pure

2004 Annual Report

Agropur cooperative

agropur

A past that bodes well for the future...

Summary

Enhancing the value of milk

A vocation for Agropur

Each waking day, Agropur cooperative responds to the call of some 4,200 dairy farmers who rely on this organization, which they jointly own, to enhance the fruit of their labour.

Over 1.7 billion litres of milk are processed annually in 19 plants, one in the United States and the others in four Canadian provinces. The resulting products grace the tables of thousands of Canadians from coast to coast. But before these products reach their tables, 3,000 employees and many contract agents assigned to milk collection and distribution combine their efforts and expertise to ensure that the final product meets all expectations.

OUR PRODUCTS GREET YOU AT THE CRACK OF DAWN.

Tradition and progress co-exist in perfect harmony at Agropur. Their interaction generates amazing results for this Cooperative, which was founded in 1938 and remains rooted in its original values. Its success is, above all, a human story. It is reflected in the quality of services offered and a highly diversified product line, which is in keeping with the latest trends and makes milk, this indispensable resource, ever more enjoyable.

Sense of values

Nature is our source

Closely involved in its members' activities, Agropur cooperative has made a vocation of enhancing the value of their product, milk. Derived straight from nature, milk comes to the Cooperative full of richness and freshness. Charged with generating a return on this asset, thousands of people invest their genius and talents in this major group project, which is reinvented on a daily basis to respond to needs, expectations and market signals. Their collective know-how is complemented by cutting-edge technology and sophisticated distribution networks, which act as a springboard to propel the Cooperative to new heights, while nurturing its fundamental values.

Investing in purity

Established on broad-based cooperative principles, Agropur, a major Canadian dairy processor, is building its future on a solid foundation. Its rich 66-year history serves as a platform for securing its strategies. Under the care of a devoted team, milk reveals the multiple facets of its personality. Delivering products that are always in keeping with the times is a priority for Agropur. Another priority is to ensure that its criteria of authenticity and health are satisfied. The challenge for the Cooperative is to make these products even more accessible and inviting, to promote their versatility, and to create excitement through innovation.

With a view to reinforcing its relations with consumers, Agropur meets this challenge through investments, leadership and carefully designed strategies. In its hands, this natural resource called milk can only increase in value. Investing in purity, in the natural benefits everyone.

DISTANCE IS NO OBSTACLE FOR OUR AGENTS WHO BRING FRESHNESS, AUTHENTICITY AND ADDED VALUE.

Pure values

Message from the Chairman

Renewal in a context of continuity, thanks to a strong succession. Consolidation of our financial stability through an unwavering quest for efficiency. It is against this backdrop that fiscal 2004 unfolded. Without being a landmark year, 2004 was still one of significant progress. At the end of this fiscal year, the Cooperative is in a better position than ever to deal with the challenges of the future, to seize business opportunities and to reap the benefits of its values.

The unveiling of a revamped logo at a general meeting held for the first time in Quebec City, the relocation of the head office to Longueuil, and the changes to certain key positions held by senior officers are among the highlights of the fiscal year.

This year also brought to light the capabilities of our back-up management resources. The position of Chief Executive Officer, left vacant by a departure, was filled from within. This appointment had a ripple effect on Natrel in particular, whose management team welcomed a new President and a new Vice-President of Sales, positions that were also filled from within. Despite a vastly renewed leadership, the extensive experience and many years of service of the holders of these positions allowed for a smooth transition and transfer of knowledge, without losing sight of the objectives shared by all.

Cooperatives are known for their ability to rebound in difficult times. Agropur's cooperative status proved useful once again during the conflict stemming from the renewal of two collective agreements. Some 230 members who participated in the daily life of the plants concerned showed solidarity in their desire to maintain the plants' core operations.

In the Canadian dairy industry, business is now conducted nationwide as regards the decision-making process for both production and processing. With our dual role as farmers and processors, we must be aware of what we are and of the force that we represent, in order to establish stronger relations with other players in the Canadian dairy industry. Agropur's development over the years, which has boosted the number of plants we operate to 19, has increased our representation and visibility on this stage.

For Agropur, the situation is as follows: our Cooperative is more able than ever to consolidate its growth through acquisitions. It is also in a better position to play a key role within the dairy industry. It is therefore up to us to create the opening that will allow us to forge ties and partnerships in this new national context.

Whether in the industry as a whole or within the Cooperative, good human relations in an atmosphere of mutual respect are definitely the best way to create this opening. It is by establishing a climate for dialogue that our future projects, big and small, will be able to blossom.

A rich soil for cultivating pure values – this is the avenue to pursue for the prosperity of our business.

Serge Riendeau
Chairman

Added values

Message from the Chief Executive Officer

Fiscal 2004 ended with an improved financial position despite lower earnings when compared with 2003, due primarily to a decrease in export sales and a labour conflict. With an improved balance sheet, a decreased debt and an enhanced equity, Agropur is on a solid footing for future development.

The renewal of the collective agreements that were at the source of the conflict helped us make some progress in this regard. These important gains stand the Cooperative in better stead to face the challenges of the future and to maintain its competitiveness. Both the organization and the employees are benefiting accordingly.

Innovation and know-how continue to inject new life into the Cooperative to ensure that it maintains its leadership position. In this regard, the Canadian Grand Prix New Product Awards is an excellent barometer of our ability to innovate. The Cooperative stood out for a third straight year at this prestigious competition, which proclaimed Natrel Omega-3 the *Dairy Product of the Year,* following on the heels of Natrel Nutrition 24 and Oka Providence, winners of the two previous contests.

During the year, some changes were made to strategic management positions. One of these changes involved Pierre Gignac, a major contributor to the development of Yoplait in Canada, who, before he retired, completed the acquisition of Olympic Dairy Products in British Columbia. This acquisition provides an entry point into the growing sector of organic products.

While three players, including Agropur, control about 70% of the Canadian dairy market, the consolidation of this market shows the possible impact of any future changes on the landscape. This is why it is important for the employees to rally behind the Cooperative's objectives. In this regard, their commitment, sense of duty and integrity are highly valuable assets.

Moreover, the situation requires that our officers and managers be more strategic and visionary than ever. While Agropur is present in the United States through the Deutsch Käse Haus cheese plant, the horizon for the future development and consolidation of our position extends to our neighbours to the South and to the Canadian provinces in which we are less active.

As a result of the growing operational needs of Ultima Foods, head office was relocated from Granby to Longueuil (photo below) at the end of the fiscal year. Given also that the Industrial Division is managed from Granby, this city remains a hub for Agropur's activities in Canada. In addition to bringing us closer to our business centre, the move to Longueuil allowed us to merge our corporate services under one roof. Also, establishing its head office on the south shore of Montreal, the confluence of major highways, gives the Cooperative easier access to a wide variety of customers and suppliers.

