



More growth *in store...*

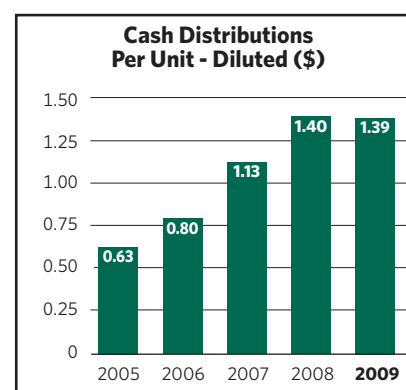
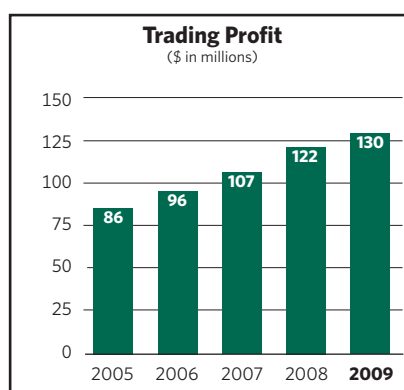
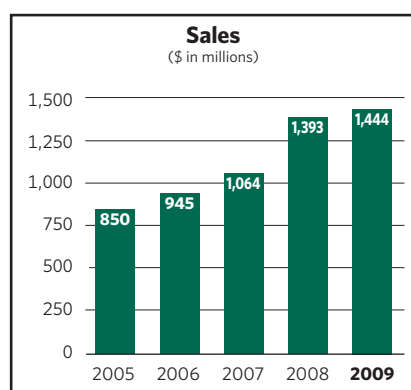
NORTH WEST COMPANY FUND 2009

# Management's Discussion & Analysis

# Financial Highlights

All currency figures in this report are in Canadian dollars, unless otherwise noted

(\$ in thousands, except per unit information)	Year Ended January 31, 2010	Year Ended January 31, 2009	Year Ended January 31, 2008
<b>RESULTS FOR THE YEAR</b>			
Sales	\$ 1,444,366	\$ 1,392,634	\$ 1,064,490
Same store sales % increase <sup>1</sup>	0.1%	2.7%	6.7%
Trading profit <sup>2</sup> (earnings before interest, income taxes and amortization)	\$ 130,274	\$ 122,257	\$ 106,557
Earnings before interest and income taxes <sup>2</sup> (EBIT)	95,124	90,203	79,607
Net earnings	81,813	75,378	62,991
Cash flow from operations <sup>2</sup>	116,486	106,324	94,739
<b>FINANCIAL POSITION</b>			
Total assets	\$ 623,800	\$ 609,173	\$ 529,670
Total debt	209,170	213,026	159,833
Total equity	289,926	274,410	256,301
<b>FINANCIAL RATIOS</b>			
Debt-to-equity	.72:1	.78:1	.62:1
Return on net assets <sup>3</sup>	18.7%	19.8%	21.0%
Return on average equity	29.3%	28.6%	24.9%
Sales blend: Food	77.0%	75.0%	70.0%
General Merchandise	20.0%	22.0%	26.0%
Other	3.0%	3.0%	4.0%
<b>PER UNIT (\$) - DILUTED <sup>4</sup></b>			
Trading profit	\$ 2.69	\$ 2.52	\$ 2.20
Net earnings	1.69	1.56	1.31
Cash flow from operations	2.40	2.20	1.96
Market price - January 31	17.94	16.14	18.42
- high	19.60	19.99	22.68
- low	14.88	13.00	15.01



1 Same store sales, excluding the foreign exchange impact, on an equivalent year basis

2 See Non-GAAP measures section on page 26

3 Earnings before interest and income taxes as a percent of average net assets employed

4 All per unit information has been restated to reflect the three-for-one unit split that occurred on September 20, 2006

# Management's Discussion & Analysis

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Unless otherwise stated, this Management's Discussion & Analysis (MD&A) for the North West Company Fund ("NWF" or "Fund") and its subsidiaries (collectively, "North West Company", the "Company", "North West", or "NWC") is based on the financial information included in the Consolidated Financial Statements and Notes to the Consolidated Financial Statements on pages 30 to 47 which have been prepared in accordance with Canadian generally accepted accounting principles (GAAP) and are in Canadian dollars. The information contained in this MD&A is current to April 7, 2010, unless otherwise stated.

**Forward-Looking Statements** This Management's Discussion & Analysis (MD&A) contains forward-looking statements about the North West Company Fund, including its business operations, strategy and expected financial performance and condition. Forward-looking statements include statements that are predictive in nature, depend upon or refer to future events or conditions, or include words such as "expects", "anticipates", "plans", "believes", "estimates", "intends", "targets", "projects", "forecasts" or negative versions thereof and other similar expressions, or future or conditional future financial performance (including sales, earnings, growth rates, distributions, dividends, debt levels, financial capacity, access to capital, and liquidity), ongoing business strategies or prospects, the proposed conversion from an income trust to a corporation and the timing thereof, and possible future action by the Fund, are also forward-looking statements. Forward-looking statements are based on current expectations and projections about future events and are inherently subject to, among other things, risks, uncertainties and assumptions about the Fund, economic factors and the retail industry in general. They are not guarantees of future performance, and actual events and results could differ materially from those expressed or implied by forward-looking statements made by the Fund due to, but not limited to, important factors such as general economic, political and market factors in North America and internationally, interest and foreign exchange rates, changes in accounting policies and methods used to report financial condition, including uncertainties associated with critical accounting assumptions and estimates, the effect of applying future accounting changes, business competition, technological change, changes in government regulations and legislation, changes in tax laws, unexpected judicial or regulatory proceedings, catastrophic events, the Fund's ability to complete strategic transactions and integrate acquisitions and the Company's success in anticipating and managing the foregoing risks. The reader is cautioned that the foregoing list of important factors is not exhaustive. Other risks are outlined in the Risk Management section of this MD&A and in the Risk Factors sections of the Annual Information Form and Management Information Circular. The reader is also cautioned to consider these and other factors carefully and not place undue reliance on forward-looking statements. Other than as specifically required by applicable law, the Company has no specific intention to update any forward-looking statements whether as a result of new information, future events or otherwise.

Additional information on the Fund, including our Annual Information Form, can be found on SEDAR at [www.sedar.com](http://www.sedar.com) or on the Company's website at [www.northwest.ca](http://www.northwest.ca).

# Management's Discussion & Analysis

## OUR BUSINESS TODAY

The North West Company (NWC or North West) is a leading retailer to underserved rural communities and urban neighbourhood markets in the following regions: northern Canada, western Canada, rural Alaska, the South Pacific and the Caribbean. Our stores offer a broad range of products and services with an emphasis on food. Our value offer is to be the best local shopping choice for everyday household and local lifestyle needs.

North West's core strengths include our ability to adapt our product mix to each market we serve; our logistics expertise in moving product to, and operating stores within, remote or difficult-to-serve locations; our knowledge in serving indigenous and lower-income customers; and our ability to apply these strengths to serve customers within complementary niche businesses.

North West owns a rich enterprising legacy as one of the longest continuing retail enterprises in the world. The Company traces its roots back to 1668 with many of our stores in northern Canada and Alaska having continuously served their communities for over 200 years. Today these northern stores operate in communities with populations from 500 to 7,000. A typical store is 7,500 square feet in size and offers food, family apparel, housewares, appliances, outdoor products and services such as post offices, income tax return preparation, quick-service prepared food, commercial business sales, money transfers and cheque cashing.

Growth at North West has come from market share expansion within existing locations and from applying our expertise and infrastructure to new markets and complementary businesses. These include wholesaling to independent stores, opening Giant Tiger junior discount stores in rural communities and urban neighbourhoods in western Canada, and our late 2007 acquisition of Cost-U-Less, Inc. (CUL), a chain of mid-size warehouse format stores serving the South Pacific and the Caribbean.

Adapting to unique local lifestyles, cultures and selling opportunities better than our competition is a key strength and ongoing strategy for North West. Store development flexibility, store management selection and learning programs, store-level merchandise ordering, community relations and profit-sharing incentive plans are all ingredients of the model we have built to support this strategy. We believe that continued, efficient enhancement of our localization skills, is an essential component in meeting the customer needs within each market we serve.

North West delivers its products and services through the following retail banners and wholesale businesses, in two reporting segments:

### Canadian Operations

- **127 Northern** stores, offering a combination of food, financial services and general merchandise to remote northern Canadian communities;
- **31 Giant Tiger** junior discount stores, offering family fashion, household products and food to urban neighbourhoods and larger rural centres in western Canada;
- **7 NorthMart** stores, targeted at larger northern markets with an emphasis on an expanded selection of fresh foods, fashion and health products and services;
- **11 Quickstop** convenience stores, offering ready-to-eat foods, petroleum products and related services;
- **1 Valu Lots** clearance center;
- **1 Solo Market** test store, targeted at less remote, rural markets;
- **Crescent Multi Foods (CMF)**, a distributor of produce and fresh meats to independent grocery stores in Saskatchewan, Manitoba and northwestern Ontario;
- **2 North West Company Fur Marketing** outlets, trading in wild furs and offering Aboriginal handicrafts and authentic Canadian heritage products; and
- **The Inuit Art Marketing Service**, Canada's largest distributor of Inuit art.

### International Operations

- **29 AC Value Centers**, stores similar to Northern and NorthMart, offering a combination of food and general merchandise to communities across remote and rural regions of Alaska;
- **4 Quickstop** convenience stores;
- **Pacific Alaska Wholesale** (formerly **Frontier Expeditors** and **SPAN Alaska**), a leading distributor to independent grocery stores and individual households in rural Alaska;
- **12 Cost-U-Less (CUL)**, mid-size warehouse stores, offering discount food and general merchandise products to island communities in the South Pacific and the Caribbean; and
- **1 Island Fresh Supermarket**, neighborhood stores offering convenience with an emphasis on fresh and prepared foods.

## VISION

At North West our vision is to be a leading community retailer within underserved and less developed markets. We want to maximize our customers' desire and ability to shop with us by being a trusted local store. We do this by being more accessible, more flexible, friendlier and lower cost. For our investors we want to deliver superior, top-quartile returns over the long term.

## PRINCIPLES

The way we work at North West is shaped by six core principles: *Customer Driven, Enterprising, Passion, Accountability, Trust, and Personal Balance.*

**Customer Driven** is our practice of always looking through the eyes of our customers while recognizing our stores' unique role as a supportive community citizen.

**Enterprising** is our spirit of innovation, improvement and growth, reflected in our unrelenting focus on new store formats, products, services and processes.

**Passion** refers to our connection to our work, our role as a community store and our opportunity to do great things at North West.

**Accountability** is our management approach to getting work done through clear roles, tasks and resources.

**Trust** at North West means doing what you say you will do, with fairness, integrity and respect.

**Personal Balance** is our commitment to sustaining ourselves and our organization, so that we work effectively for our customers and communities over the long term.

## STRATEGIES

The Company's long-range plans (LRP) are developed in five-year cycles and are reviewed and adjusted on an annual basis or as required at the senior management and board levels. 2009 was the start of a LRP cycle and included an in-depth assessment of North West's past performance, opportunity gaps within each business segment, and new business growth potential.

As a result of our 2009 LRP work, we have identified operational excellence as the first priority within our existing retail network, themed as "More Growth in Store". This finding and subsequent direction-setting is based on gaps that we see within our current store base which, if effectively addressed, will deliver attractive financial returns over the next three years and set the foundation for accelerated new market, product and service growth over the long term.

The strategic rationale for this approach fully considered our past successes and unrealized opportunities. Over the past five years, food market share and margin rates increased through better sourcing, through more store-branded products that offered a value alternative to national brands and by building on our store-level capability with training, new technology and best practices. Our food growth strategy was augmented by opportunistically pursuing complimentary everyday products and services. These included financial services, post offices, fuel and pharmacies. New store growth was achieved by acquiring independent stores in northern Canada and Alaska, through Giant Tiger store expansion in western Canada and through our acquisition of Cost-U-Less, Inc. in late 2007.

While our business successfully developed beyond our core northern markets and merchandise mix, resources and executive attention were stretched. The effect was that other, high potential elements within our business were left without the necessary degree of investment and leadership.

The specific areas we have now highlighted for attention further protect, grow and optimize the performance of our food business, which accounts for 77% of our sales base. Within this important merchandise group there are three priority initiatives:

### 1. Improve food categories with significant financial gaps.

For North West these categories are perishable foods that attract higher activity costs and that require more complex execution. The solutions being identified and acted on will deliver a simpler, streamlined business with implications for assortment breadth, packaging, refrigeration, and merchandising. The emphasis in 2010 will be produce and

meat, followed by prepared foods and other frozen and chilled categories in 2011, and then general merchandise in 2012.

**2. Optimize In-Stock Position.** While the number one potential for margin improvement lies within our perishable categories, the top sales driver for North West depends on improving our in-stock ability. A core element of each banner's value offer is convenience, which in turn is driven by in-stock performance. Our biggest gains in this area will be in shelf-stable (non-refrigerated) merchandise, ranging from paper products to canned goods and snack foods. Similar to our work on perishables, the strategies will apply to how we order and ship products, and will seek to achieve more streamlined, better forecasted and automated processes while ensuring that we focus on allocating the appropriate selling space to the items our customers value the most.

**3. Be "Priced Right".** We consider improved price management to be a strategic opportunity at North West, especially in our more remote banners. Market-based pricing is more difficult due to limited local shopping options in many of these locations and this requires a deeper, more sophisticated understanding of consumer purchase behaviour relative to price. At the outset this initiative will focus on accurate and timely price checking and price adjusting, coupled with the testing of new, lower pricing approaches.

Supporting these "More Growth in Store" selling initiatives are three foundational strategies:

**1. Ensure store teams are capable and stable.** With such a diverse store network, our people, especially at store level, have always made the difference at North West. Through our LRP assessment work we identified a critical need to solidify our store teams so that they stay together longer in specific locations, deepening customer and community relationships, and building their business. For this to happen consistently, we are revamping recruitment, retention and store work processes to ensure we attract and retain highly productive, capable store personnel.

