



# Management's Discussion and Analysis

## First Quarter 2004

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*This document has been prepared for the purpose of providing management's discussion and analysis (MD&A) of our financial condition and results of operations for the three months ended March 31, 2004, compared to the corresponding period in 2003. The MD&A should be read in conjunction with our unaudited interim consolidated financial statements and accompanying notes for the three months ended March 31, 2004, and with our MD&A contained in our 2003 annual report for the year ended December 31, 2003. This MD&A is based on financial statements prepared in accordance with Canadian generally accepted accounting principles (Canadian GAAP). All amounts in this MD&A are in millions of Canadian dollars, except where otherwise noted.*

*Quarterly reports, annual reports and supplementary information can be found under "financial reports" on our corporate website at [www.aliant.ca](http://www.aliant.ca). Additional information, including our annual information form and other continuous disclosure documents, have been filed electronically through the System for Electronic Document Analysis and Retrieval (SEDAR) and are available online at [www.sedar.com](http://www.sedar.com).*

*Throughout this MD&A, "we", "us", "our" and "Aliant" refer to Aliant Inc. or our Telecommunications and Information Technology segments.*

*This document contains certain statements and information about potential future circumstances and developments. Such forward-looking statements and information are qualified by any of the inherent risks and uncertainties surrounding future expectations generally and may differ materially from our actual future experience. Reference is made to the "Risk and risk management" and "Forward-looking*

*statements” sections for further discussion about the inherent risks and uncertainties surrounding future expectations. We disclaim any intention or obligation to update or revise any forward-looking statements or information, whether as a result of new information, future events or otherwise. Forward-looking statements in this MD&A describe our expectations on April 28, 2004, unless otherwise noted.*

*This MD&A is dated April 29, 2004, which is the date of filing in conjunction with our press release announcing our results for the first quarter of 2004. Disclosure contained in this document is current to that date, unless otherwise stated.*

#### Reclassification of prior year results

*Where indicated, prior year results have been reclassified to conform to the presentation adopted in the current year. Generally, these reclassifications were made to realign revenues as a result of new information.*

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## **About our business**

### **Who we are**

Aliant is an information and telecommunications technology company based in Atlantic Canada. We operate through two segments, Telecommunications and Information Technology.

The Telecommunications segment provides a full range of voice and data communications services including local, long distance, cellular, Internet and other wireline and wireless services. Aliant Telecom Inc. (“Aliant Telecommunications”) carries out the primary business of this segment, with complementary strengths in knowledge service applications offered by our wholly owned subsidiary, Innovatia Inc. (“Innovatia”), and in telephone directory advertising through an 87.1 per cent interest in Aliant ActiMedia (a joint venture).

The business of the Information Technology segment is carried out through Xwave Solutions Inc. (“xwave”). xwave delivers systems integration and software engineering, infrastructure services and product fulfillment to clients in several industry and geographic markets.

### **Advancing our strategy in 2004**

During the first quarter of 2004, we made progress on our strategy to grow Aliant profitably through our focus on revenue growth, customer service, operational excellence and fostering employee learning and growth. Some of our significant accomplishments in each of the four underlying areas of our strategy are highlighted below.

#### *Maximizing shareholder value*

At Aliant, we strive to provide our shareholders with a stable and rewarding investment. By increasing our earnings per share and generating strong cash flow in the first quarter of 2004, we were able to return cash to our investors through the following activities:

- the payment of a quarterly dividend of \$0.275 per common share to shareholders of record on March 15, 2004; and
- the purchase and cancellation of 616,116 shares under our current Normal Course Issuer Bid (NCIB) during the three months ended March 31, 2004.

Refer to the “Financial and capital management” section for a complete discussion of dividends and progress under our NCIB.

We have been able to return cash to our shareholders by generating profitable growth through investment and innovation. We have demonstrated this growth in our wireless and Internet business, generating customer growth over the first quarter of 2003 of 10.2 per cent and 7.6 per cent, respectively. This in turn has contributed to year-over-year operating revenue growth of 18.3 per cent in wireless revenues and 14.2 per cent in Internet revenues. This growth is in part the result of:

- Continued high-speed Internet expansion - We launched 22 new sites in the first quarter of 2004. Our high-speed Internet services now pass 66 per cent of the homes in Atlantic Canada, up from 61 per cent at March 31, 2003. Throughout 2004, we will continue to aggressively roll-out new sites, and partner with various government organizations and community groups to provide high-speed access to rural areas of Atlantic Canada with initiatives such as the Broadband Rural and Northern Development (BRAND) program.
- Continued expansion of the digital wireless network - During the first quarter of 2004, we completed 21 new digital sites. As a result, approximately 84 per cent of Atlantic Canada’s population had access to our digital wireless network as at March 31, 2004, up from 70 per cent at March 31, 2003. Throughout 2004, we plan to invest a total of \$26.0 million to further expand our digital wireless network. This will bring digital wireless to approximately 90 per cent of Atlantic Canadians.
- Improved coverage and data speed of one times radio transmission technology (1xRTT) - We completed our wireless 1xRTT data network expansion to mirror our digital coverage. In addition, we doubled the speed on our 1xRTT network giving our customers speeds of up to 153 kilobits per second. As we expand our digital wireless voice network, we will continue to overlay our 1xRTT data network to ensure the most expansive coverage for our customers.

In addition, we have invested in new products and services to position us for continued growth in 2004 and beyond.

- Launched ultra high-speed Internet service - Designed with the advanced Internet user in mind, ultra high-speed provides customers with download speeds up to 3.0 megabits per second, the fastest dedicated connection speed in Atlantic Canada. In addition, ultra high-speed includes free access to Music on my PC™ and the choice of one of our other enhanced services. Ultra high-speed is available to 85 per cent of our current high-speed service area and will grow as high-speed coverage grows.
- Launched Wireless Fidelity (Wi-Fi) service - In February 2004, we began a six-month service trial providing Wi-Fi service in five key high-traffic areas throughout Atlantic Canada, including three international airports. This service provides business customers and travelers convenient access to the Internet, e-mail and corporate networks without the need for a physical connection. During the trials, free unlimited access is available to all Internet customers with a wireless Internet-enabled laptop, within a 50 to 100 metre range of the designated hot spot at each of the trial locations.

- Launched an Automatic Vehicle Location (AVL) service - Our AVL solution provides customers with the ability to track the location and monitor the activity of each vehicle in their fleet. This solution can provide productivity savings, more efficient utilization of the vehicle fleet, the ability to develop reports on vehicle utilization and maintenance, as well as enhanced employee safety.
- Launched Voice over Internet Protocol (VoIP) demonstration centres - We have continued our investment in the next generation infrastructure by opening VoIP demonstration centres in Saint John and Halifax, as well as a mobile demo that will be available across the Atlantic provinces. These centres will provide customers and employees with the opportunity to learn about this emerging technology.

We continue to focus on improving our Information Technology segment's performance by leveraging their core strengths in combination with the strengths of our Telecommunications segment. During the first quarter of 2004, the success of this combined effort resulted in the award of new business, such as a contract with Newfoundland and Labrador Hydro.

Our financial performance in the first quarter of 2004 indicates that we are well positioned to deliver on our 2004 outlook as evidenced by the following comparison:

<b>Full Year 2004 Outlook</b>		<b>First Quarter 2004 Actual Performance</b>
Operating revenues	Low single digit growth	0.7 per cent growth
Earnings per share	Low double digit growth	16.0 per cent growth
Cash from operations	Generate over \$550.0 million in the year	\$146.8 million
Capital investments	Similar to 2003 capital investment of \$335.8 million for the year	\$84.8 million

The operating revenue growth was driven by solid growth in the wireless and Internet service areas, partially offset by competition and current year impacts from previous year regulatory rulings on traditional local and long distance revenue sources. This growth combined with cost containment strategies, productivity initiatives and increased interest income, generated earnings per share growth of 16.0 per cent. In the first quarter, we also generated approximately 27 per cent of our anticipated annual cash from operations through solid earnings growth and effective management of working capital. We have expended approximately 25 per cent of our projected annual capital investments during the first quarter, reflecting a capital plan focused on generating additional revenue sources.

