



Calgary Co-operative Association Limited Management Discussion and Analysis

Overview

Calgary Co-operative Association Limited (Calgary Co-op) operates as an Alberta co-operative under the *Cooperatives Act* (revised March 6, 2003).

Locally owned and operated, Calgary Co-op was incorporated on July 13, 1955, and opened its first store in November 1956. Today, Calgary Co-op has grown into one of the largest retail co-operatives in North America with over 425,000 members and 4,000 employees, assets of \$ 351.9 million, and sales of \$997.6 million as at November 3, 2007.

Formed for the benefit of its member-owners Calgary Co-op currently operates 22 retail food centres, 26 gas bars, 9 travel offices and 15 liquor stores located in Calgary, Airdrie, Strathmore, and Okotoks, Alberta.

Vision

Calgary Co-op's vision is to be the premier shopping destination in the communities we serve. Guided by this vision, Calgary Co-op strives to put into action critical initiatives for achieving its vision by focusing on delivering quality products and valued-added services to members/customers at competitive prices.

Calgary Co-op is committed to expanding, upgrading and enhancing overall operations while maintaining a financially strong operation. It seeks sustainable growth and profitability that will provide members with a reasonable annual patronage return, while balancing the need to re-invest in the business.

Calgary Co-op also takes corporate social responsibility seriously. It believes that investing in the community through corporate and store-based initiatives is imperative. As such, Calgary Co-op contributes to a wide variety of organizations including the Alberta Children's Hospital, Calgary Public Library, Ronald McDonald House, food banks, schools, educational bursaries, employee volunteerism, recycling and environmental initiatives, and a number of community partnerships.

Responsibility for the environment is also a key priority at Calgary Co-op. Energy management, resource conservation and environmental protection are important to our members/customers and make good business sense.

Strategic Goals

To successfully achieve its vision, Calgary Co-op focuses on achieving four long-term strategic goals that are key to delivering lasting value to members/customers and maintaining a financially healthy co-operative.

The strategic goals are to:

1. Ensure the financial health and sustainability of the organization.
2. Exceed member and customer expectations with exceptional service, selection and value.
3. Implement new and innovative processes and solutions to improve productivity and execution throughout the organization.
4. Implement training, retention and career building programs to develop well-trained, knowledgeable, motivated and empowered employees.

Various operating and financial strategies are in place to support the strategic goals. In the case of operating strategies, these include:

- continuing focus on the primary lines of business (food, petroleum, pharmacy, liquor and travel);
- focusing on our fresh food offering
- executing existing plans and programs impeccably;
- offering the highest quality fresh foods, innovative new products and value-added services;
- owning real estate, when economically feasible;
- improving the shopping experience by investing in new facilities and renovating existing facilities;
- creating customer loyalty through competitive pricing and marketing the “co-op” advantage;
- providing a work place that offers opportunities for growth and development.

The financial strategies for Calgary Co-op include:

- minimizing risks and controlling costs;
- maintaining a strong balance sheet;
- allocating capital to projects that earn a rate of return in excess of the internal rate of return;
- providing a reasonable patronage return to members while retaining sufficient earnings to ensure the ongoing financial health of Calgary Co-op; and
- maximizing utilization and return on assets.

The board and management of Calgary Co-op believes that by successfully implementing and executing the strategies outlined above, Calgary Co-op will be well-positioned for future growth and be able to best serve its members/customers.

Governance Structure

Members of Calgary Co-op elect its board of directors through a formal democratic voting process. There are nine director positions, including a chair, vice chair and board secretary.

The board of directors supervises the management of the business and affairs of the Calgary Co-operative Association Limited, subject to the *Cooperatives Act*, regulations, articles, any unanimous agreement, and the by-laws. The board may exercise all of the powers of the Association that are not required to be exercised by the Association in a general meeting.

Each year, Calgary Co-op members elect three directors to the board, each for a three-year term or as required to fill additional vacancies. The term of office for each of the nine director positions expire on a staggered yearly basis to ensure that a certain number of experienced directors remain on the board to assist newly elected directors in learning their roles and responsibilities.

The board operates with four standing committees: Audit Committee; Governance Committee; Member Relations Committee; Performance and Compensation Committee.

Each year, in collaboration with the executive management team, the board reviews the vision, mission and values for Calgary Co-op, and sets strategic direction for a three-year planning period. The board also sets annual goals for itself, which form the basis of the annual work plan for the board.

Key Performance Indicators

Calgary Co-op monitors the success of its operations and implementation of its strategies through the use of key performance indicators that assess financial performance and condition. Some of the key performance indicators are sales, earnings before patronage returns and return on member equity.

