,156	6.7 %	1,079
Logistics segment	**146**	**8.3 %**	134	(6.1) %	143	5.0 %	137	10.6 %	124
All other segments	**175**	**(1.4) %**	177	(2.3) %	181	(4.8) %	192	(9.2) %	210
Elimination of intersegment	**(250)**		(225)		(221)		(216)		(234)
The Canada Post Group	**7,474**	**2.5 %**	7,264	4.6 %	6,944	5.3 %	6,651	4.4 %	6,344

HISTORICAL FINANCIAL INFORMATION

	2007	**% Change**	2006	% Change	2005*	% Change	2004	% Change	2003
LINE OF BUSINESS DIMENSIONS									
VOLUME (unaudited, in millions of pieces/ trading day adjusted per cent)									
Transaction mail									
Domestic mail/mail to foreign postal administrations	**5,116**	**(1.3)%**	5,161	0.8 %	5,122	1.3 %	5,099	0.3 %	5,064
Mail from foreign postal administrations**	**290**	**(6.8)%**	310	(6.2)%	331	6.1 %	314	8.9 %	287
Canada Post segment	**5,406**	**(1.6)%**	5,471	0.3 %	5,453	1.5 %	5,413	0.7 %	5,351
Elimination of intersegment	**(7)**		(7)		(7)		(7)		(6)
The Canada Post Group	**5,399**	**(1.6)%**	5,464	0.3 %	5,446	1.5 %	5,406	0.7 %	5,345
Parcels									
Domestic mail/mail to foreign postal administrations	**123**	**(0.2)%**	123	(8.1)%	134	(3.3)%	139	(6.4)%	148
Mail from foreign postal administrations**	**51**	**(2.2)%**	51	135.4 %	22	37.7 %	16	17.4 %	14
Canada Post segment	**174**	**(0.7)%**	174	12.0 %	156	0.9 %	155	(4.4)%	162
Purolator segment	**142**	**1.5 %**	140	0.3 %	139	4.4 %	134	4.2 %	129
Elimination of intersegment	**(2)**		(2)		(2)		(1)		(1)
The Canada Post Group	**314**	**0.1 %**	312	6.4 %	293	2.4 %	288	(0.7)%	290
Direct marketing									
Addressed Admail™	**1,525**	**3.3 %**	1,470	5.0 %	1,400	2.1 %	1,383	0.6 %	1,369
Unaddressed Admail™	**3,940**	**5.4 %**	3,722	9.1 %	3,411	8.1 %	3,180	2.0 %	3,105
Publications Mail™	**535**	**(0.4)%**	536	0.8 %	531	(0.8)%	540	(1.5)%	546
Other	**66**	**9.5 %**	60	(7.4)%	65	(8.2)%	71	10.4 %	64
The Canada Post Group	**6,066**	**4.4 %**	5,788	7.0 %	5,407	5.4 %	5,174	1.4 %	5,084
Total volume									
Canada Post segment	**11,646**	**1.5 %**	11,433	3.8 %	11,016	3.4 %	10,742	1.0 %	10,597
Purolator segment	**142**	**1.5 %**	140	0.3 %	139	4.4 %	134	4.2 %	129
Elimination of intersegment	**(9)**		(9)		(9)		(8)		(7)
The Canada Post Group	**11,779**	**1.5 %**	11,564	3.7 %	11,146	3.4 %	10,868	1.0 %	10,719
EMPLOYMENT ***									
Full-time employees	**61,557**	**0.8 %**	61,064	1.1 %	60,405	(1.6)%	61,409	10.3 %	55,683
Part-time employees	**10,937**	**1.2 %**	10,805	(2.0)%	11,028	(3.8)%	11,465	5.5 %	10,867
Total employees	**72,494**	**0.9 %**	71,869	0.6 %	71,433	(2.0)%	72,874	9.5 %	66,550
MAIL NETWORK									
Post offices	**6,614**	**0.2 %**	6,602	(1.8)%	6,724	(1.0)%	6,795	(0.9)%	6,860
Points of delivery (in thousands)	**14,493**	**1.4 %**	14,293	1.7 %	14,053	1.8 %	13,808	1.9 %	13,548
Pick-up points (in thousands)	**1,015**	**(0.3)%**	1,019	0.1 %	1,018	2.1 %	997	(0.7)%	1,004

* The 2005 Canada Post segment revenues and volumes have been restated to reflect the 2006 change in methodology that now allocates the sales of commemorative stamps to transaction mail and parcels. The % change from 2004 to 2005 on transaction mail without this change is 2.0% and 1.0% for revenues and volumes respectively (no significant impact on parcels).

** In 2005, Canada Post redesigned and increased sampling activity to achieve statistical validity and improved receipt verification reports and processes for international mail settlements. The scope of this initiative was subsequently expanded to include a joint effort with the United States Postal Service (USPS) to modify and improve the processes and procedures governing mail settlement between the two organizations. As a result of this, the inbound mail 2006 values are not comparable to the prior years.

*** Includes paid full-time and part-time employees and excludes temporary, casual and term employees.

ADDITIONAL INFORMATION

The following chart presents the financial ratios over the past five years:

Consolidated Ratios (unaudited)	Policy Framework	**2007**	2006	2005	2004	2003
Profitability						
(1) Return on equity of Canada *	11.0 %	**3.8 %**	8.4 %	15.0 %	12.1 %	10.5 %
(2) Operating profit margin		**1.7 %**	2.0 %	3.8 %	3.6 %	2.9 %
(3) Productivity	97.0 %	**98.3 %**	98.0 %	96.2 %	96.4 %	97.1 %
Leverage						
(4) Total debt to total capital	40.0 %	**4.9 %**	4.9 %	5.8 %	7.8 %	9.6 %
(5) Cash flow to debt		**457.6 %**	364.9 %	246.3 %	(124.0) %	38.4 %
Liquidity						
(6) Current ratio		**1.31**	1.25	1.33	1.18	1.09
(7) Gross interest coverage		**12.47**	14.58	25.62	21.29	14.72
Investment						
(8) Cash flow to capital expenditures		**103.7 %**	87.8 %	127.0 %	(59.2) %	19.0 %
(9) Capital asset investment rate		**5.7 %**	6.7 %	3.5 %	5.1 %	5.9 %
Dividend payout						
(10) Dividend payout ratio	25.0 %	**40.0 %**	40.0 %	40.0 %	40.0 %	25.0 %
Dividend payout ratio once return on equity of Canada ≥ 11%	40.0 %					

* For 2003, the return on equity of Canada has been adjusted to take into consideration the income tax benefit of $142 million resulting from the curtailment of the employee termination benefit plan.

(1) Net income ÷ ((equity of Canada beginning of year + equity of Canada end of year) ÷ 2)
(2) Income from operations ÷ revenue from operations
(3) Cost of operations ÷ revenue from operations
(4) (Total debt + long-term financial obligation) ÷ (total debt + long-term financial obligation + equity of Canada)
(5) Cash flows from operating activities ÷ (total debt + long-term financial obligation)
(6) Current assets ÷ current liabilities
(7) Income from operations ÷ (interest expense + long-term financial expense)
(8) Cash flows from operating activities ÷ cash acquisition of capital assets
(9) (Acquisition of capital assets – proceeds from sale of capital assets) ÷ ((cost of capital assets beginning of year + cost of capital assets end of year) ÷ 2)
(10) Dividend ÷ net income

AUDITORS' REPORT ON ANNUAL COST STUDY CONTRIBUTION ANALYSIS

To the Board of Directors

Canada Post Corporation

We have audited the Annual Cost Study Contribution Analysis of Canada Post Corporation for the year ended December 31, 2007, prepared in accordance with the Cost Methodology described in the notes to the Annual Cost Study Contribution Analysis. This financial information is the responsibility of the Corporation's management and has been prepared using Canada Post Corporation segment revenues and expenses contained in note 22 to the audited consolidated financial statements for the year ended December 31, 2007, and other unaudited operational data extracted from Canada Post Corporation's systems. Our responsibility is limited to expressing an opinion, based on our audit, on the financial information resulting from the application of the Cost Methodology.

We conducted our audit 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 information is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial information. An audit also includes assessing the application of the methodology used and significant estimates made by management, as well as evaluating the overall presentation of the financial information.

We did not perform any audit work on the validity of the methodology nor on Canada Post's operational systems and special studies that yield operational data used to allocate costs to products.

In our opinion:

(a) the Annual Cost Study Contribution Analysis presents fairly, in all material respects, the contribution of services by lines of business and the contribution by exclusive privilege, competitive and concessionary services for the year ended December 31, 2007, in accordance with the Cost Methodology described in the notes to the Annual Cost Study Contribution Analysis, and using Canada Post Corporation segment revenues and expenses contained in note 22 to the audited consolidated financial statements for the year ended December 31, 2007, and other unaudited operational data extracted from Canada Post Corporation's systems; and
(b) using the Cost Methodology described in the notes, Canada Post Corporation did not cross-subsidize its competitive services group by, using revenues protected by exclusive privilege for the year ended December 31, 2007.

PricewaterhouseCoopers LLP

Chartered Accountants, Licensed Public Accountants
Ottawa, Canada
March 27, 2008

ANNUAL COST STUDY CONTRIBUTION ANALYSIS

Canada Post Corporation

As a multi-service firm, Canada Post Corporation employs a common infrastructure to provide its various services in each of the three lines of business in which it operates. Canada Post Corporation has developed over many years, in conjunction with expert accountants and economists, an activity-based, incremental costing methodology that allocates costs among its services. Canada Post Corporation applies this methodology each year in its Annual Cost Study. The Annual Cost Study provides costing data that serves as the basis for ensuring that Canada Post Corporation is not competing unfairly by cross-subsidizing its competitive services with revenues from exclusive privilege services.

The methodology, which is summarized in the notes to the Annual Cost Study Contribution Analysis below, recognizes that some costs are caused by the provision of individual services or groups of services while others are common costs of Canada Post Corporation's infrastructure. Approximately 64% of the total non-consolidated costs of Canada Post Corporation are allocated to the competitive grouping of services in the Annual Cost Study.

As the Annual Cost Study Contribution Analysis indicates, for the year ended December 31, 2007, the competitive grouping of services generated positive long-run incremental contribution. Under the methodology in the Annual Cost Study, a positive long-run incremental contribution for the competitive grouping of services establishes that this grouping of services has not been cross-subsidized using revenues from exclusive privilege services.

Annual Cost Study Contribution Analysis

Year ended December 31, 2007

(in millions of dollars)

I – Long-Run Incremental Contribution by line of business:

	Transaction Mail	Parcels	Direct Marketing	Other	Total
Revenue from operations	$ 3,214	$ 1,226	$ 1,404	$ 111	$ 5,955
Long-run incremental costs	(1,645)	(1,081)	(854)	(105)	(3,685)
Long-run incremental contribution to the fixed costs	**$ 1,569**	**$ 145**	**$ 550**	**$ 6**	**$ 2,270**
	49%	12%	39%	5%	38%
Unallocated fixed costs					(2,243)
Contribution before the under noted items					**$ 27**
Investment and other income					57
Interest and other expense					(6)
Income from the Canada Post segment before income taxes					**$ 78**

II – Long-Run Incremental Contribution of exclusive privilege, competitive, and concessionary services:

	Exclusive Privilege	Competitive	Concessionary	Other	Total
Revenue from operations	$ 3,808	$ 1,742	$ 188	$ 217	$ 5,955
Long-run incremental costs	(2,047)	(1,394)	(182)	(173)	(3,796)
Long-run incremental contribution to the fixed costs	**$ 1,761**	**$ 348**	**$ 6**	**$ 44**	**$ 2,159**
	46%	20%	3%	20%	36%
Unallocated fixed costs					(2,132)
Contribution before the under noted items					**$ 27**
Investment and other income					57
Interest and other expense					(6)
Income from the Canada Post segment before income taxes					**$ 78**

The accompanying notes are an integral part of the Annual Cost Study Contribution Analysis.

