CANADA POST CORPORATION

Summary of the 2014 to 2018 Corporate Plan

Summary of the 2014 Capital Budget

CANADA POST POSTES CANADA

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SUMMARY OF 2014 TO 2018 CORPORATE PLAN

SUMMARY OF 2014 CAPITAL BUDGET

These documents are being submitted in accordance with section 125 of the *Financial Administration Act* (FAA) and summarize the Corporate Plan and Capital Budget as approved by the Board of Directors of Canada Post on October 23, 2013. The first year of the Plan and the Budget received Governor in Council approval on December 12, 2013.

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1. EXECUTIVE SUMMARY

<u>Poised to transform for the 21st century</u>

At a pivotal point in its history, Canada Post is poised to transform its business for the 21st century.

Canada Post's successful transformation, as detailed in this plan, will ensure its continued relevance and viability and achieve a return to profitability by 2019. Most importantly, by transforming, Canada Post will continue its crucial role as a key enabler of the Canadian economy. With its unique reach and other capabilities, its enabling role supports participation in the economy by all Canadians, no matter where they live, and by all businesses, regardless of their size, sophistication or setting.

The historic, irreversible and global trends in demand for Lettermail™ delivery are not merely regular declines seen in typical economic cycles. They are, in fact, a structural shift in demand away from traditional Lettermail. Simply put, Canadians need less Lettermail because they and mailers are adopting electronic alternatives – but at the same time, they are becoming heavily reliant on parcel delivery. In a few short years, millions of them have become online shoppers spending billions of dollars on items that need delivery to their doors.

Although Canada Post faces serious challenges due to the shift from paper-based to digital communications, its products and services remain crucial to the economy. Canada Post's:

- marketing mail enables roughly $10 billion in annual retail sales, largely for small and medium-sized businesses;
- parcels business enables more than $22 billion in annual trade for retailers and consumers of all sizes;
- Transaction Mail enables more than $200 billion a year in financial transactions through the bills and payments it carries; and
- directly and indirectly enables an estimated 8 to 10 per cent of Canada's $1.58 trillion Gross Domestic Product.

Canadians have told Canada Post that they value and need postal services, albeit of a different type than in the past. They expressed these views in the dialogue Canada Post fostered through 46 community meetings held across Canada following the release of the April 2013 report by The Conference Board of Canada on the future of postal services, as well as in thousands of comments received online and by letter. Furthermore, they expressed a nearly universal expectation that Canada Post transform its business without taxpayer funding.

<u>E-commerce will anchor opportunities for growth</u>

Driven by the emergence of e-commerce, Canada Post's parcels business is gaining momentum every year and provides the greatest opportunity for growth.

Canadians ordered an estimated $9 billion worth of goods for delivery from businesses to consumers in 2012, a figure that is forecast to climb to $16.9 billion by 2017. Canada Post has rapidly built new capabilities to support its parcels business, resulting in a strong record of growth. Overall parcel volumes increased 6.7 per cent in 2012 alone.

Canada Post is already the leading provider of business-to-consumer (B2C) delivery of parcels. Furthermore, its integration with subsidiaries Purolator Inc. and SCI Group allows the Canada Post Group of Companies to provide shippers with comprehensive end-to-end logistics solutions, such as warehousing and order fulfillment.

In addition to the e-commerce opportunity, Canadian consumers, businesses and governments will continue to need physical mail beyond traditional Lettermail.

Canada Post is ideally positioned to respond to other growth opportunities. Mail of a changing size and shape will include evidence mail such as licences, loyalty cards and credit cards, as well as prescription medications. As well, marketing mail, with its proven return on investment, has a future amid the electronic clutter of this digital age. Product samples are another emerging growth opportunity. The growth of e-commerce will also cross-pollinate growth in other mail, such as catalogues. Canada Post will continue to diversify and enhance its marketing mail offerings.

As it pursues opportunities for growth, Canada Post will also prudently manage the gradual decline in Lettermail through its pricing strategy and continued efficiencies in its processing and delivery network.

The plan to transform for the 21st century

Canada Post has a comprehensive plan to realign how it prices and delivers postal services in order to meet Canadians' emerging and future needs while reducing costs substantially.

This plan includes the following measures:

- standardizing the mode of delivery across Canada by transitioning the remaining one third of Canadian addresses still receiving door-to-door delivery, almost all of which are in urban Canada, to community mail and parcel boxes (a convenient way to retrieve parcels being delivered to Canadians as a result of online shopping);
- expanding convenience by opening more franchise postal outlets, while adjusting our retail network to more closely align with customer needs and usage and enhancing online product and service offerings, enabling a 24/7 postal service;
- streamlining operations by leveraging technology and consolidation in order to yield cost-effective, reliable delivery to Canadians;
- adopting a tiered pricing model, based on volumes, that reflects the different costs of selling and processing Lettermail;
- addressing the cost of labour to bring it closer in line with competitors, through attrition and collective bargaining, over time. Canada Post plans to reduce the number of non-unionized and management positions in line with the changes to its operations and unionized workforce.

The successful realization of our plan required resolution of the immediate cash pressure facing the company as a result of its pension solvency deficit, as well as a solution to the long-term challenge of the plan's obligation, which is disproportionately large compared to the size of the company. This Plan assumes that the Government will grant a four-year moratorium on special payments so that Canada Post in working with its unions and other representatives of pension plan members, can make the necessary structural changes to the plan to ensure its long-term sustainability.

Bold steps to reduce costs will continue

The most dramatic changes Canada Post has undertaken in decades will build on a foundation we have already begun. This foundation includes determined efforts to reduce costs and adapt to changing customer needs.

These efforts include:

- Postal Transformation, the multi-year, $2-billion program to renew our processing and delivery infrastructure and processes. Roughly midway, Postal Transformation is surpassing its annual cost-savings targets, due mostly to leveraging attrition, and is forecast to surpass its end-state annual savings of $250 million.

- Reducing our labour costs for both management and unionized segments. Under the Five-point Action Plan, Canada Post forecasts a reduction of some 6,000 to 8,000 positions.

- A 50-50 cost-sharing of pension contributions beginning in 2014 for all employees.

Conclusion

Mail volumes and other quantifiable indicators are clear evidence that the needs for postal services are evolving. In their feedback to Canada Post, Canadians have told us they continue to require postal services, albeit with a greater emphasis on parcels, and they are open to realigned approaches to delivery and pricing. However, they were virtually unanimous in their insistence that Canada Post not reach a stage in which it would need taxpayers to fund its operations.

We have tackled major challenges in the past, and will continue to do so in the coming years. Our track record leaves us confident that by executing this plan, we can adapt to meet the needs of Canadians, grow significantly where opportunities exist, remain relevant, become more cost-effective, competitive and customer-driven, and return to profitability by 2019.

2. CORPORATE PROFILE AND GOVERNANCE

2.1 Corporate Profile and Mandate

The Canada Post Group of Companies consists of Canada Post and three non-wholly owned subsidiaries, Purolator Holdings Ltd., SCI Group Inc., and Innovapost Inc. The Group is one of Canada's largest employers, with approximately 68,000 employees. The Canada Post segment operates the largest retail network in Canada, with almost 6,300 retail post offices. Every year, Canada Post employees deliver some 10 billion pieces of mail, parcels and messages to over 15 million addresses in urban, rural and remote locations across Canada.

Pursuant to the *Canada Post Corporation Act*, Canada Post has a mandate to provide postal services to all Canadians, rural and urban, individuals and businesses, in a secure and financially self-sustaining manner. Canada Post's universal service obligation is further detailed in the *Canadian Postal Service Charter*, established by the Government in 2009.

All Posts have traditionally financed their universal service obligation through a legislated exclusive privilege, or monopoly, over a portion of the postal market. Through its legislation, Canada Post is granted an exclusive privilege on letters up to 500 grams.

2.2 Corporate Governance

An agent Crown corporation since 1981, Canada Post Corporation currently reports to Parliament through the Minister of Transport. It has a single shareholder, the Government of Canada. Although Canada Post operates at arm's length from the Government, Government approval is needed for the company's corporate plan, capital budget, restricted transactions, borrowing activities, regulatory rate changes and certain other activities.

Canada Post's Board of Directors is responsible for overseeing the Corporation on behalf of the Shareholder. All 11 members, including the President and CEO, are appointed by the Government. While its role is set out in the *Canada Post Corporation Act* and the *Financial Administration Act*, the Board is also governed by its by-laws, Statement of Board Values, and Board Charter.