#### *Everything begins with the customer*

Our customers want their experience with us to be simple and enjoyable and we continuously strive to deliver on these expectations. In the first quarter of 2004, we rolled out our customer service transformation initiative, embarking upon the "road to simplicity". This is a multi-year effort to ensure our customers receive the highest possible quality of service in a positive and consistent manner each and every time they interact with us.

### *Simplifying internal processes*

Delivering simplicity to our customers requires us to look internally to continually streamline our processes and systems. This allows us not only to better serve our customers but also to reduce our costs. In the first quarter of 2004, we achieved the following:

- Continued developing an industry leading cost structure - This includes loyalty and retention activities to reduce churn in addition to operational productivity initiatives to reduce servicing costs and improve efficiency. Productivity initiatives include continuing the consolidation of server platforms across the four Atlantic provinces that began in 2003, renegotiating vendor contracts, initiating a customer service transformation program and implementing a world-class sales program.
- Achieved additional productivity savings through our relationship with Bell Canada - We leveraged our relationship with Bell Canada to access their buying power for items such as materials and customer hardware. We have established operational agreements to improve technology and network planning with capital and expense savings to be realized through many such initiatives. Other shared initiatives include market research, contact centre integration, various customer contact workforce management tools and intellectual property.

### *Fostering employee learning and growth*

We are continuing to build an environment that maximizes our employees' potential because we know our success depends on it. In particular, in the first quarter of 2004, we accomplished the following:

- Held a clerical training symposium - This three-day symposium brought together nearly 1,500 of our employees from across Atlantic Canada and was the first of its kind in North America. At this symposium, themed "It all starts with you", our contact centre employees had the opportunity to visit information and demonstration booths, attend presentations by our subject matter experts and interact with peers.
- Launched a new safety tool on-line - The accident prevention process system is the foundation of our safety program. This automated tool delivers a number of benefits, such as identifying the courses required by each employee based on a high/low risk role categorization, with management follow-up to ensure training is completed.

## **Operating results**

The following is a summarized discussion of our consolidated operating results for the three months ended March 31, 2004, in comparison to the same period in the prior year.

## Operating revenues

For the three months ended March 31

(millions of dollars)

	2004	2003	% change
Telecommunications			
Local	\$ 188.3	\$ 190.0	(0.9)
Long distance	92.1	100.8	(8.6)
Wireless	86.5	73.2	18.3
Internet	29.0	25.4	14.2
Other revenues	36.7	40.5	(9.4)
	\$ 432.6	\$ 429.9	0.6
Information Technology			
IT services	\$ 54.0	\$ 56.5	(4.4)
Fulfillment	44.5	46.5	(4.3)
	\$ 98.5	\$ 103.0	(4.4)
Other and eliminations	(26.7)	(32.0)	16.6
Consolidated operating revenues	\$ 504.4	\$ 500.9	0.7

Telecommunications generated year-over-year growth of 0.6 per cent in the first quarter of 2004. Strong wireless and Internet growth was partially offset by lower local and long distance revenue due to a continued intensely competitive environment and the impact of regulatory decisions and advancing technology.

Information Technology operating revenue for the first quarter of 2004 was slightly lower than the same period in 2003, with the majority of the decline being related to internal sales to the Telecommunications segment. External revenues continue to be impacted by the competitive marketplace and sustained pressure by clients to scale back their information technology (IT) investments.

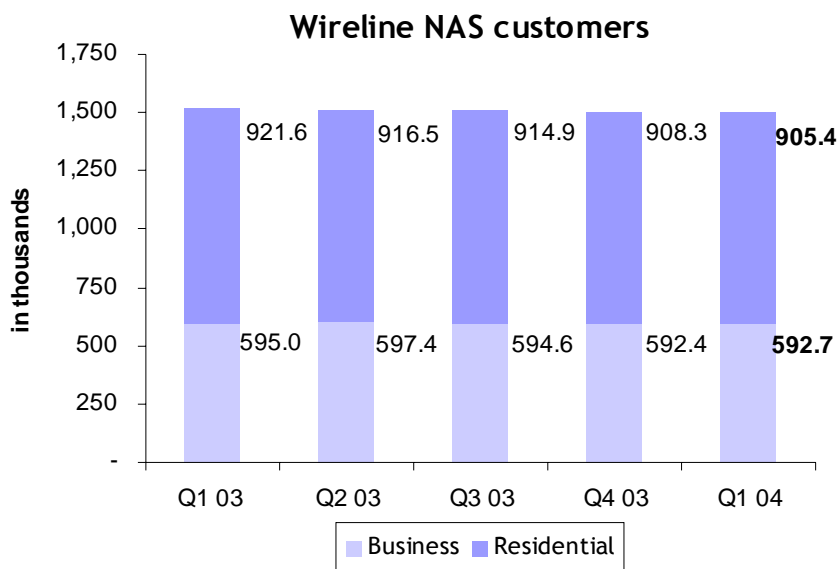
### Local revenue

Local revenue is earned through the provision of network access service (NAS), enhanced service features, data access, contribution payments, competitor payments, telephone set rentals, payphone usage and service charges.

During the first quarter of 2004, we experienced a minimal decline in local revenues in comparison to the same period in the prior year primarily because of increasing competition and current year impacts from previous year regulatory decisions. Although we experienced a reduction in NAS customers, the magnitude of our net residential NAS losses declined by 14.2 per cent compared to the same period in the prior year. We were also negatively impacted by lower telephone set rentals as customers choose to purchase rather than rent telephone sets, and the continued negative impact of the Canadian Radio-television and Telecommunications Commission (“CRTC” or the “Commission”) previous year price cap decision on contribution and competitor payments. In order to mitigate these effects on local revenue we focused on maximizing our customer retention programs, generating new revenue sources in data access and aggressively marketing enhanced service features.

Regulatory restrictions on win-back promotions and the ongoing restriction on bundling and packaging of local service with other non-regulated services in the face of an increasingly competitive marketplace continues to negatively impact our residential NAS customer base and our ability to meet customer needs. As a result, on April 7, 2004, we filed an application with the CRTC requesting them to stop regulating local residential phone service within areas across Nova Scotia and Prince Edward Island where significant competition currently exists. Refer to the discussion of regulatory developments in the “Risk and risk management” section for further details.

As evidenced by our strong growth in wireless and Internet, Atlantic Canadians are increasingly choosing services such as wireless, e-mail, instant messaging and short text messaging to complement or replace traditional telecommunications services. This trend, coupled with competitive and regulatory influences, has resulted in a decline in our residential NAS customer base. Business NAS decreased due to competitive losses, in particular the loss of one large customer in late 2003 as a result of a regulatory decision. These business NAS losses were offset, in part, by growth in small- to medium-sized businesses. In combination, residential and business NAS decreased by 1.2 per cent. NAS revenue, which represents over one half of all local revenues, declined 2.0 per cent as a result. We have and will continue to focus our efforts on customer retention in our local businesses.



At March 31, 2004, our residential NAS customer base is 1.8% lower than at March 31, 2003, contributing to a 1.2% year over year decline in total NAS customers.

Data access revenues have grown approximately 7 per cent due to newer data access services, such as data broadband, despite negative impacts of the CRTC price cap decision that required us to lower data access rates. We also experienced growth of approximately 4 per cent in enhanced service features revenue by up-selling customers to full features when selling Aliant Value Packages.

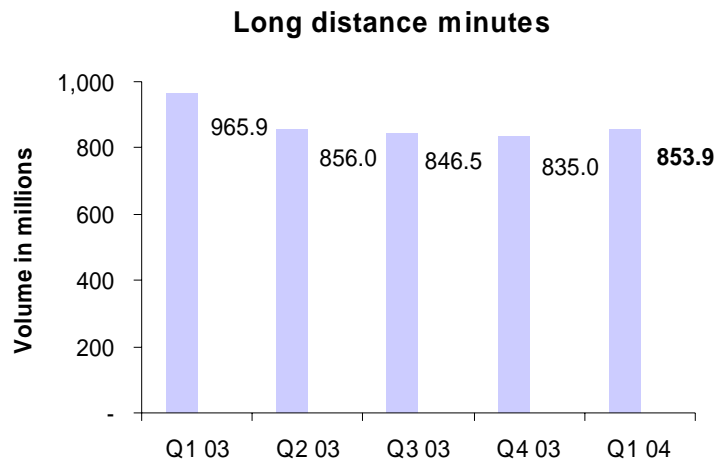
## Long distance revenue

Long distance revenue consists of toll, data network and long distance terminating services.