The highlights of this fiscal year reflect more than ever the Cooperative's desire to forge ahead. While our action plans are based on synergy of resources, strong human values are just as indispensable to us as high technology for the achievement of our objectives. While guaranteeing growth and success, innovation and stringency keep us at the forefront of the industry and consolidate our leadership position on the markets.

As I close my first term as Chief Executive Officer, I would like to thank the members of the Board of Directors for the trust they have shown in me. I would also like to thank our members, employees, agents and business partners who have all played a part in the achievement of these excellent results.

Pierre Claprood
Chief Executive Officer

Values and developments

Review of Operations

Cooperative principles, which benefit from the pooling of resources and ideas, have proven to be great assets to Agropur. In today's high-tech world, where activities are increasingly dependent on information systems, the Cooperative is relying more than ever on these basic values to meet future challenges.

During the fiscal year, Natrel completed the expansion and modernization of its Toronto facilities, now ranked among the most advanced dairies in North America. Natrel injected $19 million over two years to make this site a processing and distribution nerve centre in southern Ontario.

This resulted in, among other things, the closing of the Brantford plant, the opening of a new distribution centre in this region, and vocational changes or closures of other centres. At the heart of its cutting-edge technology, a computerized inventory management system serves as a bridge between the plant and the refrigerated warehouse.

The Saint-Hyacinthe cheese plant improved its mastery of an automation-based technology acquired over the past few years. This fine-tuning resulted in a reduction of the time and energy devoted to the manufacturing process. The addition of packaging equipment also generated efficiency gains throughout the chain.

The efforts of Ultima Foods have been rewarded with annual growth of 11% over the past decade. In the summer of 2004, a $6 million expansion project was initiated at Ultima's plant in Granby. Phase II of this project, which is even more important, will continue in 2005. Combined with work reorganization, the expansion, while increasing Ultima's processing capacity, will create some 30 jobs. An integrated warehouse management system, which uses radiofrequency, was added to an existing software package, in order to provide better support for re-stocking and the monitoring of finished products all the way to the customer.

The fine cheese sales team offers its customers service that goes beyond the traditional role of salespersons. Designed for in-depth analysis, the tools used allow these profitability counsellors to act with distinctive competence and to make business more profitable for Agropur and its customers. The effectiveness of these tools has been increased with the adoption, at a cost of $3 million, of a management system to which their computers are connected. A team of about ten employees, freed up from their regular duties for six months, combined its expertise with that of a consulting firm to ensure that the system was successfully deployed across many sectors, including sales.

Confirmed by its slogan, *Driven By Customer Needs,* the Industrial Division shows an ever-increasing desire to get closer to the retail market and the hotel, restaurant and institutional sector in particular. Meetings facilitated by members of its management committee have allowed 250 employees who provide customer service support to participate in the process. Made aware via the existing communication channels, all employees are solicited by the new challenge, which is to set the Cooperative apart through the quality of its service and a more diversified, value-added product line.

OUR ACCOMPLISHMENTS GUIDE THE WAY TO THE FUTURE.

The reinforcement of partnerships and strategic alliances are some of the means being considered in order to achieve results. A modernization project to be implemented at the Granby cheese plant, which is designed to improve the quality of its products, dovetails perfectly with this context of renewal.

Just like for Natrel, the United States remains a development avenue for fine cheeses. To ensure a leadership, Agropur plans to penetrate unexplored market segments and thereby offset declining export sales. Increasing its presence in Western Canada and the Maritimes and developing value-added products are among Natrel's priorities. Attracting and retaining major customers through the quality of its service and its capacity for innovation, while getting closer to the distribution sector, are among the strategies for Ultima Foods, which intends to consolidate its presence across Canada.

Nutritional values

Milk has not yet disclosed all its secrets. Research is reconfirming its high nutritional value and constantly revealing its new properties. Case in point: the latest discoveries are bringing to light milk's virtues in the fight against obesity.

For Agropur, privileged to have such a rich resource at its disposal, innovation has always been and continues to be an issue of health and vitality, which are nutritional values not only in terms of personal diet, but also with regard to corporate fitness.

QUALITY PRODUCTS, SYNONYMOUS WITH HEALTH

Products that promote wellbeing and double as comfort food are in keeping with current trends. The Yoplait line took a 90-degree turn in 2004, which was initiated with the launching of Yoplait Source in 2002. This yogourt, a veritable phenomenon that captured a Cassies award in the *Best Launch* category at a contest paying tribute to Canadian advertisements, is the perfect example of a product that was able to pick up market signals. In the spring of 2004, two consecutive launches aimed in the same direction introduced the Yoplait Delicieux and Yoplait Creme & fruit yogourt families.

The World of Natrel, a concept that embraces added-value milks while underpinning the notion of healthy products, continues to evolve. New Natrel chocolate Lactose Free, capitalizing on the double success of chocolate beverages and Natrel regular lactose-free milk, made its debut. Very popular in Quebec, Natrel Omega-3, a milk that benefits bodily functions in more ways than one, is making inroads into Ontario and Western Canada. The title of *Dairy Product of the Year* captured at the Canadian Grand Prix New Product Awards constitutes an excellent vehicle for conquering these horizons. Riding this wave of innovation, Natrel Café flavoured creams made their entrance in the Canadian market, where they are benefiting from the dynamism of a high-growth segment.

Minigo Duo, a new concept that has re-energized the image of these fresh cheeses, is delivering the goods: three months after its launch, sales of this new product tripled forecasts. Providing double the pleasure by offering two flavours in each unit, Minigo Duo is also appreciated for its colourful containers, which make healthy eating fun.

In terms of fine cheeses, havarti still tops the best seller list. Soft cheeses, for their part, show the strongest growth and benefit from favourable market conditions. The variety of the line, which features several imports, is an undeniable advantage. However, in 2004, this line required considerable energy in terms of adapting the packaging to the nutritional labelling rules to be applied in December 2005. In addition, the concentration of retailers in Canada, accompanied by increasingly personalized services and rising costs for manufacturers, is exerting pressure on the latter.

Agropur, which has always made a point of offering quality products, is building its reputation on major labels. Some, such as Oka and Sealtest, are centenarians, while others are setting popularity records.

Human values

Powerful and omnipresent, technology is providing new tools for asserting our leadership in a fiercely competitive world of perpetual change. While they make a difference, these tools are of little use without the men and women who control them. It is through their efforts that the desired efficiency is achieved.

Also, given the anticipated shortage of qualified workforce, Agropur is focusing its energy on enhancing its profile as an ideal employer. For the Cooperative, which continues to put the human element at the forefront, this process begins internally. Thus, greater emphasis is being given to one of its main priorities: providing employees with an environment conducive to development and adaptation while encouraging employee participation.

Thus, mobilization is a primary objective. Presenting issues and challenges in a global perspective is the starting point for communication. Adapting this communication to the reality of its employees, transposing issues into their daily activities, providing them with the information and feedback they need to integrate into the improvement process, whether in their workplace or on a broader scale, are the cornerstones of an approach based on mutual trust and respect. In such a context, where everyone receives as much as he gives and the role of manager doubles as that of coach, adherence to the organization's objectives is strengthened, helping to create a very solid partnership.