The Board of Directors holds management accountable for the Corporation's business performance and for carrying out its objectives, and has established the following committees to help it fulfil its oversight responsibilities.

- The Audit Committee is responsible for reviewing financial information, overseeing the systems of corporate controls, the audit process and the risk management framework, and assessing the Corporation's financial performance against its corporate plan.

- The Corporate Governance and Nominating Committee focuses on corporate governance, assesses corporate values and the elements that facilitate Board effectiveness, and recommends candidates for Board membership.

- The Human Resources and Compensation Committee oversees human resources and compensation matters, including labour relations issues.

- The Pension Committee oversees the assets, obligations, policies, strategies and other matters pertaining to the Canada Post Pension Plan, including Canada Post’s responsibilities as pension plan administrator.

- The Strategic Initiatives Oversight Committee has been established to assist with the development and implementation of planned strategic transformation initiatives, including structural change.

The Board has established a governance model for Canada Post’s subsidiaries to ensure that all companies in the Canada Post Group have consistent governance practices.

3. STATUS QUO AND THE CASE FOR CHANGE

3.1 Changing Business Conditions

The Canada Post Group of Companies is at a pivotal stage in its history. All segments of our business face competition. Canadians are significantly decreasing their use of traditional mail in favour of digital communications, which is having a profound effect on a business model founded on paper-based communications. In fact, since 2006 the Canada Post segment has experienced a decline of close to one billion domestic Lettermail pieces.

Volumes are declining faster than Canada Post is able to reduce costs given its current postal service obligations. In addition, large pension and post-employment benefit liabilities are putting significant pressures on the Corporation, especially given the current environment of low interest rates and their impact on the solvency funding requirements in the short term. These and other factors have resulted in significant financial pressures and create an urgent need for Canada Post to transform its business.

3.2 Our Pension and Benefits Challenge

While changing business conditions are having a material impact on profitability, funding the defined benefit pension plan solvency deficit will have an even more significant impact on the Corporation's liquidity going forward. While on a going concern basis the plan is properly funded, the market volatility and historic low solvency discount rates continue to negatively impact solvency deficits. Canada Post contributed $510 million to the pension plan in 2011, including $219 million in special payments. At the end of 2011, the company had an estimated three-year average solvency deficit to be funded of almost $4.7 billion. As at December 31, 2012, the three-year average solvency deficit to be funded had grown to $5.9 billion.

While the Corporation has continued to use pension relief to the greatest extent possible in order to avoid making solvency payments, without further relief the Corporation was expected to reach the limit for cumulative solvency payment relief, being 15 per cent of the pension plan assets, by early 2014. It was estimated that these payments would be in the realm of $2.5 billion over the five-year planning period.

This Plan assumes that the Government will grant a temporary relief to Canada Post from the requirement to make special payments during the next four years to allow the company, in working with its unions and other representatives of pension plan members, time to address the long-term sustainability of the pension plan. During the relief period, Canada Post will act with urgency to restructure the plan. Special payments are expected to resume starting in 2018, should a solvency deficit remain at the end of 2017.

This relief will enable Canada Post to execute its plans to return the business to financial self-sufficiency by 2019.

4. STRATEGIC ACTION PLAN

4.1 International Posts

Posts around the world are being challenged by structural declines in mail volumes, large pension and post-retirement health costs, and sluggish economies. The exclusive privilege, which at one time financed the cost of the universal service obligation (USO), has lost its value in a digital world.

Posts have responded to their changing environment in a number of ways. Most have undergone some form of operational restructuring. In addition to modernizing processing and delivery networks, Posts have reduced the number of owned postal outlets and their workforce and are enhancing their parcel services to take advantage of the growing e-commerce market. Some Posts now offer digital mail services to complement their physical mail products while others, especially in Europe, have expanded regionally and into adjacent businesses. More recently, some Posts have sought changes to their USO to reflect changing customer needs, the evolution of communications and their financial situation. Steps have been taking place in New Zealand, for example, to reduce the frequency of delivery in light of increasing costs and decreased reliance on physical mail.

United States

The United States Postal Service (USPS) experienced a decline of 25 per cent in mail volume between 2007 and 2012. It recorded a $15.9 billion net loss in fiscal year 2012 and in September of that year it reached its borrowing limit of $15 billion. It has subsequently defaulted on certain mandatory payments to the U.S. Treasury.

The USPS losses are in spite of significant improvements in areas of productivity, such as a reduction in the number of career employees by 24 per cent in the last six years. The Postal Service says it has run out of internal options to address its long-run financial challenges and has proposed further reforms (e.g., remove Saturday delivery, change to pre-funding requirements to retiree health care costs, pension reforms, plant rationalization), which can only be successfully achieved with the support of Congress. Congress is currently considering legislative reforms that, if passed, could address some of the reform issues the Postal Service has identified.

In September 2013, the USPS proposed across-the-board postage rate increases of approximately six per cent for virtually all of its services starting January 2014. In December 2013 the Postal Regulatory Commission allowed the proposed increases on an interim basis for up to two years.

U.K.

In 2010, an independent review of Royal Mail recommended key changes involving Royal Mail’s pension legacy costs, regulatory and pricing freedom, and retail post office management. In response, the U.K. government introduced new postal legislation addressing the changes. Ofcom, the regulator for postal services in the U.K., introduced a new regulatory framework in March 2012, which gave Royal Mail greater commercial freedom to set prices for its services.

On April 1, 2012 the U.K. government transferred Royal Mail's historic liabilities of around £40 billion from Royal Mail's pension plan to a new public sector plan to be administered by the government. At the same time around £28 billion of Royal Mail's pension assets were transferred to the government. The remaining Royal Mail Pension Plan (RMPP) was left with matching assets and liabilities. The transfer immediately removed Royal Mail's obligation to make cash payments of around £300 million every year to address the legacy pension deficit. Royal Mail continues to operate an employee pension plan and will be responsible for the payment of pension benefits built up after the transfer date.

On April 1, 2012, Royal Mail also transferred ownership and control of Post Office Limited (POL) directly to the Government. POL sells Royal Mail postage stamps and the Royal Mail Group's retail products (under the "Royal Mail" and "Parcelforce Worldwide" brands) to customers across the U.K.'s Post Office branch network. Also on that day, under its new regulatory pricing freedom Royal Mail increased First Class letter rates from 46p to 60p (a 30 per cent price increase) and Second Class rates from 36p to 50p (a 39 per cent price increase). Such postal rates were not out of line with comparable rates in other European countries.

On October 10, 2013 the British government sold a 52 per cent interest of its Royal Mail holdings to the public for £1.7 billion. The initial public offering placed the total value of the company at £3.3 billion. Its share prices rose over 40 per cent on the first day of trading in the open equity markets. The equity sale of Royal Mail follows the privatization of other European postal operators such as Deutsche Post AG, PostNL, and the Austrian postal service.

The reforms and recent business growth have placed Royal Mail on a more firm financial footing, enabling the successful privatization. In its latest financial year, revenues were up five per cent to £9.3 billion, boosted by a nine per cent rise in parcel revenues. Operating profit (stripping out exceptional costs) more than doubled to £440 million.

<u>EU Developments</u>

Though fully liberalized, the EU postal market remains formally regulated in areas of competition policy and universal service obligation. Much of the legal and regulatory framework reflects the goals and requirements of the postal sector as it existed in the early 1990s, but it is becoming apparent that many of the rules of engagement must be reconsidered in light of the rapid development of postal markets and the expansion of the EU from 12 to 28 Member States. Universal Service Providers (USPs) have been forced to adopt new price strategies, and prices have increased above inflation in some EU States (e.g., Germany, Netherlands, U.K.). As businesses look to save mailing costs, some postal operators have introduced new non-priority services (with lower delivery standards or restricted delivery days), accompanied by increased prices for priority services.

During the period 2010 to 2013, the European Commission adopted state aid decisions relating to the postal sector in several Member States. Some state aid cases dealt with compensation for providing universal services. The Commission generally found such aid justifiable where the high costs of pension systems were established when postal employees were civil servants and if the result was that the remaining social security contributions borne by the USP are equivalent to those of private competitors.

A recent report done for the EU suggests that the current "one-size-fits-all-and-always-will" approach regarding universal services (e.g., five day per week delivery, scope of products) needs to be more flexible in response to how markets and competition evolve in each Member State. The report suggests relaxing the specific EU-wide performance / quality metrics regarding the USO, to focus on general principles regarding standards of quality that should be reflective of the market condition in each Member State.