NOTES TO ANNUAL COST STUDY CONTRIBUTION ANALYSIS

Year ended December 31, 2007

1. General

The Annual Cost Study calculates the long-run incremental contribution from exclusive privilege services, competitive services and concessionary services. The long-run incremental contribution is defined as the revenues from such services, less their long-run incremental cost.

2. Cost methodology

a) **Long-run incremental cost** • The cost methodology employed by Canada Post Corporation measures the long-run incremental cost of individual services and groups of services according to the current operating plan. Long-run incremental cost is the total annual cost caused by the provision of a service.

b) **Activity base** • Services provided by Canada Post Corporation are analyzed to determine the various activities performed to deliver the services. Each activity is then analyzed to determine the causal relationship between the costs of the activity and the services that require the performance of that particular activity. Service volumes or other data are used to attribute those activity costs to services.

c) **Attribution principles** • The causal relationships between the cost of resources and the activities performed and between the activities performed and the services delivered are identified. Those activity costs, which are incurred because of the provision of a service, are attributed to that service. Costs, which cannot be attributed to the provision of a service, are business sustaining or common fixed costs to more than one service. Where a business sustaining or common fixed cost is specific to a group of services, those activity costs are attributed at that higher level of aggregation. The remaining business sustaining or common fixed costs are "unallocated fixed costs".

d) **Source data** • The source of financial data used in the costing methodology is the Canada Post Corporation general ledger revenues and costs. All Canada Post Corporation costs are categorized either into service attributable, specific fixed or non-attributable activity costs.

   Operational time, volume and weight/cubage data are used to attribute general ledger costs to activities and activity costs to services. Operational volume data is used to determine revenue by services. Where operational data is not available, an appropriate proxy is used to make the attribution.

e) **Reconciliation to financial records** • Total revenues and costs considered in the Annual Cost Study are agreed to the total revenues and expenses forming the Canada Post Corporation segment of the audited consolidated financial statements, which have been reported on by another firm of chartered accountants.

f) **Cross-subsidization test** • Under the Cost Methodology in the Annual Cost Study a positive long-run incremental contribution (revenue exceeds long-run incremental cost) for a line of business, and competitive grouping of services establishes that the grouping of services has not been cross-subsidized using revenues from other services or groups of services.

MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

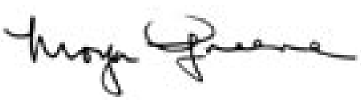
Management is responsible for the consolidated financial statements and all other information presented in this Annual Report. The *Financial Administration Act* and regulations require the consolidated financial statements to be prepared in accordance with Canadian generally accepted accounting principles. Where appropriate, the consolidated financial statements include amounts based on management's best estimates and judgments. Financial information presented elsewhere in this Annual Report is consistent with the consolidated financial statements.

In support of its responsibilities, management established a system of internal controls designed to provide reasonable assurance that assets are safeguarded from loss or unauthorized use and to produce reliable financial information in accordance with the *Financial Administration Act* and regulations, as well as the *Canada Post Corporation Act* and regulations and by-laws of the Corporation. Internal audits examine and evaluate the application of the Corporation's policies and procedures and the adequacy of the system of internal controls.

The Board of Directors has delegated responsibility for oversight of the financial reporting process to the Audit Committee. The Committee acts on behalf of the Board of Directors in fulfilling the Board's responsibilities, which are prescribed by Section 148 of the *Financial Administration Act*. The Audit Committee is entirely constituted of non-executive directors and currently composed of six members who are therefore independent in accordance with the Corporation's standards of independence. The Audit Committee is responsible for reviewing the consolidated financial statements and Annual Report and for meeting with management, internal auditors and external auditors to discuss internal controls over the financial reporting process, auditing matters and financial reporting issues. The Audit Committee meets not less than four times a year, focusing in particular on the areas of financial reporting, risk management and internal control.

The Board of Directors on the recommendation of the Audit Committee approves the consolidated financial statements.

Canada Post Corporation is a Crown corporation included since 1989 in Part II of Schedule III of the *Financial Administration Act*. The Auditor General of Canada and KPMG LLP were appointed as joint auditors of the Corporation for the year ended December 31, 2007, in accordance with the *Financial Administration Act*. The Auditor General and KPMG LLP audit the consolidated financial statements and report to the Audit Committee of the Board of Directors, as well as the Minister of Transport, Infrastructure and Communities.



President and Chief Executive Officer

Chief Financial Officer

March 28, 2008

AUDITORS' REPORT ON THE CONSOLIDATED FINANCIAL STATEMENTS

To the Minister of Transport, Infrastructure and Communities,

We have audited the consolidated balance sheet of Canada Post Corporation as at December 31, 2007 and the consolidated equity of Canada statement, the consolidated income statement and the consolidated cash flow statement for the year then ended. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit 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 Corporation as at December 31, 2007 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles. As required by the *Financial Administration Act*, we report that, in our opinion, except for the changes in accounting policies adopted in the current year as explained in Note 3 to the consolidated financial statements, these principles have been applied on a basis consistent with that of the preceding year.

Further, in our opinion, the transactions of the Corporation and its wholly-owned subsidiaries that have come to our notice during our audit of the consolidated financial statements have, in all significant respects, been in accordance with Part X of the *Financial Administration Act* and regulations, the *Canada Post Corporation Act* and regulations, the by-laws of the Corporation and its wholly-owned subsidiaries and the government directives issued pursuant to section 89 of the *Financial Administration Act*.

Sheila Fraser

Sheila Fraser, FCA
Auditor General of Canada

Ottawa, Canada
March 28, 2008

KPMG LLP

Chartered Accountants, Licensed Public Accountants

CONSOLIDATED BALANCE SHEET

As at December 31 (in millions of dollars)	2007	2006
Assets		
Current assets		
Cash and cash equivalents (note 7)	$ 386	$ 499
Marketable securities (note 7)	309	231
Accounts receivable	592	582
Income tax recoverable	10	4
Prepaid expenses	68	69
Current portion of segregated securities (note 7)	–	21
Current portion of future income tax assets (note 8)	20	63
Total current assets	1,385	1,469
Segregated securities (note 7)	632	469
Capital assets (note 9)	1,847	1,722
Accrued pension benefit asset (note 10)	944	1,010
Future income tax assets (note 8)	203	135
Goodwill (note 11)	124	123
Other assets (note 12)	16	56
Total assets	$ 5,151	$ 4,984
Liabilities and Equity of Canada		
Current liabilities		
Accounts payable and accrued liabilities	$ 446	$ 453
Salaries and benefits payable	374	385
Income tax payable	34	68
Deferred revenue	153	177
Outstanding money orders	47	52
Current portion of long-term debt (note 13)	3	3
Current portion of accrued post-employment benefit liability (note 10)	–	32
Total current liabilities	1,057	1,170
Long-term debt (note 13)	55	58
Accrued pension, other retirement and post-employment benefit liability (note 10)	2,513	2,247
Future income tax liabilities (note 8)	24	19
Other long-term liabilities	41	38
Total liabilities	3,690	3,532
Non-controlling interest	22	19
Equity of Canada	1,439	1,433
Total liabilities and equity of Canada	$ 5,151	$ 4,984

Commitments and contingencies (notes 1 and 16)
Conditional asset retirement obligations (note 14)

The accompanying notes are an integral part of these consolidated financial statements.

Approved on behalf of the Board:

Marc Courtois

Chairman of the Board of Directors

Chairperson of the Audit Committee

CONSOLIDATED EQUITY OF CANADA STATEMENT

Year ended December 31 (in millions of dollars)	**2007**	2006
Contributed capital	**$ 1,155**	$ 1,155
Retained earnings		
Balance, beginning of year	**278**	239
Transition adjustments on adoption of financial instruments standards (note 3)	**(1)**	–
Net income	**54**	119
Dividend (note 15)	**(47)**	(80)
Balance, end of year	**284**	278
Equity of Canada	**$ 1,439**	$ 1,433

The accompanying notes are an integral part of these consolidated financial statements.

CONSOLIDATED INCOME STATEMENT

Year ended December 31 (in millions of dollars)	**2007**	2006
Revenue from operations	**$ 7,474**	$ 7,264
Cost of operations		
Salaries	**3,809**	3,641
Benefits, net of transitional support of $106 million (2006 – $161 million) (note10e)	**960**	1,005
Non-labour collection, processing and delivery	**1,132**	1,049
Facilities	**292**	279
Amortization and impairment	**214**	215
Other	**939**	927
Total cost of operations	**7,346**	7,116
Income from operations	**128**	148
Non-operating income (expense)		
Investment and other income	**42**	29
Interest and other expense	**(10)**	(11)
Total non-operating income	**32**	18
Income before income taxes	**160**	166
Income tax expense (note 8)	**102**	44
Net income before non-controlling interest	**58**	122
Non-controlling interest in net income of subsidiaries	**4**	3
Net income	**$ 54**	$ 119

The accompanying notes are an integral part of these consolidated financial statements.

CONSOLIDATED CASH FLOW STATEMENT

Year ended December 31 (in millions of dollars)	2007	2006
Operating activities		
Net income	**$ 54**	$ 119
Adjustments to reconcile net income to cash provided by operating activities:		
Accrued pension, other retirement and post-employment benefits	**577**	703
Pension, other retirement and post-employment benefit payments	**(277)**	(691)
Transitional support offsetting pension reform incremental costs	**(106)**	(161)
Amortization and impairment	**214**	215
Future income tax benefit	**(23)**	(65)
Gain on sale of capital assets	**(10)**	–
Proceeds from long-term incentive	**7**	14
Other income not affecting cash, net	**–**	(9)
Change in non-cash operating working capital (note 17)	**(94)**	142
Cash provided by operating activities	**342**	267
Investing activities		
Business acquisitions (note 5)	**(14)**	–
Acquisition of securities	**(3,970)**	(2,223)
Proceeds from sale of securities	**3,740**	2,246
Acquisition of capital assets	**(330)**	(305)
Proceeds from sale of capital assets	**61**	4
Other investing activities, net	**2**	–
Cash used in investing activities	**(511)**	(278)
Financing activities		
Transitional support received from the Government of Canada	**106**	131
Repayment of long-term debt	**(4)**	(15)
Dividend paid	**(47)**	(80)
Other financing activities, net	**1**	–
Cash provided by financing activities	**56**	36
Net increase (decrease) in cash and cash equivalents	**(113)**	25
Cash and cash equivalents, beginning of year	**499**	474
Cash and cash equivalents, end of year	**$ 386**	$ 499

The accompanying notes are an integral part of these consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(December 31, 2007)

1. Incorporation, Directives and Corporate Plan

Canada Post Corporation (the "Corporation") was established by the *Canada Post Corporation Act* in 1981 to operate a postal service on a self-sustaining financial basis while providing a standard of service that will meet the needs of the people of Canada. Canada Post Corporation is a Crown corporation included in Part II of Schedule III to the *Financial Administration Act* and is an agent of Her Majesty.

In December 2006, the Corporation was issued two directives pursuant to section 89 of the *Financial Administration Act*.

The Corporation was directed to continue its financial contribution to the Publications Assistance Program until March 31, 2009. This financial contribution shall not exceed $15 million per year (note 20).