**2. Build on our supply chain advantage.** North West is a major shipper of merchandise and other freight into the remote markets that we serve. This creates an opportunity to work more collaboratively with our carrier partners to fully leverage our knowledge and forecasted volumes. The outcomes we expect from this strategy are improved delivery service within a more productive, lower cost transportation network.

**3. Cascade NWC's leadership principles into practices.** We consider our leadership principles, in action, to be a critical link to great, sustainable performance across all levels of our organization. From our cashiers to our buyers and store managers, we recognize the potential for measurable, effective practices that reflect these principles and align our work. Our LRP carries forward this commitment to making leadership at North West deeper and more effective.

Beyond our “More Growth in Store” emphasis over the next three to five years, we will maintain select growth investment in related markets, products and services. Recent examples were our expansion into pharmacies and health care and the acquisition of CUL. Going forward we will keep learning from and nurturing these ventures while ensuring that their risk/return profile is close to that of our more established retail business base and that resources are not diverted from our key LRP strategies. We will continue to carefully assess the long-term potential of any major new business, product or service and the probability of achieving threshold returns on a sustainable, consistent basis. Across this work we keep emphasizing new ideas, clear principles, execution, and the ability to track performance.

The strategies at North West reflect our total return approach to performance. We place an approximately equal emphasis on growth and income yield in delivering top quartile total returns to investors. Investment opportunities, as noted above, are considered in terms of their ability to sustain an attractive current cash return in addition to growth prospects.

Effective January 1, 2011, North West intends to convert from an income trust back to a share corporation. This restructuring is in response to changes in the income tax legislation whereby a new entity-level tax on distributions from certain income trusts, such as the Fund, will be imposed commencing January 1, 2011. As a share corporation North West will continue to deliver total returns to investors based on a combination of yield and growth. Upon converting to a share corporation, it is the Company’s intention to pay dividends of approximately the after-tax amount of the quarterly distributions prior to conversion with the balance of the after-tax cash flow reinvested to sustain and grow our business. These allocations are consistent with our current practice under the income trust structure. Additional information on the conversion to a share corporation is included under Conversion to a Share Corporation on page 15.

## KEY PERFORMANCE DRIVERS AND CAPABILITIES TO DELIVER RESULTS

**The ability to protect and enhance the profitability of northern store locations.** These stores in Alaska and northern Canada represent approximately 80% of our profitability. Although we expect this percentage to diminish over the next five years as we add more stores in new markets and grow our wholesale businesses, we believe that the focus on food within our new LRP strategies will provide us with the ability to protect and enhance profitability.

**The financial capability to sustain the competitiveness of our existing store base and to pursue growth.** Our sustaining investments include capital investment in energy-efficient equipment, replacement stores and technology. Non-capital expenditures are centred on improvements to our in-store capabilities through more in-depth training programs and the ongoing implementation of “best practice” work processes.

**The ability to be a leading community store in every market we serve.** This depends on our ability to tailor our store formats, product/service mix, community support and store associate employment offer while still realizing the scale efficiencies of our size or the size of our alliance partners. This is our localization strategy. A broad range of products, services and store sizes, combined with flexible technology platforms and “best practice” work processes, are all required to give us the ability to achieve this goal.

**The ability to successfully add new stores.** Our new store opening success depends on finding viable locations, willing sellers of independent stores or chains and being able to integrate and accelerate their full contribution potential. Other success factors include achieving product sourcing, operating and transportation cost advantages while building strong, entrepreneurial store teams.

**Our ability to achieve best selling practices and build supportive community relations.** Enhancing store stability and capability is an ongoing priority that aligns with our goal of being as localized as possible. We continually invest in recruiting, retention and best practice work methods. We modify store processes to fully leverage our technology, specifically in the areas of communications, merchandise ordering, staff scheduling and training. This recognizes the important role played by our store managers and other key store-level personnel and the reality that remoteness and other conditions of our markets creates challenges in attracting and keeping talented people. Related to this is our ongoing ability to develop local management and to foster positive community relationships, especially within the indigenous markets we serve.

**Our ability to reduce costs across all of our store banners, improve competitiveness and create more time and skill at store level to order and sell merchandise.** A key goal is to shift more staff time and skill towards ordering and selling merchandise tailored to the unique markets we serve while reducing costs in the non-selling facets of store work. Cost savings are continually targeted at labour scheduling, energy usage and product shrinkage. We have developed alliances with other non-competing retailers to provide sales and distribution services for certain products and services where we do not have the scale to achieve a lower cost structure on our own. For example, under our alliance with *Dufresne Furniture and Appliances* of Winnipeg, Dufresne manages product assortment, marketing and distribution for the furniture and appliance categories in our Northern and NorthMart store banners. This has given us access to expertise and buying power and has allowed us to reduce inventories. Our new store banners and recent acquisitions have further enabled us to achieve cost efficiencies in direct importing, freight consolidation and general administration expenses while enabling us to share our specialized retail knowledge and ideas among our retail, wholesale and support service groups.



# Consolidated Results

## 2009 Highlights

- Sales increased 3.7% to \$1.444 billion, led by food same store sales growth.
- Trading profit increased 6.6% to \$130.3 million, our tenth consecutive year of growth.
- Return on equity improved to 29.3% as a result of net earnings growth.
- Total returns to unitholders were 20.5% for the year and were 19.7% on a compound annual basis over the past five years.
- Consolidation of the International procurement and marketing functions was completed which is expected to deliver annualized savings of US\$300,000.
- New warehouse management information systems were implemented in Canada and distribution centers were opened in our Canadian and International Operations which are expected to provide increased productivity and efficiency.

## 2009 CORPORATE STRATEGIC INITIATIVES

### Initiative #1

#### Build leadership capabilities

##### Result

By the end of the year, all senior management direct reports have been instructed on the key elements of our Leadership practices. The focus for 2010 is to introduce the Leadership practices to the next level of the organization and continue to refine the effectiveness of the practices at higher levels.

### Initiative #2

#### Business planning

##### Result

The planning framework developed at the Board level in 2008 was utilized in our 2009 long range plan and the subsequent roll-out of our 2010 operating plan and key LRP initiatives.

### Initiative #3

#### Energy conservation programs

##### Result

High-payback energy efficient lighting systems were installed in 10 of the CUL stores. Energy conservation upgrades including energy efficient refrigeration, heat reclaim systems and building control systems were completed in 18 Northern stores.

Some of the key performance indicators used by management to assess results are summarized in the following table:

### Key Performance Indicators

(\$ in thousands, except per unit)	2009	2008	2007
Sales	\$ 1,444,366	\$ 1,392,634	\$ 1,064,490
Same store sales % increase <sup>1</sup>	0.1%	2.7%	6.7%
Trading profit <sup>2</sup>	\$ 130,274	\$ 122,257	\$ 106,557
EBIT <sup>2</sup>	\$ 95,124	\$ 90,203	\$ 79,607
Net earnings	\$ 81,813	\$ 75,378	\$ 62,991
Net earnings per unit—basic	\$ 1.71	\$ 1.58	\$ 1.32
Net earnings per unit—diluted	\$ 1.69	\$ 1.56	\$ 1.31
Cash distributions in the year	\$ 1.39	\$ 1.40	\$ 1.13
Total assets	\$ 623,800	\$ 609,173	\$ 529,670
Total long-term liabilities	\$ 161,928	\$ 162,547	\$ 138,470
Return on net assets <sup>3</sup>	18.7%	19.8%	21.0%
Return on average equity	29.3%	28.6%	24.9%

1 All references to same store sales excludes the foreign exchange impact

2 See Non-GAAP measures section on page 26

3 Earnings before interest and income taxes as a percentage of average net assets employed

**Consolidated Sales** Sales for the year ending January 31, 2010 ("2009") increased 3.7% to \$1.444 billion compared to \$1.393 billion for the year ending January 31, 2009 ("2008") and were up 35.7% compared to \$1.064 billion for the year ending January 31, 2008 ("2007"). Excluding the foreign exchange impact, sales increased 2.4% from 2008 and were up 31.7% from 2007. On a same store basis, sales increased 0.1% compared to increases of 2.7% in 2008 and 6.7% in 2007.

Food sales increased 7.4% over 2008 and were up 5.8% excluding the foreign exchange impact as a result of new stores and strong same store sales growth across all banners. Same store food sales increased 3.1% over last year with quarterly same store increases of 4.3%, 3.6%, 1.7% and 2.8% in the fourth quarter. Canadian food sales increased 5.9% and International food sales were up 5.5% excluding the foreign exchange impact.

General merchandise sales decreased 7.5% compared to 2008 and were down 8.1% excluding the foreign exchange impact. Same store general merchandise sales decreased by 9.5%, although the trend improved during the year with same store sales decreases of 16.5%, 11.5%, 10.3% and 1.6% from the first to fourth quarter respectively. General merchandise sales were adversely affected by a sharp drop in discretionary spending power, caused principally by lower natural resource and tourism activity compared to the previous five years.

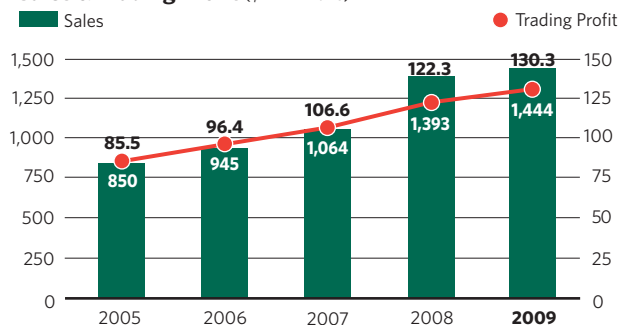
Other revenue, which includes fuel, fur and service charge revenue, decreased 3.1% compared to 2008 largely due to lower oil prices.

**Sales Blend** The table below shows the consolidated sales blend over the past three years:

	2009	2008	2007
Food	77.2%	74.6%	70.1%
General merchandise	19.8%	22.2%	26.1%
Other	3.0%	3.2%	3.8%

Canadian Operations accounted for 63.8% of total sales (64.6% in 2008 and 80.1% in 2007) while International Operations contributed 36.2% (35.4% in 2008 and 19.9% in 2007).

### Sales & Trading Profit (\$ in millions)



**Cost of sales, selling and administrative** Cost of sales, selling and administrative expenses (expenses) increased 3.4% to \$1.314 billion but decreased 24 basis points as a percentage of sales compared to last year. New and non-comparable store expenses and the impact of the weaker Canadian dollar on the translation of International Operations expenses accounted for all of the dollar increase. On a comparable store basis excluding



the foreign exchange impact, expenses decreased 30 basis points as a percentage of sales. Lower operating costs in the Canadian Operations as a result of expense reduction initiatives, higher staff productivity and income earned from financial services contributed to the decrease in expenses.

**Amortization** Amortization expense increased \$3.1 million or 9.7% to \$35.2 million from 2008 due in part to amortization of new stores.

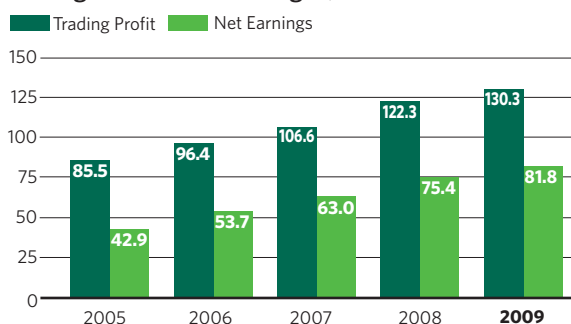
**Interest expense** Interest expense decreased 34.2% to \$5.5 million compared to \$8.3 million last year. The impact of lower interest rates during the year more than offset higher average debt levels compared to 2008. The average cost of borrowing was 2.4% compared to 4.3% in 2008 which more than offset higher average debt levels in 2009 compared to 2008.

**Income tax expense** The provision for income taxes increased 20.3% from \$6.5 million to \$7.8 million, for an effective tax rate of 8.8% in 2009 compared to 8.0% in 2008. This increase was due to higher earnings in the International Operations and a reduction in future income tax assets.

In the ordinary course of business, the Company is subject to ongoing audits by taxation authorities. While the Company believes that its tax filing positions are appropriate and supportable, the possibility exists that certain matters may be reviewed and challenged by the taxation authorities. The Company regularly reviews the potential for adverse outcomes and the adequacy of its tax provisions. The Company believes that it has adequately provided for these matters. If the final outcome differs materially from the tax provisions, the Company's income tax expense and its earnings could be affected positively or negatively in the period in which the matters are resolved.

A more detailed explanation of the income tax provision and future tax assets is provided in Note 14 to the consolidated financial statements.

#### Trading Profit & Net Earnings (\$ in millions)



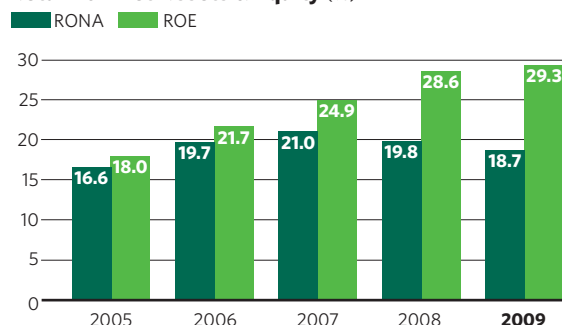
**Net earnings** Consolidated net earnings increased 8.5% to \$81.8 million or \$1.69 per unit on a diluted basis compared to \$1.56 per unit in 2008. In 2009, the Canadian dollar was on average weaker than the U.S. dollar compared to the first three quarters of 2008. The Canadian dollar's depreciation versus the U.S. dollar in 2008 had the following net impact on the 2009 results:

Sales .....increase of \$19.0 million or 1.4%  
 Trading profit .....increase of \$1.2 million  
 Net earnings.....increase of \$573,000

**Total Assets** Consolidated assets increased 2.4% to \$623.8 million compared to \$609.2 million in 2008 and were up 17.8% compared to \$529.7 million in 2007. The increase in consolidated assets is mainly due to new stores. Additional information on total assets for the Canadian and International Operations is included under operational net assets employed on page 9 and page 11 respectively.