4.2 Our Strategy

In Canada, we are facing a monumental shift in our business, as electronic means of communications are replacing paper to communicate, invoice and pay bills, and advertise. Our revenues are declining due to this shift, but our cost base is largely fixed and cannot be significantly reduced under the requirements of the current *Canadian Postal Service Charter*. As Canadians change how they are using the postal service, Canada Post must adapt and provide them with the kinds of services they require, where and when they want them, not simply continue to provide services as we traditionally have.

The initiatives we plan to undertake will enable us to meet the emerging postal needs of Canadians, while tackling the company's financial challenges and reducing the size of our workforce and the associated costs. These initiatives are an integral part of the strategic priorities that will guide our operations over the Plan period:

- redefining postal service for the 21st century;
- becoming a leader in enabling e-commerce;
- repositioning direct marketing in the age of digital and social media;
- an unrelenting focus on cost-savings;
- labour transformation;
- strengthening digital commercialization; and
- establishing a clear mandate for each subsidiary.

5. OUR STRATEGIC PRIORITIES

5.1 A Post Office for the 21st Century

5.1.1 Canada Post's Five-point Action Plan

In its April 2013 report entitled *The Future of Postal Service in Canada*, The Conference Board of Canada reflected on the challenges faced by Canada Post and the urgent need for the company to transform to serve the changing needs of Canadians. They detailed a number of options which, alone or in combination, would help Canada Post meet those needs and return to profitability: large price increases, wage restraint, alternate-day delivery, the elimination of door-to-door service, conversion of corporate postal outlets and the reduction of service standards.

We know that no single initiative will be sufficient to stem the losses from the steep decline in letter volumes. To meet the evolving postal needs of Canadians in the 21st century without becoming a burden on taxpayers, we have a comprehensive plan that will help bring us back to profitability in 2019 and position us for a successful and financially sustainable future.

5.1.2 Community Mailboxes

The biggest change in our operations over the next five years will be in delivery, which accounts for some 40 per cent of our operating costs. With only one third of Canadian addresses (some five million) receiving door-to-door delivery today, we plan to convert most of those addresses to CMBs. CMBs offer a safe location, close to home, for Canadians to pick up their mail and parcels at their convenience.

The vast majority of businesses, including those with large volumes of mail or parcels and those located in well-established business areas, such as main streets, or "business corridors" will retain door-to-door delivery. This conversion will help standardize the mode of delivery across the country, allowing for significant gains in efficiency. This conversion also supports our plans to grow parcel volumes and encourage e-commerce.

The change is crucial to the financial viability of Canada Post. CMB conversion is forecasted to contribute an estimated $400 to $500 million in annual savings on full implementation. Canada Post plans to undertake a comprehensive communications and community outreach process to smooth the implementation of this change with Canadians.

5.1.3 Dealer Post Offices

Canada Post has the most extensive retail network in Canada, with close to 3,900 corporate post offices and 2,500 post offices operated by private dealers. However, Canadians are using post offices differently than in the past, now that they have digital options at their fingertips. To optimize coverage for all Canadians, we need to better align our retail network with customer needs.

Although 60 per cent of our post offices are corporately owned and operated, corporate post offices provide less than half the revenue from our retail network. Dealer post offices – the "shop within a shop" – are popular with customers because they are located where people shop and are open at more convenient times than many corporate outlets. They also have a much lower cost structure. In order to expand convenience for Canadians, we will be adding new dealers to our retail network and are also investigating less expensive alternatives for serving customers, such as kiosks.

The changes to the retail network contained in this Corporate Plan are expected to provide annual savings of approximately $40 million to $50 million.

5.1.4 A More Streamlined Operations Network

Given that in the future the mail will consist of more parcels and packets and even fewer letters, we are realigning our operations network to improve efficiency while focusing on parcels growth.

Some of the initiatives currently underway to streamline our operations include:

- a realization of economies of scale by consolidating Lettermail processing into major plants within the major urban centres;
- the rationalization of delivery operations in response to a reduction in Lettermail volumes; and
- a reduction in the amount of manual processing required, inside both plants and depots.

These changes, which are expected to result in savings of approximately $100 million to $150 million per year, are being made with minimal expected impact on service levels and a focus on competitive parcel delivery standards. The streamlining of operations will continue, leveraging technology and opportunities to consolidate.

5.1.5 A New Pricing Approach

Lettermail volumes are now declining at a rate of about six per cent a year, but we know that the need for certain types of mail will never disappear. This is especially true of "evidence mail" such as identification cards, credit cards, licences and proofs of transactions. We believe that, even though the traditional mail market is now fully mature, valuable niche opportunities for revenue remain in Lettermail.

A new approach to pricing is necessary to better align price with the cost of serving the different types of mailers. In 2014 we plan to introduce a differentiated pricing structure for domestic Lettermail, which will provide volume-based discounts to those who use the mail most. Once we receive regulatory approval, basic stamps bought in booklets, panes or coils will cost $0.85, while an individual or business using a postage meter will pay a lower, commercial rate of $0.75. The price of a single basic stamp will increase to $1.00. This new pricing approach will result in approximately $160 million to $200 million of additional revenue annually.

5.1.6 Delivery Frequency

In our recent consultations with Canadians, we often heard that delivery less than five days a week would be acceptable to consumer receivers. However, small- and medium-sized businesses told us that they still rely on delivery each business day. Less frequent delivery could be detrimental to their businesses given their reliance on mail, particularly for and the invoicing and receipt of payments that generate steady cash flow. Much of the direct marketing mail currently being delivered in Canada is date-sensitive. Most importantly, the growing e-commerce sector depends on daily delivery and our competitors are delivering five days a week across the country.

Although reducing the frequency of delivery would result in cost savings, now is not the time to reduce days of service. We will continue to monitor volumes and uses of the mail to determine when a change in the frequency of delivery might become appropriate.

5.2 Opportunities in E-Commerce – Delivering the Online World™

The growth of e-commerce presents significant opportunity for Canada Post. With the increasing popularity of online shopping among Canadians, the parcels market is poised to continue to grow considerably both worldwide and in Canada. Canada Post is well positioned to capture that growth. Even though we face fierce competition for volumes from well-funded international courier companies, we are the undisputed leader in business to consumer (B2C) delivery in Canada.

Canada Post has invested heavily in promoting its suite of e-commerce services, catering to the needs of online shoppers by making delivery more convenient and offering more delivery options. In our continued efforts to reinforce our position in the Canadian e-commerce market and to showcase and celebrate the best eTailers of all sizes in Canada, we held the 2nd annual Canada Post E-commerce Innovation Awards™ in September 2013. Also in September we launched same-day delivery in the Greater Toronto Area in partnership with leading Canadian retailers under the name "Delivered Tonight", which coincided with a television ad campaign to support our new brand position of "Delivering the Online World". We will continue to modify, enhance and market our web services to ensure we maintain our role as leaders and innovators in the eyes of both businesses and consumers.

It is clear that Canadians have developed a taste for international shopping. In order to capitalize on this and increase our share of the international parcels market, Canada Post is working to facilitate relationships with those who enable international trade into Canada and to remove barriers to cross-border commerce. In 2013, we launched our outbound tracked packet service to the U.S. and 19 other countries, and enabled the launch of PuroPost in conjunction with Purolator, servicing customers shipping northbound and providing them with access to our residential delivery network. We will continue to make investments in our core technological capabilities to improve scanning and tracking.

Going forward, Canada Post will continue to position itself to be the preferred shipping provider for B2C deliveries in Canada, with a focus on improving our relationships with e-commerce shippers, enhancing our delivery options to differentiate us from the competition in residential delivery, and further reducing our operating costs.

Parcels revenues are forecast to grow to $1.4 billion in 2013 or 23 per cent of our overall revenue. By the end of 2018, parcels will represent over 29 per cent of revenues for the Canada Post segment.

5.3 Repositioning Direct Marketing in the Age of Digital and Social Media

In this age of digital and social media, the competitive market place is very fragmented and marketers are now freer than ever to convey their messages using a variety of products. Nevertheless, direct mail remains an important part of a multi-media mix for both large and small businesses – a very affordable product with an excellent return on investment. Smaller businesses such as restaurants, owner-operated stores and trades continue to see the value of flyers to advertise their products and services to the local community.