The increasingly competitive marketplace contributed to the 8.6 per cent decline in long distance revenues as a result of continued price changes and rationalization by customers. We also experienced declines in terminating revenue due to lower per minute rates, however, this decline was offset by savings we achieved in terminating expenses for our customers' calls to other regions.

Residential long distance minutes declined due to a lower customer base, increased substitution of long distance calling with wireless and Internet options and the restructuring of our customer plans during 2003. Components of this restructuring, such as capping of the minutes available under certain unlimited calling plans, have enabled us to optimize the usage of our network and improve profitability of this segment.

In the business long distance market, competitive pressure and a decline in contact centre activity has led to reduced business long distance minutes and has had a negative impact on business long distance revenues overall. We continue to aggressively respond to the strongly competitive marketplace through offers designed to continually meet the needs of our customers.

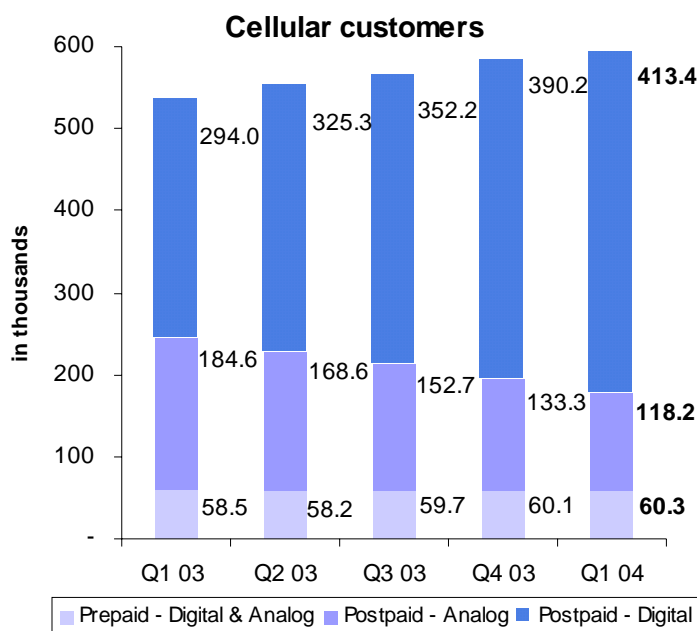


In the first quarter of 2004, our long distance minute volumes decreased by 11.6% over the first quarter of 2003, due in part to our decision to cap the minutes of usage with unlimited plans.

## Wireless revenue

Wireless revenue is earned through the provision of cellular, paging and mobile radio services.

Our wireless revenues for the first quarter of 2004 grew 18.3 per cent over the same period last year. We provide the most extensive and reliable cellular and data network available in Atlantic Canada. Our commitment to digital conversion has enabled us to achieve a 43.1 per cent increase in the number of digital customers. We have also achieved a 39.6 per cent increase in postpaid customer net additions, a 10.2 per cent increase in average minutes of use, an improved churn to 1.29 per cent and very strong growth in our data services portfolio. We experienced solid growth in postpaid customers of 11.1 per cent and average revenue per customer (ARPC) of 8.1 per cent.



Our cellular customers at March 31, 2004 grew 10.2% over March 31, 2003. Included in this result is 43.1% growth in our digital customers and 11.1% growth in our postpaid customers.

Customer growth remained strong at 10.2 per cent as a result of competitive pricing offers, the continued rollout of our dealer branded stores, the packaging of wireless services with other non-regulated services, extensive handset selection and continued expansion of our digital cellular service into new areas. We experienced a 6.1 per cent increase in net activations over the same period last year. As at March 31, 2004, approximately 84 per cent of Atlantic Canada's population had access to our digital wireless network, up from 70 per cent at the same time last year. We also completed the expansion of our 1xRTT network to 100 per cent of our digital wireless network. Our expanded 1xRTT network is now carrying over 42 per cent of all digital voice traffic.

## Wireless - statistics

<i>For the three months ended March 31</i>	<b>2004</b>	<b>2003</b>	<b>% change</b>
<b>Monthly - Average revenue per customer</b>			
Postpaid	\$ 50.84	\$ 47.02	8.1
Prepaid	\$ 9.64	\$ 7.97	21.0
Total	\$ 46.62	\$ 42.80	8.9
<b>Monthly - Average minutes of use per customer</b>	<b>237</b>	215	10.2
<b>Churn</b>	<b>1.29%</b>	1.41%	(8.5)

The 8.9 per cent growth in total ARPC results from an increase in the average minutes of use, select price increases, increase in the percentage of customers choosing digital service and postpaid plans and an increase in data usage. Digital customers generate higher monthly ARPC than analog, likewise postpaid customers generate higher monthly ARPC than prepaid. Our digital customers represent 72.4 per cent of our cellular customer base compared to 55.7 per cent for the same point in time in 2003. Our postpaid customer mix of 89.8 per cent continues to lead the industry. Our churn, or customer turnover rate, has improved 8.5 per cent over the same period last year to 1.29 per cent. This improvement is due to a higher base of customers on long-term contracts, driven by hardware upgrades and customer service incentive programs focused on customer retention.

### *Internet revenue*

Internet revenue consists of high-speed and dial-up service to residential and business markets, which include enhanced services such as Music on my PC™ and Personal Firewall.

Internet continues to perform extremely well, delivering strong growth of 14.2 per cent over the first quarter of 2003. We have generated this growth through attractive introductory offers, valued-added service offerings, dedicated high-speed service and expansion of our high-speed network coverage. Initiatives to aggressively manage churn and programs to improve ARPC have also contributed to continued strong customer and revenue growth.

## Internet - statistics

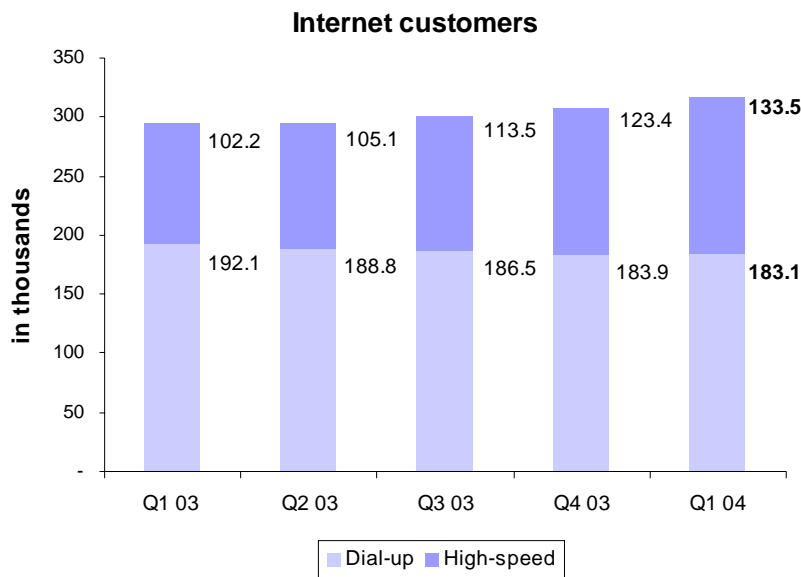
<i>For the three months ended March 31</i>	<b>2004</b>	<b>2003</b>	<b>% change</b>
<b>Monthly - Average revenues per customer</b>			
Consumer dial-up*	\$ 19.68	\$ 19.36	1.7
Consumer high-speed*	\$ 33.48	\$ 34.03	(1.6)
Business dial-up	\$ 45.49	\$ 43.77	3.9
Business high-speed	\$ 98.49	\$ 91.55	7.6
<b>Churn</b>	<b>2.14%</b>	<b>1.90%</b>	<b>12.6</b>

\* This statistic has been restated to include revenues from enhanced services. This restatement was necessary to conform to the new industry standard of including all revenue derived from consumer Internet service in the calculation of average revenue per customer.

All Internet product categories have seen improvement in ARPC year over year with the exception of consumer high-speed, which has remained relatively stable. The increases are attributable to the growing popularity of enhanced services and targeted price restructuring, mainly in the business market. Since early 2003, we have expanded our enhanced service offerings to include TV on my PC™, various Internet security services and other service offerings. During the first quarter of 2004, we passed the 10,000 subscriber mark for our Internet security services, Anti-Virus, Personal Firewall and Parental Control. We have been successful in attracting new customers through promotional programs. This has had a minimal impact on consumer high-speed ARPC in the short-term and will bring long-term benefits through an increased customer base.

