*Management's discussion and analysis (MD&A) relates to the financial condition and results of operations of Canadian National Railway Company (CN) together with its wholly owned subsidiaries, including the railroads and related holdings of Great Lakes Transportation LLC (GLT) as of May 10, 2004 and BC Rail as of July 14, 2004. As used herein, the word "Company" means, as the context requires, CN and its subsidiaries. CN's common shares are listed on the Toronto and New York stock exchanges. Except where otherwise indicated, all financial information reflected herein is expressed in Canadian dollars and determined on the basis of Canadian generally accepted accounting principles (Canadian GAAP). The Company also prepares consolidated financial statements in accordance with U.S. GAAP, which are different in some respects from these financial statements, principally in the treatment of track replacement costs, expenditures relating to improvements of bridges and other structures and freight cars, derivative instruments and stock-based compensation. A reconciliation of the Canadian to U.S. GAAP financial statements is provided in Note 21 to the Company's Consolidated Financial Statements. The Company's objective is to provide meaningful and relevant information reflecting the Company's financial condition and results of operations. In certain instances, the Company may make reference to certain non-GAAP measures that, from management's perspective, are useful measures of performance. In such instances, the reader is advised to read all information provided in the MD&A in conjunction with the Company's 2004 Annual Consolidated Financial Statements and notes thereto.*

**BUSINESS PROFILE**

CN, directly and through its subsidiaries, is engaged in the rail and related transportation business. CN's network of approximately 19,300 route miles of track spans Canada and mid-America, connecting three coasts: the Atlantic, the Pacific and the Gulf of Mexico. CN's revenues are derived from seven commodity groups consisting of the movement of a diversified and balanced portfolio of goods which positions it well to face economic fluctuations and enhances its potential to grow revenues. In 2004, no individual commodity group accounted for more than 22% of revenues. The sources of revenue also reflect a balanced mix of destinations. In 2004, 23% of revenues came from U.S. domestic traffic, 34% from transborder traffic, 23% from Canadian domestic traffic and 20% from overseas traffic. The Company originates approximately 85% of traffic moving along its network, which allows it both to capitalize on service advantages and build on opportunities to efficiently use assets.

**STRATEGY**

CN is committed to creating value for both its customers and shareholders. By providing quality and cost-effective service, CN seeks to create value for its customers, which solidifies existing customer relationships, while enabling it to pursue new ones. Sustainable financial performance is a critical element of shareholder value, which CN strives to achieve by pursuing revenue growth, steadily increasing profitability, solid free cash flow generation and an adequate return on investment. CN's business strategy is guided by five core values: providing good service, controlling costs, focusing on asset utilization, committing to safety and developing employees.

**OVERVIEW**

For 2005 and the foreseeable future, CN's challenge is to remain at the forefront of rail industry financial performance and to build value for shareholders and customers by aiming to make the railroad the continent's best-performing transportation company.

CN's plan is premised on the deployment of its business model to generate quality revenues, while leveraging capacity and maintaining its current level of plant quality.

The "scheduled railroad" is the foundation for the Company's business model. For CN's merchandise business, the scheduled railroad, which is defined as a trip plan for every car measured in hours, has reduced transit times, improved the consistency of CN's transportation product, dramatically improved productivity and helped to improve network capacity. In 2003, the Company began to apply the same principles of scheduled railroading to its intermodal business through the IMX initiative. IMX is designed to smooth demand and balance the flow of intermodal traffic through pre-defined daily train capacity, slot, gate and equipment reservations, and day-of-the-week pricing.

CN's acquisition and control of Illinois Central and Wisconsin Central, in 1999 and 2001, respectively, extended the Company's reach into the central and southern United States. Among the benefits of single line service afforded by these transactions have been improved transit and cycle times for freight cars and the penetration of new markets.

The acquisition of GLT in May 2004 has permitted new efficiencies in train operations north of Duluth/Superior in the key Winnipeg-Chicago corridor and positioned CN as a major player in the supply chain for the United States steel industry in the midst of a strong recovery. The purchase of BC Rail in July 2004 not only grew CN's forest products business substantially, but also expanded the railroad's capacity in British Columbia, where the Port of Prince Rupert has the potential to become an important gateway for traffic moving to and from Asia and the heartland of North America.

Over the past five years, the Company has also invested heavily in new locomotives and freight cars, extended sidings and centralized traffic control to permit the operation of longer, more efficient trains. These strategic initiatives have improved service, reduced costs and created a fluid North American rail network that can accommodate business growth at low incremental cost. The Company intends to continue to make targeted capital expenditures to improve plant capacity as warranted by market conditions and satisfactory returns on investment.

The Company intends to pursue further operating efficiencies by optimizing its workforce, improving asset utilization, reducing accidents and related costs, and continuing to focus on legal claims and health care costs. The Company partners with connecting carriers to implement routing protocol agreements for carload freight and pursues co-production initiatives to further improve service, generate system capacity and gradually reduce costs.

The Company's ultimate goal is to generate profitable, sustainable growth at low incremental cost by striving to improve yield and increase market share to maximize its return on assets.