Canada Post's Direct Marketing (DM) products ($1.3 billion) compete within the $16.5 billion advertising market in Canada, which is estimated to grow at approximately four per cent annually over the next five years. We are working hard to promote the value of direct mail through a variety of awareness and relevancy campaigns and by encouraging greater use of mail as part of multi-channel advertising campaigns. To retain existing customers and attract new ones we are eliminating customer irritants and redesigning our products from a customer point of view to simplify pricing, make it easier to work with us and make our products easier to use.

Over the Plan years we will continue to promote the value of direct mail in helping companies build their business and will continue to improve the customer experience and encourage growth.

5.4 An Unrelenting Focus on Cost-Savings

5.4.1 Cost-Saving Initiatives

Given the continuing challenges to our financial self-sustainability, Canada Post has worked very hard in recent years to reduce costs wherever possible while minimizing the impact on our service to Canadians. We will continue to improve our processes in the future to ensure that our service to customers is of a consistently high quality.

We will be seeking to reduce our retail costs through a number of customer self-service options, such as self-service kiosks and the virtual post office. We will also be closely monitoring the work effort required to operate our retail outlets and optimizing staffing levels to align with customer traffic. Major cost savings are expected from improved productivity, through redesigned processes enabled by technology. More mail will be processed by machines and where possible, we will be consolidating mail processing into larger plants, capitalizing on the processing capabilities and speed afforded by state-of-the-art technology.

5.4.2 Postal Transformation

The $2 billion PT project was launched in 2008 to replace outdated mail and parcel processing plants and equipment, automate manual sorting processes, reduce costs and consolidate delivery processes, and increase productivity. Close to 82 per cent of the $250 million in project benefits planned for 2017 are expected to be achieved by the end of 2013, with labour reduced, via attrition, by close to 2,900 full-time equivalent employees (FTEs). PT benefits are on track to reach the targeted level of savings.

New systems, supported by a centralized computer system, now provide the capability to automatically sort mail and parcels and sequence mail for an increased number of locations, and allow for standardized sorting strategies across the network. Completion of the deployment of the parcel automated sortation infrastructure will significantly improve parcel tracking and the customer experience, and along with the new container handling systems installed in Toronto, Montreal and Vancouver, will significantly increase our parcel processing capability and provide us with much needed capacity.

Going forward, we will complete the remaining deployments of our new delivery model in Toronto. The Vancouver city transition will peak in the early part of 2014 with the transfer and consolidation of our city sort operations to the new processing centre (the Pacific Processing Centre). This centre will include our first automated exchange office for international mail. Over the Plan period we will continue to work with the Canada Border Services Agency to modernize our exchange offices, not only in Vancouver, but also in Toronto and Montreal, which will make the processing of international mail more efficient and improve customer service.

Even as we implemented PT, in 2012 the frequency of employee injuries resulting in time lost from work was down 12 percent from the previous year, which made it the best result in 30 years and a reduction of some 40 per cent since 2006.

5.4.3 IT Savings

The newly restructured Innovapost is an important part of our strategy to strengthen synergies among the Group of Companies by building increased business capabilities on common platforms wherever possible. Under its first year of restructured operations, Innovapost has re-organized to deliver services more efficiently, continued to reduce ongoing operating costs, and embarked on a multi-year transformation program to enter into new market-based contracts to deliver its services. Moving from exclusive supplier contracts to multiple supplier arrangements will allow the Group to take advantage of industry expertise and best practices, new technologies, and reduced labour costs to optimize the value and cost of service delivery across all IT services.

On behalf of the Group, Innovapost has initiated Request for Proposal (RFP) processes for Data Centre services, application development services and end user computing services. The transition to the new vendors is expected to be complete in 2015.

Innovapost operates on a cost-recovery basis, hence there is no expectation of profit in the Innovapost financial plan. The Group of Companies will see the cumulative annual savings reach over $50 million once the Innovapost transformation program is fully implemented.

5.5 Labour Transformation

5.5.1 Objectives

Labour transformation is our fifth strategic priority. The future health of our business depends on our ability to be as cost-competitive and operationally flexible as possible. A realignment of our labour costs to reflect the changes we are making in the business is therefore crucial for our future success.

The changes to our service model as described in the Five-point Action Plan will result in between 6,000 and 8,000 fewer positions. Management and non-unionized employee positions will be reduced in line with the changes to our operations and unionized workforce. Canada Post has already reduced its management cadre by 18 per cent since 2008.

Canada Post's objectives in all collective bargaining are to permanently address pension cost volatility, align our costs more closely with those of our competitors and improve operational flexibility.

5.5.2 Collective Bargaining

Canadian Union of Postal Workers (CUPW)

Canada Post Corporation and the CUPW signed a new four-year collective agreement for urban employees in December 2012. The new agreement includes:

- lower starting wages for new hires;
- no wage increase for the year 2015/16;
- changes to pension eligibility for new employees (30 years of service and 60 years of age rather than 55);
- a higher employee premium for post-retirement health care benefits; and
- elimination of the traditional sick leave program in favour of the same short-term disability program that has been in place for all other Canada Post employees for a number of years.

In December 2012 Canada Post also signed a new collective agreement with CUPW-RSMC, which represents approximately 7,000 rural and suburban mail carriers. The new four-year collective agreement includes wage and benefit improvements that are more aligned to those of our competitors.

Public Service Alliance of Canada/Union of Postal Communications Employees (PSAC/UPCE)

PSAC/UPCE represents almost 1,500 administrative and technical employees at Canada Post. Canada Post and the PSAC/UPCE have been negotiating since September 2012 for the renewal of the four-year collective agreement that expired on August 31, 2012. Canada Post's aim is to negotiate an affordable settlement that protects a viable future for the company by reducing costs.

Association of Postal Officials of Canada (APOC)

APOC represents supervisors and supervisory support groups such as trainers, route measurement officers and sales employees. Negotiations for a new collective agreement will begin in spring 2014. The APOC collective agreement provides for final offer selection arbitration as a means of resolving outstanding issues when a negotiated settlement cannot be reached. The process is used in place of a strike or lockout.

Canadian Postmasters and Assistants Association (CPAA)

The Corporation is in the last year of a five-year collective agreement with the CPAA, which represents rural post office postmasters and assistants. As with the APOC collective agreement, the CPAA agreement refers to the final offer selection process as a means of resolving outstanding issues.

5.6 Strengthening Digital Commercialization

5.6.1 Introduction

Given the pace at which digital technology is evolving and Canadians are changing the ways in which they communicate, Canada Post must strengthen its digital capabilities to remain relevant to Canadians. We intend to invest to further develop the Digital Delivery Network over the next five years. These investments will help see revenue growth from digital products, and will support new revenue growth in our DM and parcels businesses as well as cost-reduction initiatives across our business.

We will have three main areas of focus over the Plan period:

1) the creation of a Virtual Post Office;
2) building an authenticated platform leveraging epost™; and
3) monetizing the value of our address-based data assets.

5.6.2 The Virtual Post Office

As Canadians become more accustomed to conducting business and communicating online, they are expecting Canada Post's products and services to be available electronically, as well as at post offices. Through our Virtual Post Office (VPO), our products and services will be available any day, all day, with the assurance of personal online support. Using a single sign-on, businesses and consumers will be able to initiate and manage their transactions electronically, knowing that their orders will be delivered as they require through our vast physical network. The VPO will be available on all platforms, including mobile, where Canada Post already has one of the most widely used apps (track a package, with 1.2 million downloads and over 17 million parcels tracked in the first 9 months of 2013).

As we expect the demand for online services to increase over the planning period, the VPO is an important component of our customer engagement and management plan. We intend for the VPO to be a secure open platform to which products and services from our partners can be added in the future. The VPO will help reinforce the Canada Post brand with Canadians as trusted, secure, available and innovative in both the physical and the digital realms.

5.6.3 The epost platform

A second area where Canada Post intends to focus its efforts over the Plan period is on the continued enhancement of epost.

Launched in 2000, epost was the first electronic bill consolidator in Canada. Today it is the largest, with over eight million subscribers registered since inception and 250 bills and statements available from over 100 mailers in a safe and secure way. Since its inception, epost has been expanded to enable subscribers to access their favorite magazines in digital format and track their monthly bills and payments. A secure and encrypted electronic storage capability known as Canada Post Vault™ also allows people to store important digital files.