Return on net assets employed decreased to 18.7% from 19.8% in 2008 while return on equity improved to 29.3% from 28.6% in 2008. Return on net assets decreased due to higher average net assets related to investments in information systems, new distribution centers and our head office renovation that have a longer term impact on productivity. Net assets were also higher due to planned increases in inventory in stores serviced by sea and winter road as well as temporary increases in inventory during the launch of new systems and distribution centers. Return on equity improved due to net earnings growth.

#### Return on Net Assets & Equity (%)



**Total long-term liabilities** Consolidated long-term liabilities decreased \$619,000 or 0.4% to \$161.9 million from 2008 but increased 16.9% from 2007. The increase in long-term liabilities from 2007 is largely due to the senior notes that were issued in June 2009 and increases in the Canadian Operations revolving loan facilities. Further information on long-term debt is included in the sources of liquidity and capital structure sections on page 12 and page 13 respectively.

# Canadian Operations

## 2009 CANADIAN OPERATIONS STRATEGIC INITIATIVES

### Initiative #1

**Continue the development of store selling and control capability in the Northern Canada Retail division**

#### Result

Progress on this initiative was mixed in 2009. Inventory shrinkage and controllable store operating expense initiatives met targets. Store selling initiatives fell short of target throughout the year but improvements were made towards meeting target in the fourth quarter.

### Initiative #2

**Improve store brand penetration**

#### Result

147 new store brand products were launched in the year for a total of 361 and the penetration rate increased to 14.0% compared to 12.4% in 2008.

### Initiative #3

**Open three Giant Tiger stores**

#### Result

Two Giant Tiger stores were opened.

### Initiative #4

**Warehouse efficiency improvements**

#### Result

Warehouse efficiency improvements focused on three initiatives. Warehouse processing and shipping schedules were realigned in February 2009 which achieved the planned annualized savings of \$1.0 million. A warehouse management system was implemented mid-year with the anticipated benefits starting to be realized at the end of the year. The Alberta warehousing activity was transferred to Edmonton from Calgary to improve service to the stores. The savings from these initiatives were offset by training and start-up costs incurred during the system conversion and transition to a new distribution center in 2009 but the efficiencies gained are expected to provide ongoing benefits.

### Initiative #5

**Financial Services expansion**

#### Result

The streamlined in-house version of our "Link" personal income tax service increased the number of returns prepared by 32% and revenue by 187% compared to last year.

**Financial Performance** Results of Canadian Operations are summarized by the key performance indicators used by management as follows:

### Key Performance Indicators

(\$ in thousands)	2009	2008	2007
Sales	\$ 921,621	\$ 899,263	\$ 852,773
Same store sales % increase	1.1%	1.9%	6.9%
Trading profit <sup>1</sup>	\$ 96,599	\$ 90,606	\$ 87,410
EBIT <sup>1</sup>	\$ 69,872	\$ 66,105	\$ 64,776
Return on net assets	20.0%	20.9%	20.8%

1 See Non-GAAP measures section on page 26

**Sales** Canadian sales increased 2.5% to \$921.6 million compared to \$899.3 million in 2008 and were up 8.1% or \$68.8 million compared to 2007. Same store sales increased 1.1% compared to a 1.9% increase in 2008. Food sales accounted for 72.0% (69.6% in 2008) of total Canadian sales. The balance was made up of general merchandise sales at 23.8% (25.9% in 2008) and other sales, which consists primarily of fuel sales and service charge revenue at 4.2% (4.5% in 2008).

Food sales increased by 5.9% over 2008 and were up 15.3% compared to 2007. Annual same store food sales increased 4.4% compared to 5.8% in 2008. Same store food sales were strong throughout the year with quarterly increases of 3.9%, 4.2%, 3.8% and 5.5%. Food sales increased in all categories with grocery, chilled foods, tobacco and non-food grocery categories contributing the largest gains. More aggressive key selling day promotions, more opportunity buys and the expansion in value-priced, control-label products were factors in driving sales gains across all banners. Net inflation was 1.5% with product cost inflation being partially offset by lower fuel-related transportation costs.

General merchandise sales decreased 5.8% from 2008 and were down 8.6% compared to 2007. Same store sales decreased 7.7% compared to a decrease of 7.8% in 2008. On a quarterly basis, same store sales decreased 17.3%, 11.4% and 4.8% in the first three quarters before showing signs of recovery in the fourth quarter with an increase of 0.5%. The decrease in general merchandise sales was largely due to lower discretionary income related to general economic conditions in southern Canada and significantly lower resource development activity in the north. The decrease in discretionary income had the largest impact on sales in home furnishings and transportation which combined, accounted for 55.0% of the general merchandise sales decrease.

Other revenues, which include fuel, fur and service charge revenue, were down 3.1% from 2008 but increased 4.9% over 2007. The decrease in other revenues is primarily due to oil price deflation.

**Sales Blend** The table below shows the sales blend for the Canadian Operations over the past three years:

	2009	2008	2007
Food	72.0%	69.6%	67.5%
General merchandise	23.8%	25.9%	28.2%
Other	4.2%	4.5%	4.3%

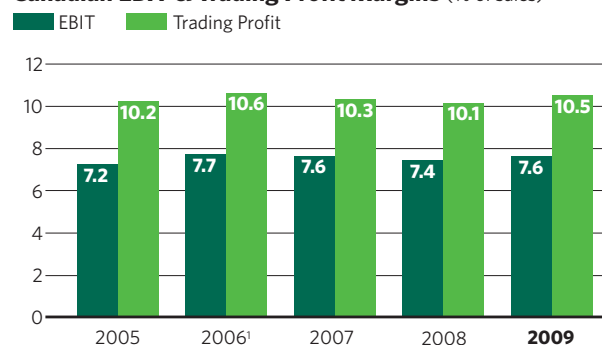
**Same Store Sales** Canadian Operations have consistently achieved top-quartile same store food sales reflecting the Company's local market position as an everyday product and service provider amid generally robust consumer spending on these categories. Same store general merchandise sales have been more volatile because they are heavily weighted to big-ticket durable goods that depend upon customers' discretionary income. Same store sales for the past three years are shown in the following table:

### Same Store Sales

(% change)	2009	2008	2007
Food	4.4%	5.8%	6.8%
General merchandise	(7.7%)	(7.8%)	7.3%
Total sales	1.1%	1.9%	6.9%

**Profitability** Gross profit dollars for Canadian Operations increased by 1.3% as sales growth more than offset a 37 basis point decrease in gross profit rates. An increase in food gross profit, largely driven by sales gains, offset lower gross profit in general merchandise as a result of higher markdowns required to clear slow-moving seasonal and big-ticket merchandise and the impact of a lower mark-up strategy on electronics. Operating expenses were down 0.3% from 2008 and were down 60 basis points as a percentage of sales compared to last year. Expense reduction initiatives, staff productivity gains and income growth from financial services largely offset operating expenses from new stores. Trading profit from Canadian Operations increased \$6.0 million or 6.6% to \$96.6 million and was 10.5% as a percentage of sales compared to 10.1% in 2008.

#### Canadian EBIT & Trading Profit Margins (% of sales)



<sup>1</sup> EBIT and Trading Profit Margins on an equivalent year basis

**Operational Net Assets Employed** Operational net assets employed at January 31, 2010, increased 6.5% to \$329.3 million compared to \$309.3 million at January 31, 2009, as summarized in the following table:

#### Operational Net Assets Employed

(\$ millions at the end of the fiscal year)	2009	2008	2007
Property and equipment	\$ 183.8	\$ 173.9	\$ 160.4
Inventory	122.3	120.1	113.2
Accounts receivable	61.7	57.5	55.8
Other assets	41.4	34.7	23.5
Liabilities	(79.9)	(76.9)	(72.3)
<b>Total</b>	<b>\$ 329.3</b>	<b>\$ 309.3</b>	<b>\$ 280.6</b>

Property and equipment balances increased reflecting the opening of new stores, gas bars and pharmacies, store renovation projects, a new distribution facility in Edmonton, Alberta, the replacement of our food warehouse management system, corporate information systems upgrades and a major head office renovation project.

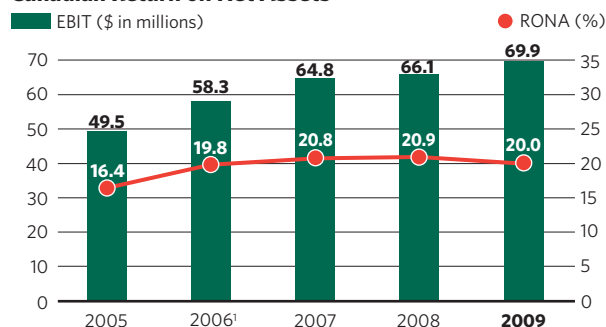
Inventory increased from the prior year primarily due to new stores and higher food inventories related to the opening of a new distribution center late in the fourth quarter. Average inventory levels were also higher throughout 2009 compared to 2008 due to an increase in food inventories in stores serviced by sea and winter road in order to realize cost advantages compared to air freight.

The increase in accounts receivable outstanding at year end is due to higher amounts owing on customer and commercial accounts receivable compared to 2008. Accounts receivable throughout the year was on average \$634,000 higher than 2008 but was \$1.8 million lower than 2007. From 2005 to 2009, average accounts receivable have decreased \$4.5 million reflecting a higher volume of cash sales.

Other assets increased largely due to a \$4.0 million special contribution to the Company's defined benefit pension plan to reduce the unfunded liability. The increase in liabilities over the prior year is due to higher trade accounts payable and an increase in accrued expenses.

**Return on Net Assets** The return on net assets employed for Canadian Operations decreased to 20.0% from 20.9% in 2008 due to the impact of higher average net assets compared to last year.

#### Canadian Return on Net Assets



<sup>1</sup> EBIT and Return on net assets on an equivalent year basis

# International Operations

(Stated in U.S. dollars)

International Operations include Alaska Commercial Company (“AC”), Cost-U-Less, Inc. (“CUL”) which was acquired on December 13, 2007 and Span Alaska Enterprises, Inc. (“Span”) acquired on March 3, 2008. AC, CUL and Span were merged into The North West Company (International) Inc. (“NWCI”) on December 31, 2008.

## 2009 INTERNATIONAL OPERATIONS STRATEGIC INITIATIVES

### Initiative #1

#### Cost-U-Less integration

##### Result

The integration of the merchandising systems was completed by July 1, 2009 and the procurement and marketing function between AC and CUL was consolidated into our NWCI Bellevue, Washington office. This completes the final phase of our post CUL acquisition integration with the additional expected annualized savings of \$300,000 being realized.

### Initiative #2

#### Warehouse efficiency improvements

##### Result

The objective of this initiative was to improve the efficiency of NWCI warehouse operations by reducing the number of warehouse facilities from three to two. Two warehouse operations in Anchorage were consolidated into one facility and a distribution center in Monroe, Washington was replaced by a better suited facility at the Port of Tacoma, Washington. This restructuring of the warehouse activities was largely completed by the end of the year with full integration completed in February 2010. The changes will improve productivity in the warehouse and service to the stores and are expected to result in annualized savings of \$600,000 per year.

### Initiative #3

#### Wholesale integration

##### Result

The branding, sales, systems and distribution integration was completed in February 2010, with NWCI’s Span and Frontier Expeditors wholesale operations consolidated under the new name of Pacific Alaska Wholesale (“PAW”).

**Financial Performance** International Operations results for the year are summarized below by the key performance indicators.

### Key Performance Indicators

(\$ in thousands)	2009	2008	2007
Sales	\$ 464,167	\$ 454,636	\$ 199,714
Same store sales %	(2.1%)	6.9%	5.6%
Trading profit <sup>1</sup>	\$ 29,902	\$ 29,165	\$ 18,062
EBIT <sup>1</sup>	\$ 22,422	\$ 22,205	\$ 13,991
Return on net assets	16.0%	17.2%	21.7%

<sup>1</sup> See Non-GAAP measures section on page 26

**Sales** International sales increased 2.1% to \$464.2 million compared to \$454.6 million in 2008 and were up 132.4% or \$264.5 million compared to 2007 largely due to new stores. Same store sales decreased 2.1% compared to a 6.9% increase in 2008. Food sales accounted for 86.4% (83.6% in 2008) of total sales with the balance comprised of general merchandise at 12.8% (15.5% in 2008) and other sales, which consists primarily of fuel sales and service charge revenues, at 0.8% (0.9% in 2008).

Food sales increased 5.5% over 2008 and were up 148.2% compared to 2007 primarily due to new stores and strong sales growth in our wholesale operations, PAW. Same store food sales were up 0.6% compared to a 7.3% increase in 2008. Food sales started the year strong with quarterly same store sales increases of 4.9% and 2.3% but softened in the back half of the year with decreases of 2.1% and 2.2%. Food sales benefited from an increase in payments to low-income consumers under the U.S. federal government’s Supplemental Nutrition Assistance Program however, deteriorating economic conditions combined with lingering high utility costs in rural Alaska negatively impacted same store food sales in the second half of the year. Sales in grocery, frozen foods and snack food categories had the largest gains compared to more expensive, highly perishable categories.

General merchandise sales decreased 15.9% from 2008 but were up 69.1% over 2007. On an annual basis, general merchandise same store sales were down 15.6% compared to an increase of 5.1% in 2008. General merchandise same store sales were weak all year with quarterly decreases of 13.8%, 11.6%, 25.4%, and 9.6%. Weaker economic conditions and the consequential impact on both tourism in our southern island markets and resource royalties in Alaska constrained consumer discretionary spending. In particular, a decrease in the Permanent Fund Dividend (PFD) in Alaska, which was \$1,305 this year compared to \$3,269 in 2008, was a significant factor contributing to the 25.4% same store general merchandise sales decrease in the third quarter. The largest impact was in the big-ticket categories of home furnishings, electronics and transportation which had a combined sales decrease of 23.9% compared to 2008 and accounted for approximately 48% of the overall decrease in general merchandise sales.