**Financial highlights**

| *In millions, except per share data* | | **2004** | | 2003 | | 2002 |
|---|---|---|---|---|---|---|
| **Financial results** | | | | | | |
| Revenues | **$** | **6,548** | $ | 5,884 | $ | 6,110 |
| Operating income | **$** | **2,230** | $ | 1,368 | $ | 1,098 |
| Net income | **$** | **1,297** | $ | 734 | $ | 553 |
| Operating ratio | | **65.9%** | | 76.8% | | 82.0% |
| Basic earnings per share | **$** | **4.55** | $ | 2.56 | $ | 1.85 |
| Diluted earnings per share | **$** | **4.48** | $ | 2.52 | $ | 1.82 |
| Dividend declared per share | **$** | **0.78** | $ | 0.67 | $ | 0.57 |
| **Financial position** | | | | | | |
| Total assets | **$** | **19,271** | $ | 17,150 | $ | 18,924 |
| Total long-term financial liabilities | **$** | **9,665** | $ | 8,693 | $ | 10,108 |

## FINANCIAL RESULTS

### Change in property capitalization policy

Effective January 1, 2004, the Company changed its capitalization policy, on a prospective basis, to conform with the Canadian Institute of Chartered Accountants (CICA) Handbook Section 3061, "Properties, Plant and Equipment." The change was made in response to the CICA Handbook Section 1100, "Generally Accepted Accounting Principles," issued in July 2003, as explained in Note 2 – Accounting changes, of the Company's Annual Consolidated Financial Statements.

The Company's accounting for Properties had been based on the rules and regulations of the Canadian Transportation Agency's (CTA) Uniform Classification of Accounts, which for railways in Canada, were considered Canadian GAAP prior to the issuance of Section 1100. Under the CTA rules, the Company capitalized only the material component of track replacement costs, to the extent it met the Company's minimum threshold for capitalization. In accordance with the CICA Handbook Section 3061, "Properties, Plant and Equipment," the Company now capitalizes the cost of labor, material and related overhead associated with track replacement activities provided they meet the Company's minimum threshold for capitalization. Also, all major expenditures for work that extends the useful life and/or improves the functionality of bridges, other structures and freight cars, are capitalized. The change in policy had the effect of decreasing 2004 operating expenses by $464 million, $312 million after tax.

### 2004 compared to 2003

In 2004, net income increased by $563 million, or 77%, when compared to 2003, with diluted earnings per share rising 78%. Excluding the change in capitalization policy as discussed herein, net income increased by $251 million, or 34% , when compared to 2003.

Revenues increased by $664 million, or 11%, due to the inclusion of $351 million of GLT and BC Rail revenues, core business growth in a strong North American economy, and an improved Canadian grain crop, which were partly offset by the translation impact of the stronger Canadian dollar on U.S. dollar denominated revenues of $255 million.

Operating expenses decreased by $198 million, or 4%. The decrease was mainly due to the change in the property capitalization policy, which mainly affected labor, purchased services and material, and casualty and other, the translation impact of the stronger Canadian dollar on U.S. dollar denominated expenses of $170 million and lower equipment rents. Partly offsetting the decrease was the inclusion of GLT and BC Rail expenses of $228 million, and otherwise higher labor and fringe benefits, increased fuel costs and higher casualty and other expense.

The operating ratio, defined as operating expenses as a percentage of revenues, was 65.9% in 2004 compared to 76.8% in 2003, a 10.9-point betterment, mainly due to the change in the property capitalization policy.

The results for the year ended December 31, 2004 included the results of operations of GLT as of May 10, 2004 and BC Rail as of July 14, 2004. Also in 2004, a strike by the Company's employees represented by the Canadian Auto Workers (CAW) union (the "CAW strike") in the first quarter, negatively impacted operating income and net income by $35 million and $24 million, respectively. The significant appreciation in the Canadian dollar relative to the U.S. dollar which has impacted the conversion of the Company's U.S. dollar denominated revenues and expenses, resulted in a reduction in net income of approximately $45 million for 2004.

For the year ended December 31, 2003, the Company's results of operations included a fourth-quarter deferred income tax expense of $33 million resulting from the enactment of higher corporate tax rates in the province of Ontario.

**2004 compared to 2003 – Adjusted performance measures**

The year ended December 31, 2003 included an item impacting the comparability of the results of operations (see reconciliation of adjusted performance measures presented herein).

In 2003, the Company recorded a fourth-quarter deferred income tax expense of $33 million resulting from the enactment of higher corporate tax rates, as discussed herein.

Excluding this item, net income was $1,297 million ($4.55 per basic share or $4.48 per diluted share) in 2004 compared to adjusted net income of $767 million ($2.67 per basic share or $2.63 per diluted share) in 2003, an increase of $530 million, or 69%.