Over the planning period, we intend to improve the technological platform and the capabilities of epost and integrate epost into the VPO. We will be building our identity management capabilities to link digital addresses with physical addresses, thereby creating new commercial opportunities to link credentialed consumers with specific business- and government-related services while maintaining their personal privacy.

A major emphasis in 2014 and 2015 will be to accelerate consumer engagement by making it easier for them to access key business and government services. We will be forming strategic partnerships with mailers to attract more consumers and mailers to epost and to promote its value, particularly for transactions requiring authenticated content.

5.6.4 Commercialization of Data Assets

The third component of our digital strategy is to leverage our address-based data assets that are anchored on the Postal Code and National Change of Address databases. By incorporating unique data and privacy compliance into every initiative, Canada Post will be in a position to fully commercialize the value of our assets while maintaining our trusted brand and our strong data governance principles.

Over the Plan period we plan to pursue monetization of our postal code and address assets when they are used for commercial purposes.

5.7 Establishing a Clear Mandate for Each Subsidiary

5.7.1 Synergies and Focus

Over the planning horizon, we will be working to achieve further synergies within the Canada Post Group of Companies in terms of both costs and revenues by integrating and coordinating activities where appropriate, bearing in mind the need to respect the interests of all individual company shareholders.

On the cost front, the restructuring of Innovapost as the supplier of IT services for the entire Group will generate savings while ensuring that the companies all benefit from the same top quality expertise in information technology. We also expect to generate savings for the Group by coordinating large scale activities such as procurement and network management.

On the revenue front, our priority over the planning period will be to ensure that each company is focused on activities for which it enjoys a competitive advantage. In this way, each company will be able to focus on its respective strengths but complementary activities can be coordinated in a seamless manner. This approach is expected to generate a greater market share for all participants, as well as better customer experience.

5.7.2 Purolator

Purolator Inc., Canada's largest courier company, is 91 per cent owned by Canada Post. Purolator has an extensive service network within Canada. Its fleet of more than 3,700 vehicles includes one of the largest hybrid electric fleets in North America.

As a Canadian market leader for over 50 years, Purolator's key strength lies in its strong brand and reputation, and proprietary Canadian express network reach and speed. Purolator was ranked the fifth Canadian brand out of 100 ranked brands in the 2012 Marketing / Leger Corporate Reputation Survey, surpassing all other transportation brands. Purolator was also the only Canadian 3PL recognized at the *Logistics Management* magazine's 2012 Quest for Quality Awards, reflecting its strength in the U.S. and its success in its market expansion effort.

Purolator will strive to refresh its strategic direction over the Plan period, leveraging its key strengths while addressing its vulnerabilities. Purolator's overall strategic priorities include building a sustainable operating model, protecting core markets, and generating new profit streams. First and foremost, the company will sharpen its focus on optimizing its operating processes. This focus will enhance its cost competitiveness, improving profitability, while building capabilities to enable growth. Strategic focus areas will include efforts to optimize the product portfolio for both courier and freight to improve yield and drive profitable volume and to capitalize on the Group of Companies' retail and e-commerce market growth.

5.7.3 SCI Group

Through its operating entities SCI Logistics, Progistix and First Team Transport (operating as SCI-White Glove Services), the SCI Group offers its clients expertise in B2C, business to business (B2B) and field service logistics, while delivering innovation, intelligence and integration to supply chains across Canada. SCI allows the Canada Post Group of Companies to offer end-to-end supply chain services to Canadian businesses. Canada Post owns 90 per cent of SCI Group and Purolator holds the remaining 10 per cent.

SCI is acting on its strategy to become Canada's leader of integrated forward and reverse supply chain solutions for high-value and high-growth segments in Canada. Leveraging opportunities within the Canada Post Group of Companies to provide scale and reach will also enable SCI to increase overall market share within Canada.

In 2014, SCI will continue to focus on profitable growth. This will come from targeted verticals such as retail, e-commerce, health care and technology, the growth of contract logistics and transportation services, and operational savings driven by continuous improvement initiatives.

5.7.4 Innovapost

Innovapost was created in 2002 as a joint venture with the private-sector firm CGI. Under an agreement approved by the Government in 2012, Innovapost was restructured. Canada Post became the majority shareholder with an 80 per cent ownership share and Purolator holds the remaining 20 per cent.

Innovapost is the shared IT services entity for the Group of Companies. Its services currently include the development, maintenance and operation of the computing and information systems required by the Group of Companies. The restructured Innovapost is an important part of our strategy to strengthen synergies among the Group of Companies and increase our competitive advantage by building increased business capabilities on common platforms wherever possible. This will help the Group keep pace with overall technological change (e.g., the next generation of hand-held personal data terminals), increase efficiencies, and improve service delivery while reducing overall IT costs.

6. FINANCIAL MANAGEMENT STRATEGIES

6.1 2014 Capital Budget

The Canada Post segment's 2014 Capital Budget is planned at $323 million.

Area of Responsibility		**2014 Capital Budget ($ millions)**
Postal Transformation	Toronto and Vancouver depot construction, real estate and equipment for parcel processing in Montreal and Vancouver, Vancouver plant construction, Exchange Office modernization and mail sorting equipment.	95*
Five-point Action Plan	Investments aimed at aligning the Retail network to optimize coverage, processing changes and standardizing the mode of delivery through CMBs.	84
All Other	Asset maintenance, Lines of Business, Information Technology, Operations service and quality tools, equipment, and process improvements, health and safety programs, retail outlet maintenance and other capital projects/ expenditures including minor technology upgrades.	144
Canada Post segment		**323**

*The overall PT program is $2.0 billion; $1.61 billion is related to capital. Almost 90 per cent of the capital ($1.45 billion) is forecasted to be spent by the end of 2013 with $95 million planned in 2014 and the remaining $69 million in 2015 to 2018.

In 2014, we will focus on those initiatives that are critical to achieving our strategic priorities, and invest in maintaining our infrastructure. A top priority will be our Five-point Action Plan, with a focus on CMB and Retail initiatives, as an essential means to bring ourselves back to long-term financial self-sufficiency.

We will continue to invest in PT, operational tools, equipment, processes, and infrastructure to drive improvements in costs, service, and health and safety. Capital requirements for the Lines of Business will be focused on growing e-commerce and Direct Marketing, building the Virtual Post Office and leveraging epost to create a platform that connects credentialed users with authenticated content.

6.2 Pension Plan

Canada Post has the largest pension plan of all Canadian Crown corporations and one of the largest single employer-sponsored pension plans in Canada, at approximately $17 billion in assets at fair market value and a $23 billion obligation on a solvency basis at the end of 2012. It is a significant challenge to plan for and deal with the pension given its size and volatility relative to the earnings generated.

Canada Post is obliged to maintain sufficient funding of the pension assets to finance the pension plan in the event of a wind-up. As at December 31, 2012, the valuation showed that the pension plan has a going-concern surplus of approximately $100 million and a solvency deficit to be funded of $5.9 billion, with a three-year average solvency funded ratio of 75 per cent.

Volatility in year-over-year changes in discount rates and investment returns are major drivers in determining the financial position of the pension plan, and in the current environment volatility may be higher than in the past. If the combination of low or falling bond yields (used to value the liability) and the current uncertainty of the equity markets continues, it would cause the liability to remain high and the asset returns to be below expected returns, the worst possible outcome for a pension plan.

The Corporation has entered into an agreement with the Government to reduce its special solvency payments in accordance with the *Pension Benefits Standards Regulations, 1985* and associated Regulations. This has allowed the company to reduce its aggregate special solvency payments by approximately $1.3 billion as at December 31, 2012. This Plan assumes that the Government will grant pension solvency relief for the first four years of this Corporate Plan to enable Canada Post in working with its unions and other representatives of pension plan members, to make permanent changes to the pension plan that would help address its future viability.

6.3 Canada Post Segment Borrowing Plan

6.3.1 Financing Strategy

This Corporate Plan reflects changes associated with implementation of our seven strategic priorities described above, which will result in a greatly improved outlook for cash flow generation and profitability. However, these changes alone would not be sufficient to address the Corporation's financial difficulties without relief from the obligation to fund solvency payments into the pension plan.

The combination of improved operating cash flow from the implementation of the Five-point Action Plan with ongoing relief from pension plan solvency payments will enable the Corporation to once again be financially viable, and borrowing requirements will be minimal. We anticipate that no new borrowing, other than short-term borrowing for cash management purposes, will be required in 2014, 2015 and 2016. Cumulative borrowing of approximately $700 million will be needed in 2017 and 2018 due to the high level of capital expenditures incurred to implement our strategic priorities during the Plan period. We do not expect any further borrowings beyond 2018.