Other revenues, which consist of fuel and service charge revenue, were down 6.5% from 2008 due to oil price deflation.

**Sales Blend** The table below reflects the importance of food sales to the total sales of the International Operations:

	2009	2008	2007
Food	86.4%	83.6%	80.9%
General merchandise	12.8%	15.5%	17.6%
Other	0.8%	0.9%	1.5%

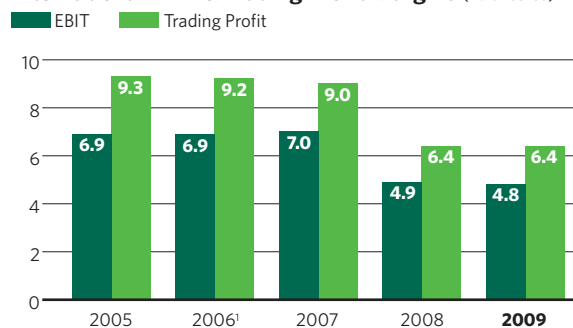
Same store sales for the past three years are shown in the following table:

### Same Store Sales

(% change)	2009	2008	2007
Food	0.6%	7.3%	4.8%
General merchandise	(15.6%)	5.1%	8.8%
Total sales	(2.1%)	6.9%	5.6%

**Profitability** Gross profit dollars increased 3.3% over 2008 driven by new store sales growth and a 30 basis point gross profit rate improvement. The increase in gross profit rate was partially due to more efficient purchasing processes and lower buying costs facilitated by the consolidation of the NWCI procurement and marketing functions into our Bellevue, Washington office. A decrease in the sales blend of lower margin, big-ticket general merchandise categories was also a contributing factor. Operating expenses increased 4.0% over last year and were up 38 basis points as a percent of sales. Higher staff costs caused by a sharp rise in Company-funded medical insurance costs and one-time expenses related to the consolidation of our procurement and marketing functions in our Bellevue office and the consolidation of our wholesale operations and distribution facilities were the leading factors contributing to the increase in operating expenses. These factors were partially offset by a reduction in energy-related occupancy costs in southern island locations as a result of lower utility rates and investments in new energy efficient store lighting. Trading profit increased 2.5% to \$29.9 million compared to \$29.2 million in 2008 and as a percentage of sales was consistent with last year at 6.4%.

### International EBIT & Trading Profit Margins (% of sales)



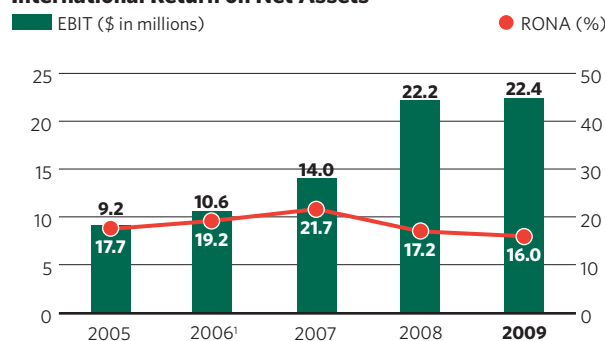
<sup>1</sup> Equivalent year basis excluding \$1.4 million IRS housing benefit assessment

### Operational Net Assets Employed

(\$ millions at the end of the fiscal year)	2009	2008	2007
Property and equipment	\$ 70.6	\$ 60.7	\$ 62.8
Inventory	52.2	49.9	49.2
Accounts receivable	9.4	8.9	6.9
Other assets	12.7	14.8	12.8
Liabilities	(31.3)	(30.0)	(37.0)
Total	\$ 113.6	\$ 104.3	\$ 94.7

International Operational net assets employed increased \$9.3 million or 8.9% from 2008 due largely to two stores opened during the year and the acquisition of a store and retail mall in Sitka, Alaska (see Note 22 to the consolidated financial statements).

### International Return on Net Assets



<sup>1</sup> Equivalent year basis excluding \$1.4 million IRS housing benefit assessment

## Consolidated Liquidity and Capital Resources

The following table summarizes the major components of cash flow:

(\$ in thousands fiscal year)	2009	2008	Change
Cash flows from (used in):			
Operating activities	\$ 107,973	\$ 90,178	\$ 17,795
Investing activities	\$ (59,372)	\$ (49,435)	\$ (9,937)
Financing activities	\$ (47,053)	\$ (36,745)	\$ (10,308)
Net change in cash	\$ 1,548	\$ 3,998	\$ (2,450)

**Cash from operating activities** Cash flow from operating activities increased \$17.8 million to \$108.0 million from \$90.2 million in 2008. Changes in non-cash working capital negatively impacted cash flow from operating activities by \$6.7 million compared to a decrease in cash flow of \$17.5 million in 2008. The change in non-cash working capital is largely due to an increase in accounts receivable and inventories as noted in the Canadian and International operational net assets employed on pages 9 and 11 respectively. The decrease in cash flow from other non-cash items is due to the change in other assets in the Canadian Operations related to a \$4.0 million special contribution to the Company's defined benefit pension plan.

**Cash used in investing activities** Net cash used in investing activities was \$59.4 million compared to \$49.4 million in 2008. Net investing in Canadian Operations was \$39.6 million (\$36.0 million in 2008). A summary of the Canadian Operations investing activities is included in operational net assets on page 9. Net investing in International Operations was \$19.8 million compared to \$13.4 million in 2008. Investing activities in the International Operations include the \$12.2 million acquisition of the retail mall and store in Sitka, Alaska, store renovations, equipment replacements and energy conservation projects.

The following table summarizes the number of stores and selling square footage under NWC's various retail banners at the end of the fiscal year:

	Number of Stores		Selling square footage	
	2009	2008	2009	2008
Northern	127	127	720,773	718,690
NorthMart	7	7	148,306	152,141
Quickstop	15	14	28,571	24,463
Giant Tiger	31	29	509,078	479,660
AC Value Centers	29	28	290,403	271,892
Cost-U-Less	12	12	336,138	336,138
Other Formats	5	4	42,841	29,611
Total at year end	226	221	2,076,110	2,012,595

During the year, two Giant Tiger stores were opened in Canada. Total selling square feet in Canada increased to 1,423,329 from 1,395,661 in 2008.

In our International Operations, new stores included one AC Value Center and one Quickstop in Alaska and our first store under the Island Fresh banner in Chalan Pago, Guam (included in Other Formats). International selling square feet increased to 652,781 from 616,934 in 2008.

Net capital expenditures for 2010 are expected to be in the range of \$59 million (\$59.4 million in 2009) reflecting the opening and acquisition of new stores, store renovation and energy conservation projects, pharmacy openings and acquisitions, store point-of-sale system upgrades and the completion of a major head office renovation project.

**Cash used in financing activities** Cash used in financing activities was \$47.1 million compared to \$36.7 million in 2008. The decrease in bank advances is due to lower borrowings in the International Operations. Cash provided from long-term debt, net of repayments, was \$20.4 million compared to \$29.4 million in 2008. On June 15, 2009, the Company completed the private placement issuance of US\$70 million 6.55% senior notes which will mature June 15, 2014. The net proceeds were used to repay the US\$39 million senior notes which matured on June 15, 2009, to reduce bank debt and for general corporate purposes. The senior notes are secured by the assets of the Company. The Fund paid distributions of \$67.2 million or \$1.39 per unit, compared to \$67.7 million or \$1.40 per unit last year. Repayments of loans granted under the Company's Unit Purchase Loan Plan (UPLP) were \$4.9 million compared to \$1.0 million in 2008. There were no new loans granted during the year and the remaining loans under the UPLP mature January 31, 2011.

**Sources of liquidity** The Canadian Operations have available extendible, committed, revolving loan facilities of \$140.0 million that mature on December 31, 2011. These facilities are secured by a floating charge on the assets of the Company and rank pari passu with the senior notes. These facilities bear interest at Bankers Acceptance rates plus stamping fees or the Canadian prime rate. At January 31, 2010, the Company had drawn \$72.9 million (January 31, 2009 - \$90.0 million) on these facilities.

The Company's International Operations have available committed, non-revolving loan facilities of US\$52.0 million that mature on December 31, 2010. These facilities are secured by a floating charge against the assets of the Company and rank pari passu with the senior notes. These facilities bear interest at London Interbank Offered Rate (LIBOR) plus stamping fees or the U.S. prime rate. At January 31, 2010, the Company had drawn US\$52.0 million (January 31, 2009 - US\$52.0 million) on these facilities. The Company has started the process of refinancing the US\$52.0 million loan facility. Global economic conditions continue to result in uncertainty and volatility in the credit markets which may negatively impact the availability of credit, interest rates and covenants for companies seeking to refinance debt. Based on the current economic conditions, the Company does not anticipate any difficulty in securing financing to satisfy its maturing long-term debt however, these conditions could change which could impact the Company's ability to obtain financing. For further information on risks related to refinancing, see liquidity risk in the risk management section on page 20.



The International Operations also have available demand revolving loan facilities of US\$15.0 million at interest rates of U.S. prime. These loans are secured by a floating charge against accounts receivable and inventories of the International Operations. At January 31, 2010, the Company had US\$293,000 (January 31, 2009 - US\$4.8 million) in bank advances drawn on these facilities.

At January 31, 2010, the Canadian Operations have outstanding US\$70.0 million senior notes compared to US\$39.0 million at January 31, 2009. The US\$70.0 million senior notes have been designated as a hedge against the U.S. dollar investment in the self-sustaining International Operations. Of this amount, there is US\$42.0 million of the senior notes at a fixed interest rate of 6.55%. Interest on US\$28.0 million has been converted by an interest rate swap from fixed to floating rates at three-month LIBOR plus spreads. For more information on the senior notes and financial instruments see Note 9 and Note 20 to the consolidated financial statements.

The coverage ratio of EBIT to interest improved to 17.3 times from 10.9 times in 2008. The coverage ratio improved due to the impact of lower interest rates and an increase in EBIT.

#### Interest Costs and Coverage

	2009	2008	2007
Coverage ratio	<b>17.3</b>	10.9	10.6
EBIT (\$ in millions)	<b>\$ 95.1</b>	\$ 90.2	\$ 79.6
Interest (\$ in millions)	<b>\$ 5.5</b>	\$ 8.3	\$ 7.5

The bank credit facilities and senior notes contain covenants and restrictions including the requirement to meet certain financial ratios and financial condition tests. The financial covenants include a fixed charge coverage ratio, minimum current ratio, a leverage test and a minimum net worth test. At January 31, 2010, the Fund is in compliance with all covenants under these facilities. Current and forecasted debt levels are regularly monitored for compliance with debt covenants.

#### Contractual Obligations and Other Commitments

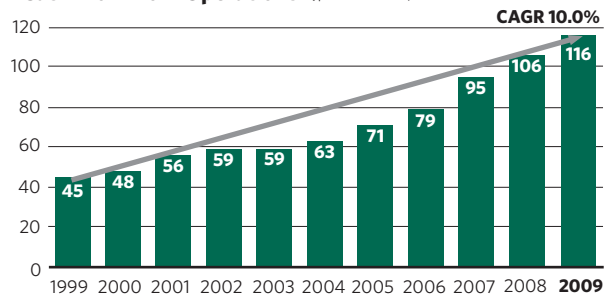
Contractual obligations of the Company are listed in the chart below:

(\$ in thousands)	Total	0-1 Year	2-3 Years	4-5 Years	6 Years+
Long-term debt (including capital lease obligations)	\$ 208,858	\$ 56,339	\$ 74,535	\$ 74,348	\$ 3,636
Operating leases	138,309	19,397	33,577	26,279	59,056
Other long-term liabilities	7,641	160	4,995	250	2,236
<b>Total</b>	<b>\$ 354,808</b>	<b>\$ 75,896</b>	<b>\$ 113,107</b>	<b>\$ 100,877</b>	<b>\$ 64,928</b>

Cash flow from operations and unutilized credit available on existing credit facilities are expected to be sufficient to fund operating requirements, sustaining and growth-related capital expenditures as well as anticipated distributions during 2010.

The compound annual growth rate (CAGR) for cash flow from operations over the past 10 years is 10.0% as shown in the following graph:

#### Cash Flow from Operations<sup>1</sup> (\$ in millions)



<sup>1</sup> See Non-GAAP measures section on page 26

#### Trustee, Director and Officer Indemnification Agreements

The Company has agreements with its current and former trustees, directors and officers to indemnify them against charges, costs, expenses, amounts paid in settlement and damages incurred from any lawsuit or any judicial, administrative or investigative proceeding in which they are sued as a result of their service. Due to the nature of these agreements, the Company cannot make a reasonable estimate of the maximum amount it could be required to pay to counterparties. The Company has also purchased trustees', directors' and officers' liability insurance. No amount has been recorded in the financial statements regarding these indemnification agreements.

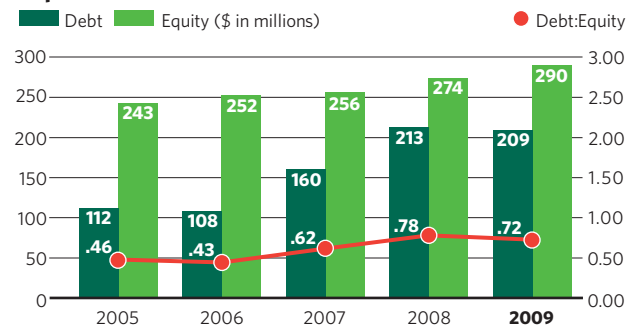
#### Other Indemnification Agreements

The Company provides indemnification agreements to counterparties for events such as intellectual property right infringement, loss or damage to property, claims that may arise while providing services, violation of laws or regulations, or as a result of litigation that might be suffered by the counterparties. The terms and nature of these agreements are based on the specific contract. The Company cannot make a reasonable estimate of the maximum amount it could be required to pay to counterparties. No amount has been recorded in the financial statements regarding these agreements.