**Reconciliation of adjusted performance measures**

*Management believes that non-GAAP measures such as adjusted net income and the resulting adjusted performance measures for such items as operating income, operating ratio and per share data are useful measures of performance that can facilitate period-to-period comparisons as they exclude items that do not arise as part of the normal day-to-day operations or that could potentially distort the analysis of trends in business performance. The exclusion of specified items in the adjusted measures below does not imply that they are necessarily non-recurring. These adjusted measures do not have any standardized meaning prescribed by GAAP and may, therefore, not be comparable to similar measures presented by other companies. The reader is advised to read all information provided in the MD&A in conjunction with the Company's Annual Consolidated Financial Statements and notes thereto.*

*$ in millions, except per share data, or unless otherwise indicated*

| *Year ended December 31,* | 2004 | 2003 | | |
|---|---|---|---|---|
| | **Reported** | **Reported** | **Rate enactment** | **Adjusted** |
| Revenues | $ 6,548 | $ 5,884 | $ - | $ 5,884 |
| Operating expenses | 4,318 | 4,516 | - | 4,516 |
| **Operating income** | **2,230** | **1,368** | **-** | **1,368** |
| Interest expense | (282) | (317) | - | (317) |
| Other income (loss) | (20) | 21 | - | 21 |
| Income before income taxes | 1,928 | 1,072 | - | 1,072 |
| Income tax expense | (631) | (338) | 33 | (305) |
| **Net income** | **$ 1,297** | **$ 734** | **$ 33** | **$ 767** |
| **Operating ratio** | **65.9%** | **76.8%** | | **76.8%** |
| **Basic earnings per share** | **$ 4.55** | **$ 2.56** | | **$ 2.67** |
| **Diluted earnings per share** | **$ 4.48** | **$ 2.52** | | **$ 2.63** |

### Revenues

| Year ended December 31, | 2004 | 2003 | % Δ |
|---|---|---|---|
| Total revenues *(millions)* | **$ 6,548** | $ 5,884 | 11% |
| **Rail freight:** | | | |
| Revenues *(millions)* | **$ 6,252** | $ 5,694 | 10% |
| RTMs *(millions)* | **175,355** | 162,901 | 8% |
| Revenue/RTM *(cents)* | **3.57** | 3.50 | 2% |
| Carloads *(thousands)* | **4,654** | 4,177 | 11% |
| Revenue/Carload *(dollars)* | **1,343** | 1,363 | (1%) |

Revenues for the year ended December 31, 2004 totaled $6,548 million compared to $5,884 million in 2003. The increase of $664 million, or 11%, was mainly due to the inclusion of GLT and BC Rail revenues of $351 million, strong merchandise revenue, an improved Canadian grain crop, and a higher fuel surcharge. Partially offsetting these gains was the translation impact of the stronger Canadian dollar on U.S. dollar denominated revenue. Revenue ton miles, measuring the volume of freight transported by the Company, increased by 8% relative to 2003. Freight revenue per revenue ton mile, a measurement of yield defined as revenue earned on the movement of a ton of freight over one mile, increased by 2% when compared to 2003. In 2004, freight revenue per revenue ton mile was positively affected by freight rate increases and an overall decrease in the average length of haul, and was negatively affected by the translation impact of the stronger Canadian dollar.

### Petroleum and chemicals

| Year ended December 31, | 2004 | 2003 | % Δ |
|---|---|---|---|
| Revenues *(millions)* | **$ 1,123** | $ 1,058 | 6% |
| RTMs *(millions)* | **32,618** | 30,901 | 6% |
| Revenue/RTM *(cents)* | **3.44** | 3.42 | 1% |

Petroleum and chemicals comprise a wide range of commodities, including chemicals, sulfur, plastics, petroleum and gas products. Most of the Company's petroleum and chemicals shipments originate in the Gulf of Mexico, Alberta and eastern Canada, and are destined for customers in Canada, the United States and overseas. The performance of this commodity group is closely correlated with the North American economy. For the year ended December 31, 2004, revenues for this commodity group increased by $65 million, or 6%, from 2003. The increase was due to freight rate improvements in several key segments, particularly in the first half of the year, the inclusion of $25 million of BC Rail revenues (primarily sulfur), higher offshore demand for Canadian sulfur, a shift from offshore to Canadian suppliers for petroleum gas and a higher fuel surcharge. These gains were partially offset by the translation impact of the stronger Canadian dollar. Freight revenue per revenue ton mile increased by 1% due to freight rate improvements and a decrease in the average length of haul, partly offset by the translation impact of the stronger Canadian dollar.

| | Percentage of revenues |
|---|---|
| Petroleum and plastics | 57% |
| Chemicals | 43% |

| | 2000 | 2001 | 2002 | 2003 | 2004 |
|---|---|---|---|---|---|
| Carloads* *(In thousands)* | 512 | 519 | 587 | 604 | 637 |

**Includes Wisconsin Central Transportation Corporation (WC) from October 9, 2001, GLT from May 10, 2004 and BC Rail from July 14, 2004.*