The development of talents and skills makes it possible for each and everyone to achieve new heights. Employees can acquire the knowledge required to effectively perform their duties, while enhancing their personal experience. Since these positive effects are widespread, the organization reaps the benefits of professionalism and efficiency, concepts that will set it apart, primarily among its clientele, where there is an increasingly strong desire to establish closer ties.

A corporate culture centered on customers underpins the actions of an organization like Agropur, where the fragility of the product establishes the rules of the game. Flexibility, speed and efficiency, which stand out as the main qualities of its operations, are achieved through, among other things, better work organization and optimum use of skills and infrastructures. The result: increased product quality and customer satisfaction.

Occupational health and safety (OHS) is establishing itself as a major group project. No matter how much Agropur invests in the wellbeing of its human resources in order to protect their most precious assets, namely life and health, the exercise would be futile without their commitment. On the one hand, employees develop safe behaviours. On the other hand, the organization is assured of its compliance with industry requirements and a high level of operational efficiency. The importance given to this priority is such that an annual event aimed at all local OHS committees has taken on a national dimension for the purpose of more constructive discussions. An excellent opportunity for sharing experiences and promoting initiatives, this forum also puts the organization's orientations and vision into perspective.

HUMAN CAPITAL, PRIMARY RESOURCE OF THE ENTERPRISE OF THE FUTURE

Sure values

Agropur invites you to taste quality and excellence. The gateway to healthy and balanced meals, a line of dairy products lending itself to a host of occasions. For you, bountiful, versatile and imaginative food that meets your every expectation. The guarantee accompanying this food is the verdict of some major contests in which the Cooperative participated in 2004.

For the third consecutive year, the *Canadian Grand Prix New Product Awards* bestowed the title of *Dairy Product of the Year* to an Agropur product. Well-adapted to a modern lifestyle, Natrel Nutrition 24, Providence Oka and Natrel Omega-3 have, one by one, achieved this feat.

At the *World Championship Cheese Contest,* Agropur's mild cheddar missed out on the title of the *World's Best Cheddar* by just a few decimals. The samples entered captured the silver and bronze in their category. Anco smoked gouda received the bronze medal in the firm cheese category.

At the *Canadian Cheese Grand Prix,* first prizes were awarded to St-Paulin Anco, Britannia mild yellow cheddar and Providence Oka, the latter for its packaging design.

At the *Royal Agricultural Winter Fair* in Toronto, a foursome comprising plain Havarti Danesborg, plain Délicrème and two Britannias, two and three years old, earned four first prizes. Two-year-old Britannia and Havarti each walked away with a *Championship* title in their respective categories.

At the *World Dairy Expo,* held in Wisconsin, the U.S. cheese plant Deutsch Käse Haus, which received the USDA's seal of quality approval in 2004, brought home second prize in the Colby – Monterey Jack category.

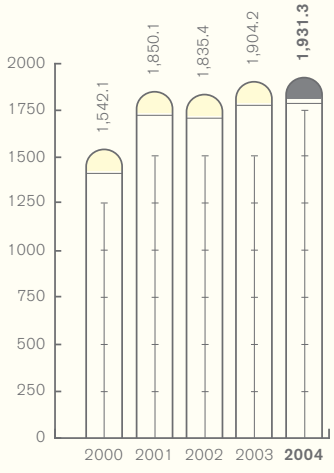
There is nothing better than television to put this know-how into perspective. Since September 2004, Agropur has been a major sponsor of the show, *Par-dessus le marché.* The purpose of this show, aired every Saturday on the TVA network, is to give voice to the architects of the agrifood world and answer consumers' questions, while promoting the farming profession.

THE TABLE IS SET.

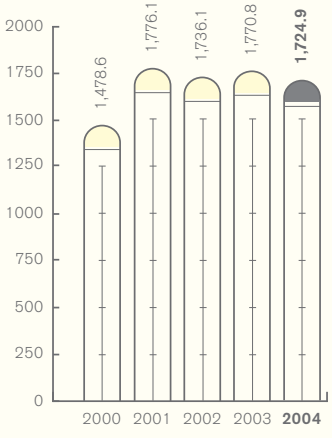
HIGHLIGHTS

	2004	2003	
Sales	**1,931.3**	1,904.2	(in millions of dollars)
Milk processed	**1,724.9**	1,770.8	(in millions of litres)
Earnings before patronage dividends	**82.3**	90.7	(in millions of dollars)
Asset acquisitions	**39.9**	31.0	(in millions of dollars)
Total assets	**690.0**	691.9	(in millions of dollars)
Number of employees	**3,000**	3,000	

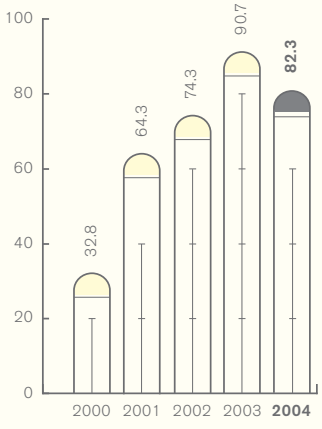
THE PAST FIVE YEARS



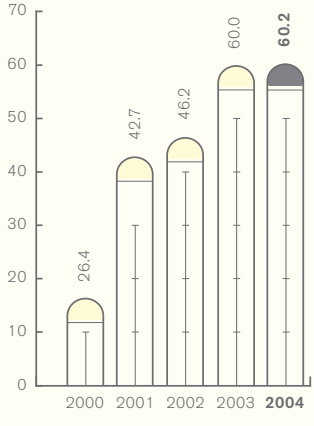
Sales
(in millions of dollars)



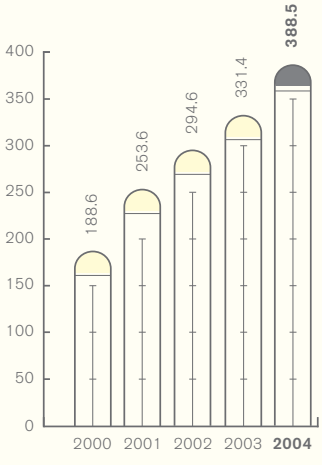
Milk processed
(in millions of litres)



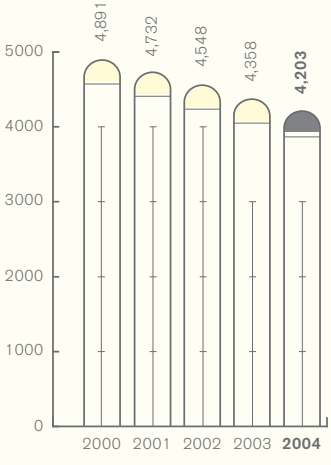
Earnings before patronage dividends
(in millions of dollars)



Patronage dividends
(in millions of dollars)



Equity
(in millions of dollars)



Number of members

FINANCIAL REVIEW

The financial results for 2004 reflected the setback of the labour dispute experienced at two of the Industrial Division's plants and settled after a four-month strike. The WTO's final decision rendered in December 2002, which limits Canadian dairy exports, also had an impact on the fiscal year, with a full effect on sales in 2004, while certain volumes were exempt from this decision in early 2003.