#### Capital Structure

On a consolidated basis, NWF had \$209.2 million in debt and \$289.9 million in equity at the end of the year and a debt-to-equity ratio of .72:1 compared to .78:1 last year. The decrease in the debt-to-equity ratio from last year is due in part to the strengthening Canadian dollar and the impact on the translation of U.S. denominated debt.

#### Capital Structure





The strength of the Fund's capital structure is reflected in the preceding chart. Over the past five years, the Fund's debt-to-equity ratio has ranged from .43:1 to .78:1 while annual cash distributions to unitholders have ranged from \$0.63 to \$1.40 over the same period. Equity has increased 19.5% to \$289.9 million over the past five years and interest-bearing debt has increased to \$209.2 million from \$111.7 million in 2005.

Loans receivable from officers and selected senior management under the unit purchase loan plan (UPLP) have decreased to \$6.4 million at January 31, 2010 from \$11.3 million at January 31, 2009. These loans, which are recorded as a reduction of equity, are secured by a pledge of 361,318 units of the Company with a quoted value at January 31, 2010 of \$6.5 million. The loans are non-interest bearing and repayable from the after-tax distributions or if the officer sells the units or leaves the Company. In 2008, the Trustees approved new unit-based long-term incentive plans for officers and senior management as a replacement for loans granted under the UPLP which mature January 31, 2011. The unit-based long term incentive plans include restricted and performance based units introduced in 2008 and options granted under the unit option plan approved in 2009. Further information on security-based compensation is provided in Note 19 to the consolidated financial statements.

Consolidated debt at January 31, 2010 decreased \$3.9 million or 1.8% to \$209.2 million compared to \$213.0 million in 2008 and was up 30.9% from \$159.8 million in 2007. The decrease in debt is due in part to an increase in U.S. denominated debt and the impact of the stronger Canadian dollar on the translation of U.S. denominated debt. The exchange rate used to translate U.S. denominated debt into Canadian dollars was 1.0650 at January 31, 2010 compared to 1.2364 at January 31, 2009 which resulted in a \$22.1 million decrease in long-term debt. The Company's U.S. denominated debt that was not subject to cross-currency swaps increased to US\$129.0 million in 2009 compared to US\$99.3 million in 2008 and US\$103.5 million in 2007. This increase was largely due to the US\$70.0 million 6.55% senior notes issued in 2009, the proceeds of which were used to repay the remaining US\$39.0 million of the US\$65.0 million 5.89% senior notes that matured on June 15, 2009 and to reduce amounts outstanding under the revolving loans. The debt outstanding at the end of the fiscal year is summarized as follows:

#### Debt

(\$ in thousands at the end of the fiscal year)	2009	2008	2007
Senior notes	\$ 73,481	\$ 48,411	\$ 57,292
Revolving loan facilities	72,853	90,031	41,919
Non-revolving loan facilities	55,380	64,293	52,114
Notes payable	5,567	1,799	1,726
Capital leases	1,577	2,518	2,446
Bank advances	312	5,974	4,336
<b>Total</b>	<b>\$ 209,170</b>	<b>\$ 213,026</b>	<b>\$ 159,833</b>

**Unitholder Equity** The Fund has an unlimited number of units authorized and had issued and outstanding units at January 31, 2010 of 48,378,000 (48,378,000 as at January 31, 2009). Further information on the Fund's capital is provided in Note 11 to the consolidated financial statements.

Book value per unit, on a diluted basis, at the end of the year increased to \$6.12 from \$5.90 in 2008. Book equity was positively impacted by an increase in retained earnings of \$15.1 million (\$9.9 million in 2008) after distributions of \$66.8 million (\$65.3 million in 2008).

**Unitholder Distributions** The Fund paid distributions of \$67.2 million or \$1.39 per unit compared to \$67.7 million or \$1.40 per unit paid in 2008. In 2009, the Company made a \$4.0 million special contribution to reduce the unfunded liability of the defined benefit pension plan which reduced the amount of income available for distribution to unitholders by approximately \$0.08 per unit. The following table shows the quarterly cash distributions per unit paid for the past three years:

	2009	2008	2007
First Quarter	\$ 0.32	\$ 0.32	\$ 0.22
Second Quarter	0.32	0.32	0.27
Third Quarter	0.34	0.32	0.27
Fourth Quarter	0.34	0.32	0.27
Special	0.07	0.12	0.10
<b>Total</b>	<b>\$ 1.39</b>	<b>\$ 1.40</b>	<b>\$ 1.13</b>

The determination to declare and make payable distributions from the Fund is subject to the terms of the Fund's Declaration of Trust and the discretion of the Board of Trustees. The Fund's distribution policy is to make distributions to unitholders equal to the taxable income of the Fund. Historically, distributions from the Fund represented taxable income and did not include a return of unitholder capital. Management believes distributions in 2010 will continue to represent taxable income.

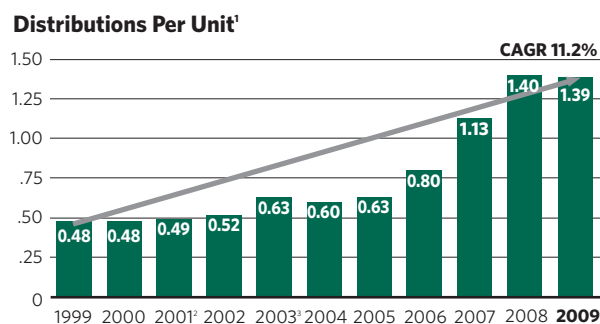
In determining the quarterly distributions, the Trustees consider, among other factors, the seasonal variations in earnings inherent in the retail industry in order to maintain stable distributions throughout the year. On an annual basis, distributions are funded by cash flow from operations. Due to the seasonal nature of the retail business, whereby income and cash flow are historically lower in the first quarter and higher in the fourth quarter, distributions in a quarter may exceed cash flow from operations. The taxable income of the Fund is primarily based on an allocation of the taxable income of The North West Company LP less Fund expenses. In addition to the quarterly distributions, a special year end distribution will be declared to unitholders if the taxable income of the Fund exceeds the cumulative distributions for the year. A special distribution of \$0.06 per unit was paid February 19, 2010 to unitholders of record on December 31, 2009 (\$0.07 per unit was paid February 20, 2009 to unitholders of record on December 31, 2008). Further information on distributions is included in Note 23 to the consolidated financial statements.

The following table shows distributions paid in comparison to cash flow from operations and cash flow from operating activities for the past three years:

	2009	2008	2007
Distributions	\$ 67,245	\$ 67,730	\$ 54,667
Cash flow from operations <sup>1</sup>	\$ 116,486	\$ 106,324	\$ 94,739
Distributions as a % of cash flow from operations	57.7%	63.7%	57.7%
Cash flow from operating activities	\$ 107,973	\$ 90,178	\$ 93,591
Distributions as a % of cash flow from operating activities	62.3%	75.1%	58.4%

<sup>1</sup> See Non-GAAP measures section on page 26

The compound annual growth rate (CAGR) for distributions over the past 10 years is 11.2% as shown in the following graph:



<sup>1</sup> All per unit information has been restated to reflect the three-for-one unit split that occurred on September 20, 2006

<sup>2</sup> The Fund issued 4,305,000 additional units on a split adjusted basis

<sup>3</sup> The Fund paid a special distribution of \$0.11 per unit on a split adjusted basis

## CONVERSION TO A SHARE CORPORATION

Management and the Board of Trustees have reviewed the impact of the specified investment flow-through entities ("SIFT") Tax Rules and the related tax implications on the Fund. The SIFT Rules impose a new entity-level tax on distributions from certain SIFTs, such as the Fund, commencing January 1, 2011. Our assessment is that the Fund should remain structured as a trust until this date at which time we expect to use the SIFT conversion rules to complete a tax-deferred conversion into a publicly-traded share corporation. Conversion of the Fund to a publicly-traded share corporation is expected to provide the following benefits:

- A simplified tax and legal structure that is more comparable to public companies operating in Canada and internationally;
- Greater access to capital markets as the business continues to expand; and
- The potential of attracting new investors thereby improving the liquidity of the securities.

A number of income trusts in Canada have either converted or announced their intention to convert to a corporate structure. Management and the Board of Trustees believe that the conversion of the Fund to a publicly-traded share corporation is in the best interests of unitholders and the business and we will

be seeking unitholder approval of the proposed conversion at the Fund's annual and special meeting of unitholders scheduled for June 10, 2010. In addition to unitholder approval, the conversion to a corporate structure is also subject to customary court, regulatory, and third party approvals. The details of the conversion, which will be completed through a plan of arrangement, is contained in the Management Information Circular which is anticipated to be mailed to unitholders on or before April 30, 2010.

Whether or not the Fund converts to a corporation or remains structured as an income trust, the Canadian earnings will be subject to income taxes commencing January 1, 2011 at a combined federal and provincial tax rate of approximately 30%. Upon converting back to a corporate structure, it is the Company's intention to pay quarterly dividends of approximately the after-tax amount of the quarterly distributions prior to conversion. While higher corporate taxes will reduce NWC's net earnings available for distribution, the after-tax impact on personal income is largely offset for taxable investors benefiting from the dividend tax credit. The following illustration\* shows the impact of taxation on distributions and the dividend tax credit available to qualifying owners based on 2009 tax rates:

	Trust	Corporation
Taxable income <sup>1</sup>	\$ 1.36	\$ 1.36
Corporate income tax at 31% <sup>2</sup>	–	(0.42)
After-tax income available for distribution/dividend	\$ 1.36	\$ 0.94
Individual income tax		
Trust distribution (other income) marginal tax rate <sup>3</sup>	46.4%	–
Eligible dividend marginal tax rate <sup>4</sup>	–	23.1%
Individual income tax payable	\$ (0.63)	\$ (0.22)
After-tax distribution/dividend	\$ 0.73	\$ 0.72
Implied after-tax yield (March 26, 2010 closing price \$18.31)	4.0%	3.9%

<sup>1</sup> Annualized income based on current distribution of \$0.34 per quarter

<sup>2</sup> The effective tax rate based on substantively enacted tax rates applicable to the Fund is approximately 31%

<sup>3</sup> Based on combined federal and provincial tax rates for individuals residing in Ontario with taxable income greater than \$126,000 in 2009

<sup>4</sup> Based on combined federal and provincial eligible dividend tax rates for qualifying individuals residing in Ontario with taxable income greater than \$126,000 in 2009

\* Readers are cautioned that the illustration is based upon the corporate and individual tax rates in effect in 2009. The results will vary based upon corporate and individual income tax rates in effect, the province of residence and the taxable income for the taxpayer

Based on the current annualized distributions of \$1.36, the Company anticipates paying dividends of approximately \$0.96 annually or \$0.24 per quarter in 2011. As noted above, the dividends paid will provide qualifying owners with the benefit of the dividend tax credit which is not applicable to current distributions from the Fund. Dividends will be subject to the approval of the Board of Directors and will be based on, among other factors, the financial performance of the Company and its anticipated business needs.

## QUARTERLY FINANCIAL INFORMATION

Historically, the Company's first quarter sales are the lowest and fourth quarter sales are the highest, reflecting consumer holiday buying patterns. Weather conditions are often more extreme compared to other retailers and can affect sales in any quarter. Net earnings generally follow higher sales but can be dependent on markdown activity in key sales periods to reduce excess inventories. Net earnings are historically lower in the first quarter due to lower sales and fixed costs such as rent and overhead that apply uniformly throughout the year.

The following is a summary of selected quarterly financial information:

(\$ thousands)	Q1	Q2	Q3	Q4	Total
<b>Sales</b>					
2009	\$ 345,621	\$ 367,469	\$ 360,764	\$ 370,512	\$ 1,444,366
2008	\$ 315,468	\$ 342,358	\$ 359,081	\$ 375,727	\$ 1,392,634
<b>Trading profit</b>					
2009	\$ 27,548	\$ 34,318	\$ 36,062	\$ 32,346	\$ 130,274
2008	\$ 25,922	\$ 30,642	\$ 33,522	\$ 32,171	\$ 122,257
<b>Net earnings</b>					
2009	\$ 16,133	\$ 20,483	\$ 24,970	\$ 20,227	\$ 81,813
2008	\$ 15,235	\$ 18,434	\$ 22,065	\$ 19,644	\$ 75,378
<b>Earnings per unit—basic</b>					
2009	\$ 0.34	\$ 0.43	\$ 0.52	\$ 0.42	\$ 1.71
2008	\$ 0.32	\$ 0.39	\$ 0.46	\$ 0.41	\$ 1.58
<b>Earnings per unit—diluted</b>					
2009	\$ 0.33	\$ 0.43	\$ 0.51	\$ 0.42	\$ 1.69
2008	\$ 0.32	\$ 0.38	\$ 0.46	\$ 0.40	\$ 1.56

**Fourth Quarter Highlights** Fourth quarter consolidated sales decreased 1.4% to \$370.5 million compared to \$375.7 million in 2008. Excluding the foreign exchange impact, sales increased 3.9% and were up 1.6% on a same store basis. Food sales<sup>1</sup> increased 5.3% and were up 2.8% on a same store basis. General merchandise sales<sup>1</sup> decreased 0.6% and were down 1.6% on a same store basis. Sales growth in our Canadian Operations partially offset softer performance and the negative impact of foreign exchange on the conversion of U.S. denominated sales in our International Operations.

Cost of sales, selling and administrative expenses decreased 1.6% to \$338.2 million and decreased 17 basis points as a percentage to sales compared to the fourth quarter of 2008. The decrease was mainly due to the impact of the stronger fourth quarter average Canadian dollar on the translation of U.S. denominated International Operations expenses compared to last year.