### Metals and minerals

| Year ended December 31, | 2004 | 2003 | % Δ |
|---|---|---|---|
| Revenues *(millions)* | **$ 713** | $ 527 | 35% |
| RTMs *(millions)* | **16,421** | 13,876 | 18% |
| Revenue/RTM *(cents)* | **4.34** | 3.80 | 14% |

The metals and minerals commodity group consists primarily of nonferrous base metals, iron ore, steel, equipment and parts and construction materials. The Company's superior rail access to major mines, ports and smelters throughout North America has made the Company a transportation leader of copper, lead, zinc concentrates, iron ore, refined metals and aluminum. Construction materials are mainly aggregates (stone and sand) and cement. The Company has access to major cement and aggregate producers in Canada as well as in the U.S. Metals and minerals traffic is sensitive to fluctuations in the economy. For the year ended December 31, 2004, revenues for this commodity group increased by $186 million, or 35%, from 2003. The increase is mainly due to the inclusion of $126 million of GLT revenues, higher volumes of iron ore, largely from new business, freight rate improvements, and increased shipments of raw materials and metal bars. Partially offsetting these gains was the translation impact of the stronger Canadian dollar. Revenue per revenue ton mile increased by 14% in 2004, mainly due to GLT shorter-haul traffic which was partly offset by the translation impact of the stronger Canadian dollar.

| | Percentage of revenues |
|---|---|
| Metals | 55% |
| Minerals | 24% |
| Iron ore | 21% |

| | 2000 | 2001 | 2002 | 2003 | 2004 |
|---|---|---|---|---|---|
| Carloads* *(In thousands)* | 256 | 287 | 388 | 396 | 809 |

**Includes WC from October 9, 2001, GLT from May 10, 2004 and BC Rail from July 14, 2004.*

### Forest products

| Year ended December 31, | 2004 | 2003 | % Δ |
|---|---|---|---|
| Revenues *(millions)* | **$ 1,452** | $ 1,284 | 13% |
| RTMs *(millions)* | **38,414** | 34,516 | 11% |
| Revenue/RTM *(cents)* | **3.78** | 3.72 | 2% |

The forest products commodity group includes various types of lumber, panels, wood chips, wood pulp, printing paper, linerboard and newsprint. The Company has superior rail access to the western and eastern Canadian fiber-producing regions, which are among the largest fiber source areas in North America. In the United States, the Company is strategically located to serve both the midwest and southern U.S. corridors with interline capabilities to other Class 1 railroads. The key drivers for the various commodities are: for newsprint, advertising lineage and overall economic conditions in the United States; for fibers (mainly wood pulp), the consumption of paper worldwide; and for lumber and panels, housing starts and renovation activities in the United States. Although demand for forest products can be cyclical, the Company's geographical advantages and product diversity tend to reduce the impact of market fluctuations. For the year ended December 31, 2004, revenues for this commodity group increased by $168 million, or 13%, from 2003. The increase was largely due to the inclusion of $85 million of BC Rail revenues (mainly lumber and panels), continued solid demand for lumber, freight rate improvements and a higher fuel surcharge. The translation impact of the stronger Canadian dollar partially offset these gains. Revenue per revenue ton mile increased by 2% in 2004 as the benefit of freight rate improvements and a positive change in traffic mix were partially offset by the translation impact of the stronger Canadian dollar.

| | Percentage of revenues |
|---|---|
| Lumber | 33% |
| Fibers | 29% |
| Paper | 26% |
| Panels | 12% |

| | 2000 | 2001 | 2002 | 2003 | 2004 |
|---|---|---|---|---|---|
| Carloads* *(In thousands)* | 486 | 501 | 600 | 594 | 653 |

**Includes WC from October 9, 2001, GLT from May 10, 2004 and BC Rail from July 14, 2004.*

### Coal

| Year ended December 31, | 2004 | 2003 | % Δ |
|---|---|---|---|
| Revenues *(millions)* | **$ 284** | $ 261 | 9% |
| RTMs *(millions)* | **13,614** | 13,659 | - |
| Revenue/RTM *(cents)* | **2.09** | 1.91 | 9% |

The coal commodity group consists primarily of thermal grades of bituminous coal. Canadian thermal coal is delivered to power utilities primarily in eastern Canada, while in the United States, thermal coal is transported from mines served in southern Illinois, or from western U.S. mines via interchange with other railroads, to major utilities in the Midwest and southeast United States. The coal business also includes the transport of metallurgical coal, which is largely exported to steel markets in Japan and other Asian markets. For the year ended December 31, 2004, revenues for this commodity group increased by $23 million, or 9%, from 2003. The increase was due to higher coal shipments to U.S. utilities and the inclusion of GLT and BC Rail revenues of $20 million, partly offset by metallurgical mine closures in western Canada and the translation impact of the stronger Canadian dollar. The revenue per revenue ton mile increase of 9% was mainly due to a decrease in the average length of haul and a positive change in traffic mix that were partly offset by the translation impact of the stronger Canadian dollar.

| | Percentage of revenues |
|---|---|
| Coal | 82% |
| Petroleum coke | 18% |

| | 2000 | 2001 | 2002 | 2003 | 2004 |
|---|---|---|---|---|---|
| Carloads* *(In thousands)* | 528 | 517 | 499 | 471 | 486 |