6.3.2 Short-Term Borrowing Approval for 2014

Canada Post requires sufficient liquidity, defined as cash and cash equivalents on hand plus immediately available short-term borrowings, to ensure that it can meet its obligations as they come due, as cash balances fluctuate significantly on an intra-month basis. The Corporation also requires sufficient liquidity to absorb unfavourable outcomes, whether related to revenues, expenses or capital expenditures, relative to plan. The Minister of Finance has provided approval for up to $100 million of short-term borrowing for 2014 in accordance with section 127.3 of the *Financial Administration Act*.

From time to time, as a result of unforeseen financial market conditions or unexpected variances in approved corporate activity, there may be a need to amend the terms and conditions of borrowing activities as approved by the Minister of Finance. In such an instance, Canada Post will seek approval of the proposed changes from the Minister of Finance. Any approved changes will be reported in the subsequent Corporate Plan.

6.3.3 Borrowing Plan and Five-Year Overview

The Canada Post segment's debt levels for the 2014 to 2018 planning period are summarized below:

Forecasted Debt Summary

(in millions of dollars)	**2014**	**2015**	**2016**	**2017**	**2018**
Opening balance	1,057	1,055	1,058	1,041	1,400
Net borrowings/(repayments)	(4)	(4)	(19)	356	296
Other changes	2	6	2	2	6
Ending balance	1,055	1,058	1,041	1,400	1,703

Numbers may not add due to rounding.

6.4 Dividend Policy

The approved five-year Financial Framework covers the period from 2010 to 2014. The Framework includes a dividend payout of 0 per cent to 20 per cent until 2012, and a payout of 15 per cent to 20 per cent in 2013 and 2014.

Given our projected financial outlook, and pursuant to section 130.1 of the *Financial Administration Act*, Canada Post is proposing that no dividend payment be made during the course of this Plan.

6.5 Economic Forecast

The Bank of Canada projects modest global economic growth in 2013, with a rate of 2.8 per cent. Growth is expected to strengthen to 3.5 per cent in 2014 and 3.7 per cent in 2015. U.S. economic expansion is continuing at a modest pace despite growing concerns as the country again breaches its debt ceiling. However, global economic factors such as a continuing European recession and slower growth than expected in emerging countries after a strong second half of 2012 could put this expansion at risk.

Following a weaker than expected 2012, Canada's economy is not expected to pick up momentum until the latter part of 2013. Despite a fairly strong first quarter result of 2.2 per cent, economic growth is projected to be less than two per cent for the second straight year, largely due to continued restraint in government and business investment spending. The Bank of Canada does not see Canada's economy returning to full capacity until mid-2015.

Housing starts are expected to continue to add an average of 175,000 addresses to Canada Post's network per year, increasing the cost pressure on delivery operations.

The uncertain nature of Canada's economic recovery continues to be a primary contributing factor to the pace of mail volume erosion. Parcel volumes grew in 2012 and through the first part of 2013 on the strength of the growing e-commerce market, but Canada Post will need to closely control its costs in order to maintain this growth and remain competitive in the current economic climate.

	History		**Economic Projections**			
Calendar Years	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**
ECONOMIC (% change)						
Real Gross Domestic Product	2.5%	1.8%	1.7%	2.5%	2.6%	2.3%
Inflation (Consumer Price Index)	2.9%	1.5%	1.1%	1.8%	2.1%	2.0%
Core Inflation	1.7%	1.7%	1.4%	1.8%	2.0%	2.0%
DEMOGRAPHIC (% change)						
Total Population Growth	1.2%	1.1%	1.1%	1.1%	1.1%	1.1%
Total Points of Delivery	1.0%	1.0%	1.2%	1.1%	1.1%	1.1%

Sources: All projections are based on the October 2013 quarterly projections by the major banks, as well as the July 2013 Bank of Canada projections. Points of Delivery projections also take CMHC Q3 housing starts projections into account.

6.6 Financial Framework

When the five-year Financial Framework was initially approved in December 2009, it was recognized that revisions would be needed to take into consideration the conversion of accounting standards from Canadian Generally Accepted Accounting Principles (GAAP) to International Financial Reporting Standards (IFRS). In approving the 2012 to 2016 Corporate Plan, the Government approved a revised Financial Framework for the period from 2010 to 2014 to reflect the adoption of IFRS.

The table below presents the Framework and the Corporation's anticipated performance over the five-year planning period.

Canada Post Corporation
Consolidated Financial Ratios

	Financial Framework	Forecast	Five Year Plan				
		2013	2014	2015	2016	2017	2018
Profitability							
(1) EBITDA margin	5.0% - 7.5%	2.1%	1.3%	1.8%	1.7%	1.4%	3.2%
(2) Return on adjusted book equity	0% - 5%	(7.7%)	(13.5%)	(14.5%)	(18.9%)	(27.6%)	(22.5%)
Leverage							
(3) Total debt to EBITDAR	2.5x - 4.0x	7.1	8.7	7.5	7.6	9.3	6.9
(4) Total debt to adjusted book capital	45% - 65%	57.8%	61.4%	65.0%	69.2%	77.6%	82.9%
Liquidity							
(5) (EBITDAR - capex)/interest	1.0x - 2.5x	1.7	(0.4)	(2.0)	(2.6)	(3.0)	(1.1)
Dividend payout							
(6) Dividend payout ratio	0% - 20%* 15%-20%**	0%	0%	0%	0%	0%	0%

* Dividend payout ratio is 0%-20% until 2012, then 15%-20%.
**The 0% dividend payout projection is due to negative net income going forward as per section 6.4.

Ratio Definitions

(1) Earnings before interest, taxes, depreciation and amortization ÷ revenue
(2) Net profit (loss) ÷ ((adjusted book equity$_E$ of Canada beginning of year + adjusted book equity$_E$ of Canada end of year) ÷ 2)
(3) (Total debt + long-term financial obligations$_A$) ÷ (earnings before interest, taxes, depreciation and amortization with adjustment for operating leases$_B$)
(4) (Total debt + long-term financial obligations$_A$) ÷ (total debt + long-term financial obligations$_A$ + adjusted book equity$_E$ of Canada)
(5) (Earnings before interest, taxes, depreciation and amortization with adjustment for operating leases$_B$ - capex$_C$)/interest$_D$
(6) Dividends paid ÷ prior year net profit (loss)

Notes

(A) Long term financial obligations include asset retirement obligations, obligation to repurchase shares (Purolator) and capitalization of operating leases.
(B) Operating leases are removed from earnings and capitalized using a factor of 7.0x .
(C) Capex refers to maintenance capital. In this plan, maintenance capital includes all capital purchases and capital leases but excludes approximately $400 million of capital purchases for Postal Transformation.
(D) Interest includes imputed interest on capitalized operating leases (calculated as 1/3 of lease expense).
(E) Adjusted book equity is reported equity with the impact of other comprehensive income (loss) non-reclassifying items removed.

7. RISK MANAGEMENT

7.1 Risk Management Framework

Under Canada Post's Enterprise Risk Management (ERM) practice, risk updates are produced on a quarterly basis and provide an overview of strategic and operational risks as well as associated mitigation plans. Deeper risk identification activities occur on a semi-annual cycle. The consolidated results are brought to the Board of Directors twice a year, in April and October, which aligns with the strategy setting and planning cycles of the company. The ERM framework helps inform the Board's direction for the development of the Corporate Plan.

Ongoing risk assessment occurs through external monitoring of our environment, internal reporting on key performance indicators and the management structure. Day-to-day management of risks resides with functional or subject-matter experts within the company. Basic risk controls, including proper governance, performance management, decision-making policies and other internal controls, act as the foundation of risk management.

The current ERM was prepared during the summer of 2013. It reflects the necessity of the Five-point Action Plan to help mitigate some fundamental risks associated with the financial sustainability of the Corporation.

7.2 Strategic and Operating Risks

7.2.1 Introduction

A summary of the top strategic and operating risks as identified by the ERM framework is set out below. The order of presentation roughly reflects the relative degree of either importance or immediacy to the Corporation. Canada Post feels that the assumptions made in this Plan are reasonable and are neither overly optimistic nor pessimistic. Nevertheless, it is possible that future performance will deviate materially from our stated projections.

7.2.2 Strategic Risks

The top strategic risks identified by the ERM framework are as follows.