A key focus for us is loyalty management. The continuation of customer retention programs including loyalty bulletins and emphasis on long-term customer contracts, as well as the integration of Internet offers with our other product lines, has served to minimize the impact of competition on Internet churn. We continuously strive to add value to our customers' Internet experience and in March 2004, we launched our ultra high-speed service to meet the needs of the advanced Internet user.

Competitive pricing and the continued expansion of our high-speed Internet network combined to grow our Internet customer base by 7.6 per cent and our high-speed customer base by 30.6 per cent over the first quarter of 2003. Our high-speed Internet service now passes 66 per cent of the homes in Atlantic Canada, up from 61 per cent at March 31, 2003, and continues to expand.



Our Internet customer base at March 31, 2004 grew 7.6% over March 31, 2003, including 30.6% growth in our number of high-speed customers.

### Other revenue

For the three months ended March 31

(millions of dollars)

	2004	2003	% change
Product	\$ 25.2	\$ 24.6	2.4
Directory	2.0	1.8	11.1
Innovatia	6.0	5.6	7.1
Miscellaneous	3.5	8.5	(58.8)
<b>Other revenues</b>	<b>\$ 36.7</b>	<b>\$ 40.5</b>	<b>(9.4)</b>

Product revenues reflect growth in customer premise equipment and terminal equipment sales. Directory (yellow pages) revenues have grown despite increased competitive pressure, demonstrating the strong value that our customers place in our directories throughout Atlantic Canada. Innovatia revenue grew 7.1 per cent over the same period last year driven by strong performance in the contact centre solutions business launched in 2003. Miscellaneous revenues have decreased as a result of lower pole attachment revenues due to sales of poles in Newfoundland and Labrador, lower late pay rates driven by interest rate declines and lower revenues from broadcast circuits due to the presence of large broadcast events in our region in 2003, which did not recur in 2004.

## IT services revenue

IT services revenue consists of systems integration, software engineering, infrastructure services and other IT consulting.

IT services revenue declined slightly during the first quarter of 2004 over the same period in 2003 due largely to reduced revenue from the Telecommunications segment. Services provided internally to the Telecommunications segment have declined over the past year due to role alignment and productivity improvement initiatives. Internally generated IT services revenues have decreased by \$3.4 million or 14.2 per cent compared to the first quarter of last year. During the quarter, services to external clients increased by \$1.0 million or 3.1 per cent over the same period last year. This increase reflects, in part, increased consumer demand for IT services. During the first quarter of 2004, xwave renewed contracts with existing clients and secured new business with customers, including Newfoundland and Labrador Hydro and Airbus, that will help sustain and grow revenues into the future.

## Fulfillment revenue

Fulfillment revenue includes the sale of computer hardware, accessories and packaged software.

Fulfillment revenue declined slightly due primarily to a slowdown in both provincial and federal government spending in Atlantic Canada. Several government departments and agencies have implemented spending freezes in response to budgetary constraints. This slowdown has been partially offset by stronger sales in Ontario in both the private and public sectors.

Internal fulfillment revenues are \$0.5 million lower than the first quarter of 2003 due to reduced procurement activity by our Telecommunications segment.

## Cost of operating revenues

*For the three months ended March 31  
(millions of dollars)*

	2004	2003	% change
Cost of operating revenues	\$ 74.5	\$ 83.4	(10.7)

We decreased our cost of operating revenues by improving margins on product sales in both the Telecommunications and Information Technology segments despite a very competitive marketplace. The combination of improved margins and lower overall product and fulfillment sales has contributed to lower cost of operating revenues. We have also benefited from lower terminating costs in our long distance portfolio and lower payments to the national contribution pool.

## Operating expenses

For the three months ended March 31  
(millions of dollars)

	2004	2003	% change
Operating expenses	\$ 244.0	\$ 236.0	3.4

Operating expenses have increased in the first quarter over the same period in 2003 due primarily to a \$6.4 million increase in pension and other post employment benefits expense.

### *Pension and other post employment benefits expense*

For the three months ended March 31  
(millions of dollars)

	2004	2003	% change
Defined benefit	\$ 12.9	\$ 8.2	57.3
Defined contribution	3.3	2.0	65.0
Other post employment benefits	3.9	3.5	11.4
	\$ 20.1	\$ 13.7	46.7

The increase in pension and other post employment benefits expense relates primarily to the defined benefit (DB) pension expense. DB pension expense and other post employment benefits (OPEBs) expense are made up of a number of components. Each of these components is dependent on the actuarial valuations of the plans (see “Description of pension and other post employment benefit obligations and related cash funding requirements”) and management’s assumptions about future events. These assumptions and the components of DB pension and OPEBs expense are disclosed in notes 1 and 5 to our unaudited interim consolidated financial statements for the three months ended March 31, 2004.

For the first quarter of 2004, the DB pension expense increased primarily due to the increase in the amortization of net actuarial losses attributable to the higher balance of accumulated actuarial losses. The balance of accumulated actuarial losses has increased, in part, because plan asset returns have been lower than expected and, in part, due to the plan liabilities being higher than anticipated. The liability growth has largely come from lower interest rates being used to discount the future expected payments to pensioners. In particular, the amortization of accumulated actuarial losses has grown as the size of the losses has grown in recent years. In 2003, we amortized \$8.9 million of the losses through pension expense. In 2004, we estimate that our pension expense will include loss amortization in the range of \$18.0 to \$20.0 million, of which \$4.7 million was recorded in the first quarter.

The expense related to defined contribution (DC) pension plans is simply equal to the amount of the employer’s required contribution to the employees’ accounts. The increase is due to higher short-term salary incentive payments in the first quarter, which also attract pension contributions. We do not expect this large an increase in the DC pension expense through the remaining quarters of 2004.

Our OPEBs expense has increased due to the interest on the unfunded obligation as the OPEBs liability has grown.

### *Other operating expenses*

The remaining \$1.6 million increase in operating expenses reflects increases of \$6.1 million in the Telecommunications segment, a reduction of intercompany activity which increased operating expenses by \$6.4 million, offset by a decrease of \$10.9 million in the Information Technology segment.

The growth of Telecommunications' wireless and Internet services and an ever increasing customer focus throughout the organization have resulted in an increase in some operating expenses. These increases have been partially offset by various ongoing productivity and cost reduction initiatives, some of which involved our Information Technology segment and others which involved our majority shareholder, Bell Canada. These initiatives are outlined in the "Simplifying internal processes" section.

Information Technology's operating expenses declined significantly as a result of savings from workforce reductions initiated in the prior year as well as a sustained focus on cost management. Operating expenses for the first quarter of 2003 also included a \$5.2 million charge for severance costs associated with downsizing activities. This downsizing combined with restructuring activities in the second half of the year resulted in a new operating model with a reduced cost structure for this segment.

### **Depreciation and amortization**

*For the three months ended March 31  
(millions of dollars)*

	<b>2004</b>	<b>2003</b>	<b>% change</b>
Depreciation and amortization	\$ 101.0	\$ 98.2	2.8

Telecommunications' depreciation and amortization increased due to the higher proportion of capital investment in recent years being in broadband and wireless assets, which have depreciable lives as short as three years.

Information Technology's depreciation and amortization expense has decreased as some of its capital investment reaches maturity, becomes fully depreciated, and is retired.

### **Restructuring charge**

*For the three months ended March 31  
(millions of dollars)*

	<b>2004</b>	<b>2003</b>	<b>% change</b>
Restructuring charge	\$ 3.1	\$ -	-

During the first quarter of 2004, Telecommunications executed a restructuring plan, which resulted in a charge of \$1.9 million. This plan consisted of a comprehensive restructuring of Innovatia's eLearning operations and other costs associated with workforce reduction. These costs are largely severance and related benefits. The objective of this plan is to improve productivity and profitability.

Information Technology incurred \$1.2 million in restructuring charges during the first quarter of 2004. This is a continuation of xwave's strategy realignment and business model simplification and consists of severance and related benefits.