Results

Sales increased by $27 million compared with last year. The cheese divisions processed 5.4% litres less than in 2003, a decline attributable mainly to the reasons cited previously.

The launch of the new Yoplait Creme & fruit and Yoplait Delicieux products, combined with the popularity of the Yoplait Source yogourt, resulted in a 9.5% increase in volume for the Ultima Foods joint venture. Growth continued at a rate of 6.2% for fine cheeses sold in Canada. In terms of fluid milk, Natrel saw its volume increase by 1.4%.

Operating earnings stood at $85.3 million compared with $95.4 million a year earlier. This decline is linked mainly to the labour dispute as well as to the decrease in export sales. Modernization work at the Toronto facilities, which focused on the construction of a state-of-the-art distribution centre linked to the plant, was completed during the year. However, Natrel will benefit fully, in 2005, from investments made in this project - which also resulted in the closing of the Brantford plant.

The low financial expenses can be explained by a healthy financial situation and low interest rates. Earnings before patronage dividends and income taxes stood at $82.3 million, down $8.4 million compared with 2003. The Board of Directors approved patronage dividends of 5.45% of the value of members' milk deliveries, for a total amount of $60.2 million, similar to that of last year. These dividends are payable in a proportion of 25% cash and 75% investment shares.

Cash flow

Cash flow from operations reached $122 million, a decrease of $5.5 million. The variation in non-cash assets, composed of working capital and employee future benefits, resulted in an outflow of $50.9 million in 2004. Excluding inventories on consignment to the Canadian Dairy Commission, stocks were up by $22 million, particularly those of cheese. Accounts payable were reduced by $10 million following the special payment, in November 2003, of a redemption of capital of active members which had been approved and recorded in September 2003. The reduction in milk payables and income taxes for an amount of $13 million completes this profile.

In October 2004, the Ultima Foods joint venture acquired all of the shares of Olympic Dairy Products. The Cooperative's share represents an outflow of $4.7 million. Capital investments totalled $39.9 million in 2004, $10 million of which was earmarked for the Toronto distribution centre. It should be noted that the high share redemptions in 2003 included an early redemption of shares of active and resigning members.

Balance sheet

The financial situation improved once again in 2004. Non-cash assets stood at $617 million, an increase of 4%, stemming mainly from stocks and capital investments. During the same period, equity rose by 17%. As at October 30, 2004, this equity stood at $388 million.

In conclusion

After another good year, which nevertheless endured the negative impact of a few non-recurring events, Agropur will continue to exert its characteristic financial discipline in order to be able to meet the challenge of future growth.

Benoit Gagnon
Chief Financial Officer

AUDITORS' REPORT

DECEMBER 8, 2004 (DECEMBER 20, 2004 FOR NOTE 4)

To the Members of Agropur cooperative

We have audited the consolidated balance sheet of **Agropur cooperative** as at October 30, 2004 and the consolidated statements of earnings and reserve and cash flows for the year then ended. These financial statements are the responsibility of the Cooperative's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of **Agropur cooperative** as at October 30, 2004 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

PricewaterhouseCoopers LLP

Chartered Accountants

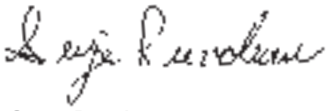
CONSOLIDATED STATEMENT OF EARNINGS AND RESERVE

(in thousands of dollars)	notes	2004	2003
Sales		**1,931,271**	1,904,228
Operating expenses	3	**1,845,954**	1,808,791
Earnings from operations before the following items		**85,317**	95,437
Net financial expenses	3	**522**	1,972
Loss (gain) on disposal of assets		**(10)**	188
Income taxes of subsidiaries and joint ventures		**2,529**	2,617
Earnings before patronage dividends and the Cooperative's income taxes		**82,276**	90,660
Patronage dividends	4	**60,188**	60,041
Cooperative's income taxes		**7,444**	12,190
Net earnings		**14,644**	18,429
Reserve – Beginning of year		**114,806**	96,377
Reserve – End of year		**129,450**	114,806

CONSOLIDATED BALANCE SHEET

(in thousands of dollars)	notes	October 30 2004	November 1 2003
ASSETS			
Current assets			
Cash and temporary investment		**72,460**	100,084
Accounts receivable		**116,660**	114,380
Inventories	5	**164,418**	148,458
Income taxes		**4,277**	–
Prepaid expenses		**9,760**	7,562
Future income taxes	6	**2,392**	3,322
		369,967	373,806
Employee future benefits	16	**4,328**	2,545
Fixed assets	7	**218,569**	207,092
Other assets		**97,134**	108,466
		689,998	691,909
LIABILITIES			
Current liabilities			
Accounts payable and accrued liabilities	9	**249,528**	271,623
Income taxes		–	2,577
Current portion of long-term debt	10	**4,928**	14,406
		254,456	288,606
Long-term debt	10	**33,197**	58,787
Future income taxes	6	**13,877**	13,160
		301,530	360,553
EQUITY			
Share capital	11	**259,018**	216,550
Reserve		**129,450**	114,806
		388,468	331,356
		689,998	691,909

Approved by the Board of Directors



Serge Riendeau
Director

René Grimard
Director

CONSOLIDATED STATEMENT OF CASH FLOWS

(in thousands of dollars)	notes	2004	2003
CASH FLOWS FROM			
Operating activities			
Earnings before patronage dividends and the Cooperative's income taxes		**82,276**	90,660
Cooperative's payable income taxes		**(5,705)**	(10,692)
Items not involving use of funds			
Depreciation and amortization		**45,692**	47,315
Future income taxes of subsidiaries and joint ventures		**(186)**	88
Other		**(9)**	193
		122,068	127,564
Change in non-cash items	12	**(50,946)**	37,897
		71,122	165,461
Financing activities			
Issuance of long-term debt		**4,500**	–
Repayment of long-term debt		**(42,145)**	(19,580)
Pension plans' funding	16	**–**	(5,156)
		(37,645)	(24,736)
Investing activities			
Business acquisition	14	**(4,650)**	–
Purchase of fixed assets		**(39,928)**	(30,976)
Proceeds on disposal of assets		**444**	1,305
Variance on cross-currency swap agreement renewal to hedging		**753**	1,678
		(43,381)	(27,993)
Activities with members and on share capital			
Patronage dividends payable in cash	4	**(15,047)**	(15,010)
Issuance of shares	11	**129**	213
Redemption of shares	11	**(2,802)**	(26,930)
		(17,720)	(41,727)
Net change in cash position during the year		**(27,624)**	71,005
Cash and temporary investment – Beginning of year		**100,084**	29,079
Cash and temporary investment – End of year		**72,460**	100,084

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. STATUTES OF INCORPORATION

Agropur cooperative ("the Cooperative") was established on August 29, 1938 under the Act Respecting Cooperative Agricultural Associations and, since October 26, 2000, has been governed by the Canadian Cooperatives Act.