The Corporation was also directed to restore and maintain its mail delivery at rural roadside mailboxes that were serviced by the Corporation on September 1, 2005. In 2007, the Corporation continued assessing the safety risks related to all the rural roadside mailboxes, initially focusing on those mailboxes affected by the directive.

As of March 28, 2008, the Corporation's 2007 Corporate Plan had not been approved by the Government of Canada.

2. Significant Accounting Policies

These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles. Canadian generally accepted accounting principles require management to make estimates and assumptions that affect reported amounts and disclosures in the consolidated financial statements and accompanying notes. The significant areas requiring the use of management estimates and assumptions are: useful lives of capital assets; fair value measurement; pension, other retirement and post-employment benefits; income taxes; conditional asset retirement obligations; measuring the impairment of long-lived assets and goodwill; and assessing the resolution of contingent liabilities. Actual results may differ from those estimates.

Certain comparative figures have been reclassified in order to conform to the presentation adopted in 2007.

A summary of the significant accounting policies used in these consolidated financial statements follows:

(a) Consolidation • These consolidated financial statements include the accounts of the Corporation and its subsidiaries, as well as its proportionate share of the accounts of its joint ventures (collectively referred to as "The Canada Post Group"). The results of any subsidiary or joint venture acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate. On January 9, 2007, the Corporation disposed of its joint venture interest in Intelcom Courrier Canada Inc. (Intelcom). The operations of Intelcom were not significant to the Corporation. On March 29, 2007, the name of Progistix-Solutions Inc. was changed to SCI Logistics Inc. As at December 31, 2007, Purolator Courier Ltd (Purolator), SCI Logistics Inc. (SCI Logistics) and Canada Post International Limited (CPIL) are the principal subsidiaries of the Corporation, and Innovapost Inc. (Innovapost) is the only joint venture.

(b) Financial instruments • All financial assets are classified as (i) held for trading, (ii) held to maturity investments, (iii) loans and receivables or (iv) available for sale. All financial liabilities are classified as (i) held for trading or (ii) other financial liabilities. The classification depends on the nature and purpose of the financial instruments and is determined at the time of initial recognition.

2. Significant Accounting Policies (continued)

Financial instruments are recognized at fair value initially; subsequent measurement depends on the classification of the financial instrument. The Canada Post Group's financial instruments consist of the following:

(b.1) All **investments** are financial assets designated as held for trading and, therefore, are measured at fair value when presented on the consolidated balance sheet. Fair value is determined directly by reference to quoted market prices, and may not be realized on sale. If quoted market prices are not available, an appropriate valuation technique is used to determine fair value. Investments are initially recognized at the settlement date and changes in fair value are recognized as they occur. When investments are segregated to manage defined benefit plans, the interest income and gains and losses are recorded in benefit costs, whereas in all other cases, interest income and gains and losses are recorded in investment and other income.

Investments are divided into four categories for separate presentation on the consolidated balance sheet or notes referenced thereto. Each category is defined as follows:

- **Cash equivalents** are highly liquid investments that are readily convertible to known amounts of cash and subject to an insignificant risk of changes in value. Therefore, cash equivalents consist of investments with maturities of three months or less from the date of acquisition.

- **Marketable securities** are investments with initial maturities greater than three months. Marketable securities are classified as current assets since reasonably prompt liquidation is possible.

- **Illiquid securities** are investments that are not traded actively and would be difficult to sell.

- **Segregated securities** are segregated funds invested by the Corporation. Although the liquidity of segregated securities varies, only the portion offsetting a current liability is presented as a current asset.

For the year ended December 31, 2006, investments in money market instruments are recorded at cost whereas investments in bonds are recorded at amortized cost.

(b.2) **Accounts receivable** are financial assets classified as loans and receivables. These financial assets are subsequently measured at amortized cost using the effective interest method, less any impairment. Where the time value of money is not material due to their short-term nature, accounts receivable are carried at the original invoice amount less allowances for doubtful receivables.

(b.3) **Accounts payable and accrued liabilities, salaries and benefits payable** and **outstanding money orders** are classified as other financial liabilities. After initial recognition at fair value, these financial liabilities are measured at amortized cost using the effective interest method. Where the time value of money is not material due to their short-term nature, the financial liabilities are carried at payment or settlement amounts.

(b.4) **Long-term debt** instruments are classified as other financial liabilities and initially recognized at fair value, net of any transaction costs. After initial recognition, long-term debt instruments are measured at amortized cost using the effective interest method. Amortized cost is calculated by taking into account any transaction costs, and any discount or premium on settlement. Interest expense on long-term debt is recognized in interest and other expense.

2. Significant Accounting Policies (continued)

(c) Capital assets • Property, plant and equipment and intangible assets other than goodwill are referred to collectively as capital assets. The carrying value of capital assets is calculated as follows:

(c.1) Cost • Capital assets acquired or developed internally are initially recorded at cost, with the exception of property, plant and equipment transferred from the Government of Canada on incorporation in 1981 that were recorded at their estimated fair value at that date. Fair values of land and buildings were determined by independent appraisals, based on existing use of the land at the time and amortized replacement cost of the buildings. Fair value for other assets was based on amortized replacement cost or original cost less estimated amortization.

(c.2) Amortization • Amortization commences when the assets are placed into service and is recognized over the estimated useful lives of the assets, using the following methods:

Type of asset	Amortization method	Amortization period or rate
Buildings	Straight-line	15, 30 and 40 years
Leasehold improvements	Straight-line	Initial fixed lease term plus period of first renewal option
Plant equipment	Straight-line	5 to 20 years
Vehicles:		
Passenger and light-duty commercial	Declining balance	Annual rate of 30%
Other	Straight-line	3 to 10 years
Sales counters, office furniture and equipment	Straight-line	3 to 20 years
Other equipment	Straight-line	5 to 20 years
Software	Straight-line	3 to 5 years
Customer contracts	Straight-line	Term of contract plus period of renewal options, maximum of 10 years in 2007
Customer relationships	Straight-line	Estimated period of future benefit, based on historical experience and future projections of customer business, maximum of 20 years in 2007

(c.3) Asset retirement obligations • Asset retirement obligations associated with the retirement of property, plant and equipment are recorded when those obligations result from the acquisition, construction, development or normal operation of the assets. The Corporation recognizes asset retirement obligations in the period in which they are incurred if a reasonable estimate of fair value can be determined. The liability is initially measured at fair value, and is subsequently adjusted each period to reflect the passage of time through accretion expense and any changes in the estimated future cash flows underlying the initial fair value measurement. The associated costs are capitalized as part of the carrying value of the related asset and amortized over its remaining life.

(c.4) Impairment • Capital assets that are held for use are reviewed for impairment whenever events or changes in circumstances indicate that their net carrying value may not be recoverable from estimated undiscounted future cash flows generated by their use and eventual disposition. For the purpose of assessing recoverability, capital assets are grouped at the lowest level for which identifiable cash flows are largely independent of cash flows of other assets and liabilities. If it is determined that the net carrying value is not recoverable, an impairment loss is recognized during the year and presented with amortization expense. The impairment loss is equal to the amount by which the net carrying value of the asset exceeds its fair value, determined using the expected present value of future cash flows.

(c.5) Capital assets to be disposed of by sale • Capital assets classified as held for sale are presented separately on the consolidated balance sheet, and recognized at the lower of carrying amount or fair value less disposal costs. A write-down to fair value less disposal costs is recorded as a charge to net income and no further amortization is recorded.

2. Significant Accounting Policies (continued)

(d) Goodwill • Goodwill, arising on the acquisition of a business, represents the excess of the cost of acquisition over The Canada Post Group's interest in the net fair value of the identifiable assets and liabilities of the business recognized at the date of acquisition. Goodwill is initially recognized at cost and is subsequently measured at cost less any accumulated amortization and impairment losses. As of January 1, 2002, goodwill is no longer amortized but is instead tested for impairment annually, or more frequently, if events and circumstances indicate that there may be impairment.

For the purpose of impairment testing, goodwill is allocated to reporting units. Reporting units comprise business operations with similar economic characteristics and may represent either an operating segment or a business unit within an operating segment. Potential impairment is identified when the carrying value of a reporting unit, including the allocated goodwill, exceeds its fair value. Fair value of the reporting unit is determined using the expected present value of future cash flows. Goodwill impairment is measured as the excess of the net carrying value of the reporting unit's allocated goodwill over the implied fair value of the goodwill, based on the fair value of the assets and liabilities of the reporting unit. An impairment loss is recognized in the year in which it is determined.

(e) Revenue recognition • The Canada Post Group's revenue is mostly derived from providing the products and services that comprise the three lines of business: Transaction Mail, Parcels and Direct Marketing. Transaction Mail includes the physical and electronic delivery of bills, invoices, notices and statements. The Parcels line of business includes regular parcels, all expedited delivery and courier services, as well as third-party logistics services. Direct Marketing includes Addressed Admail™, Unaddressed Admail™ and Publications Mail™, such as newspapers and periodicals. Other mail products and services include money orders and postal box rentals, as well as retail and philatelic products.

Revenue is recognized when the service has been rendered, goods have been delivered or work has been completed. Revenue from meter customers, for which services have not been rendered prior to year end, is deferred based on a sampling methodology that closely reflects the meter resetting practices of customers. Likewise, payments received in advance are deferred until services are rendered or products are delivered and customer acceptance given. Deferred revenue is also recorded when resellers are billed for postal products shipments prior to the Corporation rendering the related services to customers.

The Canada Post Group may enter into arrangements with subcontractors to provide services to customers. If The Canada Post Group acts as the principal in such an arrangement, the amount billed to the customer is recognized as revenue. Otherwise, the net amount retained (i.e. the amount billed to the customer less the amount paid to the subcontractor) is recognized as revenue.

When no identifiable and separable benefit is received by The Canada Post Group in return for consideration given to a customer, such as a benefit that might arise in a customer loyalty program, the consideration is recorded as a reduction of revenue rather than as an expense.

(f) Incentive and lease inducement • The incentive received upon signing of a 10 year outsourcing contract in 2002 was deferred, and is being amortized on a straight-line basis over the term of the contract. Lease inducements are also deferred, and are amortized on a straight-line basis over the initial fixed lease term. Amortization of the incentive is presented as reduction of other cost of operations while amortization of the lease inducements is presented as reduction of facilities expense. The current portion of the deferred incentive and lease inducement is presented in deferred revenue, and any remaining unamortized balance is presented in other long-term liabilities.

2. Significant Accounting Policies (continued)

(g) Defined pension, other retirement and post-employment benefit plans • The obligation for providing defined pension, other retirement and employee termination benefit plans is recognized over the period of employee service. However, the obligation for providing workers' compensation benefits and the continuation of certain benefits for employees on long-term disability is recognized when the event triggering the obligation occurs. Therefore, defined benefit plans can be divided into two types as follows:

(g.1) Service-related defined benefit plans • The estimated costs and accrued benefit obligations are determined annually, on an actuarial basis, using the projected benefit method prorated on service. For accounting purposes, accrued benefit obligations and fair value of plan assets are measured annually as at December 31.

The actuarial calculations include management's best estimate of the rates of return on plan assets, inflation, rates of compensation increase, retirement age, rates of employee disability, mortality, growth rates of health care costs and dental costs, as applicable. The expected long-term rates of return on plan assets are based on historical long-term returns provided by various asset categories weighted according to each pension plan's targeted asset allocations. The discount rates used to value the accrued benefit obligations are determined by reference to market conditions at year end, assuming a portfolio of Corporate AA bonds with terms to maturity that, on average, match the terms of the respective accrued benefit obligations.