### Other income (expenses)

For the three months ended March 31  
(millions of dollars)

	2004	2003	% change
Interest income	7.1	3.1	-
Provincial large corporation tax	(1.9)	(1.2)	58.3
Accounts receivable securitization	(1.0)	(1.1)	(9.1)
Miscellaneous charges	(1.2)	(1.1)	9.1
	3.0	(0.3)	-

Other income has increased by \$3.3 million due to interest earned on previous years' tax reassessments partially offset by higher provincial large corporation tax.

### Interest charges

For the three months ended March 31  
(millions of dollars)

	2004	2003	% change
Interest charges	\$ 19.2	\$ 20.9	(8.1)

Interest charges have decreased in 2004 compared to the prior year due to a decrease in the amount of outstanding debt held by Telecommunications. Telecommunications repaid \$72.5 million in debentures and bonds in June and July of 2003.

### Income taxes

#### Calculation of effective income tax rate

For the three months ended March 31  
(millions of dollars)

	2004	2003	% change
Net income from continuing operations	\$ 40.7	\$ 37.5	8.5
Addback:			
Income taxes	24.5	24.7	(0.8)
Non-controlling interest	0.5	(0.1)	-
Net income from continuing operations before income taxes and non-controlling interest	\$ 65.7	\$ 62.1	5.8
Effective income tax rate	37.36%	39.75%	(6.0)

The income tax provision decreased despite an increase in net income from continuing operations due to the decline in the effective income tax rate. The decline in the rate is mainly attributable to lower statutory rates in 2004, compared to 2003, as detailed in the following table:

## Factors impacting effective income tax rate

<i>For the three months ended March 31</i>	<b>2004</b>	<b>2003</b>
Statutory income tax rate (including surtax)	<b>35.85 %</b>	40.31 %
Federal large corporation tax	<b>1.67</b>	0.31
Tax rate change - future asset	<b>(0.44)</b>	(0.48)
Non-taxable gain	<b>(0.02)</b>	(0.08)
Non-deductible goodwill	<b>0.07</b>	-
Benefit of non-capital losses not recognized	<b>0.02</b>	-
Other permanent differences	<b>0.21</b>	(0.31)
<b>Effective income tax rate</b>	<b>37.36 %</b>	<b>39.75 %</b>

## Non-controlling interest

<i>For the three months ended March 31</i> <i>(millions of dollars)</i>	<b>2004</b>	<b>2003</b>	<b>% change</b>
Non-controlling interest	<b>\$ 0.5</b>	\$ (0.1)	-

Non-controlling interest mainly represents the proportionate results of Atlantic Mobility Products.

## Net income and earnings per share

<i>For the three months ended March 31</i> <i>(millions of dollars except per share amounts)</i>	<b>2004</b>	<b>2003</b>	<b>% change</b>
Net income:			
Continuing operations	<b>\$ 40.7</b>	\$ 37.5	8.5
Discontinued operations	-	1.4	-
<b>Total net income</b>	<b>\$ 40.7</b>	\$ 38.9	4.6
Earnings per common share:			
Continuing operations	<b>\$ 0.29</b>	\$ 0.25	16.0
Discontinued operations	-	0.01	-
<b>Total earnings per common share</b>	<b>\$ 0.29</b>	\$ 0.26	11.5

Our exit from non-core businesses in 2003 resulted in the reclassification of prior period results of these businesses as discontinued operations. In the first quarter of 2003, the results from discontinued operations reflect the operating activities of the businesses prior to their disposition.

The increase in net income from continuing operations for the first quarter of 2004 over 2003, is due to higher operating income resulting from our strength in wireless and Internet, higher interest income and lower interest charges. These factors outweighed any negative impact of the restructuring charge and year-over-year increase in pension and OPEBs expense as detailed in the consolidated quarterly results analysis table in the "Supplementary financial information" section.

## Financial and capital management

### Summary of consolidated cash flows

Cash and cash equivalents at March 31, 2004, were \$323.6 million. During the first quarter, we have generated \$146.8 million in cash from operations and we anticipate that we will continue to generate strong cash flow from operations throughout the year. We will deploy cash that is not required in our operations at this time in a manner consistent with our objective of maximizing shareholder value. This involves the buyback of common shares under the existing NCIB in order to optimize our cost of capital while keeping our debt ratio at an appropriately conservative level. We plan to buy back the remaining 1,116,014 shares allowed under our current NCIB. We also plan to invest in new opportunities to support our future growth through strategic investment in operations complementary to our core business.

Our cash requirements for the remainder of 2004 will consist of purchases of shares under our current NCIB, dividend payments, repayment of debt, funding of required pension plan contributions, required capital investments and scheduled contractual obligations. The only significant debt repayment that is scheduled for 2004 is a \$100.0 million bond maturing in October and we expect to repay this out of cash from operations. DB pension plan funding required in 2004 is anticipated to be in the range of \$50.0 to \$70.0 million, of which \$16.0 million has been paid to March 31, 2004.

### Operating activities

#### Summary of cash flows from operating activities

*For the three months ended March 31*

*(millions of dollars)*

	2004	2003	% change
Net income from continuing operations	\$ 40.7	\$ 37.5	8.5
Non-cash items	116.7	86.4	35.1
	157.4	123.9	27.0
Change in non-cash working capital balances related to operations	(10.6)	98.4	-
Cash from continuing operations	\$ 146.8	\$ 222.3	(34.0)

Cash generated from continuing operating activities has decreased by \$75.5 million, which represents a \$21.4 million increase due to improved earnings and working capital management offset by a \$96.9 million decrease related to income and other taxes payable and future income taxes.

## Change in non-cash working capital balances related to operations

For the three months ended March 31

(millions of dollars)	2004	2003	% change
Accounts receivable	\$ 37.2	\$ 7.7	-
Income and other taxes payable	(26.0)	92.8	-
Prepayments	(3.9)	(6.1)	(36.1)
Inventory	(0.7)	(1.3)	(46.2)
Accounts payable and other liabilities	(17.2)	5.3	-
Change in non-cash working capital balances related to operations	\$ (10.6)	\$ 98.4	-

During the first quarter of 2004, non-cash working capital absorbed cash of \$10.6 million, compared to \$98.4 million in cash generated in the first quarter of 2003. Of this decrease, \$118.9 million relates to income and other taxes payable, as there was a lower amount of income and other tax related refunds in the current year due to the receipt of \$55.0 million for the settlement of prior years' claims for Scientific Research and Experimental Development investment tax credits in the first quarter of 2003, the increase in income taxes receivable as a result of higher pension funding in the first quarter of 2004 and the timing of tax installments.

## Financing activities

### Summary of cash flows from financing activities

For the three months ended March 31

(millions of dollars)	2004	2003	% change
Repayments of notes payable and bank advances	\$ (8.7)	\$ (41.7)	(79.1)
Repayments of long-term debt	(0.2)	(1.1)	(81.8)
Net repurchase of common shares	(18.7)	(19.0)	(1.6)
Preferred and common share dividends	(37.7)	(35.0)	7.7
Other financing activities	(5.5)	-	-
Cash from (used in) financing	\$ (70.8)	\$ (96.8)	(26.9)

Cash used in financing activities in the first quarter of 2004 has been related to common share repurchases made under our current NCIB and payment of dividends. The increased use of cash from other financing activities related primarily to the repurchase of accounts receivable under our accounts receivable securitization program.

### Liquidity and financing resources

As at March 31, 2004, we maintain lines of credit totalling \$557.0 million in aggregate with our bankers. These lines of credit are unchanged from December 31, 2003, and consist of \$350.0 million in a committed facility supporting our commercial paper program, \$150.0 million in uncommitted operating lines and \$57.0 million in bank operating lines of credit within our business segments. There were no balances outstanding under our commercial paper program or uncommitted operating lines as at March 31, 2004.

Bank operating lines of credit within our business segments include:

- \$42.0 million in Telecommunications - which had \$4.3 million outstanding as at March 31, 2004, compared to \$4.5 million at December 31, 2003.
- \$15.0 million in Information Technology - there were no amounts drawn at March 31, 2004, on this line of credit compared to a balance of \$6.0 million at December 31, 2003. Letters of credit committed against this line of credit total \$6.1 million at March 31, 2004, compared to \$6.9 million at December 31, 2003.