2. SIGNIFICANT ACCOUNTING POLICIES

These consolidated financial statements include the accounts of the Cooperative and its subsidiaries as well as its share of the assets, liabilities, revenues and expenses of joint ventures.

The preparation of financial statements requires management to make estimates and assumption that affect the reported amounts in the financial statements.

New accounting standard

Effective November 2, 2003, the Cooperative adopted Accounting Guideline 13 (AcG-13) related to hedging relationships. In accordance with AcG-13, the Cooperative documents the risk management strategy for establishing the relationship to apply hedge accounting. At the signing of the hedging contract, management documents the hedged item (an asset, a liability or an anticipated transaction), details of the hedge instrument used and the valuation method of effectiveness.

The accounting policies effective November 1, 2003 are maintained for the hedging relationships that are defined as effective. Therefore, realized or unrealized gains or losses on hedges are deferred until realization of the hedged item for best matching in the statement of earnings.

Inventories

Finished goods and goods in process are valued at the lower of average cost and net realizable value. Raw materials are valued at the lower of cost and replacement value, cost being determined under the first-in, first-out method.

Fixed assets

Fixed assets are recorded at cost, net of applicable government grants.

Depreciation is calculated over the estimated useful lives of the assets based on the following methods and rates:

• Buildings	Diminishing balance	5%
• Equipment	Diminishing balance	15% and 20%
• Office furniture	Diminishing balance	20%
• Computer equipment	Straight-line	20% and 25%
• Rolling stock	Diminishing balance	30%

Other assets

Other assets consist mainly of goodwill which is amortized on a straight-line basis over periods not exceeding 20 years. The Cooperative determines if a permanent impairment in the value of goodwill has occurred. To support this valuation, the Cooperative determines mainly whether estimated future cash flows on an undiscounted basis exceed the net book value of assets purchased.

Furthermore, deferred charges for procurement contracts are accounted for and amortized on a straight-line basis according to the duration of the agreements.

Employee future benefits

Following the review of Section 3461 of the Canadian Institute of Chartered Accountants' Handbook, the Cooperative applied the new supplemental disclosure standard related to assets, cash flows and net cost benefit for defined benefit plans. The effect of adopting the new recommendations does not have an impact on the statement of earnings.

The Cooperative accounts for its obligations under the employee benefit plans and related costs net of the plan assets. The cost of pension and other retirement benefits earned by employees is determined from actuarial calculations according to the projected benefit method prorated on years of service based on management's best estimate assumptions about the investment returns on the plans, salary projections and the retirement ages of employees. Assets and accrued benefit obligations are evaluated three months before the date of the financial statements.

The fair value of assets is determined using the fair market value. The estimated rate of return on the plan assets is based on the long-term estimated rate of return and the value of the plan assets assessed at fair value. The excess of the net actuarial gain (loss) over 10% of accrued benefit obligations, or over 10% of the fair value of the plan assets where such amount is higher, is amortized over the average remaining service life of employees. The cost of past services resulting from changes to the plans is amortized over the average remaining service life of employees.

Income taxes

Income taxes are accounted for using the liability method of tax allocation. Under this method, future income taxes are calculated on the difference between the tax basis and the carrying amount of the various assets and liabilities. Future income tax assets and liabilities are measured using the tax rates that are expected to be in effect in the years when the timing differences are expected to reverse. Income tax assets are recognized when it is more likely than not that the asset will be realized.

Translation of foreign currencies

Foreign currency transactions

Monetary assets and liabilities denominated in foreign currencies are translated into Canadian dollars at the exchange rate prevailing at the balance sheet date, whereas transactions denominated in foreign currencies are translated at the average monthly exchange rates for the period. The resulting foreign currency translation gains and losses, net of hedging operations, are included in the consolidated statement of earnings.

Foreign operation

All assets and liabilities of the self-sustaining subsidiary operating in the United States are translated into Canadian dollars at the exchange rate prevailing at the balance sheet date. Revenues and expenses are translated at the average exchange rates for the period. Foreign currency gains and losses are mitigated through hedging operations using cross-currency swaps.

3. EARNINGS

The following items are included with operating and financial expenses shown in the consolidated statement of earnings:

(in thousands of dollars)	**2004**	2003
Depreciation of fixed assets	**30,424**	30,908
Amortization of other assets	**15,268**	16,407
Interest on long-term debt	**2,196**	3,757

4. PATRONAGE DIVIDENDS

The patronage dividends to members are paid $15,047,000 (2003 – $15,010,000) in cash and $45,141,000 (2003 – $45,031,000) through the issuance of shares.

5. INVENTORIES

(in thousands of dollars)	**2004**	2003
Finished goods	**145,667**	130,194
Raw materials, goods in process and supplies	**18,751**	18,264
	164,418	148,458

6. FUTURE INCOME TAXES

The main components of the Cooperative's future income tax assets and liabilities are as follows:

(in thousands of dollars)	2004	2003
Future income tax assets		
Accrued expenses, provisions and other reserves that are tax deductible only at the time of disbursement	**2,392**	3,322
Future income tax liabilities		
Fixed and other assets	**13,877**	13,160

7. FIXED ASSETS

(in thousands of dollars)			2004	2003
	Cost	Accumulated depreciation	**Net**	Net
Land	13,114	–	**13,114**	12,313
Buildings	125,039	60,074	**64,965**	64,266
Equipment	349,833	232,912	**116,921**	110,336
Office furniture	5,324	4,618	**706**	792
Computer equipment	37,807	22,236	**15,571**	11,284
Rolling stock	30,631	23,339	**7,292**	8,101
	561,748	343,179	**218,569**	207,092

8. BANK LOANS

The Cooperative and its joint ventures have lines of credit to a maximum of $75,500,000 which bear interest at variable rates generally not exceeding the prime rate. As at October 30, 2004, the lines of credit are unused, except for letters of credit of a total value of $1,019,000.

9. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

(in thousands of dollars)	2004	2003
Members	**92,970**	98,402
Third parties	**156,558**	173,221
	249,528	271,623

10. LONG-TERM DEBT

(in thousands of dollars)	2004	2003
Loans contracted under a term credit agreement:		
Bearing interest at an average rate of 6.48% (1)	**31,696**	35,657
Bearing interest at a floating rate generally not exceeding the lenders' prime rate (1)	–	34,673
Other loans (2)	**6,429**	2,863
	38,125	73,193
Current portion	**4,928**	14,406
	33,197	58,787

(1) The loans are secured by Series A - 2000 bonds with a par value of $225,000,000. The bonds, bearing interest at prime rate, were issued and pledged under a trust deed signed on December 1, 2000 to guarantee loans contracted by the Cooperative under a term credit agreement which limits the lenders' rights over the pledged bonds to the real loan amounts.