Defined benefit costs include, as applicable, the estimated cost of employee benefits for current year's service, interest on accrued benefit obligations, expected return on plan assets, gain or loss on curtailment or settlement, expense recognized for special termination benefits and adjustments to allocate actuarial gains (losses), plan amendments, transitional obligation and funding excess to different years consistent with the long-term nature of employee future benefits.

To calculate the expected return on plan assets, these assets are valued at market-related values, whereby actuarial gains (losses) on plan assets for a year are recognized on a straight-line basis over five years.

Actuarial gains (losses) on plan assets for a year arise from the difference between the actual return on plan assets and the expected return. Actuarial gains (losses) on the accrued benefit obligations arise from the differences between actual and expected experience and changes in the assumptions used to determine the accrued benefit obligations. For each plan, the unrecognized net actuarial gain or loss exceeding 10% of the greater of the accrued benefit obligation or the market-related value of plan assets at the beginning of the year is recognized over the average remaining service period of active employees. Actuarial estimates indicate that the average remaining service periods of active employees covered by service-related defined benefit plans are as follows:

As at December 31	**2007**		2006	
	Pension benefit plans	**Other benefit plans**	Pension benefit plans	Other benefit plans
Canada Post Corporation	11 years	5 to 11 years	11 years	9 to 11 years
Purolator	11 to 14 years	N/A	11 to 17 years	N/A
SCI Logistics	15 years	17 years	15 years	17 years
Innovapost	9 years	N/A	11 years	N/A

Past service costs arising from plan amendments are recognized on a straight-line basis over the expected average remaining service period of employees active on the date of amendment, up to the date of full eligibility.

On October 1, 2000, the Corporation assumed responsibility for a defined benefit provincial health insurance premium retirement plan and applied the accounting standards on employee future benefits to this obligation on a prospective basis. The transitional obligation, representing the unrecognized deficit in the plan at that date, is recognized on a straight-line basis over 8 years, being the expected average remaining service period, up to the date of full eligibility, of employees expected to receive benefits as of that date.

2. Significant Accounting Policies (continued)

The funding excess, resulting from the *Federal Public Sector Pension Reform* effective October 1, 2000, represents the excess amount of the assets, transferred from the Government of Canada to the Corporation's pension plan, over the obligations assumed for the defined benefit pension plan. The funding excess is recognized on a straight-line basis over 11 years, being the expected average remaining service period of active employees covered by the pension plan as of that date.

The asset and liability recorded in the consolidated balance sheet represent the cumulative difference between the defined benefit costs and the total cash payments for the defined benefit plans.

(g.2) Event-driven defined benefit plans • The same methodology and assumptions as service-related defined benefit plans apply, except for the following:

- The projected benefit method is not prorated on service since the obligations are recognized when the event triggering the obligation occurs;
- Management's best estimate also takes into account the experience and assumptions of provincial workers' compensation boards;
- Actuarial gains (losses) are recognized over the average duration of the accrued benefit obligation; and
- Actuarial estimates indicate that the average duration of the accrued benefit obligations ranges from 3 to 9 years (2006 – from 3 to 9 years).

(h) Defined contribution and multiemployer pension plans • Defined contribution plan accounting was applied to the multiemployer defined benefit pension plan of CPIL's subsidiary. Employer contributions to the defined contribution and multiemployer pension plans are expensed as incurred.

(i) Transitional support from the Government of Canada • The Government of Canada, as part of the *Federal Public Sector Pension Reform*, committed to provide declining transitional support to assist the Corporation with the incremental costs incurred as a result of establishing the Canada Post Corporation Pension Plan and the associated ancillary benefits. Receipt of the transitional support is conditional on the Corporation maintaining other retirement enhancements similar to those offered to the *Public Service Superannuation Act* participants and, also, the Corporation showing visible commitment and progress towards achieving the financial and service performance objectives set out in the Policy Framework and reflecting them in future corporate plans. Therefore, transitional support is accounted for only when received. The entire amount of transitional support is deferred and drawn down on a first-in, first-out, basis to cover the incremental costs incurred. The draw down from deferred transitional support is recorded as a reduction of expense.

The Corporation is scheduled to receive the remaining $150 million of transitional support over the next three years as follows: $81 million in 2008; $56 million in 2009; and $13 million in 2010.

(j) Income taxes • Future income tax assets and future income tax liabilities are recognized for the tax effect of the difference between the carrying values and tax basis of assets and liabilities. Future income tax assets are recognized for deductible temporary differences, for unused tax losses and income tax reductions to the extent that it is more likely than not that future income tax assets will be realized. Income tax assets and income tax liabilities are measured using substantively enacted income tax rates and income tax laws. These amounts are reassessed each year in the event of changes in income tax rates. Each change resulting from a revaluation is recognized in the financial results of the year of change.

Scientific research and experimental development ("SR&ED") tax credits are recorded using the cost reduction method, whereby the credits are recorded as a reduction of current cost of operations or property, plant and equipment, when there is reasonable assurance that the SR&ED tax credit will be realized.

(k) Foreign currency translation • Transactions in foreign currencies are translated into Canadian dollars at the rate of exchange in effect at the transaction dates. Monetary assets and liabilities denominated in foreign currencies are adjusted to reflect the rates of exchange in effect at the balance sheet date. All exchange gains and losses are included in determining net income for the current year.

3. Changes in Accounting Policies

Financial instruments • Effective January 1, 2007, The Canada Post Group prospectively adopted the Canadian Institute of Chartered Accountants ("CICA") Handbook Section 3855 "Financial Instruments – Recognition and Measurement", Section 3861 "Financial Instruments – Disclosure and Presentation", Section 3865 "Hedges", Section 1530 "Comprehensive Income" and the amendments to Section 3251 "Equity" with no restatement of prior years. These new sections provide standards for recognition, measurement, presentation and disclosure of financial assets, financial liabilities and non-financial derivatives and describe how and when hedge accounting should be applied. Section 1530 provides standards for the reporting and presentation of other comprehensive income.

The Canada Post Group's financial assets and financial liabilities have been classified according to the provisions of these standards, as outlined in note 2(b), and January 1, 2003 was selected as the transition date for embedded derivatives. The adjustments on initial adoption of these new standards have had no material impact on these consolidated financial statements. More specifically, the adjustments resulted in a decrease of $1 million to retained earnings and segregated securities on January 1, 2007.

4. Recent Accounting Pronouncements Requiring Implementation in Future Years

(a) Capital disclosures • In December 2006, the Canadian Institute of Chartered Accountants ("CICA") issued a new accounting standard, Handbook Section 1535 "Capital Disclosures", to converge with recent amendments to International Financial Reporting Standard IAS 1 "Presentation of Financial Statements". This new standard is effective for fiscal years beginning on or after October 1, 2007 although earlier adoption is permitted. Section 1535 requires an entity to disclose information about its objectives, policies and processes for managing capital, quantitative data about what the entity regards as capital, as well as its compliance with any externally imposed capital requirements. The Canada Post Group will adopt this standard in 2008.

(b) Financial instruments disclosures and presentation • The CICA issued Handbook Section 3862 "Financial Instruments – Disclosures" in December 2006. This standard is converged with International Financial Reporting Standard IFRS 7 "Financial Instruments: Disclosures". Section 3862 improves upon the disclosure requirements in existing Handbook Section 3861 "Financial Instruments – Disclosure and Presentation", and places an increased emphasis on risk disclosures compared with Section 3861. Entities are required to provide both qualitative and quantitative information about exposures to risks arising from financial instruments, including credit, interest rate, liquidity, currency and other price risks.

Concurrent with the release of Section 3862, the Accounting Standards Board ("AcSB") issued Handbook Section 3863 "Financial Instruments – Presentation", which carries forward unchanged the presentation requirements of Section 3861 and must be applied at the same time that Section 3862 is adopted.

Sections 3862 and 3863 are effective for annual and interim financial statements relating to fiscal years beginning on or after October 1, 2007, although early adoption is permitted. The Canada Post Group will adopt these standards in 2008.

(c) International Financial Reporting Standards • On February 13, 2008, the AcSB confirmed that use of International Financial Reporting Standards ("IFRS") will be required in 2011 for publicly accountable profit-oriented enterprises. IFRS will replace Canada's current generally accepted accounting principles for listed companies and other profit-oriented enterprises that are responsible to large or diverse groups of stakeholders. Entities will be required to provide comparative IFRS information for 2010 and an opening IFRS consolidated balance sheet at the beginning of 2010. The Canada Post Group has commenced its initial assessment of the impact to its consolidated financial statements of adopting IFRS.

5. Significant Business Acquisitions

On March 30, 2007, a subsidiary of the Corporation, SCI Logistics, acquired all of the outstanding common shares of AMG Logistics Inc., First Team Transport Inc. and Partnership Inc. (collectively referred to as "The AMG Group") for a total cost of $13 million, which was paid in cash. The AMG Group provides logistics and transportation services in the small to medium enterprise market. Goodwill recognized in the transaction amounted to $3 million and was assigned to the Logistics segment (note 11). Intangible assets acquired consist of customer contracts and relationships of $10 million.

6. Regulation of Customer Postage Rates

The Corporation establishes customer postage rates through regulations under the *Canada Post Corporation Act* ("the Act") for domestic Lettermail and international Letter-post items, as well as fees for certain other services such as Registered Mail. These regulations are subject to approval by the Government of Canada, the sole shareholder and, therefore, a related party of the Corporation. The Act permits the Corporation to offer rates that differ from approved rates under certain circumstances, such as when the customer agrees to mail in bulk.

The Act states that regulated postage rates must be fair and reasonable, and consistent so far as possible with providing revenue, together with any revenue from other sources, sufficient to defray the costs incurred by the Corporation in the conduct of its operations under the Act. The domestic basic letter rate prescribed under the *Letter Mail Regulations* is determined by a price-cap formula, which limits increases to 66.67% of increases in the Consumer Price Index, implemented no more than once a year. In January 2007, the domestic Lettermail rate increased by one cent from $0.51 to $0.52 (January 2006 – from $0.50 to $0.51) based on the price-cap formula.

The regulated pricing approval process requires that proposed rate changes be published in the *Canada Gazette* to provide interested persons with 60 days to make representations to the Minister responsible for Canada Post. These representations are considered by the Corporation's Board of Directors. Subsequently, the final form of the proposed rate changes is approved by the Board of Directors and submitted to the Minister responsible for Canada Post for approval by the Government of Canada, specifically the Governor in Council. The rate changes are deemed approved 60 days after submission to the Governor in Council, unless the Governor in Council previously approved or refused to approve the changes.

Under the provisions of the Act, the Corporation is required to provide services free of charge for certain Government mailings and for mailing of materials for the blind. The Government of Canada provides compensation to the Corporation in respect of these services (note 19).

The fact that postage rates for certain products and services are subject to regulation does not affect the application of Canadian generally accepted accounting principles to these consolidated financial statements.

Revenue from products and services charged to customers at regulated rates comprises 33% (2006 – 34%) of the Canada Post segment revenue.