Trading profit or earnings before interest, income taxes, depreciation and amortization (EBITDA) increased 0.5% to \$32.3 million compared to \$32.2 million in the fourth quarter last year. Trading profit gains in Canada driven largely by sales growth offset a decrease in International Operations trading profit. Interest expense decreased 29.2% to \$1.3 million as a result of lower interest rates in the quarter.

<sup>1</sup> Excluding the foreign exchange impact

Net earnings increased \$583,000 or 3.0% to \$20.2 million. Diluted earnings per unit were up 5.0% to \$0.42 compared to \$0.40 last year. The stronger Canadian dollar in the quarter compared to last year negatively impacted the conversion of earnings from the International Operations by \$0.01 per unit on a fully diluted basis.

Working capital increased 0.9% or \$1.0 million compared to the fourth quarter last year due to lower bank advances in the International Operations. The increase in the current portion of long-term debt is due to the US\$52.0 million credit facility which matures December 31, 2010 compared to the US\$39.0 million of senior notes which matured June 15, 2009.

Cash flow from operating activities in the quarter decreased \$3.2 million to \$37.7 million from \$40.9 million last year. The decrease in cash flow from operating activities is due to the change in non-cash working capital largely due to an increase in accounts receivable and a decrease in accounts payable in the quarter compared to the prior year. The change in other non-cash items is due to the increase in other assets related to a \$4.0 million special contribution to the Company's defined benefit pension plan. Cash flow from operations increased \$4.3 million or 15.6% to \$32.2 million due primarily to the increase in net earnings and the change in future income taxes in the quarter compared to last year.

Cash used for investing activities in the quarter decreased to \$11.7 million compared to \$16.9 million last year due to a difference in the timing of capital investments.

Cash used for financing activities in the quarter was \$35.0 million compared to \$26.4 million last year. The change in bank advances is due to a reduction in the amount outstanding under the International Operations credit facility. Repayments received on loans issued to officers under the Unit Purchase Loan Plan (UPLP) were \$3.0 million in the quarter. The remaining UPLP loans mature January 31, 2011. The Fund paid distributions of \$16.4 million, an increase of 6.2% compared to \$15.5 million last year.

## DISCLOSURE CONTROLS

Management has established and maintained disclosure controls and procedures for the Company in order to provide reasonable assurance that material information relating to the Company is made known to them in a timely manner. There are inherent limitations to the effectiveness of any system of disclosure controls and procedures, including the possibility of human error and the circumvention or overriding of the controls and procedures. Accordingly, even effective disclosure controls and procedures can only provide reasonable assurance of achieving their control objectives. Based on an evaluation of the Company's disclosure controls and procedures, as required by National Instrument 52-109, the Company's Chief Executive Officer and Chief Financial Officer have concluded that these controls and procedures were designed and operated effectively as of January 31, 2010 to provide reasonable assurance that the information to be disclosed is recorded, summarized and reported as required.

## INTERNAL CONTROLS OVER FINANCIAL REPORTING

Management is responsible for establishing and maintaining internal controls over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Canadian generally accepted accounting principles. All internal control systems, no matter how well designed, have inherent limitations. Therefore, even those systems determined to be effective can only provide reasonable assurance with respect to financial reporting. Based on an evaluation of the Company's internal controls over financial reporting using the framework published by The Committee of Sponsoring Organizations of the Treadway Commission (COSO Framework), the Company's Chief Executive Officer and Chief Financial Officer have concluded that the internal controls over financial reporting were designed and operated effectively as of January 31, 2010 to provide reasonable assurance with respect to financial statement preparation and presentation. There have been no changes in the internal controls over financial reporting during the year ended January 31, 2010 that have materially affected or are reasonably likely to materially affect the internal controls over financial reporting.

## OUTLOOK

2010 sales are expected to be generally stronger, led by our Canadian business. The contributing factors should be the momentum of the Canadian economic recovery, as reflected by government infrastructure investment and recovery in natural resource development spending. Durable goods sales are also expected to recover modestly due to customer replacement needs.

Sales and margin pressure are expected to continue within NWCI's CUL banner due to ongoing weakness in the tourism sector coupled with more intense competition. NWCI's other major market, Alaska, is expected to demonstrate the recovery characteristics of our Canadian business, although to a lesser degree.

Net earnings will be affected by several other factors, most notably higher pension expense in Canadian Operations due to the interest rates used to determine pension liabilities, expected higher floating interest rates and continuing health insurance cost pressures at NWCI. The strengthening of the Canadian dollar in the fourth quarter of 2009 is expected to carry forward into 2010 and, if this occurs, there will be a negative effect on the conversion of U.S. denominated NWCI sales and earnings.

## RISK MANAGEMENT

North West Company Fund is exposed to a number of risks in its business. The descriptions of the risks below are not the only ones facing North West Company Fund. Additional risks and uncertainties not presently known to the Company, or that the Company deems immaterial, may also impair the operations of the Company. If any of such risks actually occur, the business, financial condition, liquidity, and results of operations of the Company could be materially adversely affected. Readers of this MD&A are also encouraged to refer to North West Company Fund's Annual Information Form and Management Information Circular which provides further information on the risk factors facing the Company. While the Company employs strategies to minimize these risks, these strategies do not guarantee that events or circumstances will not occur that could negatively impact the Company's financial condition and performance. Careful consideration should be given to the following risk factors which include, but are not limited to, the following:

**Retail Industry and Economic Environment** External factors which affect customer demand, and over which the Company exercises no influence, include general economic growth, inflation, interest rates, personal debt levels, unemployment rates and levels of personal disposable income. In an economic downturn, discounting by major retailers may result in more out-shopping by consumers from the Company's markets which may negatively impact sales and gross profit. Changes in the inflation rate are unpredictable and may impact the cost of merchandise and the prices charged to consumers which in turn could negatively impact sales and net earnings. Although our core customer is a lower income shopper with relatively stable income sources, a recession or significant and prolonged decline in consumer spending could have an adverse effect on the financial condition and results of operations. Management regularly monitors economic conditions and considers factors which can affect customer demand in making operating decisions and the development of strategic initiatives and long-range plans.

**Consumer Income** Our largest customer segment derives most of its income directly or indirectly from government infrastructure spending or direct payment to individuals in the form of social assistance, food subsidy programs, child tax benefits and old age security. These tend to be stable sources of income, independent of economic cycles. A major source of employment income is generated from local government and spending on infrastructure projects. This includes new housing, schools, healthcare facilities, military facilities, roads and sewers. Local employment levels will fluctuate from year-to-year depending on a community's fiscal health, especially near the end of the government budget year. A similar fluctuating source of income is employment related to tourism and natural resource development and extraction activities. A significant or prolonged reduction in government transfers, spending on infrastructure projects, natural resource development and tourism spending would have a negative impact on consumer income which in turn could result in a decrease in sales and gross profit, particularly for more discretionary general merchandise items.

**Competition** We have a leading market position in a large percentage of the markets we serve. Sustaining and growing this position depends on our ability to continually identify and pursue new sales opportunities while defending our current positions through a superior value offer to our customers. We actively monitor competitive activity and we are proactive in adjusting and enhancing our value offer elements, ranging from in-stock position to service and pricing.

**Community Relations** Approximately 40% of our sales are derived from communities and regions that restrict commercial land ownership and usage by non-indigenous or non-local owned businesses or which have enacted policies and regulations to support locally-owned businesses. We successfully operate within these environments through initiatives that promote positive community and customer relations. These include store lease arrangements with community-based development organizations, initiatives to recruit local residents into management positions, increase indigenous or Aboriginal participation in our Board of Trustees, and direct investment in the North West Company Fund by locally-owned entities.

**Employee Development and Retention** Retaining and developing high calibre employees is essential to effectively managing our business, executing our strategies and meeting our objectives. Due to the vast geography and remoteness of the Company's markets, there is significant competition for talent and a limited number of experienced personnel, particularly at the store management level. The degree to which the Company is not successful in retaining and developing employees and establishing appropriate succession plans could lead to a lack of knowledge, skills and experience required to effectively run our operations and execute our strategies. In addition to compensation programs that are designed to attract and retain qualified personnel, the Company also continues to implement and refine initiatives such as comprehensive store-based manager-in-training programs and the Company's in-depth leadership development program, "@NWC". These types of programs are long term change management investments that continue to be refined.

**Food Safety** The Company is exposed to risks associated with food safety and product handling. Food sales represent approximately 77% of total Company sales. A significant outbreak of a food-borne illness or increased public concerns with certain food products could have an adverse effect on the financial condition and results of operations. The Company has food preparation, handling and storage procedures which help mitigate these risks. The Company also has product recall procedures in place in the event of a food-borne illness outbreak however, the existence of these procedures does not eliminate the underlying risks.

**Energy Costs** Compared to other retailers, the Company is more exposed to fluctuations in the price of energy, particularly oil. Due to the vast geography of the store network, transportation costs are a significant component of the Company's expenses. The majority of stores are inaccessible by all-weather roads and as a result, stores are serviced by different modes of transportation including sealift, barge, trucks via winter roads, rail and air. In addition to transportation costs, heating costs also comprise a relatively large portion of the general overhead costs. To the extent that escalating fuel and utility costs cannot be offset by energy conservation practices or offsetting productivity gains, they may result in lower margins or higher retail prices. Consumer spending, especially on discretionary items, may also be adversely effected.

**Income Taxes** The Company accounts for income taxes using the liability method of tax allocation. Under the liability method, future income tax assets and liabilities are determined based on the differences between the financial reporting and tax base of assets and liabilities and are measured using substantively enacted tax rates and laws that are expected to be in effect in the periods in which the future income tax or liabilities are expected to be realized or settled. The provision for income taxes is recorded in the Company at applicable statutory rates.

In the ordinary course of business, the Company is subject to ongoing audits by tax authorities. While the Company believes that its tax filing positions are appropriate and supportable, the possibility exists that certain matters may be reviewed and challenged by the tax authorities. The Company regularly reviews the potential for adverse outcomes and the adequacy of its tax provisions. The Company believes that it has adequately provided for these matters. If the final outcome differs materially from the tax provisions, the Company's income tax expense and its earnings could be effected positively or negatively in the period in which the matters are resolved.

The Fund is an inter vivos trust for income tax purposes. All income of the Fund is distributed to unitholders and, as such, no income tax is payable by the Fund. On June 22, 2007, new legislation was passed (the "SIFT Rules") which imposes a new entity-level tax on distributions from certain specified investment flow-through entities (SIFTs) such as the Fund commencing January 1, 2011. The application of the SIFT Rules is delayed until January 1, 2011 provided the Fund is not considered to have undergone an "undue expansion" in the interim period. The SIFT Rules will result in a reduction in the cash available for distribution to unitholders by the amount of the tax paid or payable by the Fund and the distributions to unitholders will be characterized as dividends. In the event that "undue expansion" has occurred, the adverse tax consequences resulting from SIFT Rules could be realized sooner than January 1, 2011.

On March 12, 2009, the SIFT Rules were passed into legislation. This legislation specifies that the SIFT tax rate will be the federal general corporate income tax rate (which is anticipated to be 16.5% in 2011 and 15.0% in 2012) plus the provincial SIFT tax rate. The provincial SIFT tax rate is based on the general provincial corporate income tax rate in each province in which the Trust has a permanent establishment. For purposes



of calculating this component of the tax, the general corporate taxable income allocation formula is used. Taxable distributions that are not allocated to any province would instead be subject to a 10.0% rate constituting the provincial component. Based on the application of the SIFT Rules and substantively enacted tax rates, the Fund expects to have an effective tax rate of approximately 30% in 2011 and 28% in 2012.

Amendments to the SIFT Rules include rules (the "Conversion Rules") which facilitate the tax-deferred conversion of publicly-traded income trusts into publicly-traded corporations, provided that certain conditions set out therein are met, including that the conversion occur before 2013.

Management and the Board of Trustees have reviewed the impact of the SIFT Rules and the related tax implications on the Fund. Our current assessment is that the Fund should remain structured as a trust until January 1, 2011 at which time we expect to complete a tax deferred conversion into a publicly-traded share corporation (See Conversion to a Share Corporation on page 15). The conversion to a publicly-traded share corporation is subject to approval by unitholders as well as customary court and regulatory approvals.

**Insurance** The Company manages its exposure to certain risks through an integrated insurance program which combines an appropriate level of self-insurance and the purchase of various insurance policies. The Company's insurance program is based on various lines and limits of coverage. Insurance is arranged with financially stable insurance companies as rated by the professional rating agencies. There is no guarantee that any given risk will be mitigated in all circumstances.

**Climate** Weather conditions can play a significant role in the operation of the stores of the Fund's operating subsidiaries. These weather conditions can range from blizzards to hurricanes and cyclones, and can cause loss of life, damage to and destruction of key stores. Such losses may have an adverse effect on the financial condition and results of operations. As well, any global warming conditions would have a more pronounced effect, both positive and negative, on the Fund's most northern latitude stores. The stores located in the South Pacific, Caribbean and coastal areas of Alaska are also at risk from tsunamis which can result in loss of life and destruction of assets.

**Information Technology** The Company relies on information technology (IT) to support the current and future requirements of the business. IT systems are relied upon to provide essential information to management for decision making. Any significant failure or disruption in IT systems, or the failure to successfully upgrade legacy systems or implement new systems could have an adverse effect on the financial condition and results of operations.

**Laws and Regulations** The Company is subject to various laws and regulations administered by federal, provincial and foreign regulatory authorities, including but not limited to taxes, duties, currency repatriation, zoning, health and safety, employment standards and licensing requirements. These laws and their interpretation by various courts and agencies are subject to change. In the course of complying with such changes, the Company may incur significant costs. Failure by the Company to fully comply with applicable laws and regulations could result in financial penalties, assessments, sanctions, or legal action that could have an adverse effect on the business, financial condition or results of operations.

**Management of Inventory** Success in the retail industry is dependent upon the ability to manage merchandise inventories in proportion to the demand for such merchandise. A miscalculation of consumer demand for merchandise could result in having excess inventory for some products and missed sales opportunities for others. Excess inventory may result in higher markdowns or inventory shrinkage all of which could have an adverse effect on the financial condition and results of operations.