1) <u>Costs associated with employee pensions and post-retirement benefits</u>

The scale of the Canada Post Registered Pension Plan relative to the Corporation's earnings and revenue, and funding volatility pose an ongoing risk to the Corporation's cash flows and its ability to fund needed investments in modernization and growth. A four-year moratorium on special payments to the pension plan would ensure that the Corporation has sufficient liquidity for operations. Canada Post will closely manage costs through the initiatives outlined in this Corporate Plan.

2) <u>Acceleration of core revenue decline</u>

High levels of erosion for transaction and marketing mail could further compromise our cash flow and long-term financial sustainability. Reasonable forecasts for volumes have been included in the Plan. Implementation of Canada Post's seven strategic priorities, including pricing and cost management measures and service enhancements, will address this risk.

3) Ability to achieve financial sustainability

Without significant structural changes, the Corporation anticipates substantial annual losses. Canada Post plans to mitigate this risk through implementation of its Five-point Action Plan.

4) Ability to achieve revenue growth

Specific risks associated with executing an effective growth strategy include strong competition from global integrators, talent gaps and legacy processes that limit flexibility in the market place. Canada Post is expanding its parcel capacity in physical delivery and is increasing its marketing activities through a new campaign entitled "Delivering the Online World". Our presence in the digital marketplace is being strengthened with the enhancement of epost, which will provide revenue opportunities. Opportunities for growth that leverage synergies in the Group of Companies are also being pursued.

5) Key strategic procurement risks related to major suppliers' transition

Significant procurement activities are underway in IT, air cargo and real estate. Failure to execute a successful transition could impact Canada Post's finances, reputation and operations. We are addressing this risk through robust procurement processes, with guidance from a fairness commissioner and the hiring of third party industry and legal experts during the transition.

6) Information systems and technology (IS&T) performance could hinder transformation and growth agendas

Lack of funds for investment could result in obsolete systems that prevent us from developing growth opportunities. External risks could include cyber attacks and data breaches. The restructuring of Innovapost and careful planning processes are designed to address this risk. Prevention and mitigation measures have been implemented as part of the Information Security Framework to address key areas of risk, threats and vulnerabilities.

7) Labour transformation could impact costs, service and core revenues

Legacy collective agreements continue to constrain Canada Post's ability to compete in the market place. Labour disruptions would impact the brand and service. Canada Post's approach to collective bargaining is to protect its financial viability and long-term sustainability.

8) Failure to capture Group of Companies synergies

The Group of Companies has had some success in recent years in leveraging the synergies that exist between Canada Post, Purolator and SCI. Inability to capture these in the future would lead to foregone revenue opportunities and unnecessary operating costs. To minimize this risk, the Corporation has developed a co-ordinated strategy to increase market share and improve profitability and alignment.

9) Brand erosion could impact trust and ability to transform and grow the business

Erosion of trust could hinder our ability to make the necessary operational changes and enter into new services. Ongoing efforts to build and sustain the brand include a strong focus on quality and service performance, as well as promoting our core competitive advantages and record of environmental responsibility.

7.3 Operational Risks

The top operational risks identified by the ERM framework are as follows.

1) Attrition and overall talent management

Approximately half of Canada Post's current full-time employees are expected to leave the company in the next ten years, mostly through retirement. Loss of corporate knowledge and skills, and failure to capture planned attrition, could complicate modernization plans and affect the company's operational effectiveness. Failure to attract and retain top talent could impact the Corporation's ability to compete, grow and innovate. Canada Post is closely monitoring short- and long-term operational requirements and actively managing attrition risks and opportunities.

2) Privacy and security of mail, electronic information and enterprise assets

Risks to security and privacy involving physical mail, electronic information and enterprise assets affect our reputation, brand, customer loyalty and financial sustainability. Canada Post has invested heavily in physical and electronic security, the protection of employee and customer data and the avoidance of fraudulent use of its products and services. The company also works with external regulators and companies to manage emerging or new risks.

3) Achieving operational excellence and financial benefits from change initiatives

If the Corporation is unable to maintain productivity and service levels while implementing significant changes, it risks not achieving the benefits expected from change initiatives. Cost savings will partly depend on the company's ability to maintain operational excellence and labour co-operation throughout a period of rapid change. Detailed execution plans, rigorous project management and cost control, benefit measurement tools and periodic reviews to validate assumptions and finalize operating targets are in place to ensure that the expected savings are achieved.

4) Business continuity

Factors such as service failures due to outdated infrastructure and labour disruptions, and environmental factors such as floods and earthquakes can seriously impact service quality and cost management. The Corporation has a business continuity management program in place to ensure the delivery of its critical physical and digital services. Business continuity plans are regularly tested and updated.

5) Working environment for employees

As the Corporation evolves its operations to address the changing nature of its business, there is a risk that recent safety performance improvement will not be sustained. An aging workforce may require more accommodations. The company is addressing these issues through health and safety training, safety assessments and the new short-term disability program.

6) Service quality

Failure to maintain service quality during periods of transition poses risks for cost management and customer retention. Over the long term, cost savings from our transformation efforts will depend on our ability to maintain operational excellence. The incompatibility of postal customs clearance processes with regulatory requirements may impede our ability to grow e-commerce. A Quality and Security of Mail system has been in place since 2011 to identify issues and root causes and to resolve service problems. The PT team has been reintegrated into Operations to improve management of the end-to-end network and facilitate assessment and correction of issues. Our exchange offices are being modernized to facilitate the processing of mail by Canada Border Services.

7) Environmental concerns of customers and consumers

The possibility that Canada Post could be perceived as not environmentally responsible could have negative consequences on its brand reputation and customer loyalty, and could accelerate volume erosion. We continue to follow leading environmental and ethical business practices and proactively disclose our environmental performance through our Corporate Social Responsibility Report. All new building projects are registered for LEED™ (Leadership in Energy and Environmental Design) certification.

8) Legal risks

Risks associated with legal challenges and regulatory changes can have consequences for the brand as well as the future capability to invest in improvements.

8. PUBLIC POLICY PROGRAMS

8.1 Introduction

In addition to its universal service obligation and core postal services, Canada Post delivers certain public policy programs on behalf of the Government of Canada. We receive an annual appropriation of $22.2 million from the Government for the delivery of parliamentary mail and materials for the blind. This amount has been in place for close to a decade, despite changes in volume and costs. Canada Post estimates the difference between the compensation it received for these programs and the amount it would have earned at normal commercial levels (the "foregone revenue") to be $6 million for 2012.

8.2 Parliamentary (Government) Mail and Materials for the Blind

The *Canada Post Corporation Act* allows for mailing of letters free of charge between citizens and the Governor General, members of Parliament, the Speakers of the Senate and House of Commons, the Parliamentary Librarian, and the Ethics Commissioner. Members of the House of Commons (MPs) can also send up to four flyer mailings free of charge to their constituents in any calendar year, and receive a deeply discounted postage rate, unchanged since 1995, for mailings above that number. In 2012, about 4.2 million letters were mailed as Government Mail (excluding mail from constituents to parliamentarians) and MPs mailed more than 117 million Unaddressed Admail™ items. Volumes so far in 2013 are similar to 2012.

The Act also provides for the mailing of materials for the blind, such as talking books and DVDs, free of postage. Approximately two million shipments benefited from this program in 2012.

8.3 Library Materials

For many years, Canada Post offered a Library Book Rate, a service that provided for the movement of printed library books between libraries and between libraries and library users at significantly reduced postage rates. Further to amendments made to the *Canada Post Corporation Act* in June 2013, Canada Post has renamed the service Library Materials, as magazines, records, CDs, DVDs and other audiovisual materials, in addition to printed books, are now eligible to be mailed at reduced rates.

In 2012, approximately 747,000 shipments of books benefited from the Library Book Rate, which generated $857,000 for Canada Post. The foregone revenue was estimated at almost $9 million. Canada Post receives no appropriation or compensation of any kind from the Government to offset the discounted postage.

Since 2012, the company has implemented a small annual increase to the library rates, by a weighted average of five per cent. These increases, which do not cover Canada Post's operational costs, will continue over the life of this Corporate Plan.