7. Cash and Cash Equivalents, Marketable Securities, Illiquid Securities and Segregated Securities

(a) Nature and extent of investments

The nature and extent of the investments for each category are as follows:

As at December 31 (in millions of dollars)	**Remaining term to maturity***			**2007**	2006
	Within 3 months	**Three to 12 months**	**One to 8 years**	**Total**	Total
Cash and cash equivalents					
Cash	$ 95	$ –	$ –	$ 95	$ 86
Money market instruments issued by:					
Government of Canada	–	–	–	–	4
Provincial governments	92	–	–	92	–
Financial institutions	110	–	–	110	115
Corporations	89	–	–	89	294
Total cash and cash equivalents	**$ 386**	**$ –**	**$ –**	**$ 386**	$ 499
Marketable securities					
Money market instruments issued by:					
Government of Canada	$ 42	$ 221	$ –	$ 263	$ 105
Provincial governments	10	10	–	20	–
Financial institutions	23	–	–	23	53
Corporations	3	–	–	3	73
Total marketable securities	**$ 78**	**$ 231**	**$ –**	**$ 309**	$ 231
Illiquid securities					
Non-bank-sponsored asset-backed commercial paper	**$ –**	**$ –**	**$ 7**	**$ 7**	$ –
Segregated securities					
Money market instruments issued by:					
Government of Canada	$ –	$ 392	$ –	$ 392	$ 45
Provincial governments	27	–	–	27	–
Financial institutions	126	–	–	126	116
Corporations	64	–	–	64	201
Bonds issued by:					
Government of Canada	–	–	–	–	128
Non-bank-sponsored asset-backed commercial paper	–	–	23	23	–
Total segregated securities	217	392	23	632	490
Less current portion	–	–	–	–	21
Segregated securities, non-current	**$ 217**	**$ 392**	**$ 23**	**$ 632**	$ 469

* Remaining term to maturity classifications are based on the contractual maturity of the investments or expected maturities for non-bank-sponsored asset-backed commercial paper.

7. Cash and Cash Equivalents, Marketable Securities, Illiquid Securities and Segregated Securities (continued)

(b) Fair value of non-bank-sponsored asset-backed commercial paper

At December 31, 2007, the Corporation held non-bank-sponsored asset-backed commercial paper ("ABCP") with an original cost and principal amount of $38 million, comprising $18 million in Whitehall Trust Series A and $20 million in Rocket Trust Series A. These investments matured during the months of September and October 2007 but, as a result of liquidity issues in the ABCP market, did not settle on maturity. As a result, the Corporation has classified its ABCP as long-term assets, either in illiquid securities or segregated securities.

On August 16, 2007, an announcement was made by a group representing banks, asset providers and major investors that they had agreed in principle to a long-term proposal and interim agreement to convert the ABCP into pooled long-term floating rate notes maturing no earlier than the scheduled maturity of the underlying assets. On September 6, 2007, the Pan-Canadian Investors Committee for Third-Party Structured Asset-Backed Commercial Paper ("the Committee") consisting of major investors was created to propose a solution to the liquidity problem affecting the ABCP market, and has retained legal and financial advisors to oversee the proposed restructuring process.

Effective March 17, 2008, a court order was put in place that commits investors not to take any action that would precipitate an event of default. It is expected that the restructuring of the ABCP will occur in April or May 2008, if approval by investors is obtained to do so. On December 23, 2007, the Committee provided certain details about the expected restructuring.

The Corporation plans to participate in the Committee's proposed Master Asset Partnership ("MAP") 2 restructuring option, which does not require the investor to participate in the margin funding facility. Participants in MAP 2 will pay an additional fee for the provision of the margin funding facility by third parties. Rocket Trust Series A was assumed to hold 13% of assets that are ineligible for participation in the pooled trusts, due to exposure to U.S. sub-prime assets, and these assets are to be managed independently. It was assumed that 87% of the remaining assets of Rocket Trust Series A, and 85% of Whitehall Trust Series A, would qualify for senior note status within MAP 2, expected to obtain a AAA credit rating. The remaining assets are expected to be unrated subordinated notes within MAP 2.

Since there is no active market for the valuation of ABCP, the fair value of the Corporation's investment in ABCP was determined using a valuation technique. The principal amount of the investments was discounted for certain factors related to underlying assets of the original investments, and the terms and conditions which may apply to the restructured investments. General market observations, prices and rates were used in developing the discount assumptions. The discount ranges considered by the Corporation for the valuation within MAP 2 are as follows:

Restructured / ineligible assets	Discount rate range
Ineligible assets	45% – 55%
Senior notes	7% – 13%
Subordinated notes	30% – 43%

The total adjustment to the Corporation's ABCP at December 31, 2007 reflecting the assumptions above is between $5 million and $8 million. To adequately reflect the uncertainty associated with the assumptions, the more conservative assessment of $8 million was applied, resulting in a fair value of ABCP at December 31, 2007 of $30 million.

Continuing uncertainties regarding the value of the assets that underlie the ABCP, the credit and liquidity risks associated with the restructured notes and the final outcome of the restructuring process, could give rise to further changes in the fair value of the Corporation's investment in ABCP, although this would not result in a significant impact on the Corporation's future earnings.

7. Cash and Cash Equivalents, Marketable Securities, Illiquid Securities and Segregated Securities (continued)

(c) Risk management and interest rates

Investments are held for liquidity purposes, or for longer terms, to achieve the highest possible rate of return in the long-term consistent with the investment policies approved by the Board of Directors. Liquidity and credit risks are mitigated by way of differing investment maturity dates, placement with issuers who meet specific investment criteria and the imposition of dollar limits by financial product type and debt issuer. Investments in financial institutions and corporations have a minimum rating of R1 low.

All investments held as at December 31, 2007 were issued by Canadian entities at fixed interest rates or discounted values. The weighted average effective interest rate as at December 31, 2007 was 4.4% for money market instruments (2006 – 4.3% for money market instruments and 3.7% for bonds)

(d) Income from investments

Interest income and gains and losses on cash and cash equivalents, marketable and illiquid securities amounted to $26 million (2006 – $26 million). Interest income and gains and losses on segregated securities amounted to $18 million (2006 – $20 million). The portion of income relating to the defined benefit plans was $16 million (2006 – $20 million) and was used to offset benefit costs. The remaining $2 million relates to internally restricted funds and was recognized in investment and other income.

(e) Segregated securities

Funds have been segregated for the following purposes:

As at December 31 (in millions of dollars)	**2007**	2006
Employee termination benefits	$ –	$ 21
Other retirement dental and life insurance benefits	497	469
Internally restricted funds	135	–
Total segregated securities	**$ 632**	$ 490

Funds were segregated either to conform with externally imposed restrictions or in anticipation of future cash flow requirements as explained below:

– External restrictions were imposed on other retirement dental and life insurance benefit plans repatriated through the *Federal Public Sector Pension Reform*. These defined benefit plans are partially funded by the transitional support and, therefore, the Corporation is obligated to use these funds exclusively for related benefit payments.

– In 2007, the Corporation decided to segregate certain funds in anticipation of future cash flow requirements. These new segregated funds would be used either for significant projects to renew the future operational capability of the Corporation or required regulatory contributions to the Corporation's pension plan in the event of either a solvency or going-concern shortfall.

8. Income Taxes

On March 27, 1994, the Corporation became a prescribed Crown corporation for tax purposes and, as such, is subject to federal income taxation under the *Income Tax Act*. The Corporation's subsidiaries and joint ventures are subject to federal and provincial income taxes.

The sources of the temporary differences giving rise to net future income tax assets (liabilities) are as follows:

As at December 31 (in millions of dollars)	**2007**	2006
Net future income tax assets		
Capital assets	$ 13	$ 29
Salaries and benefits payable	15	20
Accrued pension, other retirement and post-employment benefits	148	84
Recognition of losses carried forward	–	28
Other	23	18
Net future income tax assets	**$ 199**	$ 179
Presented in the consolidated balance sheet as:		
Future income tax assets:		
Current	$ 20	$ 63
Long-term	203	135
Total future income tax assets	223	198
Future income tax liabilities:		
Long-term	(24)	(19)
Net future income tax assets	**$ 199**	$ 179

Deductible temporary differences for which no future income tax assets have been recognized amount to $780 million (2006 – $772 million) and relate mainly to the accrued other retirement and post-employment benefit liability. These differences are not expected to reverse in the foreseeable future.

8. Income Taxes (continued)

The major components of the income tax expense are as follows:

Year ended December 31 (in millions of dollars)	**2007**	2006
Current income tax expense	$ 125	$ 109
Future income tax expense (benefit) relating to:		
Origination and reversal of temporary differences	(42)	(50)
Previously unrecognized losses carried forward	–	(22)
Reduction in tax rate	19	7
Income tax expense	**$ 102**	$ 44

A reconciliation of the income tax expense, related to income before income taxes, to the amount of income tax using the statutory federal tax rate follows:

Year ended December 31 (in millions of dollars)	**2007**	2006
Income before income taxes	$ 160	$ 166
Federal income taxes at parent's statutory tax rate	$ 52	$ 54
Subsidiaries and joint ventures' provincial income taxes less federal tax abatement	3	4
(Increase) decrease in future income taxes resulting from:		
Previously unrecognized losses carried forward	–	(22)
Reduction in future tax rate	40	11
Other	7	(3)
Income tax expense	**$ 102**	$ 44

9. Capital Assets

As at December 31 (in millions of dollars)			**2007**			2006
	Cost	**Accumulated amortization and impairment**	**Net carrying value**	Cost	Accumulated amortization and impairment	Net carrying value
Property, plant and equipment						
Land	$ 214	$ –	$ 214	$ 198	$ –	$ 198
Buildings	1,718	971	747	1,641	935	706
Leasehold improvements	185	123	62	164	115	49
Plant equipment	907	680	227	862	657	205
Vehicles	215	133	82	211	115	96
Sales counters, office furniture and equipment	346	278	68	374	322	52
Other equipment	739	447	292	687	420	267
Assets under development	10	–	10	48	–	48
Total property, plant and equipment	4,334	2,632	1,702	4,185	2,564	1,621
Intangible assets						
Software	382	290	92	322	269	53
Software under development	42	–	42	38	–	38
Customer contracts and relationships	27	16	11	29	19	10
Total intangible assets	451	306	145	389	288	101
Total capital assets	**$ 4,785**	**$ 2,938**	**$ 1,847**	$ 4,574	$ 2,852	$ 1,722

Amortization of property, plant and equipment amounted to $172 million in 2007 (2006 – $161 million) while amortization of intangible assets amounted to $34 million (2006 – $54 million). In 2007, the Corporation recorded a $5 million impairment charge for customer contracts related to epost.

During the year, The Canada Post Group invested $330 million (2006 – $305 million) in capital assets, comprising $257 million (2006 – $269 million) of property, plant and equipment and $73 million (2006 – $36 million) of intangible assets.

10. Pension, Other Retirement and Post-Employment Benefit Plans

(a) Description of benefit plans

The Corporation has a number of funded and unfunded defined benefit plans that provide pension, other retirement and post-employment benefits for most of its employees. Unfunded plans are plans where benefits are paid directly by the Corporation. With funded plans, funds are transferred to external trusts and the benefits are paid directly from these trusts. The Corporation's defined benefit pension plan is a funded plan based on length of pensionable service, the average of the best five consecutive years of pensionable salary and retirement age. The plan provides for retirement pension, survivor's pension or a refund after termination of employment or death. Pension benefits are covered by the registered pension plan and the retirement compensation arrangement, for benefits in excess of statutory limits as defined under the *Income Tax Act*. Pension benefits in pay are indexed annually. Both the Corporation's contributions and the employees' contributions to the external trusts are made in accordance with the provisions of the plan. In addition, the Corporation's contributions are determined by actuarial valuations, in compliance with the requirements of regulatory authorities, to ensure that the external trusts have sufficient assets to pay pension benefits when employees retire.