**Vendor and Service Partner Management** The Company relies on a broad base of manufacturers and suppliers to provide goods and services. Events or disruptions affecting these suppliers outside of the Company's control could in turn result in delays in the delivery of merchandise to the stores and therefore negatively impact the results of operations. A portion of the merchandise the Company sells is purchased offshore. Offshore sourcing could provide products that contain harmful or banned substances or do not meet the required standards. The Company uses offshore consolidators and sourcing agents to monitor product quality and reduce the risk of sub-standard products however there is no certainty that these risks can be completely mitigated in all circumstances.

**Ethical Business Conduct** The Company has a Code of Conduct Policy which employees and Trustees are required to acknowledge and confirm their compliance on a regular basis. The Business Ethics Committee monitors compliance with the Code of Conduct policy. The Company also has a Vendor Information Manual which outlines the Company's expectations for the ethical conduct of its vendors. Unethical business conduct could negatively impact the Company's reputation and relationship with its customers, investors, and employees, which in turn could have an adverse effect on the financial condition and results of operations.

**Geopolitical** Changes in the domestic or international political environment may impact the Company's ability to source and provide products and services. Acts of terrorism, riots, and political instability could have an adverse effect on the financial condition and results of operations.

**Employee Future Benefits** The Company engages professional investment advisors to manage the assets in the defined benefit pension plans. The performance of the Company's pension plans and the plan funding requirements are impacted by the returns on plan assets, actuarial valuations and regulatory funding requirements. The Company regularly monitors and assesses the performance of the pension plan assets and the impact of changes in capital markets, changes in plan member demographics, and other economic factors that may impact funding requirements, employee future benefit plan expenses and actuarial assumptions. In 2009, the Company made a \$4.0 million special contribution to reduce the unfunded liability of the defined benefit plans. If capital market returns are below the level estimated by management, or if the discount rate used to value the liabilities of the plans decreases, the Company may be required to make contributions to its defined benefit pension plans in excess of those currently contemplated, which may have an adverse effect on the Company's financial condition and results of operations.

**Financial Risks** In the normal course of business, the Company is exposed to financial risks that have the potential to negatively impact its financial performance. These risks and the actions taken to minimize the risks are described below. See Note 20 to the consolidated financial statements for additional information on the Company's financial instruments and associated risks.

**Credit Risk** Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations. The Company is exposed to credit risk primarily in relation to individual and commercial accounts receivable. The Company manages credit risk by performing regular credit assessments of its customers and provides allowances for potentially uncollectible accounts receivable. The Company does not have any individual customers greater than 10% of total accounts receivable.

**Liquidity Risk** Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they come due or can do so only at excessive cost. The Company manages liquidity risk by maintaining adequate credit facilities to fund operating requirements and sustaining and growth-related capital expenditures and regularly monitoring actual and forecasted cash flow and debt levels. At January 31, 2010, the Company has a US\$52.0 million credit facility that matures on December 31, 2010. The Company has started the process of refinancing this credit facility. Global economic conditions continue to result in uncertainty and volatility in the credit markets which may negatively impact the availability of credit, interest rates and covenants for Companies seeking to refinance debt. To the extent the Company cannot meet its obligations or refinance its debt when it comes due, or can do so only at an excessive cost, this may have an adverse effect on the financial condition and results of operations. For further information on credit facilities see Note 8 and Note 9 to the consolidated financial statements.

**Currency Risk** Currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. The Company is exposed to currency risk, primarily the U.S. dollar, through its net investment in self-sustaining International Operations and its U.S. dollar denominated borrowings. The Company manages its exposure to currency risk by hedging the net investment in self-sustaining foreign operations with a portion of U.S. dollar denominated borrowings. The Company is also exposed to currency risk relating to the translation of International Operations earnings from U.S. dollars to Canadian dollars. During 2009, the Canadian dollar was on average weaker than the U.S. dollar compared to 2008. The weakening Canadian dollar increased the translation of U.S. denominated net earnings from International Operations by \$573,000 in 2009.

**Interest Rate Risk** Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Company is exposed to interest rate risk primarily through its long-term borrowings. The Company manages exposure to interest rate risk by using a combination of interest rate swaps and a mixture of fixed and floating interest rate debt.



## CRITICAL ACCOUNTING ESTIMATES

The preparation of financial statements in accordance with Canadian GAAP requires management to make estimates and assumptions that affect the reported amounts and disclosures made in the consolidated financial statements and accompanying notes. Management continually evaluates the estimates and assumptions it uses. These estimates and assumptions are based on management's historical experience, knowledge of current events, expectations of future outcomes and other factors that management considers reasonable under the circumstances. Actual results could differ from these estimates as confirming events occur. The estimates and assumptions described in this section depend upon subjective or complex judgments about matters that may be uncertain and changes in these estimates and assumptions could materially impact the consolidated financial statements.

**Valuation of Accounts Receivable** The Company records an allowance for doubtful accounts related to accounts receivable that may potentially be impaired. The allowance is based on the aging of the accounts receivable, our knowledge of our customers' financial condition, the current business environment and historical experience. A significant change in one or more of these factors could impact the estimated allowances for doubtful accounts recorded in the consolidated balance sheet and the provisions for debt loss recorded in the consolidated statement of earnings and retained earnings.

**Valuation of Inventories** Retail inventories are stated at the lower of cost and net realizable value. Significant estimation or judgment is required in the determination of: (1) discount factors used to convert inventory to cost after a physical count at retail has been completed; (2) recognizing merchandise for which the customer's perception of value has declined and appropriately marking the retail value of the merchandise down to the perceived value; and (3) estimating inventory losses, or shrinkage, occurring between the last physical count and the balance sheet date.

Food inventories counted at retail are converted to cost by applying a discount factor to retail selling prices. This discount factor is calculated in relation to historical gross margins and is reviewed on a regular basis for reasonableness. General merchandise inventories counted at retail are converted to cost by applying average cost factors by merchandise category. These cost factors represent the average cost-to-retail ratio for each merchandise category based on beginning inventory and purchases made throughout the year.

Inventory shrinkage is estimated as a percentage of sales for the period from the date of the last physical inventory count to the balance sheet date. The estimate is based on experience and the most recent physical inventory results. To the extent that actual losses experienced vary from those estimated, both inventories and cost of sales may be impacted.

Changes or differences in these estimates may result in changes to inventories on the consolidated balance sheet and a charge or credit to cost of sales in the consolidated statement of earnings and retained earnings.

**Employee Future Benefits** The cost and accrued benefit plan obligations of the Company's defined benefit pension plans are accrued based on actuarial valuations which are dependent on assumptions determined by management. These assumptions include the discount rate used to calculate benefit plan obligations, the expected long-term rate of return on plan assets, the rate of compensation increase, retirement ages, and mortality rates. These assumptions are reviewed by management and the Company's actuaries.

The discount rate used to calculate benefit plan obligations, the expected long-term rate of return on plan assets and the rate of compensation increase are the three most significant assumptions. The discount rate used to calculate benefit plan obligations is based on market interest rates, as at the Company's measurement date of January 31, 2010 on a portfolio of Corporate AA bonds with terms to maturity that, on average, match the terms of the accrued benefit plan obligations. The discount rates used to measure the benefit plan obligations for fiscal 2009 and 2008 were 6.0% and 7.0% respectively. The expected long-term rate of return on plan assets is based on historical returns, the asset mix and current investment yields. The expected long-term rate of return on plan assets for fiscal 2009 and 2008 is 6.5%. Management assumed the rate of compensation increase for fiscal 2009 and 2008 at 4%.

These assumptions may change in the future and may result in material changes in the accrued employee future benefit asset on the Company's consolidated balance sheet and the benefit plan expense on the consolidated statement of earnings and retained earnings. The magnitude of any immediate impact, however, is mitigated by the fact that net actuarial gains and losses in excess of 10% of the greater of the accrued benefit plan obligations and the market value of the benefit plan assets are amortized on a straight-line basis over the average remaining service period of the employees expected to receive the benefits under the plan. Changes in financial market returns and interest rates could also result in changes to the funding requirements of the Company's defined benefit pension plans. Additional information regarding the Company's employee future benefits is provided in Note 17 of the consolidated financial statements.

**Impairment of Long-lived Assets** The Company periodically assesses the recoverability of values assigned to long-lived assets after considering potential impairment indicated by such factors as business and market trends, future prospects, current market value and other economic factors. In performing its review of recoverability, management estimates the future cash flows expected to result from the use of the asset and its eventual disposition. If the sum of the expected future cash flows is less than the carrying value of the asset, an impairment loss would be recognized based on the excess of the carrying value of the asset over the fair market value calculated using discounted future cash flows. The underlying estimates for cash flows include estimates for future sales, gross margin rates and store expenses, and are based upon the stores' past and expected future performance. Changes which may impact future cash flows include, but are not limited to, competition, general economic conditions and unrecoverable increases in operating costs. To the extent that management's estimates are not realized, future assessments

could result in impairment charges that may have a significant impact on the Company's consolidated balance sheet and consolidated statement of earnings and retained earnings.

**Goodwill** Goodwill is not amortized but is assessed for impairment at the reporting unit level at least annually. The potential for goodwill impairment is determined by comparing the fair value of a reporting unit to its carrying value. If the fair value of the reporting unit exceeds its carrying value, goodwill is not impaired. If the carrying value of the reporting unit exceeds its fair value, a more detailed goodwill impairment test must be undertaken. A goodwill impairment loss is recorded when the carrying value of goodwill exceeds the implied fair value of the reporting unit and is recognized as an expense in the period the impairment is determined. The process of determining fair value requires management to make estimates and assumptions including, but not limited to, future sales, gross profit rates, earnings, capital investment, discount rates, weighted average cost of capital and growth rates. These estimates and assumptions are subject to change in the future due to changes in competitive and economic market conditions or changes in business strategies. To the extent that management's estimates are not realized, future assessments could result in impairment charges that may have a significant impact on the Company's consolidated balance sheet and consolidated statement of earnings and retained earnings.

The Company performed the annual goodwill impairment test in 2009 and it was determined that the fair value of the reporting unit exceeded its carrying value and therefore, no goodwill impairment was identified.

**Income Taxes** Future income tax assets and liabilities are recognized for the future income tax consequences attributable to temporary differences between the financial statement carrying values of assets and liabilities and their respective income tax bases. Future income tax assets or liabilities are measured using enacted or substantively enacted income tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The calculation of current and future income taxes requires management to make estimates and assumptions and to exercise a certain amount of judgment regarding the financial statement carrying values of assets and liabilities which are subject to accounting estimates inherent in those balances. The future income tax assets and liabilities are also impacted by the interpretation of income tax legislation across various jurisdictions, expectations about future operating results and the timing of reversal of temporary differences, and possible audits of tax filings by the regulatory agencies.

Changes or differences in these estimates or assumptions may result in changes to the current or future income tax balances on the consolidated balance sheet, a charge or credit to income tax expense in the consolidated statement of earnings and may result in cash payments or receipts. Additional information on income taxes is provided in Note 14 to the consolidated financial statements.

**Security-based Compensation** Security-based compensation awards are measured and recognized using a fair value based method. Security-based compensation expense is measured at the grant date based on the fair value of the award and is recognized as an expense over the vesting period. Determining the fair value of security-based compensation awards requires judgement regarding the estimation of the expected volatility of the Fund's units and the number of awards expected to be forfeited. The security-based compensation cost for awards that are dependent upon performance conditions is based on management's best estimates of the outcome of the performance conditions. To the extent that actual results differ from management's estimates, security-based compensation expense recorded on the Company's consolidated statement of earnings and retained earnings may be significantly impacted. Additional information on security-based compensation is provided in Note 19 to the consolidated financial statements.

## ACCOUNTING STANDARDS IMPLEMENTED IN 2009

In 2009, the Company implemented the following new accounting standards issued by the Canadian Institute of Chartered Accountants (CICA):

**Financial Instruments – Recognition and Measurement** In June 2009, the CICA issued amendments to Section 3855 Financial Instruments, Recognition and Measurement. These amendments included clarifications on the application of the effective interest rate method and reclassification of financial instruments with embedded derivatives.

In August 2009, the CICA further amended Section 3855 to define loans and receivables as non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. The amendment eliminated the distinction between debt securities and other debt instruments and changed the scope of the categories into which these financial instruments may be classified.

These amendments had no material impact on the Company's consolidated financial position or results of operations.

**Financial Instruments – Disclosures** In June 2009, the CICA issued amendments to Section 3862, Financial Instruments Disclosures, to improve fair value and liquidity risk disclosures. The standard now requires that all financial instruments measured at fair value be categorized using a three level hierarchy. Each level is based on the transparency of inputs used to measure the fair values of financial assets and liabilities. The additional disclosures required by the amendments are included in Note 20 to the consolidated financial statements.

**Credit Risk and the Fair Value of Financial Assets and Financial Liabilities** Effective February 1, 2009, the Company adopted EIC 173, Credit Risk and the Fair Value of Financial Assets and Financial Liabilities, issued by the CICA. This Abstract requires entities to consider both its own and counterparty credit risk in determining the fair value of its financial assets and liabilities, including derivative financial instruments. The adoption of this Abstract has had no material impact on the Company's financial statement disclosures, financial position or results from operations.

## FUTURE ACCOUNTING STANDARDS

**Business Combinations** In January 2009, the CICA issued section 1582, Business Combinations together with section 1601, Consolidated Financial Statements and section 1602, Non-Controlling Interests. These new standards will be effective for the Company on a prospective basis for business combinations occurring on or after February 1, 2011. The new standards will align Canadian GAAP for business combinations and consolidated financial statements with IFRS. Early adoption is permitted and would facilitate the harmonization of the accounting treatment of business combinations for the year ended January 31, 2011 under both Canadian GAAP and IFRS.