**Includes WC from October 9, 2001, GLT from May 10, 2004 and BC Rail from July 14, 2004.*

### Grain and fertilizers

| Year ended December 31, | 2004 | 2003 | % Δ |
|---|---|---|---|
| Revenues *(millions)* | **$ 1,053** | $ 938 | 12% |
| RTMs *(millions)* | **39,965** | 35,556 | 12% |
| Revenue/RTM *(cents)* | **2.63** | 2.64 | - |

The grain and fertilizers commodity group depends primarily on crops grown and fertilizers processed in western Canada and the U.S. Midwest. The grain segment consists of three primary commodities: food grains, mainly wheat; oilseeds and oilseed products, primarily canola seed, oil and meal; and feed grains, including feed barley, feed wheat and corn. Production of grain varies considerably from year to year, affected primarily by weather conditions. Grain exports are volatile, reflecting the size of the crop produced, international market conditions and foreign government policy. In the U.S., grain grown in Illinois and Iowa is exported, as well as transported to domestic processing facilities and feed markets. The Company also serves producers of potash, ammonium nitrate, urea and other fertilizers. For the year ended December 31, 2004, revenues for this commodity group increased by $115 million, or 12%, from 2003. The increase reflects higher

Canadian wheat and barley exports, which was partially offset by weak shipments of U.S. soybeans due to tight supply, a shift in exports from the Gulf to the Pacific Northwest and the translation impact of the stronger Canadian dollar. Revenue per revenue ton mile remained flat as the benefit of freight rate improvements was offset by an increase in the average length of haul and the translation impact of the stronger Canadian dollar.

| | Percentage of revenues |
|---|---|
| Food grain | 28% |
| Oilseeds | 24% |
| Feed grain | 23% |
| Fertilizers | 13% |
| Potash | 12% |

| | 2000 | 2001 | 2002 | 2003 | 2004 |
|---|---|---|---|---|---|
| Carloads* *(In thousands)* | 567 | 590 | 535 | 548 | 572 |

**Includes WC from October 9, 2001, GLT from May 10, 2004 and BC Rail from July 14, 2004.*

**Intermodal**

| *Year ended December 31,* | **2004** | 2003 | % Δ |
|---|---|---|---|
| Revenues *(millions)* | **$ 1,117** | $ 1,101 | 1% |
| RTMs *(millions)* | **31,002** | 31,168 | (1%) |
| Revenue/RTM *(cents)* | **3.60** | 3.53 | 2% |

The intermodal commodity group is comprised of two segments: domestic and international. The domestic segment is responsible for consumer products and manufactured goods, operating through both retail and wholesale channels while the international segment handles import and export container traffic, serving the ports of Vancouver, Montreal, Halifax and New Orleans. The domestic segment is driven by consumer markets, with growth generally tied to the economy. The international segment is driven mainly by North American economic conditions. For the year ended December 31, 2004, revenues for this commodity group increased by $16 million, or 1%, from 2003. Revenues for 2004 benefited from heavy import volumes through the Port of Vancouver, freight rate improvements and a higher fuel surcharge. Revenues were negatively affected by the first quarter CAW strike, the closure of the Company's smaller terminal facilities in the U.S., the discontinuance of the Roadrailer service and the translation impact of the stronger Canadian dollar. Revenue per revenue ton mile increased by 2% in 2004 driven by a positive change in traffic mix and freight rate improvements that were partly offset by an increase in the average length of haul and the translation impact of the stronger Canadian dollar.

| | Percentage of revenues |
|---|---|
| Domestic | 52% |
| International | 48% |

| | 2000 | 2001 | 2002 | 2003 | 2004 |
|---|---|---|---|---|---|
| Carloads* *(In thousands)* | 1,121 | 1,103 | 1,237 | 1,276 | 1,202 |

**Includes WC from October 9, 2001, GLT from May 10, 2004 and BC Rail from July 14, 2004.*

**Automotive**

| *Year ended December 31,* | **2004** | 2003 | % Δ |
|---|---|---|---|
| Revenues *(millions)* | **$ 510** | $ 525 | (3%) |
| RTMs *(millions)* | **3,321** | 3,225 | 3% |
| Revenue/RTM *(cents)* | **15.36** | 16.28 | (6%) |

The automotive commodity group moves both finished vehicles and parts, originating in southwestern Ontario, Michigan and Mississippi, destined for the United States, Canada and Mexico. The Company's broad coverage, including its access to all of the Canadian assembly plants, enables it to consolidate full trainloads of automotive traffic for delivery to connecting railroads at key interchange points. The Company also serves shippers of import vehicles via the ports of Halifax and Vancouver, and through interchange with other railroads. The Company's automotive revenues are closely correlated to automotive production and sales in North America. For the year ended December 31, 2004, revenues for this commodity group decreased by $15 million, or 3%, from 2003. The decrease was due to the translation impact of the stronger Canadian dollar that was partially offset by the benefit of new finished vehicle traffic that began in late 2003. Revenue per revenue ton mile decreased by 6% in 2004 due to the translation impact of the stronger Canadian dollar.

| | Percentage of revenues |
|---|---|
| Finished vehicles | 82% |
| Auto parts | 18% |

| | 2000 | 2001 | 2002 | 2003 | 2004 |
|---|---|---|---|---|---|
| Carloads* *(In thousands)* | 318 | 288 | 307 | 288 | 295 |

**Includes WC from October 9, 2001, GLT from May 10, 2004 and BC Rail from July 14, 2004.*

**Other**

In 2004, other revenues increased by $106 million, when compared to 2003, mainly due to revenues from GLT's maritime division of $90 million.