Other retirement defined benefit plans include unfunded health care, dental and life insurance plans. The post-employment defined benefit plans include unfunded employee termination benefits and health and dental coverage for employees receiving long-term disability benefits. The benefit costs covered by the Corporation and the costs assumed by employees and retirees are determined in accordance with the rules of each plan and the provisions of labour contracts.

By the end of 2006, the Corporation's employee termination benefit plan was fully curtailed. The curtailment of the plan froze the employees' entitlement based on the accumulation of years of service as of the curtailment date, and further benefit entitlements based on years of service was discontinued. On curtailment, employees were given the option of settlement by receiving the cash value of their accrued termination benefit or the option of deferring receipt of their benefit until departure, at which time the benefit would reflect their base salary at retirement or their base salary at the curtailment date if they resign or are terminated. Most employees chose the option of settlement. The settlement payments were made for the members of each bargaining group, and non-union employees, at different times during the last four years, resulting in a settlement loss being recognized in each year from 2004 to 2007. In 2007, the settlement loss was $9 million (2006 – $6 million).

The Corporation is subject to the *Government Employees Compensation Act* and, therefore, is not mandatorily covered under any provincial workers' compensation act. The Corporation is a self-insured employer, responsible for workers' compensation benefits incurred since incorporation. The Corporation's unfunded obligation for workers' compensation benefits is based on known awarded disability and survivor pensions and other potential future awards for accidents that occurred up to the measurement date. Workers' compensation benefits are provided according to the respective provincial workers' compensation legislation. Benefit entitlements in the three Territories are based on the Alberta legislation.

Purolator has a number of funded defined benefit pension plans. The defined benefit plans are based either on length of pensionable service and salary paid each year or on negotiated benefit rates, depending on the type of employees. Since these defined benefit plans are subject to the maximum pension payable under the *Income Tax Act*, a supplementary pension plan, based on length of pensionable service and final average salary, is offered to designated employees. Purolator also provides pension benefits to eligible employees through a defined contribution plan. Plan members are not required nor permitted to contribute to any of the pension plans.

10. Pension, Other Retirement and Post-Employment Benefit Plans (continued)

CPIL's subsidiary participates in a multiemployer defined benefit pension plan. According to the concession agreement (described in note 16 (c)), the Government of the Netherlands Antilles is responsible for all pension benefits accrued prior to May 2003.

Certain employees of SCI Logistics presently belong to a pension plan sponsored by SCI Logistics' former owner, Bell Canada. The BCE Inc. Pension Plan is a non-contributory, defined benefit pension plan that provides for benefits based on length of pensionable service and final average salary. Pension benefits in pay are indexed annually. The assets of the pension plan are invested in units of the BCE Master Trust Fund with Royal Trust acting as trustee. However, in 2001 the Corporation entered into a Share Purchase Agreement with Bell Canada whereby the employees of SCI Logistics started participating in a new pension plan, disengaged from Bell Canada. The pension plan assets and liabilities for pensions and related benefits accrued at the date of change of ownership will be transferred to the new pension plan on completion of the related actuarial valuations, pending regulatory approval. The amounts of assets and liabilities included in these consolidated financial statements represent current estimates of the amounts to be transferred to the new Pension Plan, adjusted for all activity subsequent to the change of ownership. The estimate of the transfer amount relating to plan assets includes management's best estimate of the effect of certain events related to the BCE Inc. Pension Plan that occurred prior to the purchase of SCI Logistics by the Corporation. The estimate was revised in 2007 based on a report provided by BCE Corporate Services. The amounts to be transferred into the new, separate Pension Plan will be finalized and transferred over only when regulatory approval has been obtained. In 2005, a supplementary pension plan was created for designated employees to replace the current plan, whereby employees that reach the maximum pension payable from the registered plan would receive the excess pension payable by SCI Logistics. The results for this plan are included with those of the regular plan. After the acquisition, a defined contribution provision was added to SCI Logistics' pension plan.

The other retirement benefit plans pertaining to SCI Logistics' employees consist of medical and dental benefits, and life insurance after retirement. SCI Logistics pays the full cost of these benefits, except for the dental plan which is paid 100% by the retirees who choose this coverage.

Innovapost has a funded defined benefit pension plan. Like the Corporation, pension benefits that are not permissible in the registered pension plan are provided by a retirement compensation arrangement. Pension benefits, based on length of pensionable service and average pensionable salary, are indexed according to the annual increase in the consumer price index. Employer and employees' contributions are made in accordance with the plan. After October 31, 2002, no new members are eligible to join Innovapost's pension plan.

10. Pension, Other Retirement and Post-Employment Benefit Plans (continued)

(b) Obligations and assets

A reconciliation of the defined benefit plan obligations, defined benefit plan assets and the funded status of the defined benefit plans to the amounts recorded in the consolidated balance sheet follows:

Year ended, and as at, December 31 (in millions of dollars)	2007		2006	
	Pension benefit plans	**Other benefit plans**	Pension benefit plans	Other benefit plans
Accrued benefit obligations				
Balance, beginning of year	$ 13,729	$ 3,327	$ 13,079	$ 3,260
Current service cost	449	111	464	110
Interest cost	736	176	677	165
Employee contributions	183	–	161	–
Benefits paid	(324)	(133)	(259)	(130)
Actuarial gains	(564)	(149)	(402)	(63)
Plan amendments	–	(119)	2	(17)
Corporate restructuring giving rise to special termination benefits	–	–	7	–
Curtailment	(1)	–	–	–
Settlement	–	2	–	2
Balance, end of year	14,208	3,215	13,729	3,327
Plan assets				
Fair value, beginning of year	14,928	–	12,675	–
Reduction in estimated amount of surplus transfer from BCE Inc.	(11)	–	–	–
Actual return on plan assets	263	–	1,792	–
Employer regular contributions	129	–	255	–
Employer special solvency contributions	12	–	304	–
Employee contributions	183	–	161	–
Benefits paid	(324)	–	(259)	–
Fair value, end of year	15,180	–	14,928	–
Funded status of defined benefit plans – surplus (deficit)	972	(3,215)	1,199	(3,327)
Unrecognized net actuarial (gain) loss	63	904	(64)	1,139
Unrecognized past service costs (credits)	16	(190)	17	(86)
Unrecognized transitional obligation	–	3	–	7
Unrecognized funding excess	(121)	–	(153)	–
Net amount recognized for:				
Defined benefit plans	930	(2,498)	999	(2,267)
Defined contribution plans	(1)	–	(1)	–
Total amount recognized	**$ 929**	**$ (2,498)**	$ 998	$ (2,267)
Presented in the consolidated balance sheet as:				
Accrued pension benefit asset	$ 944	$ –	$ 1,010	$ –
Current portion of accrued post-employment benefit liability	–	–	–	(32)
Accrued pension, other retirement and post-employment benefit liability	(15)	(2,498)	(12)	(2,235)
Total amount presented	**$ 929**	**$ (2,498)**	$ 998	$ (2,267)

10. Pension, Other Retirement and Post-Employment Benefit Plans *(continued)*

(c) Benefit plans in a deficit position

Included in the above accrued benefit obligations and fair value of plan assets at year end are the following amounts with respect to plans that are in a deficit position:

As at December 31 (in millions of dollars)	**2007**		2006	
	Pension benefit plans	**Other benefit plans**	Pension benefit plans	Other benefit plans
Accrued benefit obligations	**$ 323**	**$ 3,215**	$ 331	$ 3,327
Plan assets	**273**	**–**	273	–
Funded status of defined benefit plans – deficit	**$ (50)**	**$ (3,215)**	$ (58)	$ (3,327)

(d) Investment objective and plan asset allocations

The Board of Directors of the Corporation adopts and reviews at least annually a Statement of Investment Policies and Procedures (SIPP) addressing the manner in which the Corporation's pension plan assets will be invested. Investment principles and beliefs are revisited periodically to ensure that changes to the investment policies may be made if warranted. The Corporation believes that an investment portfolio with an appropriate asset allocation, the target portfolio, can over the long-term achieve the investment objective of ensuring that sufficient assets will be available to meet the obligations of the pension plan as they come due. Under the current SIPP, it is recognized that it is not always desirable to have the investment portfolio exactly match the long-term asset target allocation and therefore minimum and maximum asset category limits have been established.

The Corporation's investment objective for its pension plan assets is to achieve a long-term rate of return, net of administrative expenses, which exceeds inflation by at least 4.5%. Investments are made according to criteria and limitations set by the Board of Directors and applicable legislation. Allowable types of investment, individual investment limits, portfolio investment limits, maturity limits and minimum credit quality ratings are set by the Board to reduce the level of risk and provide diversification between industry sectors, geographic/economic areas and management styles. The asset allocations, by asset category, of the Corporation's pension plan are as follows:

As at December 31		**2007**	2006
	Target	**Actual**	Actual
Cash and money market instruments	**1 %**	**5 %**	5 %
Bonds	**36 %**	**30 %**	27 %
Canadian equities	**24 %**	**28 %**	29 %
U.S. equities	**20 %**	**16 %**	19 %
International equities	**15 %**	**17 %**	18 %
Real estate	**3 %**	**3 %**	1 %
Other assets less liabilities	**1 %**	**1 %**	1 %
Pension plan assets of the Corporation	**100 %**	**100 %**	100 %

The pension plan assets of Purolator, SCI Logistics and Innovapost are governed by similar investment objectives and policies and account for 2% (2006 – 2%) of the total plan assets of $15,180 million (2006 – $14,928 million).

Total plan assets include $2,147 million (2006 – $2,146 million) in money market instruments and bonds issued by the Government of Canada, its agencies and other Crown corporations and $112 million (2006 – $121 million) in refundable taxes held by the Canada Revenue Agency.

10. Pension, Other Retirement and Post-Employment Benefit Plans (continued)

(e) Costs

The elements of employee future benefit costs recognized in the year are as follows:

Year ended December 31 (in millions of dollars)	2007			2006		
	Incurred in year	**Adjustments***	**Recognized in year**	Incurred in year	Adjustments*	Recognized in year
Pension benefit plans						
Current service cost	$ 449	$ –	$ 449	$ 464	$ –	$ 464
Interest cost	736	–	736	677	–	677
Return on plan assets	(263)	(683)	(946)	(1,792)	948	(844)
Actuarial (gains) losses on accrued benefit obligations	(564)	567	3	(402)	470	68
Plan amendments	–	1	1	2	–	2
Curtailment gain	(1)	–	(1)	–	–	–
Special termination benefits	–	–	–	7	–	7
Amortization of funding excess	–	(32)	(32)	–	(32)	(32)
Defined benefit costs	357	(147)	210	(1,044)	1,386	342
Defined contribution costs	2	–	2	1	–	1
Multiemployer defined benefit costs	1	–	1	1	–	1
Total pension benefit costs	360	(147)	213	(1,042)	1,386	344
Transitional support from the Government of Canada	(63)	–	(63)	(120)	–	(120)
Net pension benefit costs	**$ 297**	**$ (147)**	**$ 150**	$ (1,162)	$ 1,386	$ 224
Other benefit plans						
Current service cost	$ 111	$ –	$ 111	$ 110	$ –	$ 110
Interest cost	176	–	176	165	–	165
Actuarial (gains) losses on accrued benefit obligations	(149)	228	79	(63)	150	87
Plan amendments	(119)	104	(15)	(17)	4	(13)
Settlement loss	9	–	9	6	–	6
Amortization of transitional obligation	–	4	4	–	4	4
Defined benefit costs	28	336	364	201	158	359
Return on segregated securities	(16)	–	(16)	(20)	–	(20)
Transitional support from the Government of Canada	(43)	–	(43)	(41)	–	(41)
Net other benefit costs	**$ (31)**	**$ 336**	**$ 305**	$ 140	$ 158	$ 298

* Adjustments to allocate costs to different years so as to recognize the long-term nature of employee future benefits.