Operational Results

Sales

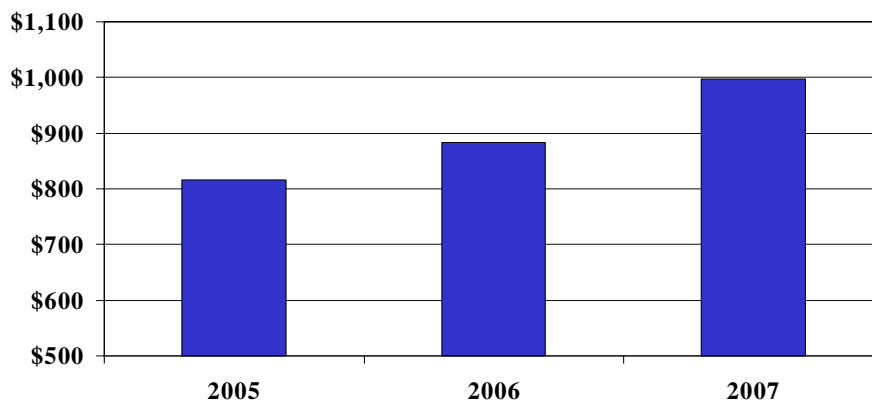
Calgary Co-op will maintain its focus on increasing sales and profitability by focusing on delivering quality products and value-added services to members/customers at competitive prices. In 2007, sales grew by \$113.7 million or 12.9% to \$997.6 million. Same store sales, which are sales from stores in the same locations in both the 2007 and 2006 financial years, grew by 7.2%.

Several factors contributed to sales growth during 2007 including: new food stores at West Springs and Creekside, the addition of the Montgomery gas bar, strong gasoline prices, existing store renovations, and a continuing focus on store level operational execution.

Calgary Co-op anticipates continued sales growth in the future as a result of:

- an emphasis on fresh products
- significant investment in training employees to provide superior customer service
- ongoing capital investment in new and existing facilities
- emphasizing merchandising and quality standards at store level
- improving operational processes and on-shelf availability of product

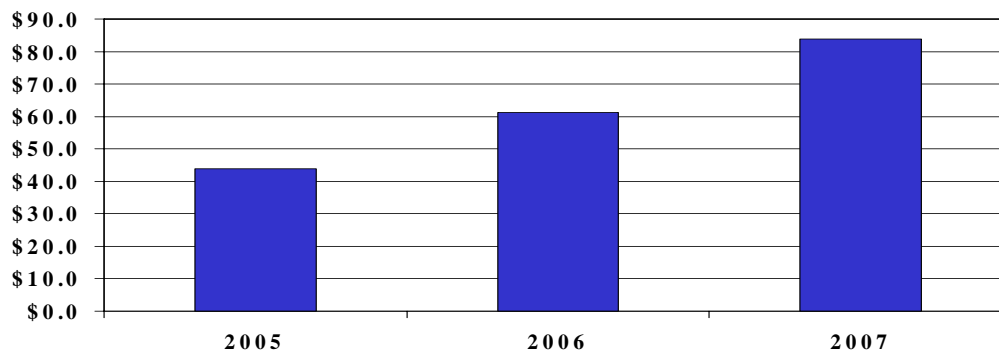
Sales (in millions)



In 2007, earnings before interest expense, taxes, depreciation, amortization, loss on disposal & write-off of property & equipment and patronage returns (EBITDA; see Non-GAAP Financial Measures) reached \$83.9 million - a \$22.6 million improvement over the 2006 financial year. As a percentage of sales, EBITDA rose to 8.4% in 2007 compared to 6.9% last year.

EBITDA

(in millions)



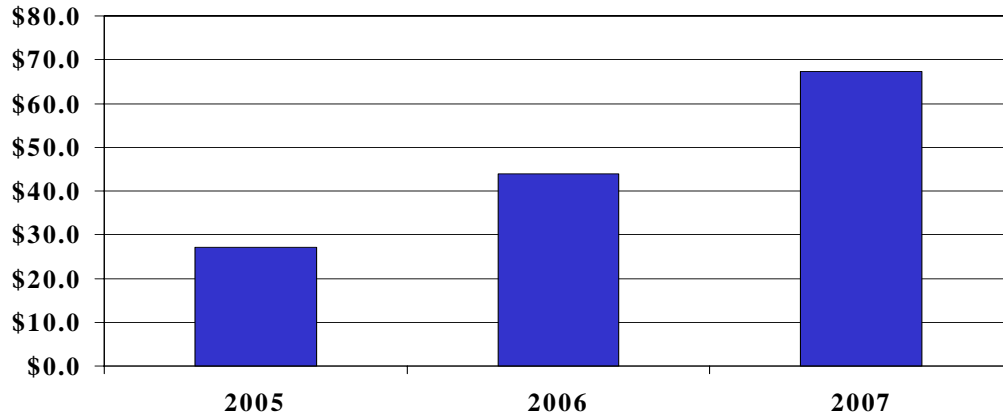
Earnings Before Patronage Return and Income Taxes