9. FINANCIAL STATEMENTS

Canada Post Corporation
Pro Forma Consolidated Statement of Financial Position

As at December 31	2012	2013	Corporate Plan				
			2014	2015	2016	2017	2018
(in millions of Canadian dollars)	Actual	Forecast					
Assets							
Current assets							
Cash and cash equivalents	298	760	495	323	112	204	202
Marketable securities	570	0	0	0	0	0	0
Trade and other receivables	702	727	761	803	837	871	908
Income tax receivable	8	3	4	0	0	0	0
Other assets	126	89	84	95	96	92	87
Total current assets	1,704	1,580	1,344	1,221	1,045	1,167	1,197
Non-current assets							
Property, plant and equipment	2,655	2,733	2,804	3,027	3,246	3,502	3,713
Intangible assets	143	143	145	149	151	153	154
Segregated securities	560	479	468	454	437	416	392
Pension benefit assets	83	81	86	91	96	106	152
Deferred tax assets	1,808	1,812	1,887	1,954	2,028	2,034	2,006
Goodwill	130	130	130	130	130	130	130
Other assets	11	10	9	9	9	9	9
Total non-current assets	5,390	5,389	5,529	5,814	6,098	6,350	6,556
Total assets	**7,094**	**6,969**	**6,873**	**7,035**	**7,143**	**7,517**	**7,753**
Liabilities and equity							
Current liabilities							
Trade and other payables	540	488	481	491	491	493	499
Provisions	85	78	76	76	77	78	79
Salaries and benefits payable and related provisions	699	572	356	356	361	366	371
Income tax payable	1	3	7	9	11	14	17
Deferred revenue	137	138	137	138	139	140	141
Loans and borrowings	20	22	20	23	63	22	23
Other long-term benefit liabilities	72	71	71	71	71	70	70
Total current liabilities	1,554	1,371	1,148	1,164	1,213	1,182	1,198
Non-current liabilities							
Loans and borrowings	1,123	1,109	1,117	1,118	1,060	1,458	1,759
Pension, other post-employment and other long-term benefit liabilities	7,007	6,971	7,247	7,531	7,807	7,756	7,512
Deferred tax liabilities	2	2	2	2	2	2	2
Provisions	5	2	2	2	1	1	1
Other liabilities	17	15	14	14	14	15	15
Total non-current liabilities	8,154	8,098	8,381	8,667	8,885	9,232	9,289
Total liabilities	9,708	9,469	9,529	9,831	10,098	10,415	10,488
Equity							
Contributed Capital	1,155	1,155	1,155	1,155	1,155	1,155	1,155
Accumulated other comprehensive income	52	(21)	(21)	(21)	(21)	(21)	(21)
Accumulated deficit	(3,840)	(3,654)	(3,813)	(3,956)	(4,119)	(4,066)	(3,908)
Equity of Canada	(2,633)	(2,520)	(2,679)	(2,822)	(2,984)	(2,932)	(2,773)
Non-controlling interests	19	20	23	26	30	34	39
Total equity	(2,614)	(2,500)	(2,656)	(2,796)	(2,954)	(2,898)	(2,734)
Total liabilities and equity	**7,094**	**6,969**	**6,873**	**7,035**	**7,143**	**7,517**	**7,753**

Numbers may not add due to rounding.
The amounts for 2012 have been restated as a result of the adoption of new or revised accounting standards.

Canada Post Corporation
Pro Forma Consolidated Statement of Comprehensive Income

For the year ended December 31 (in millions of Canadian dollars)	2012 Actual	2013 Forecast	Corporate Plan 2014	2015	2016	2017	2018
Revenue from operations	7,529	7,602	7,802	7,993	8,135	8,195	8,382
Cost of operations	7,635	7,933	8,058	8,193	8,361	8,456	8,503
Profit (loss) from operations	(106)	(332)	(256)	(201)	(226)	(261)	(121)
Investing and financing income (expense)							
Investment and other income	50	179	42	13	10	7	5
Financing costs and other expense	(54)	(48)	(60)	(63)	(62)	(69)	(82)
Investing and financing income (expense), net	(4)	131	(18)	(50)	(52)	(62)	(77)
Profit (loss) before tax	(110)	(200)	(274)	(251)	(278)	(323)	(197)
Tax expense (income)	(26)	(67)	(68)	(59)	(65)	(76)	(43)
Net profit (loss)	**(84)**	**(133)**	**(206)**	**(192)**	**(213)**	**(247)**	**(154)**
Other comprehensive income (loss)							
Items that will not be reclassified to Net profit (loss)	(1,217)	403	68	71	75	407	426
Items that may be reclassified subsequently to Net profit (loss)	9	(73)	-	-	-	-	-
Tax relating to all components of other comprehensive income (loss)	302	(82)	(17)	(18)	(19)	(102)	(107)
Other comprehensive income (loss)	(906)	248	51	53	56	305	319
Comprehensive income (loss)	**(990)**	**115**	**(155)**	**(139)**	**(157)**	**58**	**165**
Net profit (loss) attributable to							
Government of Canada	(86)	(136)	(209)	(196)	(217)	(252)	(159)
Non-controlling interests	2	3	4	4	4	5	5
	(84)	(133)	(206)	(192)	(213)	(247)	(154)
Comprehensive income (loss) attributable to							
Government of Canada	(986)	113	(159)	(143)	(162)	52	159
Non-controlling interests	(4)	2	4	4	5	5	6
	(990)	115	(155)	(139)	(157)	58	165

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Canada Post Corporation
Pro Forma Consolidated Statement of Cash Flows

For the year ended December 31 (in millions of Canadian dollars)	2012 Actual	2013 Forecast	Corporate Plan 2014	2015	2016	2017	2018
Cash flows from operating activities							
Net profit (loss)	(84)	(133)	(206)	(192)	(213)	(247)	(154)
Adjustments to reconcile Net profit (loss) to cash provided by (used in) operating activities:							
Depreciation and amortization	314	326	332	350	370	391	401
Pension, other post-employment and other long-term benefit expense	692	917	905	915	922	927	911
Pension, other post-employment and other long-term benefit payments	(615)	(550)	(566)	(564)	(577)	(581)	(777)
Gain on sale of capital assets	(35)	(170)	(34)	(7)	(5)	(5)	(2)
Tax expense (income)	(27)	(67)	(68)	(59)	(65)	(76)	(43)
Net interest expense	34	33	42	45	43	51	62
Change in non-cash operating working capital:							
(Increase) decrease in trade and other receivables	63	(26)	(34)	(42)	(34)	(35)	(37)
Increase (decrease) in trade and other payables	(32)	(52)	(7)	9	1	2	5
Increase (decrease) in salaries and benefits payable and related provisions	(39)	(127)	(216)	0	5	5	5
Increase (decrease) in provisions	9	(8)	(2)	1	1	0	2
Net (increase) decrease in other non-cash operating working capital	26	6	(2)	0	0	(0)	(0)
Other income not affecting cash, net	(22)	(23)	(20)	(20)	(19)	(19)	(18)
Cash provided by (used in) operations before interest and taxes	285	125	124	437	429	414	355
Interest received	36	29	29	26	24	21	21
Interest paid	(51)	(51)	(51)	(51)	(48)	(53)	(65)
Tax received (paid)	40	(13)	(20)	(21)	(27)	(29)	(32)
Cash provided by (used in) operating activities	310	90	82	391	379	353	279
Cash flows from investing activities							
Business acquisition, net of cash acquired	(21)	-	-	-	-	-	-
Net cash inflow (outflow) of securities	270	578	11	14	17	21	24
Acquisition of capital assets	(575)	(400)	(376)	(563)	(583)	(633)	(587)
Proceeds from sale of capital assets	63	215	42	10	18	18	8
Cash provided by (used in) investing activities	(263)	394	(323)	(539)	(548)	(594)	(555)
Cash flows from financing activities							
Payments on finance lease obligations	(17)	(21)	(24)	(23)	(25)	(25)	(25)
Net cash inflow (outflow) of loans and borrowings	(0)	-	-	-	(15)	360	300
Dividend paid	(1)	(1)	(1)	(1)	(1)	(1)	(1)
Other financing activities, net	(2)	(0)	(0)	(0)	(0)	(0)	(0)
Cash provided by (used in) financing activities	(20)	(22)	(25)	(24)	(41)	333	274
Net increase (decrease) in cash and cash equivalents	**27**	**462**	**(266)**	**(172)**	**(210)**	**92**	**(2)**
Cash and cash equivalents, beginning of year	**271**	**298**	**760**	**495**	**323**	**112**	**204**
Cash and cash equivalents, end of year	**298**	**760**	**495**	**323**	**112**	**204**	**202**

Numbers may not add due to rounding.
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