10. Pension, Other Retirement and Post-Employment Benefit Plans (continued)

(f) Assumptions

The assumptions used in measuring the costs and accrued benefit obligations for the Corporation's significant defined benefit plans were as follows:

As at December 31	**2007**		2006	
	Pension benefit plans	**Other benefit plans**	Pension benefit plans	Other benefit plans
Accrued benefit obligations:				
Discount rate	5.6%	5.5%	5.3%	5.3%
Long-term rate of compensation increase	3.0%	3.0%	3.0%	3.0%
Benefit costs:				
Discount rate	5.3%	5.3%	5.1%	5.1%
Expected long-term rate of return on plan assets	7.0%	N/A	7.0%	N/A
Long-term rate of compensation increase	3.0%	3.0%	3.0%	3.0%
Assumed health care cost trend rates:				
Initial health care cost trend rate	N/A	8.8%	N/A	8.9%
Cost trend rate declines to	N/A	5.3%	N/A	5.3%
Year that the rate reaches the rate it is assumed to remain at	N/A	year 10	N/A	year 10

(g) 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 had the following effects for 2007:

(in millions of dollars)	**Increase**	**Decrease**
Total of current service and interest costs	**$ 53**	**$ (40)**
Accrued benefit obligations	**$ 533**	**$ (409)**

The above sensitivities are hypothetical and must be used with caution. Changes in amounts based on a one-percentage-point variation in assumptions generally cannot be extrapolated because the relationship of the change in assumption to the change in amounts may not be linear. The sensitivities have been calculated independently of changes in other key assumptions. Changes in one factor may result in changes in another, which could amplify or reduce certain sensitivities.

10. Pension, Other Retirement and Post-Employment Benefit Plans (continued)

(h) Total cash payments

Cash payments for pension, other retirement and post-employment benefits are as follows:

Year ended December 31 (in millions of dollars)	**2007**	2006
Benefits paid directly to beneficiaries for unfunded other benefit plans	$ 133	$ 130
Employer regular contributions to funded pension benefit plans	129	255
Employer special solvency contributions to funded pension benefit plans	12	304
Total cash payments for defined benefit plans	274	689
Contributions to defined contribution plans	2	1
Contributions to multiemployer defined benefit plan	1	1
Total cash payments	**$ 277**	$ 691

The actuarial valuations of the defined benefit pension plans for funding purposes are conducted at least on a triennial basis and annually when a solvency or going-concern shortfall has occurred. At the end of 2006, the Corporation's pension plan solvency shortfall was eliminated. As the surplus position of the Corporation's pension plan continued to increase in the first half of 2007, both on a solvency and going-concern basis, the Corporation took a contribution holiday for the second half of the year, as permitted under the *Pension Benefits Standards Act*. The most recent actuarial valuations for funding purposes, and the next required actuarial valuations, are as of the following dates:

	Most recent actuarial valuation for funding purposes	**Next required actuarial valuation for funding purposes**
Canada Post Corporation	December 31, 2006	December 31, 2009
Purolator	December 31, 2006	December 31, 2007
SCI Logistics	December 31, 2006	December 31, 2009
Innovapost	December 31, 2004	December 31, 2007

11. Goodwill

The changes in the carrying amount of goodwill are as follows:

Year ended December 31 (in millions of dollars)				**2007**	2006
	Canada Post segment	**Purolator segment**	**Logistics segment**	**Total**	Total
Balance, beginning of year	$ 3	$ 120	$ –	$ 123	$ 123
Acquisition	–	1	3	4	–
Impairment	(3)	–	–	(3)	–
Balance, end of year	**$ –**	**$ 121**	**$ 3**	**$ 124**	$ 123

In 2007, the Corporation recorded a $3 million impairment charge, which represented all the goodwill related to epost.

12. Other Assets

As at December 31 (in millions of dollars)	**2007**	2006
Assets held for sale	$ 2	$ 48
Illiquid securities (note 7)	7	–
Other	7	8
Total other assets	**$ 16**	$ 56

The Corporation has classified one property as held for sale at the end of 2007. It is anticipated that the carrying amount of the property will be fully recovered through the sale proceeds. The two properties held for sale at the end of 2006 were sold during the year as anticipated. A gain of $8 million was recorded on the dispositions.

13. Long-Term Debt

As at December 31 (in millions of dollars)	**2007**		2006	
	Fair value	**Carrying value**	Fair value	Carrying value
Non-redeemable bonds maturing March 2016, interest at 10.35% payable semi-annually on March 15 and September 15	$ 78	$ 55	$ 80	$ 55
Notes due to BCE Emergis Inc., plus accrued interest at the Bank of Canada overnight rate plus 1%, maturing in December 2008	3	3	6	6
Total long-term debt	81	58	86	61
Less current portion	3	3	3	3
Long-term portion	**$ 78**	**$ 55**	83	$ 58

Fair value of long-term bonds is estimated by reference to quoted market prices of similar bonds. The carrying amount of the other long-term debt instrument approximates its fair value as it is expected to be settled within one year.

The effective interest rate as at December 31, 2007 was 10.5% for the non-redeemable bonds and 4.8% for the notes due to BCE Emergis Inc. Interest expense on long-term debt amounted to $6 million (2006 – $6 million).

The scheduled long-term debt repayments are as follows:

(in millions of dollars)	
2008	$ 3
2016	55
Total long-term debt	**$ 58**

14. Conditional Asset Retirement Obligations

Certain of the Corporation's owned buildings have asbestos-containing materials which the Corporation will be obligated to remove and dispose of in a special manner should the property undergo major renovations or demolition. As a result of the longevity of the Corporation's buildings where asbestos exists, ongoing asbestos management programs, and the fact that the Corporation does not have plans for major changes that would require the removal of asbestos, the timing of the removal of the asbestos is indeterminable. Consequently, as of December 31, 2007, the Corporation does not have sufficient information to reasonably estimate the fair value of conditional asset retirement obligations related to asbestos. Similarly, the fair value of conditional asset retirement obligations associated with site restoration after permanent removal of a community mailbox from a location is not reasonably estimable due to indeterminate settlement dates.

The Corporation will continue to assess its ability to estimate the fair values of its asset retirement obligations at each future reporting date. The related liability will be recognized when sufficient additional information becomes available for a particular asset.

15. Equity of Canada

The *Canada Post Corporation Act* provides for the establishment of a share capital structure. The Corporation is authorized to issue shares to the Government of Canada based on the net asset value of the Corporation on the date of the first issue of shares, as determined by the Board of Directors, with the approval of the Treasury Board. No such shares have been issued.

On May 17, 2007, a dividend of $47 million was paid to the Government of Canada. In May 2006, the dividend paid was $80 million. In respect of the current year, the directors declared that a dividend of $22 million will be paid to the Government of Canada on May 15, 2008. This dividend was approved by the Board of Directors on March 28, 2008 and has not been included as a liability in these consolidated financial statements. The dividend is based on the rate established in the Policy Framework. The Policy Framework, developed in collaboration with the Government of Canada and announced in January 1999, established service, productivity and financial performance targets for the Corporation.

16. Commitments and Contingencies

(a) Two complaints have been filed with the Canadian Human Rights Commission ("the Commission") alleging discrimination by the Corporation concerning work of equal value.

One complaint was filed by the Public Service Alliance of Canada ("PSAC") in 1983, retroactive to October 16, 1981, when Canada Post Corporation became a Crown corporation. The Commission referred the complaint to the Canadian Human Rights Tribunal ("the Tribunal") in 1992. The Tribunal rendered its decision on October 7, 2005, concluding that the Corporation had participated in "systemic discrimination" in the setting of wages for a group of PSAC members contrary to Section 11 of the *Canadian Human Rights Act*.

The Corporation appealed the decision of the Tribunal to the Federal Court Trial Division on October 7, 2005, claiming that the Tribunal had not only incorrectly applied and interpreted the law, but had also reached its conclusions in the face of substantial evidence that there had been no violation of Section 11 of the *Canadian Human Rights Act*.

On November 18, 2005, PSAC commenced its own appeal in the Federal Court against the decision.

The appeals were heard in the Federal Court Trial Division in November 2007 and January 2008. On February 21, 2008, the Federal Court Trial Division released its decision allowing Canada Post Corporation's application for judicial review setting aside the decision of the Tribunal and referred the complaint back to the Tribunal with the direction that the complaint be dismissed as not substantiated according to the legal standard of proof. PSAC's appeal against the decision of the Tribunal was dismissed.

On March 18, 2008, PSAC appealed the decision of the Federal Court Trial Division to the Federal Court of Appeal. On March 25, 2008, the Commission also appealed this decision to the Federal Court of Appeal.

Another complaint was filed by the Canadian Postmasters and Assistants Association initially in December 1982, seeking retroactivity to October 16, 1981. In December 1991, the Commission decided not to deal with the complaint. This complaint was refiled in November 1992. The Commission did not fully investigate the complaint. It did attempt to mediate/conciliate a resolution to the complaint without success. On February 28, 2006, the most recent conciliator recommended to the Commission that the Commission decline to deal with the complaint at this time because the complaint is one that could more appropriately be dealt with under the *Canada Labour Code*.

The outcome of these complaints is not currently determinable and as a result no provision has been recorded in the consolidated financial statements. Settlement, if any, arising from resolution of these matters, is presently planned to be recovered in future postal rates (as determined in accordance with the *Canada Post Corporation Act*) and/or from the Government of Canada.

(b) The Corporation and Purolator have made certain commitments that apply upon expiration or termination of certain agreements with Innovapost. These agreements were signed for a 10 year period that commenced in 2002, with an optional renewal period of five years. The Corporation and Purolator have agreed to purchase the assets, used on a dedicated basis at the time of expiration or termination of the agreements, for an amount equal to net book value and shall be required to assume certain obligations related to the purchase of these assets. In addition, on expiration or termination of the agreements, Innovapost shall have the obligation to transfer or assign to the Corporation or Purolator any contract applicable to the services provided to the Corporation or Purolator, respectively; however, should Purolator terminate its agreement for a specific event, as described in the agreement, it has the option to reject the transfer or assignment of these contracts. It is not practicable, at this time, to determine the value of assets used on a dedicated basis, nor the carrying value of the contractual obligations, at the time of expiration or termination of the agreements.

The terms of the agreements provide for no limitation to the maximum potential future payments under the above commitments, and the Corporation and Purolator do not currently possess sufficient information to estimate the maximum potential future liability.

16. Commitments and Contingencies (continued)

(c) CPIL and its subsidiary entered into an agreement with the Government of the Netherlands Antilles to provide postal and postbanking services, to the residents of the five islands that comprise the Netherlands Antilles, for a 20 year period that commenced in May 2003. Compliance with certain terms of the agreement for the concession has been in dispute, with each party alleging defaults by the other. A number of meetings were held in 2007 with the Government of the Netherlands Antilles, with the objective of negotiating an amicable settlement. As a result of these meetings, the parties signed a Memorandum of Understanding in December 2007 and Settlement Agreement in January 2008. The appropriate authorization under the *Financial Administration Act* was obtained in February 2008.

Subject to the terms and conditions set out in the Settlement Agreement, CPIL will transfer all of the shares of the subsidiary, Nieuwe Post Nederlandse Antillen N.V., to the Government of the Netherlands Antilles. As final settlement of all disputes and potential disputes between the parties arising out of the concession contract and the concession, the parties agreed to a total payment of $7 million by CPIL. This amount was recorded as an accrued liability as at December 31, 2007.