**Operating expenses**

Operating expenses amounted to $4,318 million in 2004 compared to $4,516 million in 2003. The decrease was mainly due to the change in the property capitalization policy of $464 million, which mainly affected labor, purchased services and material, and casualty and other, the translation impact of the stronger Canadian dollar and lower equipment rents. Partly offsetting the decrease was the inclusion of GLT and BC Rail expenses of $228 million, higher labor and fringe benefits, increased fuel costs and higher casualty and other expense. The month-long CAW strike had a minimal impact on overall operating expenses for the year ended December 31, 2004 as the benefit from lower labor and fringe benefit expenses was mostly offset by increases in other expense categories.

| *In millions* | *Year ended December 31,* | **2004** | | 2003 | |
|---|---|---|---|---|---|
| | | **Amount** | **% of revenue** | Amount | % of revenue |
| Labor and fringe benefits | | **$ 1,838** | **28.0%** | $ 1,929 | 32.8% |
| Purchased services and material | | **746** | **11.4%** | 879 | 15.0% |
| Depreciation and amortization | | **517** | **7.9%** | 472 | 8.0% |
| Fuel | | **528** | **8.1%** | 471 | 8.0% |
| Equipment rents | | **244** | **3.7%** | 299 | 5.1% |
| Casualty and other | | **445** | **6.8%** | 466 | 7.9% |
| *Total* | | **$ 4,318** | **65.9%** | $ 4,516 | 76.8% |

***Labor and fringe benefits:*** Labor and fringe benefits includes wages, payroll taxes, and employee benefits such as incentive compensation, stock-based compensation, health and welfare, pensions and other post-employment benefits. These expenses decreased by $91 million, or 5%, in 2004 as compared to 2003. The decrease was mainly due to the change in the property capitalization policy of $204 million, the translation impact of the stronger Canadian dollar, the effects of a reduced workforce, lower expenses for pensions and other post-retirement benefits and wage and benefits savings during the CAW strike. Partly offsetting the decrease was the inclusion of GLT and BC Rail labor expense of $91 million, higher wages and employee benefits, including increased costs for stock-based compensation, and charges and adjustments relating to the workforce reduction provision.

***Purchased services and material:*** Purchased services and material primarily includes the costs of services purchased from outside contractors, materials used in the maintenance of the Company's track, facilities and equipment, transportation and lodging for train crew employees, utility costs and the net costs of operating facilities jointly used by the Company and other railroads. These expenses decreased by $133 million, or 15%, in 2004 as compared to 2003. The decrease was mainly due to the change in the property capitalization policy of $176 million, the translation impact of the stronger Canadian dollar and lower net expenses for operating joint facilities. Partly offsetting the decrease was the inclusion of $77 million of GLT and BC Rail expenses, higher repair and maintenance expenses, partly related to the CAW strike, and other strike-related costs.

***Depreciation and amortization:*** Depreciation and amortization relates to the Company's rail operations. These expenses increased by $45 million, or 10%, in 2004 as compared to 2003. The increase was mainly due to the inclusion of GLT and BC Rail expenses of $30 million and the impact of net capital additions, partially offset by the translation impact of the stronger Canadian dollar.

***Fuel:*** Fuel expense includes the cost of fuel consumed by locomotives, intermodal equipment and other vehicles. These expenses increased by $57 million, or 12%, in 2004 as compared to 2003. The increase was mainly due to a higher average price per gallon, net of the impact of the hedging program, the inclusion of GLT and BC Rail expenses of $21 million and higher volumes. The increase was partly offset by the translation impact of the stronger Canadian dollar, increased productivity and a fuel excise tax refund in the second quarter.

***Equipment rents:*** Equipment rents includes rental expense for the use of freight cars owned by other railroads or private companies and for the short or long-term lease of freight cars, locomotives and intermodal equipment, net of rental income from other railroads for the use of the Company's cars and locomotives. These expenses decreased by $55 million, or 18%, in 2004 as compared to 2003. The decrease was due to higher car hire income, including that of BC Rail, the translation impact of the stronger Canadian dollar and a reduction in car hire expenses that were partly offset by higher lease expense for freight cars.