### *Consolidated capital structure*

<i>(millions of dollars)</i>	<b>March 31, 2004</b>		<b>December 31, 2003</b>	
Common equity	\$ 1,435.9	54.5%	\$ 1,451.6	54.7%
Preferred equity	172.3	6.5%	172.3	6.5%
Non-controlling interest	4.0	0.2%	4.1	0.1%
Long-term debt, including current portion	989.9	37.5%	990.1	37.3%
Short-term debt, including bank indebtedness and interest payable	33.3	1.3%	36.1	1.4%
	<b>\$ 2,635.4</b>	<b>100.0%</b>	<b>\$ 2,654.2</b>	<b>100.0%</b>

The percentage of debt to total capital was 38.8 per cent at March 31, 2004, virtually unchanged from December 31, 2003.

### *Corporate equity instruments*

We issued common shares in the amount of \$2.2 million for the first quarter of 2004, by way of our common shareholder dividend reinvestment and stock purchase plan, and the exercise of options under our employee stock option plan. Shares were purchased on the open market to fulfill the requirements of our employees' stock savings plan.

Under the NCIB, which commenced on August 6, 2003, for a twelve-month period ending August 5, 2004, we purchase, from time to time, our common shares for cash through the facilities of the Toronto Stock Exchange. All common shares purchased pursuant to this NCIB will be cancelled. Further details on this NCIB are provided in note 11 to our unaudited interim consolidated financial statements for the three months ended March 31, 2004. As at March 31, 2004, we had purchased for cancellation 5,808,986 common shares under this NCIB at an aggregate price of \$183.5 million, of which 616,116 common shares were purchased during the first quarter of 2004 at an aggregate price of \$19.6 million.

Despite the lower number of shares outstanding, the total dividends that we paid to our common shareholders increased \$1.9 million for the quarter over 2003 levels to \$36.7 million. This increase reflects the increase in the quarterly dividend of \$0.025 cents per common share effective with the June 30, 2003, dividend, which raised the annual rate to \$1.10 per common share. Dividends paid that were subsequently reinvested in the dividend reinvestment plan were \$2.3 million for the first quarter of 2004 compared to \$2.2 million in the prior year.

We paid preferred shareholder dividends of \$2.4 million in the first quarter of 2004, consistent with the amount paid in the first quarter of 2003.

Our outstanding shares and stock options as of April 21, 2004 are as follows:

*Authorized*

Unlimited number of preference shares, issuable in series.

Unlimited number of common shares, without par value.

*Issued*

(millions of dollars)

	April 21, 2004	
	Number of shares	Value
Preference shares, series 2	7,000,000	\$ 172.3
Common shares	132,908,211	1,031.9
		\$ 1,204.2

	April 21, 2004	
	Number of options	Weighted average exercise price
Options outstanding	2,709,246	\$ 30.56
Options exercisable	1,895,514	\$ 30.68

Between April 1, 2004, and April 21, 2004, we purchased for cancellation 178,802 common shares under the NCIB at an aggregate price of \$5.4 million.

**Investing activities**

**Summary of cash flows from investing activities**

For the three months ended March 31

(millions of dollars)

	2004	2003	% change
Capital investments	\$ (84.8)	\$ (70.6)	20.1
Other investing activities	(32.9)	5.3	-
Cash from (used in) investing	\$ (117.7)	\$ (65.3)	80.2

Cash used in investing activities has increased significantly over the same period in 2003. Other investing activities include a special deficit-funding pension contribution of \$25.0 million in January 2004, which completed the \$55.0 million additional funding approved by the board of directors in December 2003. Regular funding of the DB pension plans also increased from \$2.7 million in the first quarter of 2003 to \$16.0 million in 2004 due to the funding requirements identified in the most recent actuarial valuations.

## Capital investments

For the three months ended March 31

(millions of dollars)

	2004	2003	% change
Telecommunications	\$ 84.4	\$ 69.8	20.9
Information Technology	0.4	0.5	(20.0)
Other	-	0.3	-
Total capital investments	\$ 84.8	\$ 70.6	20.1

### Telecommunications

Telecommunications' capital investment for the first quarter of 2004 is \$14.6 million higher than the investment for the same period in 2003. This increase arises from digital subscriber line (DSL) expansion and material investment in strategic initiatives such as the Broadband and Rural Network Development (BRAND) program, our customer services transformation program and our next generation network.

Our efforts to grow our high-speed Internet network have included investment in the BRAND initiative and additional DSL expansion. In partnership with federal, provincial and municipal governments, we participated in the BRAND initiative in the first quarter of 2004 by investing in the first stage of this two-year program. In addition, our DSL investment in the first quarter of 2004 was higher than our investment in the first quarter of 2003. Through our participation in the BRAND program and our own DSL expansion, we will expand high-speed Internet access to 70 per cent of Atlantic Canadian homes by the end of 2004.

Our first quarter investment in customer service transformation was the first step in our initiative, which is anticipated to result in productivity improvements and enhanced customer care, when completed.

Continued investment in our next generation network occurred this quarter to fund the continued development of VoIP and multi-protocol label switching technology. In addition, we have enhanced the reliability of existing networks to better combat virus attacks, when they occur.

Our core investment continues to include ongoing investment to support our existing networks and asset base and to grow and support our wireless coverage.

### Information Technology

Capital investment during the quarter was consistent with the prior year. The nature of the business requires limited capital investment and capital projects continue to closely support the current business model.

## Other financial arrangements

### Off-balance sheet arrangements

Off-balance sheet arrangements involve transferring accounts receivable to a securitization trust. Further details on this arrangement are provided in notes 1 and 2 to our unaudited interim consolidated financial statements for the three months ended March 31, 2004. During the first quarter of 2004, we restructured the accounts receivable securitization agreement to lower the facility from \$150.0 million to \$125.0 million. At December 31, 2003, we had

sold accounts receivable to the trust for net cash proceeds of \$130.0 million, decreasing to \$125.0 million in the first quarter of 2004. The security supporting the facility, which represents additional accounts receivable over and above the net cash proceeds received, was also restructured requiring the transfer of a further \$10.3 million of accounts receivable to the trust. The security supporting the agreement is included in deferred charges as a retained interest in the securitization trust.

We also have various operating leases and purchase commitments for equipment and other network infrastructure. The amounts of estimated future payments are disclosed in note 18 of our unaudited interim consolidated financial statements for the three months ended March 31, 2004, and have not materially changed from those disclosed in the MD&A for the year ended December 31, 2003.

#### *Derivative financial instruments*

Our derivative financial instruments consist of interest rate swap and interest rate swaption agreements. Further details of these agreements are provided in notes 1 and 17 to our unaudited interim consolidated financial statements for the three months ended March 31, 2004. There has been no change in the purpose or terms of these derivative financial instruments during the first quarter of 2004.

#### *Pension and other post employment benefits obligations and related cash funding requirements*

Most of our employees participate in one of our pension plans in order to assist in providing for their retirement. While most new employees participate in a DC pension plan, we still have many active employees in one of our four non-contributory DB pension plans. We also offer retiring employees certain other non-pension benefits such as health and dental care and disability insurance. The DB pension plans require periodic funding payments to be made to a trust fund while the OPEB plans require cash payments to be made directly to the plan carrier or to the retired employee.

The DC pension plan requires both the employee and the employer to contribute a fixed periodic amount to an account that is administered for the benefit of the employee. As the employer, our contributions are between 4 per cent and 6 per cent of a member-employee's pensionable earnings and the employees' contributions are between 0 per cent and 6 per cent. There are no issues or risks in measuring and reporting the costs of a DC pension plan as the periodic expense is simply equal to the amount the employer must contribute to the plan.

In contrast, the DB pension plans provide for a periodic payment to the retired employee that is based on the number of years of service and their best five-year average salary prior to retirement. Therefore, the value of the total pension that is paid in a DB pension plan is dependent upon several future unknown variables such as the employee's years of service, salary, life expectancy and inflation rates. An actuarial valuation is necessary in order to project the payments in a DB pension plan and to discount those payments at a current rate of interest to place a current value on the total pension obligation. The actuarial valuation also prescribes the contributions that we must make to the trust fund that is established to pay the DB pensions.

We perform actuarial valuations on our DB pension plans at least every three years. During 2003, we completed the actuarial valuations of our DB pension plans as of December 31, 2002. This valuation identified total minimum funding requirements of approximately \$63.7

million for 2003. The valuation also showed that our DB pension plans are in deficit positions, which means the obligations under the plans exceeds the assets that are currently held in trust to satisfy those obligations. In December 2003, we decided to make an additional \$55.0 million contribution in excess of the minimum funding requirements to partially address the deficits in the plans. A \$30.0 million cash contribution was made in December 2003 with the remaining \$25.0 million cash contribution made in January 2004. Total DB pension plan funding in 2003 was \$124.7 million.