Earnings before patronage return and income taxes rose by 53.3% to \$67.3 million. Several factors impacted this change, including:

- sales improvement, particularly in petroleum;
- increased patronage return from Federated Co-operatives Limited is a combination of higher FCL earnings and increased purchase volumes by Calgary Co-op of food and petroleum from FCL;
- on a same store basis, fewer labor hours were used at store level than the prior year as a consequence of the tight labor market;
- increased rental income as additional commercial rental units were leased during the year;
- increased rental expense as a result of the new food centres, gas bar and liquor store that were open for the full year in 2007;
- increased loss on disposal and/or write-off of capital assets related primarily to the disposal of food store equipment and write-down of obsolete assets in renovated shopping centres;
- increased interest income resulting from stronger cash flows that provided additional cash for investment during the year;
- reduced interest expense in 2007 due to lower long term debt levels.



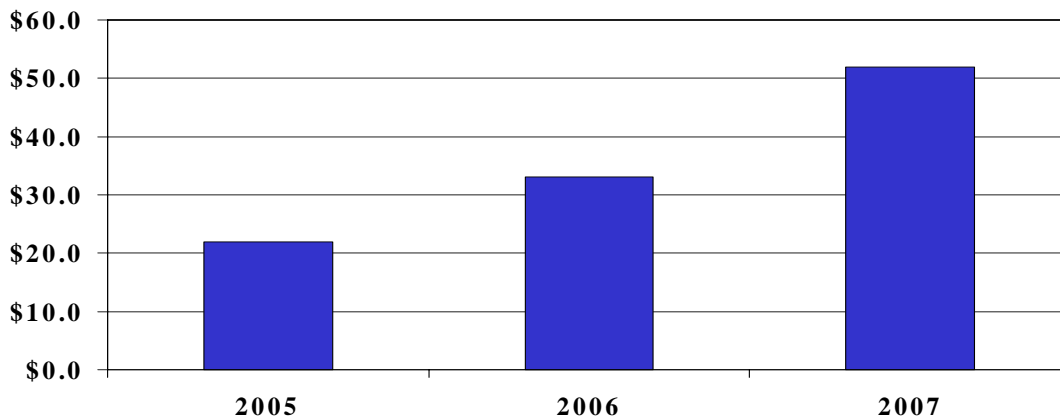
Earnings Before Patronage Returns and Income Taxes (in millions)



Patronage Returns

For fiscal 2007, the board of directors approved payment of patronage returns totaling \$51.9 million, an increase of \$18.9 million from a year ago. The cash portion of the patronage return is \$31.7 million compared to \$20.0 million last year. The share portion of the patronage return is \$20.2 million versus \$13.0 million in 2006.

Patronage Returns (in millions)

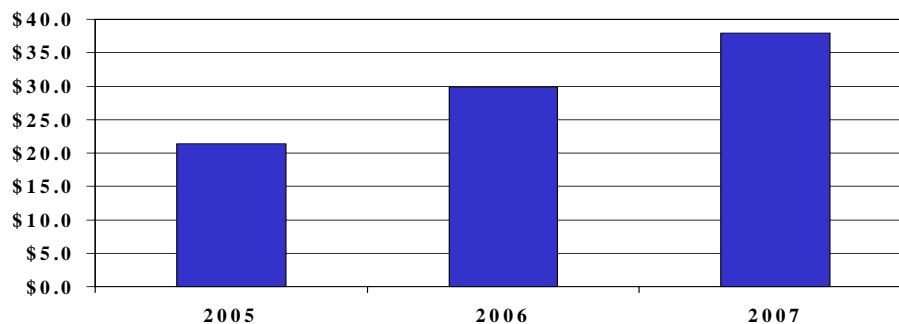


Financial Condition

Cash flows from operations before changes in non-cash working capital increased to \$38.0 million from \$29.9 million in 2006. Cash flows used in financing activities in 2007 were \$8.1 million compared to cash flows used in financing activities of \$12.7 million in 2006. Cash flows used in investing were \$34.8 million versus \$10.8 million last year.

Expenditures on property and equipment increased significantly over the previous year (\$38.9 million in 2007 compared to \$26.5 million in 2006). In 2007, \$7.1 million of Calgary Co-op's investment in FCL was repaid. The cash was used to pay down long-term debt.