***Casualty and other:*** Casualty and other includes expenses for personal injuries, environmental, freight and property damage, insurance, bad debt and operating taxes, as well as travel and travel-related expenses. These expenses decreased by $21 million, or 5%, in 2004 as compared to 2003. The decrease was due to the change in the property capitalization policy of $76 million and the translation impact of the stronger Canadian dollar. Partly offsetting the decrease were higher expenses for personal injuries, the inclusion of

GLT and BC Rail expenses of $14 million, increased environmental expenses and favorable adjustments to U.S. property taxes in 2003.

**Other**

***Interest expense:*** Interest expense decreased by $35 million, or 11%, for the year ended December 31, 2004 as compared to 2003. The decrease was due to lower interest rates on issued debt to replace matured debt, a realized gain on the settlement of interest rate swaps and the translation impact of the stronger Canadian dollar that were partly offset by interest expense on debt related to the Company's recent acquisitions.

***Other income (loss):*** In 2004, the Company recorded a loss of $20 million compared to income of $21 million in 2003. The change from income to loss in 2004 was due to lower gains on disposal of surplus properties and lower equity income from the Company's investment in English Welsh and Scottish Railway (EWS) as a result of restructured operations.

***Income tax expense:*** The Company recorded income tax expense of $631 million for the year ended December 31, 2004 compared to $338 million in 2003. The effective tax rate for the year ended December 31, 2004 was 32.7% compared to 31.5% in 2003. The increase in the effective tax rate in 2004 was mainly due to higher pre-tax income generated in the current year, which was primarily a result of the change in capitalization policy.

**2003 compared to 2002**

For the year ended December 31, 2003, the Company recorded consolidated net income of $734 million ($2.56 per basic share) compared to $553 million ($1.85 per basic share) for the year ended December 31, 2002. Diluted earnings per share were $2.52 for 2003 compared to $1.82 in 2002. The Company's operating income for 2003 was $1,368 million compared to $1,098 million in 2002, and its operating ratio, defined as operating expenses as a percentage of revenues, was 76.8% in 2003 compared to 82.0% in 2002 (see discussion on adjusted performance measures herein).

**2003 compared to 2002 – Adjusted performance measures**

The years ended December 31, 2003 and 2002 included items impacting the comparability of the results of operations (see reconciliation of adjusted performance measures presented herein).

In 2003, the Company recorded a fourth quarter deferred income tax expense of $33 million resulting from the enactment of higher corporate tax rates in the province of Ontario. The year ended December 31, 2002 included fourth quarter charges of $281 million, or $173 million after tax, to increase the Company's provision for U.S. personal injury and other claims, and $120 million, or $79 million after tax, for workforce reductions.

Excluding these items, adjusted net income was $767 million ($2.67 per basic share or $2.63 per diluted share) in 2003 compared to adjusted net income of $805 million ($2.71 per basic share or $2.65 per diluted share) for 2002, a decrease of $38 million, or 5%. Operating income for 2003 decreased by $131 million, or 9%, compared to adjusted operating income of $1,499 million for 2002. The operating ratio for 2003 was 76.8% compared to the adjusted operating ratio of 75.5% in 2002, a 1.3-point increase.

The decrease in adjusted net income and adjusted operating income in 2003 was due to the significant year-over-year appreciation in the Canadian dollar relative to the U.S. dollar. This significant appreciation in the Canadian dollar impacted the conversion of the Company's U.S. dollar denominated revenues and expenses and accordingly, reduced revenues, operating income and net income by approximately $380 million, $110 million and $55 million, respectively. This decrease in adjusted net income was partly offset by net deferred income tax recoveries of $44 million in 2003 relating mainly to the resolution of matters pertaining to prior years' income taxes.

**Reconciliation of adjusted performance measures**

*Management believes that non-GAAP measures such as adjusted net income and the resulting adjusted performance measures for such items as operating income, operating ratio and per share data are useful measures of performance that can facilitate period-to-period comparisons as they exclude items that do not arise as part of the normal day-to-day operations or that could potentially distort the analysis of trends in business performance. The exclusion of specified items in the adjusted measures below does not imply that they are necessarily non-recurring. These adjusted measures do not have any standardized meaning prescribed by GAAP and may, therefore, not be comparable to similar measures presented by other companies. The reader is advised to read all information provided in the MD&A in conjunction with the Company's Annual Consolidated Financial Statements and notes thereto.*

*$ in millions, except per share data, or unless otherwise indicated*

| *Year ended December 31,* | **2003** | | | **2002** | | | |
|---|---|---|---|---|---|---|---|
| | **Reported** | **Rate enactment** | **Adjusted** | **Reported** | **Personal injury charge** | **Workforce reductions** | **Adjusted** |
| Revenues | $ 5,884 | $ - | $ 5,884 | $ 6,110 | $ - | $ - | $ 6,110 |
| Operating expenses | 4,516 | - | 4,516 | 5,012 | (281) | (120) | 4,611 |
| **Operating income** | **1,368** | **-** | **1,368** | **1,098** | **281** | **120** | **1,499** |
| Interest expense | (317) | - | (317) | (353) | - | - | (353) |
| Other income | 21 | - | 21 | 76 | - | - | 76 |
| Income before income taxes | 1,072 | - | 1,072 | 821 | 281 | 120 | 1,222 |
| Income tax expense | (338) | 33 | (305) | (268) | (108) | (41) | (417) |
| **Net income** | **$ 734** | **$ 33** | **$ 767** | **$ 553** | **$ 173** | **$ 79** | **$ 805** |
| **Operating ratio** | **76.8%** | | **76.8%** | **82.0%** | | | **75.5%** |
| **Basic earnings per share** | **$ 2.56** | | **$ 2.67** | **$ 1.85** | | | **$ 2.71** |
| **Diluted earnings per share** | **$ 2.52** | | **$ 2.63** | **$ 1.82** | | | **$ 2.65** |