This trust deed contains certain commitments made by the Cooperative to maintain certain financial ratios and the obligation to refrain from charging the assets.

In October 2004, a portion of $25,000,000 of term loan C was reimbursed in advance.

Term loan	Original value	Repayment method	Balance at maturity
A	$40,000,000	$4,000,000 annually from October 2003 to October 2007	$20,000,000 in October 2008

(2) The loans include among others the proportionate share of the joint ventures' loans, whose share of assets are pledged to secure the loan amounts to $1,200,000.

Estimated principal repayments of the long-term debt required over the next five years are as follows:

	(in thousands of dollars)
• 2005	4,928
• 2006	4,323
• 2007	4,978
• 2008	22,492
• 2009	1,404

11. SHARE CAPITAL

The following constitutes a summary of certain privileges, rights and conditions related to the Cooperative's shares. Reference can be made to the statutes of the Cooperative for the full text of these conditions.

The share capital of the Cooperative's members is variable and unlimited as to the number of shares in each class that can be issued, with the exception of Class C investment shares whose number is limited to 100,000,000. The shares have a nominal value of $1 each, with the exception of member shares ($100), Class M investment shares, Series 1 ($20), Series 2 ($1,500), Series 3 ($400) and Series 4 (to be determined when first issued).

When joining, new members subscribe to one member share and 10 Class M investment shares.

Voting rights are restricted to one vote per member.

In consideration of patronage dividends, the following investment shares are issued: either Class A, Series A and A1 and Class B, Series B and B1, or Class C, Series AAA and BBB, as per the member's choice. Series A1 and B1 were authorized in 2004.

Class A, Series A and Class B, Series B investment shares are eligible under the Registered Retirement Savings Plan due to a conversion into Class C, Series AA and BB investment shares respectively. Class C, Series AA and BB investment shares can be held by auxiliary members. No Class A, Series D and Class B, Series E investment shares formerly signed under the Cooperative Investment Plan have been issued since January 1, 1996.

Class A, Series L investment shares were authorized to serve as partial payment for a business acquisition in 2001.

Class C, Series AAA and BBB investment shares are issued according to the terms governing the Class A, Series A and A1 and Class B, Series B and B1 investment shares respectively, under the Cooperative Investment Plan. These investment shares are also eligible under the Registered Retirement Savings Plan.

Member shares as well as all classes of the investment shares are redeemable under certain conditions at their par value upon resolution of the Board of Directors. Share redemptions are subject to certain financial ratios. In addition, for Class A, Series D, Class B, Series E and Class C, Series AAA and BBB investment shares, the law requires that the reserve be increased by 50% of the amount of the redemption since issuance.

At year-end, shares issued and fully paid were as follows:

(in thousands of dollars)	**2004**	2003
Member shares	**424**	437
Investment shares		
Class A, Series A, A1 and D	**123,561**	102,419
Class A, Series L	**18,777**	18,777
Class B, Series B, B1 and E	**62,441**	52,571
Class C, Series AA	**21,116**	16,073
Class C, Series BB	**8,501**	6,603
Class C, Series AAA	**13,248**	10,339
Class C, Series BBB	**5,418**	3,820
Class M, Series 1, 2 and 3	**5,532**	5,511
	259,018	216,550

During the year, share capital changed as follows:

(in thousands of dollars)	**2004**	2003
Balance – Beginning of year	**216,550**	198,236
Issuance of shares as payment for patronage dividends	**45,141**	45,031
Instalments on member shares and Class M investment shares	**129**	213
Redemption of shares in cash	**(2,802)**	(26,930)
Balance – End of year	**259,018**	216,550

During the year, an amount of $7,145,000 (2003 – $5,043,000) was transferred from Class A and B shares to Class C shares.

As at October 30, 2004, inactive members held shares of the Cooperative for a total amount of $7,727,000 (2003 – $6,069,000).

12. CASH FLOWS

Cash flows related to non-cash items have increased (decreased) as follows:

(in thousands of dollars)	**2004**	2003
Accounts receivable	**(1,586)**	(3,943)
Inventories	**(15,773)**	(22,043)
Prepaid expenses	**(2,196)**	(1,677)
Accounts payable and accrued liabilities	**(22,694)**	66,372
Income taxes	**(6,914)**	(1,517)
Employee future benefits	**(1,783)**	705
	(50,946)	37,897

Interest paid approximates financial expenses disclosed in note 3. Income taxes paid amount to $15,336,000 (2003 – $14,922,000).

13. FINANCIAL INSTRUMENTS

Fair value

The fair value of financial instruments is assumed to approximate their book value due to their short-term maturity. These financial instruments generally include cash and temporary investments, accounts receivable, bank overdrafts and bank loans, and accounts payable and accrued liabilities.

Interest rate risk

The financial assets and liabilities do not bear interest, except for cash, temporary investment and long-term debt.

The Cooperative's long-term debt bears interest at variable rates. Interest rate swap agreements have been contracted to fix an original loan of $40,000,000 at a weighted average rate of 6.48%. As at October 30, 2004, the cancellation agreement cost amounts to $1,600,000.

Hedging against foreign exchange risk

Currency forward contracts

The Cooperative hedges against foreign exchange risks for projected future transactions by means of currency forward contracts, mainly in U.S. dollars and euros. Foreign currency gains and losses are recorded in earnings at the expiry of these contracts. At the presentation date of the financial information, the foreign exchange contracts, spread over periods not exceeding one year, approximate the fair market value and are as follows:

Purchases	US$2,788,000
Sales	US$1,853,000
Purchases	€5,400,000

Cross-currency swaps

The Cooperative has concluded a cross-currency swap agreement to hedge the net investment in the U.S. subsidiary, having the effect of translating capital of US$11,000,000 into capital of CA$14,493,000 at maturity.

14. INVESTMENTS IN JOINT VENTURES

The Cooperative holds an interest in the following joint ventures:

- Ultima Foods Inc.: 50%
- 292806 Ontario Limited (Bright Cheese House): 49%

The Cooperative's share in the statements of earnings and balance sheets of the joint ventures is summarized as follows:

(in thousands of dollars)	**2004**	2003
Assets	**55,757**	46,590
Liabilities	**31,070**	25,559
Sales	**108,235**	96,042
Cash flows from operating activities	**5,307**	9,717

In October 2004, a joint venture of the Cooperative acquired all the shares of Olympic Dairy Products Limited. The Cooperative's share represents an outflow of $4,650,000. The transaction was accounted for using the purchase method.