The actuarial valuation completed in 2003 also identified that the plans had incurred some actuarial losses. These losses arise from time to time because actual experience in the plans (i.e. retirement rates, salary increases and mortality rates) between valuation dates has been worse than originally forecasted. Similarly, a plan can also experience actuarial gains when actual results are better than forecast. Gains and losses can also arise because assumptions about the future experience change from one valuation to another. The total actuarial loss identified in the actuarial valuation was \$83.4 million, which increased the total pension obligation and must be amortized into our pension expense over a number of years. Refer to operating expenses under the “Operating results” section for a discussion of the effect of loss amortization on pension expense.

We are currently updating our actuarial valuations for the year ended December 31, 2003, and expect these to be completed in the second quarter of 2004. These valuations could result in either lower or higher minimum required contributions to the DB pension plans than the \$63.7 million required for 2003. In the meantime, we are making periodic contributions at the 2003 rate, or \$16.0 million in the first quarter of 2004. Based on improved investment returns of the DB pension plan assets in 2003 and the extra contributions that were made in December 2003, minimum funding requirements for 2004 may decline in the updated valuations.

#### *Related party transactions*

In the normal course of business we engage in numerous transactions with our majority shareholder, Bell Canada, such as the purchase of telecommunications and other services, the provision of telecommunications services and the purchase of capital investments. We also repurchased shares for cancellation from Bell Canada through our NCIB. Refer to note 19 of our unaudited interim consolidated financial statements for the three months ended March 31, 2004, for greater detail on our related party transactions.

#### **Significant accounting policies**

Our unaudited interim consolidated financial statements have been prepared in accordance with Canadian GAAP. Greater detail on our significant accounting policies is provided in note 1 to our unaudited interim consolidated financial statements for the three months ended March 31, 2004. The accounting policies and methods, key assumptions and estimates, and choice of alternative acceptable accounting policies are consistent with those in effect in the most recent annual audited financial statements and as further disclosed in our MD&A for the year ended December 31, 2003, except as otherwise noted in the “Accounting policies adopted in 2004” section.

## Accounting policies adopted in 2004

### *Asset retirement obligation*

Effective January 1, 2004, we retroactively adopted the CICA handbook section 3110, Asset retirement obligations. This standard provides guidance on the recognition, measurement and disclosure of liabilities related to legal obligations associated with the retirement of tangible long-lived assets. These obligations are initially measured at fair value and recognized in the year in which they are incurred or when a reasonable estimate of fair value can be made. The fair value is the amount at which the liability could be settled in a current transaction. The initial fair value estimate is subject to subsequent adjustments to reflect the passage of time and any changes to the timing or the amount of the original estimate of undiscounted cash flows. The asset retirement cost is capitalized with the related asset and amortized into earnings over the asset's useful life. The adoption of this standard had no material impact on our financial position, results of operations or cash flows.

## Risk and risk management

While management is confident about our long-term prospects, we are exposed to a number of risks in the normal course of business that could have a negative effect on our financial condition or results of operations. A comprehensive discussion of these risks can be found in our MD&A for the year ended December 31, 2003, as presented on pages 37 to 40 of our 2003 annual report. Our discussion below is limited to significant changes in these risks up to and including April 26, 2004.

### Regulatory developments

A number of CRTC proceedings are currently underway that deal with issues of significance to incumbent local exchange carriers (ILECs), such as us. These proceedings include a review of bundled services, new floor price rules for ILECs' price-regulated services, costs of certain services provided to competitors and the deferral account mechanism.

The CRTC has continued its recent trend of increasing the level of regulation applicable to the local services we offer. On January 27, 2004, in its determination regarding a competitor's application, the Commission extended the previous three-month no-contact restriction to twelve months. The no-contact restriction prevents the ILECs from attempting to win-back residential customers who have switched to a competitor. The extension of the length of time the restriction applies will negatively affect our ability to provide the affected customers with choice of service provider.

On March 22, 2004, the CRTC determined that Aliant Value Packages (under which we provided regulated and non-regulated bundles of services to residential customers) were bundles that required CRTC approval. We have made the necessary changes to these service offerings to separate the regulated and non-regulated bundles so that CRTC approval is not required and we have satisfied regulatory compliance requirements.

The CRTC initiated a public proceeding on March 24, 2004, to review the amounts in each ILECs' deferral account and to determine how to dispose of any of those amounts. This proceeding will continue until late September 2004 and we do not expect that a decision will be rendered until some time in 2005. For additional information on the deferral account mechanism refer to note 21 of our unaudited interim consolidated financial statements for the three months ended March 31, 2004.

On April 7, 2004, the CRTC initiated the process that will examine how, and if, services provided over IP networks should be regulated. The outcome of this process may place additional regulatory restrictions on ILECs.

On April 7, 2004, we filed an application with the CRTC requesting the CRTC to stop regulating local residential phone service within areas of Nova Scotia and Prince Edward Island where there is significant local residential competition. This application was filed because we feel the time is right for the CRTC to enable customers to choose freely from comparable and compelling offers provided by companies that are truly focused on their needs. In addition, we asked the CRTC to provide us with immediate exemption from past CRTC decisions that negatively affect customers in competitive areas, including;

- the restriction that prevents us from providing special promotional offers to local customers in competitive areas;
- the restriction imposed on us related to when we can contact customers who have left for local service to invite them to return to us; and
- the ability to file special promotional offer requests with the CRTC in a confidential manner, so that we can launch these offers to customers without competitors having advance notice, as is appropriate in a competitive market.

A copy of this filing entitled “Forbearance application for residential wireline local services in specified exchanges” can be found at [www.aliant.ca](http://www.aliant.ca).

The outcome of future CRTC rulings could significantly impact our ability to compete and in particular our ability to generate gross profit. We are actively participating in these proceedings by providing evidence, information, and arguments to the CRTC that defend our positions and present alternatives that promote economically sound competition that will provide benefits and choice for customers.

### **Competitive developments**

The competitive intensity we face in Atlantic Canada remains consistent with what would be expected from the most competitive telecommunications market in Canada. Competitors of every type continue to pursue our business and will continue to do so in the future.

We continue to see increased local competition across all customer segments. Competitors continue to target businesses and consumers with aggressively priced offerings in an effort to encourage customer migration. The increased availability of VoIP solutions is creating increased interest in the market, however, customers continue to seek our expertise in aiding their understanding of the evolution of communications in Atlantic Canada.

Long distance competition has been impacted by the recent entry and increased awareness of a new dial-around provider, impacting us and other alternate long distance providers in this market. The relatively recent but expected entry of VoIP providers, while not expected to have an immediate impact, will contribute to the downward per minute revenue pressure already experienced. Meanwhile, we continue to aggressively promote our affordable long distance packages reinforcing our price competitiveness for most customers.

The Internet competitive environment intensified as telephone companies compete with cable companies vying for the broadband home. This increased intensity has affected not only promotional activities but also innovation and bundling of access and enhanced features.

The potential continues to exist for “free” bundling of enhanced services, reducing enhanced revenue opportunities, while potentially placing upward pressure on cost as usage increases.

Without adequate preparation, competition can place our strategies, revenue and net income at risk. For this reason we constantly monitor our competitive marketplace, modifying and creating plans to optimize our position in the Atlantic Canadian market.

### **Renegotiating labour agreements**

On February 24, 2004, we tabled an Offer for Settlement during conciliation discussions with the Council of Atlantic Telecommunications Unions (“CATU”). The CATU reviewed the offer and provided a partial response. On March 11, 2004, we tabled a revised Offer for Settlement, which incorporated minor changes to address some of the issues raised by the CATU. The CATU advised us on March 12, 2004, that our offer was unacceptable to them and conducted meetings with employees to recommend rejection of the offer and seek a strike mandate. The conciliation process ended on March 12, 2004, resulting in a 21-day cooling-off period, which ended on April 3, 2004.