(d) In the normal course of business, the Corporation has entered into agreements that include indemnities in favour of third parties. In addition, the Corporation has entered into indemnity agreements with each of its directors and officers to indemnify them, subject to the terms of these agreements, against claims and expenses incurred by them as a result of serving as a director or officer of the Corporation or as a director, officer or in a similar capacity of another entity at the request of the Corporation.

These agreements generally do not contain specified limits on the Corporation's liability and, therefore, it is not possible to estimate the potential future liability under these indemnities. No amounts have been accrued in the consolidated financial statements with respect to these indemnities.

(e) The Corporation is involved in various claims and litigation in the normal course of business. Provisions are recorded when and if losses are likely and amounts can be reasonably estimated.

(f) The Corporation's employees are permitted to accumulate unused sick leave. However, such leave entitlements do not vest and can be used only in the event of illness. The amount of accumulated sick leave entitlements which will become payable in future years cannot reasonably be determined. Payments of sick leave benefits are included in current operations.

(g) The future minimum lease payments with respect to facilities, transportation equipment and other operating leases with terms in excess of one year, are as follows:

(in millions of dollars)	
2008	$ 138
2009	123
2010	111
2011	102
2012	87
2013 and thereafter	315
Total	**$ 876**

Included in the above commitments are leases in the amount of $15 million with a related party, the Government of Canada, for premises used in postal operations.

(h) In the normal course of business, the Corporation enters into contractual arrangements for the supply of goods and services over periods extending beyond one year. Disbursements largely depend on future, volume-related requirements and are subject to the Corporation's contractual rights of termination.

17. Cash Flow Information

Year ended December 31 (in millions of dollars)	**2007**	2006
Change in non-cash operating working capital		
Increase in accounts receivable	$ (7)	$ (29)
Increase (decrease) in net income tax payable	(37)	70
Increase (decrease) in accounts payable and accrued liabilities	(8)	53
Increase (decrease) in salaries and benefits payable	(11)	19
Increase (decrease) in deferred revenue	(27)	23
Net decrease in other non-cash operating working capital items	(4)	6
Total	**$ (94)**	$ 142
Supplementary information		
Interest paid	**$ 6**	$ 6
Income tax paid	**$ 163**	$ 45

18. Significant Joint Venture

The Corporation has a 51% ownership interest in Innovapost, The Canada Post Group's primary information technology service provider. Virtually all of Innovapost's services are provided to The Canada Post Group based on consideration contractually established and agreed to by the related party. Cost of operations included in the consolidated financial statements of the Corporation, includes approximately $283 million (2006 – $276 million) of expenses related to these services. The Corporation's proportionate share of the assets and liabilities of Innovapost at year end is $63 million (2006 – $75 million) and $37 million (2006 – $50 million), respectively.

19. Related Party Transactions

The Corporation had the following transactions with related parties in addition to those disclosed elsewhere in these consolidated financial statements:

(a) **Government of Canada, its agencies and other Crown corporations** • The Government of Canada compensates the Corporation for foregone postage revenue from Government free mail services and mailing of materials for the blind (note 6). In addition, pursuant to an agreement with the Department of Indian Affairs and Northern Development, the Government of Canada compensates the Corporation for the difference between the Corporation's cost of shipping eligible goods under the Food Mail Program and the applicable postage paid by shippers. Compensation payments from the Government of Canada amounting to $68 million (2006 – $62 million) are included in revenue from operations.

In addition, the Corporation has other transactions with the Government of Canada, its agencies and other Crown corporations in the normal course of business at commercial prices and terms.

For the year ended December 31, 2007, the amounts of accounts receivable and deferred revenue from these related parties are $24 million (2006 – $19 million) and $5 million (2006 – $5 million), respectively.

(b) **Directors** • In the normal course of business, the Corporation may interact with companies whose directors or officers are directors of the Corporation. The affected directors always recuse themselves from all discussions and decisions related to transactions between the companies. Such cases of company interaction occurred during the year with: Davis + Henderson, Limited Partnership; and with Telus Corporation. The Corporation provided services to Davis + Henderson, Limited Partnership, of $17 million in the first four months of 2007 (2006 – $26 million) and to Telus Corporation of $88 million (in the last four months of 2006 – $15 million). Services received from Telus Corporation in 2007 amounted to $5 million (in the last four months of 2006 – $2 million).

(c) **Other** • During the year, a subsidiary of the Corporation had business transactions with a company controlled by a minority shareholder of that subsidiary. The minority shareholder is also a director of the subsidiary. This company provided air services to the subsidiary in the amount of $107 million (2006 – $101 million). These transactions were made at prices and terms comparable to those given to other suppliers of the subsidiary.

20. Publications Assistance Program

Under the Government of Canada's Publications Assistance Program, the Government and the Corporation subsidize a portion of the distribution costs incurred by eligible publishers of eligible publications using the Corporation's Publications Mail™ service. Although subsidy payments payable to eligible publishers vary over the Government's fiscal year, the Government's contribution to the Program was capped at $45 million in its fiscal year 2007/2008 ($45 million in 2006/2007). The Corporation's contribution to the Program was capped at $15 million in 2007/2008 ($15 million in 2006/2007) and is included in cost of operations.

21. Financial Instruments

Exposure to risks and determination of fair value not otherwise disclosed in the consolidated financial statements are addressed below:

(a) Fair values • The fair value of accounts receivable, accounts payable and accrued liabilities, salaries and benefits payable and outstanding money orders approximate their carrying values due to their expected short-term settlement.

(b) Credit risk • The Corporation is exposed to normal credit risk with respect to accounts receivable. Credit risk associated with accounts receivable is minimized by the Company's large customer base which covers substantially all business sectors in Canada. The Corporation follows a program of customer credit evaluation and limits the amount of credit extended when deemed necessary. The Corporation monitors customer accounts against these credit limits and takes corrective action when appropriate. The Corporation maintains provisions for potential credit losses and any such losses to date have been within management's expectations. The Corporation does not believe it is subject to any significant concentration of credit risk.

(c) Foreign currency risk • The Corporation's exposure to foreign currency risk mostly arises from international settlements with foreign postal administrations and from the redemption of money orders denominated in foreign currencies. The Corporation's obligation to settle with foreign postal administrations is denominated in Special Drawing Rights (SDRs) – a basket of currencies comprising the US Dollar (US$), Japanese Yen, Sterling and Euro, whereas payment is usually denominated in US$ or, in some circumstances, the Euro. The Corporation's principle exposure is to the US$, but the net overall exposure is not significant, after matching associated US payables and receivables. Net exchange losses included in revenue from operations amounted to $8 million (2006 – $6 million of net exchange gains).

(d) Available financing facilities • The Corporation's borrowing plan, as part of the Corporate Plan, is reviewed and approved annually by the Board of Directors and the Government of Canada. The detailed terms and conditions for each long-term borrowing must also be approved by the Treasury Board and the Minister of Finance. The borrowings are direct obligation of the Corporation and thus constitute undertaking on behalf of Her Majesty in Right of Canada and carry the full faith and credit of the Government of Canada. Borrowing from other than the Government of Canada's Consolidated Revenue Fund is limited to $300 million. Of this, no more than $150 million can be short-term in nature and long-term debt is also limited to $150 million. Total borrowings were $58 million as at December 31, 2007, of which $55 million was long-term. Within the above limits, the Corporation has a line of credit and a commercial paper program that were not used during 2006 or 2007.

The Corporation' subsidiaries and joint venture also have access to financing facilities; the total unused amount was $85 million at the consolidated balance sheet date.

22. Segmented Information

The Corporation manages its operations and, accordingly, determines its operating segments on the basis of the legal entities. Three reportable operating segments have been identified: Canada Post, Purolator and Logistics. The Logistics segment is comprised of SCI Logistics and Intelcom up to its disposal on January 9, 2007.

The Canada Post segment provides transaction mail, parcels and direct marketing services, as well as other mail products and services. The Purolator segment derives its revenues from specialized courier services. The Logistics segment provides third-party logistics services in supply chain management and, from March 30, 2007, transportation services in the small to medium enterprise market.

Operating segments below the quantitative thresholds, for determining reportable operating segments, are combined and disclosed in the "all other" category. Their revenues are attributable to information technology services and postal/postbanking services in the Netherlands Antilles. EPO Inc., which provided web-based electronic mail delivery services, is also included in this "all other" category until October 31, 2006, when the entity was dissolved and its operations were integrated into the Canada Post segment and Innovapost.

The accounting policies of the operating segments are the same as those described in the significant accounting policies (note 2).

Transactions occur between the operating segments at commercial prices and terms comparable to those given to other customers and suppliers and without subsidy between the operating segments. On a consolidated basis, no individual external customer's purchases account for more than 10% of total revenues.

The Logistics segment completed the restructuring plan approved in 2006 in conjunction with the renewal of its operating contract with a major customer on which it is economically dependent. Restructuring costs, mostly facility consolidation costs, of $3 million were recorded in 2007 (2006 – $10 million, mostly workforce reduction costs).

22. Segmented Information (continued)

Year ended, and as at, December 31, 2007
(in millions of dollars)

	Canada Post	Purolator	Logistics	All other	Elimination of intersegment	The Canada Post Group
Revenue from external customers	$ 5,933	$ 1,389	$ 137	$ 15	$ –	$ 7,474
Intersegment revenue	22	59	9	160	(250)	–
Revenue from operations	$ 5,955	$ 1,448	$ 146	$ 175	$ (250)	$ 7,474
Income (loss) before the undernoted items	$ 207	$ 118	$ 11	$ 9	$ (4)	$ 341
Amortization and impairment	(180)	(30)	(5)	(2)	2	(215)
Investment and other income	57	–	–	1	(16)	42
Interest and other expense	(6)	(4)	–	–	–	(10)
Income (loss) by segments	$ 78	$ 84	$ 6	$ 8	$ (18)	158
Unallocated amounts and adjustments in consolidation						(2)
Income tax expense						(102)
Net income						$ 54
Assets by segments	$ 4,719	$ 617	$ 102	$ 237	$ (523)	$ 5,152
Unallocated amounts and adjustments in consolidation						(1)
Total assets						$ 5,151
Acquisition of capital assets	$ 237	$ 83	$ 13	$ 2	$ (5)	$ 330

22. Segmented Information (continued)

Year ended, and as at, December 31, 2006
(in millions of dollars)

	Canada Post	Purolator	Logistics	All other	Elimination of intersegment	The Canada Post Group
Revenue from external customers	$ 5,811	$ 1,310	$ 124	$ 19	$ –	$ 7,264
Intersegment revenue	20	37	10	158	(225)	–
Revenue from operations	$ 5,831	$ 1,347	$ 134	$ 177	$ (225)	$ 7,264
Income (loss) before the undernoted items	$ 253	$ 99	$ 1	$ 8	$ (2)	$ 359
Amortization	(183)	(27)	(3)	(4)	2	(215)
Investment and other income	35	–	1	2	(9)	29
Interest and other expense	(6)	(3)	–	(4)	2	(11)
Income (loss) by segments	$ 99	$ 69	$ (1)	$ 2	$ (7)	162
Unallocated amounts and adjustments in consolidation						1
Income tax expense						(44)
Net income						$ 119
Assets by segments	$ 4,617	$ 548	$ 82	$ 250	$ (508)	$ 4,989
Unallocated amounts and adjustments in consolidation						(5)
Total assets						$ 4,984
Acquisition of capital assets	$ 227	$ 73	$ 5	$ 2	$ (2)	$ 305