Cash Flow from Operations (before changes in non-cash working capital) (in millions)



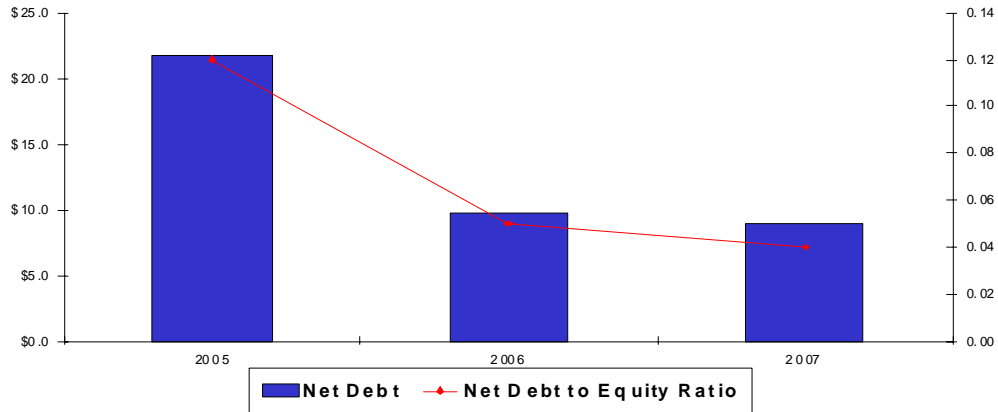
Calgary Co-op finances operations via a mix of internal and external methods. Retaining profits in the form of member shares and retained earnings provides internal financing. Member equity in Calgary Co-op at the end of the fiscal year totaled \$229.9 million compared to \$200.2 million in 2006.

Credit Union Central Alberta (CUCA) provides the majority of Calgary Co-op's external financing. In 2007 the long-term financing provided by CUCA totaled \$7.4 million. Calgary Co-op also has an \$8 million line of credit and a \$10 million evergreen loan facility available through CUCA. As of November 3, 2007, there was no outstanding balance on the evergreen loan facility; however \$2.6 million in letters of credit were outstanding on the line of credit. Federated Co-operatives Limited provides various financing options including interest-free loans and non-interest bearing capital leases. At the end of fiscal 2007, \$2.2 million of interest-free loans and \$3.7 million in capital leases were outstanding with Federated Co-operative Limited.



The net debt to equity ratio (see Non-GAAP Financial Measures) for Calgary Co-op improved over the prior year. In 2007, the net debt to equity ratio was 0.04:1 compared to 0.05:1 in 2006.

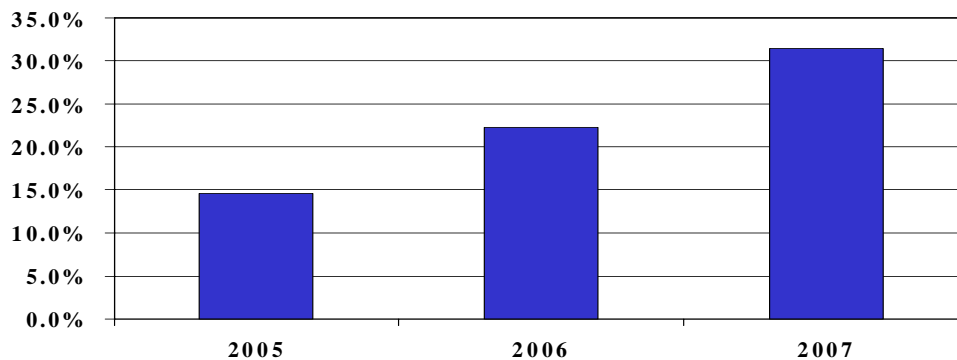
Net Debt to Equity



Return on member equity is based on after-tax earnings before patronage returns divided by opening member equity. For 2007, return on member equity was 31.5% compared to 22.3% in 2006. The three-year average return on member equity is 22.8%.

Return on Equity

(based on earnings before patronage return and opening equity)



Non-GAAP Financial Measures

Calgary Co-op reports its financial results in accordance with Canadian GAAP. Included within this MD&A are certain non-GAAP financial measures that Calgary Co-op believes may be useful information to readers of the financial statements. Because these measures do not have a standardized definition, they may or may not be comparable to similarly titled measures presented by other entities.

One of the non-GAAP measures used in assessing Calgary Co-op operating performance is EBITDA, defined as “earnings before interest, tax, depreciation and amortization, and patronage return”. EBITDA is used as an indicator of the company’s operational performance, ability to generate cash flows to fund cash requirements, investment and development projects.