On April 13, 2004, the union announced that 93.4 per cent of its membership that cast ballots voted to reject our latest Offer for Settlement as presented on March 11, 2004. On April 19, 2004, the CATU provided management with formal notice for a legal strike to take effect April 23, 2004. Despite continued negotiations throughout the week of April 19, 2004, and a new Company offer on April 23, 2004, a mutually acceptable agreement could not be reached. On April 23, 2004, a legal work stoppage began and continues to be in effect.

The ongoing process of negotiating collective agreements may result in higher labour costs or work disruptions that affect our operating results and financial condition.

### **Other legal and regulatory matters**

During the first quarter, a legal action was commenced against us by Exigen Ltd. We are in consultation with our legal counsel over the matter but are unable to determine the outcome at this time. Note 21 to our unaudited interim consolidated financial statements for the three months ended March 31, 2004, presents a discussion of significant contingencies outstanding at that time.

In addition, please refer to the discussion of regulatory developments under the “Risk and risk management” section for a description of certain regulatory initiatives and proceedings that could affect our Telecommunications segment.

### **Forward-looking statements**

Certain statements contained in this document constitute forward-looking statements. These forward-looking statements relate to our future financial condition and results of operations. These statements are based on current expectations and estimates about the markets in which we operate and management’s beliefs and assumptions regarding these markets. In some cases forward-looking statements may be identified by words such as “anticipate”, “believe”, “could”, “expect”, “plan”, “seek”, “may”, “intend”, “will”, “target”, “goal” and similar expressions. These statements are subject to important risks and uncertainties, which are difficult to predict and assumptions which may prove to be inaccurate. Some of the factors which could cause results or events to differ materially from current expectations include but are not limited to: general economic conditions; market or business conditions; increased competition; changing regulatory conditions or requirements; changing technology;

the outcome of collective bargaining; and success in implementing productivity initiatives; some of these factors are largely beyond our control. Should any factor impact us in an unexpected manner, or should assumptions underlying the forward-looking statements prove incorrect, the results or events predicted in management's discussion and analysis might differ materially from actual results or events. Consequently, all of the forward-looking statements made in this document and the documents referred to within are qualified by these cautionary statements, and there can be no assurance that the results or developments anticipated by us will be realized or, even if substantially realized, that they will have the expected consequences for us. Readers should not place undue reliance on any forward-looking statements. Further, we disclaim any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events, or any other occurrence.

## Supplementary financial information

### Consolidated quarterly financial information (unaudited)

For the eight quarters ended March 31, 2004

(millions of dollars except  
per share amounts)

	2002			2003				2004
	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1
Total operating revenues	\$ 522.6	\$ 507.4	\$ 511.4	\$ 500.9	\$ 517.3	\$ 513.9	\$ 527.0	\$ 504.4
Net income from continuing operations	\$ 61.3	\$ 44.8	\$ 2.2	\$ 37.5	\$ 61.3	\$ 50.7	\$ 45.4	\$ 40.7
Net income (loss) from discontinued operations	23.2	(0.7)	(6.7)	1.4	9.3	0.2	100.4	-
Net income (loss)	\$ 84.5	\$ 44.1	\$ (4.5)	\$ 38.9	\$ 70.6	\$ 50.9	\$ 145.8	\$ 40.7
Preferred share dividends	2.4	2.4	2.4	2.4	2.4	2.3	2.4	2.4
Net income (loss) applicable to common shares	\$ 82.1	\$ 41.7	\$ (6.9)	\$ 36.5	\$ 68.2	\$ 48.6	\$ 143.4	\$ 38.3
Basic earnings per common share:								
Continuing operations	\$ 0.42	\$ 0.30	\$ -	\$ 0.25	\$ 0.42	\$ 0.36	\$ 0.32	\$ 0.29
Discontinued operations	0.17	-	(0.05)	0.01	0.07	-	0.75	-
Total basic earnings per common share	\$ 0.59	\$ 0.30	\$ (0.05)	\$ 0.26	\$ 0.49	\$ 0.36	\$ 1.07	\$ 0.29
Diluted earnings per common share:								
Continuing operations	\$ 0.42	\$ 0.30	\$ -	\$ 0.25	\$ 0.42	\$ 0.36	\$ 0.32	\$ 0.29
Discontinued operations	0.17	-	(0.05)	0.01	0.07	-	0.74	-
Total diluted earnings per common share	\$ 0.59	\$ 0.30	\$ (0.05)	\$ 0.26	\$ 0.49	\$ 0.36	\$ 1.06	\$ 0.29

### Factors impacting comparability of quarterly results

#### Trends

Telecommunications operating revenues have generally increased quarter over quarter due to significant growth in wireless and Internet services, which has been partially offset by lower revenue from local and long distance services due to increased competition, CRTC regulations and technological advancements.

Information Technology operating revenues have decreased as clients scaled back their information technology expenditures in response to subdued market conditions and a slow down in government spending.

#### Seasonality of results

Telecommunications experiences seasonality as the recognition of the majority of our directory (yellow pages) revenues occurs in the second quarter coinciding with the timing of the issuance of the majority of our directories and the timing of product sales are typically large and sporadic in nature.

Information Technology experiences seasonality in its business with the greatest impact in the fulfillment business. In the fulfillment business, the first quarter of the year is

historically the strongest as a result of government fiscal year-end spending, although this effect has been somewhat lessened in recent years. Service revenues are contract based and fluctuate in accordance with the size and number of outstanding contracts; in particular, the third quarter is adversely impacted by client vacations.

### Other factors

Net income and earnings per share fluctuates from quarter to quarter due to items outside of the normal course of operations and the impact of pension and other post employment benefits expense.

### Consolidated quarterly results analysis (unaudited)

#### Impact of items outside of the normal course of operations

For the eight quarters ended March 31, 2004

(millions of dollars except  
per share amounts)

	2002			2003				2004
	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1
<b>Impact on net income</b>								
Increase (decrease) in net income from continuing operations								
Restructuring charge, net of tax	\$ -	\$ -	\$ -	\$ -	\$ -	\$ (9.3)	\$ 0.6	\$ (1.9)
Writedown of investments, net of tax	(4.5)	-	-	-	-	-	(12.3)	-
Writedown of goodwill related to xwave	-	-	(50.0)	-	-	-	-	-
Writedown of assets related to xwave, net of	-	(7.4)	-	-	-	-	-	-
	\$ (4.5)	\$ (7.4)	\$ (50.0)	\$ -	\$ -	\$ (9.3)	\$ (11.7)	\$ (1.9)
Increase (decrease) in net income from discontinued operations								
Gain (loss) on sale of subsidiary, net of tax	\$ -	\$ -	\$ -	\$ -	\$ 10.9	\$ (2.0)	\$ 95.7	\$ -
Stratos dilution gain and gain on foreign exchange, net of non controlling interest	45.2	-	-	-	-	-	-	-
Investment writedowns, net of tax	-	(19.7)	-	-	-	-	-	-
	\$ 45.2	\$ (19.7)	\$ -	\$ -	\$ 10.9	\$ (2.0)	\$ 95.7	\$ -
Increase (decrease) in net income	\$ 40.7	\$ (27.1)	\$ (50.0)	\$ -	\$ 10.9	\$ (11.3)	\$ 84.0	\$ (1.9)
<b>Impact on earnings per share</b>								
Increase (decrease) in:								
Earnings per share from continuing operations	\$ (0.03)	\$ (0.05)	\$ (0.36)	\$ -	\$ -	\$ (0.06)	\$ (0.09)	\$ (0.01)
Earnings per share from discontinued operations	0.33	(0.14)	-	-	0.08	(0.01)	0.71	-
Earnings per share	\$ 0.29	\$ (0.19)	\$ (0.36)	\$ -	\$ 0.08	\$ (0.07)	\$ 0.62	\$ (0.01)

**Consolidated quarterly results analysis** (unaudited)  
**Impact of pension and other post employment benefits expense**

For the eight quarters ended March 31, 2004

(millions of dollars except  
per share amounts)

	2002			2003				2004
	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1
Increase (decrease) in:								
Net income from								
continuing operations	\$ (3.0)	\$ (3.0)	\$ (3.0)	\$ (8.5)	\$ (8.7)	\$ (10.1)	\$ (9.6)	\$ (12.4)
Earnings per share from								
continuing operations	\$ (0.02)	\$ (0.02)	\$ (0.02)	\$ (0.06)	\$ (0.06)	\$ (0.07)	\$ (0.07)	\$ (0.09)