15. COMMITMENTS AND CONTINGENCIES

Commitments relating mainly to operating leases are as follows:

(in thousands of dollars)	**2004**	2003
Total commitments (including $6,315 for next year)	**29,900**	22,400

The Cooperative is party to litigations in the normal course of business. Even if the outcome of these litigations cannot be expressed with certainty, the related liability is recorded when it is likely that it will result in a loss and that the amount can be estimated. Furthermore, management estimates that the losses that could result from these litigations will be negligible.

16. EMPLOYEE FUTURE BENEFITS

Employee future benefits relate mainly to pension plans. The obligations of the defined benefit plan are based on the employee's length of service and the pay of the last years of service. The pension benefit can be adjusted according to a formula based on the return on plan assets and the consumer price index. The actuarial valuation of the plans are performed at least every three years, the last valuations were performed mainly in January 2002 and January 2003.

Net expense is as follows:

(in thousands of dollars)	**2004**	2003
Defined contribution plans		
Net expense	**3,876**	3,689
Defined benefit plans		
Current service cost	**1,708**	1,284
Interest cost on accrued benefit obligation	**3,484**	3,363
Actual return on plan assets	**(5,215)**	(2,583)
Difference between expected return and actual return	**2,048**	(407)
Actuarial loss on accrued benefit obligation	**2**	5,096
Difference between actual actuarial loss and the amount recognized for the year	**1,140**	(3,428)
Amortization of transitional balance	**(903)**	(903)
Net expense	**2,264**	2,422

The information on defined benefit plans is as follows:

(in thousands of dollars)	**2004**	2003
Plan assets		
Fair value – beginning of year	**46,910**	40,560
Actual return on plan assets	**5,215**	2,583
Employer contributions	**4,474**	6,127
Employee contributions	**713**	644
Benefits paid	**(2,684)**	(3,270)
Other plans' transfer	**–**	266
Fair value – end of year	**54,628**	46,910

The above contributions approximate the total cash payments. Equity securities included 58% (2003 – 51%) of total plan assets, invested mainly in Canada.

In July 2003, certain benefit plans secured by a letter of credit were funded for an amount of $5,156,000.

(in thousands of dollars)	2004	2003
Accrued benefit obligation		
Balance – beginning of year	**55,926**	48,543
Current service cost	**1,708**	1,284
Interest cost	**3,484**	3,363
Employee contributions	**713**	644
Benefits paid	**(2,684)**	(3,270)
Actuarial loss	**2**	5,096
Other plans' transfer	–	266
Balance – end of year	**59,149**	55,926
Employee future benefits assets		
Funding status – plan assets net of obligations (deficit)	**(4,521)**	(9,016)
Less: Transitional assets at the beginning, unrecorded and to be amortized	**(5,925)**	(6,828)
Plus: Actuarial loss, unrecorded and to be amortized	**14,246**	17,434
Plus: Employer contributions after valuation date	**528**	955
Employee future benefits assets	**4,328**	2,545

For pension plans with an accrued benefit obligation that was higher than the assets, the accrued benefit obligation is $50,825,000 (2003 – $52,842,000) and the assets are $44,216,000 (2003 – $43,097,000).

	2004	2003
Weighted-average assumptions		
Accrued benefit obligation		
Discount rate	**6.25%**	6.25%
Long-term inflation rate of salary expense	**4.00%**	4.00%
Net benefit expense		
Discount rate	**6.25%**	7.00%
Expected return on plan assets	**7.00%**	7.50%
Long-term inflation rate of salary expense	**4.00%**	5.00%

The Cooperative participates in multiemployer defined benefit plans for certain unionized employee groups. These plans are accounted for as defined contribution plans. Contributions for the year amount to $554,000.

17. SEGMENT DISCLOSURES

The Cooperative carries on the business of processing and selling dairy products within a regulated raw milk sourcing environment. Processed products are distributed to a large number of customers, including major Canadian food chains and industrial customers. Assets are located mainly in Canada. In addition, sales are made primarily in Canada. The Cooperative's Board has determined that Agropur carries on business in only one operating sector, dairy products.

Three customers represent respectively more than 10% of the sales figure, for a volume amounting to $693,000,000.

18. COMPARATIVE FIGURES

Certain comparative figures have been reclassified in order to conform with the current year's presentation.

BOARD OF DIRECTORS

01 Roger Daoust[1,2]
Salaberry,
1993

02 Michel Couture[1]
De L'Érable,
2001

03 René Grimard[1]
Vice-Chairman
Des Appalaches,
1995

04 Serge Riendeau[1]
Chairman
Estrie, 1991

05 Roger Massicotte
Mauricie / Portneuf,
2003

06 Lorna Jean Neveu[2]
Laurentides / Lanaudière,
1996

07 Darie Gagné[2]
Chaudière,
1997

01 02 03 04 05 06 07

08 François Pelletier
Yamaska,
2002

09 René Moreau[1]
Bois-Francs,
1998

10 Daniel Lamy
Berthier / Maskinongé,
2004

11 Gaétan Jodoin
Granby,
1996

12 Denis Vallée
Lac Saint-Pierre,
1991

13 Daniel Gingras
Des Seigneuries,
1997

14 Roger Beaulieu[2]
Est du Québec,
2000

15 Jean Filiatrault[2]
Acton,
1993

08 09 10 11 12 13 14 15

Legend: Director / Administrative region / Year elected to the Board
[1] Executive Committee members
[2] Directors whose term expires in 2005; however, they can be re-elected.