Another non-GAAP measure employed at Calgary Co-op is Net Debt, defined as long and short-term debt less cash, cash equivalents, and short-term investments. This measure is an important component in identifying the amount of financial leverage employed by Calgary Co-op.

Another useful non-GAAP measure is net debt to total equity ratio, which highlights how Calgary Co-op finances operations. It also provides for an overall impression of its debt situation.

Risk Management

In the normal course of business, Calgary Co-op is exposed to various risks that have the potential to impact upon its profitability. As a result, Calgary Co-op has risk management strategies in place to assist in minimizing risk exposure.

Competitive

As a retailer, Calgary Co-op continues to face intense competition from traditional and non-traditional grocery competitors, such as drug stores, mass merchandisers, warehouse clubs, discount stores and assorted other competitors. The potential arrival of new competitors, expansion of existing competitors, ethnic diversity, changing consumer expectations and demographics are all challenges to be faced. Various strategies employed by Calgary Co-op’s to face these challenges include: training and talent management initiatives, growing the private-label product line, providing products at competitive prices, enhancing customer service, continuous improvement of store level processes, being market driven, having cost effective operations, reviewing product pricing, encouraging innovation, and adjusting operating strategies as necessary.

Interest rate risk

Calgary Co-op’s interest rate risk is limited to certain cash and short-term investments and long-term debt. As was stated in the net debt to equity discussion, this ratio has improved over the last several years as long-term debt was paid down. With this reduction in debt Calgary Co-op’s sensitivity to fluctuations in interest rates has also declined.

Credit risk

Exposure to credit risk relates to accounts receivable from various customers. To assist in mitigating the risk, various policies and guidelines are in place as well as credit scoring techniques. Account receivable balances are actively monitored and reviewed on a regular basis.

Food Safety

Calgary Co-op has food safety policies and programs that address safe food handling and preparation standards, and rigorously applies these food safety procedures, practices and programs within the business. In addition, procedures are in place to effectively manage public health concerns related to specific food products or a major occurrence of a food-borne illness.



A comprehensive food safety program is in place, which includes employee certification upon completion of the program. Program attendance is mandatory for employees who handle fresh products and successful completion of the program is expected. Employees who successfully complete the initial training program must then take re-certification training on a regular basis.

Human Resources

The majority of Calgary Co-op's workforce is unionized. On October 24, 2005, unionized employees ratified a new five-year collective agreement with Calgary Co-op that will conclude in October 2009. Calgary Co-op endeavors to maintain good relations with all employees, both unionized and non-unionized.

In the current labor market it is a challenge to recruit, develop, and retain employees. Calgary Co-op is utilizing a variety of initiatives to retain existing employees and attract new employees. Some examples include: the bonus incentive program for all employees, significant investment in training, and career development plans.

Information Technology

As is the case with almost all companies today, Calgary Co-op relies on information technology to support its current and future operations. These systems are an important enabler in meeting the organizations business objectives. Various risks can arise if upgrades to existing systems or the introduction of new systems are not properly implemented to allow effective management of the business going forward.

Real Estate

The availability of sites for acquisition and development or leasing of new facilities may impact the Calgary Co-op's ability to meet its longer-term sales goals. Calgary Co-op maintains a reasonably large portfolio of owned real estate and, where possible, prefers to purchase sites for future facilities rather than lease.

Utility Prices

Calgary Co-op consumes significant amounts of electricity and natural gas at its facilities. The organization has entered into a fixed price supply contract for a large portion of its future electricity and natural gas requirements.

Environmental

Calgary Co-op has formal policies relating to the environment and energy management. Environmental audits are conducted annually by internal resources and tri-annually by certified independent external resources. Site remediation is also done in compliance with relevant legislation and using appropriate, qualified resources.

Energy management initiatives are important from the perspective of conserving resources and providing significant operating cost savings. An important component of the environmental and energy management programs is raising awareness among employees about energy usage and ways they can contribute to reducing energy consumption, as well as other conservation and environmental protection initiatives and practices.

Health and Safety

Calgary Co-op continues to invest in health and safety initiatives. A number of health and workplace safety programs are currently in place with others in development. Calgary Co-op has established policies



and procedures to assist in ensuring compliance with applicable legislative requirements. In addition, audits and assessments are completed using internal and external resources. Raising employee awareness about health and safety issues is a focus.

Internal Control

Calgary Co-op has established and maintains various internal controls and procedures over financial reporting. The systems of internal control are designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements. There are no changes in internal control that have materially affected Calgary Co-op's internal control over financial reporting.