**International Financial Reporting Standards** The Canadian Accounting Standards Board requires all publicly accountable enterprises to adopt International Financial Reporting Standards (IFRS) for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011. Companies are also required to provide IFRS comparative information for the previous fiscal year. The transition from Canadian generally accepted accounting principles (Canadian GAAP) to IFRS will be applicable for the Company's first quarter beginning February 1, 2011 when the Company will prepare comparative financial statements using IFRS.

Financial reporting under IFRS differs from Canadian GAAP in a number of respects, some of which are significant. The adoption of IFRS will have an impact on the Company's accounting, financial statements and disclosures, information systems, disclosure controls and procedures, and internal controls over financial reporting. Most adjustments required on transition to IFRS will be made retrospectively against opening retained earnings as of the date of the first comparative balance sheet. The International Accounting Standards Board (IASB) is continuing to work on new accounting standards or changes to previously issued accounting standards. IFRS on the date of adoption is expected to differ from current IFRS due to these changes, impacting the form and content of the Company's IFRS compliant financial statements. The Company continues to monitor the changes to accounting standards proposed by the IASB and assess the impact of those changes. At this time, the impact of IFRS on the Company's future financial position cannot be quantified; however such impacts may be material upon final determination.

The Company commenced its IFRS conversion project in 2008. The project plan contains milestones and timelines to ensure a timely conversion. The IFRS conversion project consists of four main phases: Phase One - Project Plan and Scope; Phase Two - Detailed Impact Assessment; Phase Three - Conversion Plan; and Phase Four - Policy Selection and Implementation. The IFRS project team is led by the Chief Financial Officer supported by a project manager and a combination of internal and external resources. Progress updates are provided to the Audit Committee of the Board of Trustees on a quarterly basis.

To date the Company has completed Phases One, Two and Three comprised of:

- Diagnostic assessment of the financial statement components that will be impacted and a priority ranking of those differences identified;
- Comprehensive analysis of the major differences between Canadian GAAP and IFRS applicable to the Company;
- Identification of accounting policy alternatives, transition elections and exemptions available under IFRS; and
- Identification of changes to accounting systems required to support the implementation of IFRS.

Work continues on Phase Four – Policy Selection and Implementation and the consequential impact of IFRS on disclosure controls and procedures, internal controls over financial reporting, key performance measures, financial covenants, contractual agreements, incentive plans and budgeting. This phase also involves the final selection and approval of accounting policies, elections and exemptions and the finalization of IFRS compliant financial statements and notes. Changes to information systems and the financial reporting processes required to prepare the opening balance sheet have been completed. During 2010, the Company will prepare its opening balance sheet and quarterly financial statements in accordance with IFRS based on management's preliminary conclusions and analysis of various policy alternatives.

The Company continues to invest in resources and training to facilitate a timely conversion. Training for finance personnel consists of courses provided by external advisors as well as internally led training. Education and training on the impact of IFRS will continue to be provided to finance personnel, senior management and the Board throughout 2010.

Differences between Canadian GAAP and IFRS that will result in modifications to our financial statements at the changeover date have been identified. These differences, together with the IFRS elections and exemptions applicable to the Company have been summarized below.

#### **Accounting Policy Differences**

**Employee benefits** International Accounting Standard (IAS) 19, *Employee Benefits* permits an entity to make an accounting policy choice regarding the treatment of actuarial gains and losses. These choices include: (a) the corridor method, which is similar to the method currently used by the Company; (b) recording the actuarial gains and losses directly in income in the year incurred; and (c) recognizing the actuarial gains and losses directly in equity through comprehensive income.

IAS 19 also requires the past service cost element of defined benefit plans to be expensed on an accelerated basis, with vested past service costs being expensed immediately and unvested past service costs being recognized on a straight-line basis until the benefits become vested. Under Canadian GAAP, past service costs are generally amortized on a straight-line basis over the expected average remaining service period of the active employees in the plan.

**Impairment of Assets** IAS 36, *Impairment of Assets* uses a one-step impairment test whereby long-lived and finite life intangible asset carrying values are compared directly to their fair value. Fair value under IFRS is based on the greater of value in use as determined by discounted cash flow analysis and fair value less costs to sell. This may result in more frequent write-downs since under Canadian GAAP asset values are first compared to undiscounted cash flows as part of a two-stage impairment test. Under IAS 36, asset impairment write-downs can be reversed when there are indications that the circumstances leading to the write-down have changed. The reversal of asset impairment write-downs is not permitted under Canadian GAAP.

**Share-based Payments** IFRS 2, *Share-based Payments* requires that cash-settled awards granted to employees be measured at the grant date and each subsequent reporting period using a fair value model. This differs from Canadian GAAP whereby cash-settled awards are measured using the intrinsic value which is based on the market price of the Fund's units at the end of the reporting period. This difference in determining fair value will impact the timing of the expense recognized over the vesting period of the long-term incentive plans.

**Provisions** IAS 37, *Provisions, Contingent Liabilities and Contingent Assets* requires a provision to be recognized when: there is a present obligation as a result of a past transaction or event; it is probable that an outflow of resources will be required to settle the obligation; and a reliable estimate can be made of the obligation. Under IAS 37 "probable" generally means more likely than not. Under Canadian GAAP, a liability is recorded in the financial statements when it is "likely", which is a higher threshold than "probable". The lower threshold used under IFRS may result in additional liabilities being recognized than under Canadian GAAP. Other differences have also been identified between the methods used for measuring provisions, including situations when there is a range of possible outcomes and when IFRS requires an entity to contemplate the effects of discounting.

**Borrowing Costs** IAS 23, *Borrowing Costs* requires entities to capitalize borrowing costs directly attributable to the acquisition or construction of a qualifying asset as part of the cost of that asset. A qualifying asset is one that necessarily takes a substantial period of time to be made ready for its intended use. Borrowing costs that must be capitalized are those that otherwise would have been avoided. Under Canadian GAAP the Company does not capitalize borrowing costs.

**Income Tax** In November 2009, the IASB withdrew an exposure draft on Income Taxes. Applicable current IFRS income tax requirements are fundamentally consistent with current practice. Any changes to Income Tax reporting are expected to be predominately caused by changes in the book value of assets and changes in tax rates applied, and not Income Tax accounting methodology.

**IFRS 1 – First-time Adoption of International Financial Reporting Standards** IFRS 1 provides entities adopting IFRS for the first time with a number of optional exemptions and mandatory exceptions to the general requirement for retrospective application of the standards. The IFRS 1 exemptions that are expected to apply to the Company upon adoption are summarized as follows:

**Employee benefits** A first time adopter must either recalculate its actuarial gains and losses at changeover in accordance with the requirements of IAS 19, *Employee Benefits* or immediately recognize all cumulative actuarial gains and losses through opening retained earnings. Retrospective recognition of actuarial gains and losses in accordance with IAS 19 requires the recalculation of gains and losses from the date the benefit plans were established.

**Cumulative translation account** IFRS 1 provides the option to reclassify all cumulative translation differences at the transition date from other comprehensive income to retained earnings. This provides relief from retrospectively applying IAS 21, *The Effects of Changes in Foreign Exchange Rates* from inception.

**Fair value as deemed cost** A choice is available between: measuring property and equipment at either its fair value at the date of transition and using those values as deemed cost; or using amortized historical cost determined in accordance with IAS 16, *Property, Plant and Equipment*. This exemption may be applied on an asset-by-asset basis.

**Business combinations** IFRS 3, *Business Combinations* may be applied retrospectively, effectively restating all business combinations in accordance with IFRS or by restating business combinations after a selected date. An entity may also elect to apply this standard prospectively from the date of transition.

These differences and options together with our comments thereon should not be deemed as a comprehensive listing of all changes that may result from the transition to IFRS. Instead, this commentary is meant to highlight areas we believe may be most significant. The reader is cautioned that our analysis of possible changes is ongoing, and will be influenced by both our final selection of accounting policies and continuing changes to IFRS in the form of new or revised standards.

The Company's IFRS project continues to be on target to meet the changeover date. Throughout 2010, the Company will continue to provide quarterly updates on its IFRS implementation plan and the impact of IFRS on the consolidated financial statements.

## NON-GAAP MEASURES

**1 Trading Profit (EBITDA)** is not a recognized measure under Canadian GAAP. Management believes that in addition to net earnings, trading profit is a useful supplemental measure as it provides investors with an indication of the Company's operational performance before allocating the cost of interest, income taxes and capital investments. Investors should be cautioned, however, that trading profit should not be construed as an alternative to net earnings determined in accordance with GAAP as an indicator of NWF's performance. NWF's method of calculating trading profit may differ from other companies and may not be comparable to measures used by other companies. A reconciliation of consolidated net earnings to trading profit or EBITDA is provided below:

### Reconciliation of Net Earnings to Trading Profit

(\$ in thousands)	2009	2008	2007
Net earnings	\$ 81,813	\$ 75,378	\$ 62,991
Add: Amortization	35,150	32,054	26,950
Interest expense	5,470	8,307	7,465
Income taxes	7,841	6,518	9,151
Trading profit	\$ 130,274	\$ 122,257	\$ 106,557

For trading profit information by business segment, see Note 16 "Segmented Information" in the notes to the consolidated financial statements on page 40

**2 Earnings Before Interest and Income Taxes (EBIT)** is not a recognized measure under Canadian GAAP. Management believes that EBIT is a useful measure as it provides investors with an indication of the performance of the consolidated operations and/or business segments, prior to interest expense and income taxes. Investors should be cautioned, however, that EBIT should not be construed as an alternative to net earnings determined in accordance with GAAP as an indicator of NWF's performance. NWF's method of calculating EBIT may differ and may not be comparable to measures used by other companies. A reconciliation of consolidated net earnings to EBIT is provided below:

### Reconciliation of Net Earnings to EBIT

(\$ in thousands)	2009	2008	2007
Net earnings	\$ 81,813	\$ 75,378	\$ 62,991
Add: Interest expense	5,470	8,307	7,465
Income taxes	7,841	6,518	9,151
EBIT	\$ 95,124	\$ 90,203	\$ 79,607

For EBIT information by business segment, see Note 16 "Segmented Information" in the notes to the consolidated financial statements on page 40

**3 Cash Flow from Operations** is not a recognized measure under Canadian GAAP. Management believes that in addition to net earnings, cash flow from operations is a useful supplemental measure as it provides investors with an indication of the Company's ability to generate cash flows to fund its cash requirements, including distributions and capital investment. Investors should be cautioned however, that cash flow from operations should not be construed as an alternative to net earnings as a measure of profitability or the statement of cash flows. NWF's method of calculating cash flow from operations may differ from other companies and may not be comparable to measures used by other companies. A reconciliation of consolidated cash flow from operating activities to cash flow from operations is provided below:

### Reconciliation of Cash Flow from Operating Activities to Cash Flow from Operations

(\$ in thousands)	2009	2008	2007
Cash flow from operating activities	\$ 107,973	\$ 90,178	\$ 93,591
Non-cash items: Change in other non-cash items	1,834	(1,396)	1,890
Change in non-cash working capital	6,679	17,542	(742)
Cash flow from operations	\$ 116,486	\$ 106,324	\$ 94,739



## GLOSSARY OF TERMS

**Basic earnings per unit** Net earnings available to unitholders divided by the weighted average number of units outstanding during the period.

**Basis point** A unit of measure that is equal to 1/100th of one percent.

**Cash flow from operations** Provides an indication of the Company's ability to generate cash flows to fund its cash requirements, including distributions and capital investment. See Non-GAAP measures on page 26.

**Control label or Private label** A brand or related trademark that is owned by the Company for use in connection with its own products and services.

**Debt loss** An expense resulting from the estimated loss on potentially uncollectible accounts receivable.

**Debt covenants** Restrictions written into banking facilities and senior notes and loan agreements that prohibit the Company from taking actions that may negatively impact the interests of the lenders.

**Debt to equity ratio** Provides information on the proportion of debt and equity the Company is using to finance its operations and calculated by total debt divided by unitholder equity.

**Diluted earnings per unit** The amount of net earnings for the period available to unitholders divided by the weighted average number of units outstanding during the period including the impact of all potential dilutive outstanding units at the end of the period.

**EBIT** Net earnings before interest and income taxes provides an indication of the performance of the Company's performance prior to interest expense and income taxes. See Non-GAAP measures on page 26.

**EBIT margin** EBIT divided by sales.

**Fair value** The amount of consideration that would be agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act.

**Gross profit** Sales less cost of goods sold and inventory shrinkage.

**Gross profit rate** Gross profit divided by sales.

**Hedge** A risk management technique used to manage interest rate, foreign currency exchange or other exposures arising from business transactions.

**Interest coverage** Net earnings before interest and income taxes divided by interest expense.

**Return on equity** Net earnings divided by average unitholder equity.

**Return on net assets** Net earnings before interest and income taxes divided by average net assets employed (average total assets less accounts payable and accrued liabilities, income taxes payable and asset retirement obligations).

**Same store sales** Retail sales from stores that have been open more than 52 weeks in the periods being compared.

**Trading profit (EBITDA)** Net earnings before interest, income taxes, depreciation and amortization provides an indication of the Company's operational performance before allocating the cost of interest, income taxes and capital investments. See Non-GAAP measures on page 26.

**Trading profit margin** Trading profit divided by sales.

**Working capital** Total current assets less total current liabilities.

**Year** The fiscal year ends on January 31. The 2009 year which ended January 31, 2010 had 365 days of operations. The 2008 year which ended January 31, 2009 had 366 days of operations as a result of the February 29 leap year. The 2007 year which ended January 31, 2008 had 365 days of operations. The 2006 year which ended January 31, 2007 has 368 days of operations as a result of the Fund adopting a fixed fiscal year end of January 31 compared to the last Saturday in January used in prior years.





Nor'Westers have consistently been associated with the vision, perseverance, and enterprising spirit of the voyageurs who pushed past limits to further our Company's growth during the fur trade. We trace our roots to 1668, and the establishment of one of North America's first trading posts at Waskaganish on James Bay. Today, we continue to embrace this pioneering culture as true "frontier merchants."

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