MANAGEMENT COMMITTEE

01 Serge Paquette
President
Natrel

02 Louis Lefebvre
President
Industrial Division

03 Pierre Claprood
Chief Executive Officer

04 Benoit Gagnon
Chief Financial Officer

05 Pierre Robert
President
Fine Cheese Division

01 02 03 04 05

06 Michel Leclair
Vice-President
Quality Assurance

07 Robert Gour
Vice-President
Human Resources
and Communications

08 Denis Lachance
Vice-President
Legal Affairs
and Corporate Secretary

09 Dominique Benoit
Vice-President
Institutional Affairs

10 Jacques R. Rolland
Vice-President
Research and Development

06 07 08 09 10

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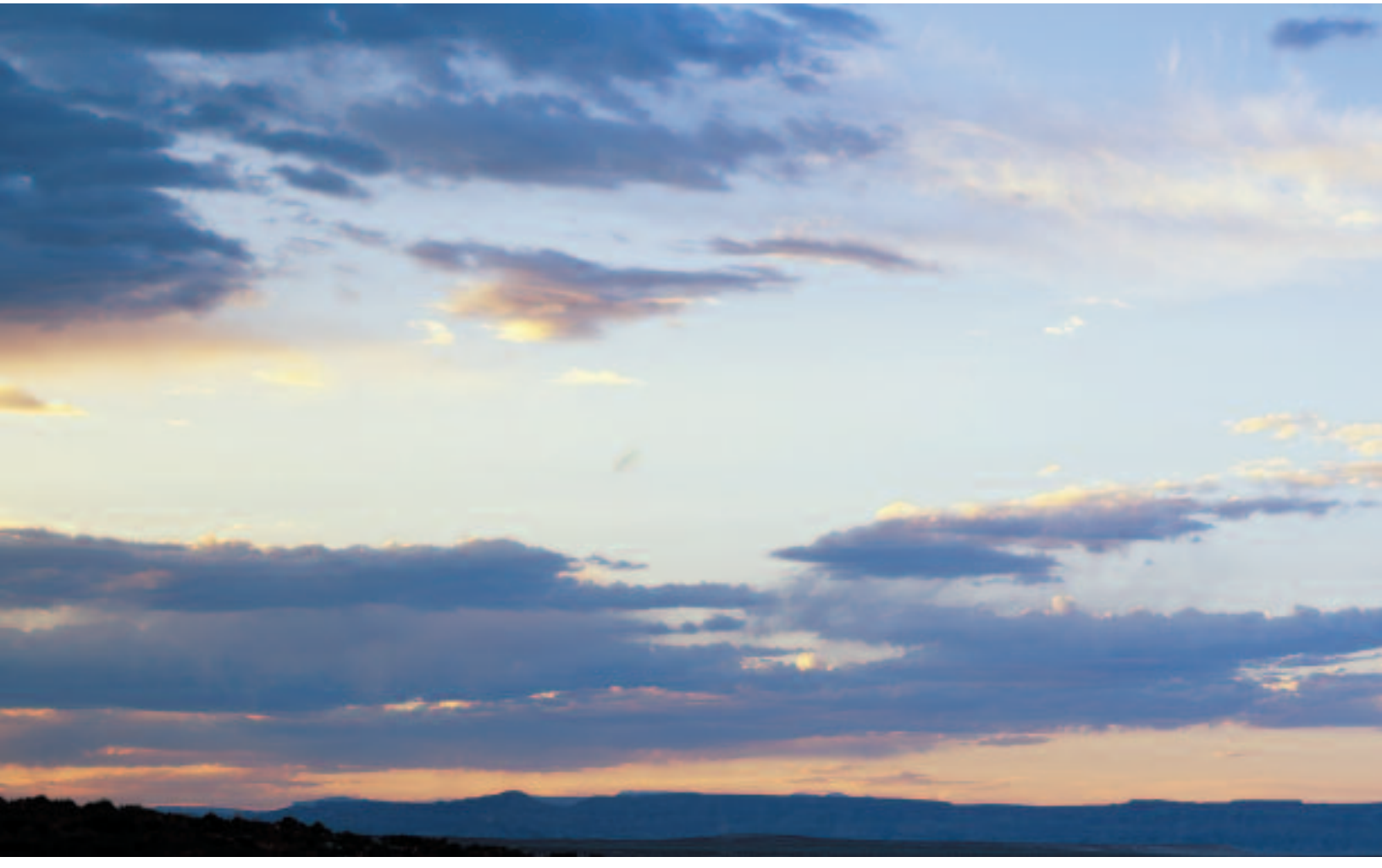

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* Joint venture

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Beauchemin Communication Marketing

Photos
Ronald Maisonneuve

Printing
Compuset

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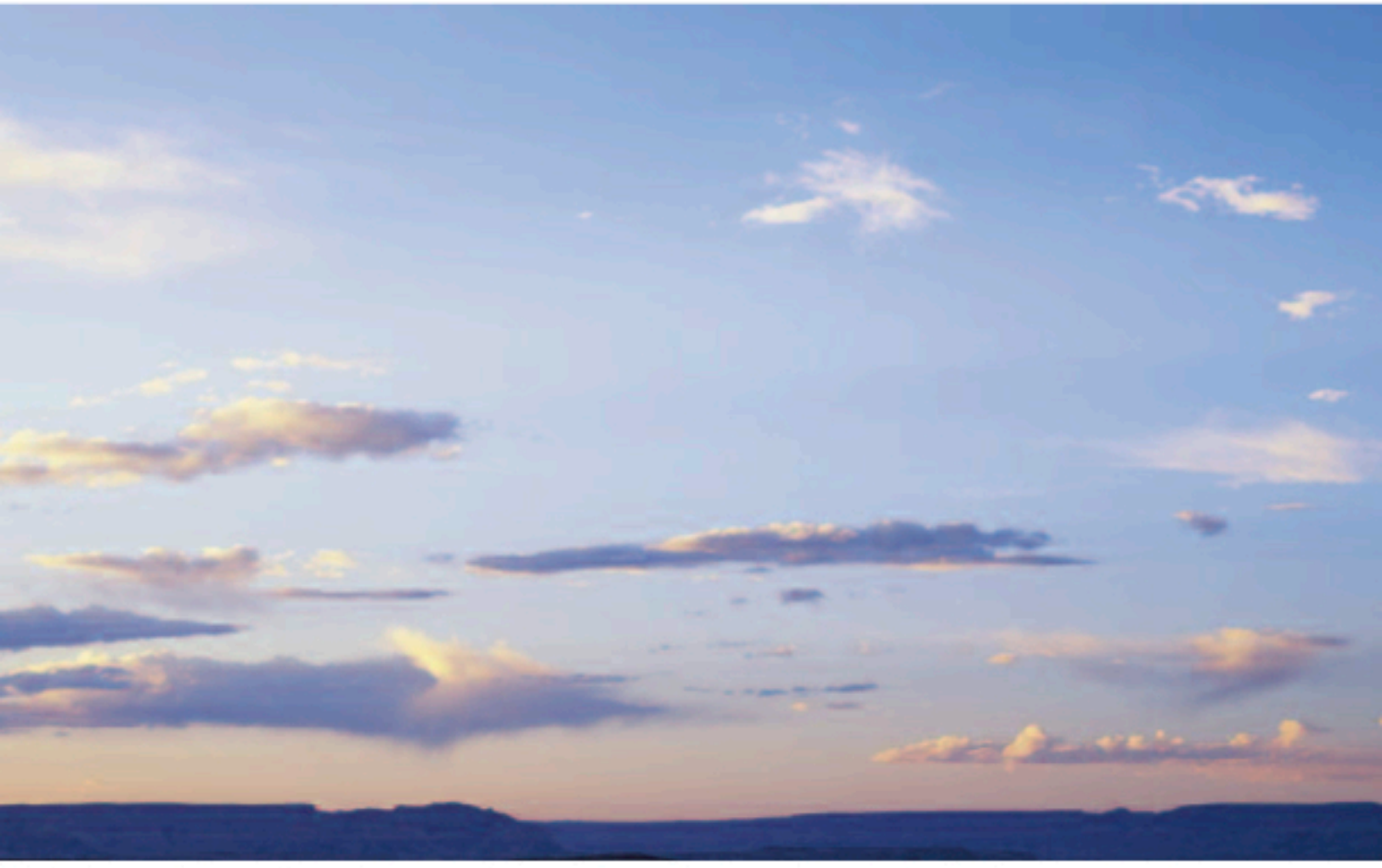


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