### Revenues

| *Year ended December 31,* | 2003 | 2002 | % Δ |
|---|---|---|---|
| Total revenues *(millions)* | $ 5,884 | $ 6,110 | (4%) |
| **Rail freight:** | | | |
| Revenues *(millions)* | $ 5,694 | $ 5,901 | (4%) |
| RTMs *(millions)* | 162,901 | 159,259 | 2% |
| Revenue/RTM *(cents)* | 3.50 | 3.71 | (6%) |
| Carloads *(thousands)* | 4,177 | 4,153 | 1% |
| Revenue/Carload *(dollars)* | 1,363 | 1,421 | (4%) |

Revenues for the year ended December 31, 2003 totaled $5,884 million compared to $6,110 million in 2002. The decrease of $226 million, or 4%, was mainly due to the higher Canadian dollar, which negatively impacted the translation of U.S. dollar denominated revenue, continued weakness in coal shipments and a slowdown in the automotive sector. Partially offsetting these losses were increased intermodal, metals and minerals and petroleum and chemicals volumes. For 2003, revenue ton miles, measuring the volume of freight transported by the Company, increased by 2% relative to 2002. Freight revenue per revenue ton mile, a measurement of yield defined as revenue earned on the movement of a ton of freight over one mile, decreased by 6% when compared to 2002, reflecting the higher Canadian dollar.

### Petroleum and chemicals

| *Year ended December 31,* | 2003 | 2002 | % Δ |
|---|---|---|---|
| Revenues *(millions)* | $ 1,058 | $ 1,102 | (4%) |
| RTMs *(millions)* | 30,901 | 30,006 | 3% |
| Revenue/RTM *(cents)* | 3.42 | 3.67 | (7%) |

Revenues for the year ended December 31, 2003 decreased by $44 million, or 4%, from 2002. The decrease was due to the translation impact of the stronger Canadian dollar, partially offset by higher U.S. and offshore demand for Canadian sulfur and strong demand for liquefied petroleum gas due to cold weather conditions at the beginning of 2003. Revenue per revenue ton mile decreased by 7% from 2002 due to the translation impact of the stronger Canadian dollar.

### Metals and minerals

| *Year ended December 31,* | 2003 | 2002 | % Δ |
|---|---|---|---|
| Revenues *(millions)* | $ 527 | $ 521 | 1% |
| RTMs *(millions)* | 13,876 | 13,505 | 3% |
| Revenue/RTM *(cents)* | 3.80 | 3.86 | (2%) |

Revenues for the year ended December 31, 2003 increased by $6 million, or 1%, from 2002. The increase was due to improved market conditions and increased market share for steel in 2003 and new ore traffic which began in the second quarter of 2002 and the last quarter of 2003. These gains were largely offset by the translation impact of the stronger Canadian dollar. Revenue per revenue ton mile decreased by 2% from 2002 due to the translation impact of the stronger Canadian dollar which was partially offset by a positive change in traffic mix.

### Forest products

| *Year ended December 31,* | 2003 | 2002 | % Δ |
|---|---|---|---|
| Revenues *(millions)* | $ 1,284 | $ 1,323 | (3%) |
| RTMs *(millions)* | 34,516 | 33,551 | 3% |
| Revenue/RTM *(cents)* | 3.72 | 3.94 | (6%) |

Revenues for the year ended December 31, 2003 decreased by $39 million, or 3%, from 2002. The decrease was due to the translation impact of the stronger Canadian dollar that was partially offset by solid demand for lumber and pulp and paper. Revenue per revenue ton mile decreased by 6% from 2002 due to the translation impact of the stronger Canadian dollar which more than offset the continued improvement in pricing and a positive change in traffic mix.

### Coal

| *Year ended December 31,* | 2003 | 2002 | % Δ |
|---|---|---|---|
| Revenues *(millions)* | $ 261 | $ 326 | (20%) |
| RTMs *(millions)* | 13,659 | 13,886 | (2%) |
| Revenue/RTM *(cents)* | 1.91 | 2.35 | (19%) |

Revenues for the year ended December 31, 2003 decreased by $65 million, or 20%, from 2002. The decrease was due to reduced coal production in western Canada, the translation impact of the stronger Canadian dollar and a metallurgical mine closure. Revenue per revenue ton mile decreased by 19% from 2002 mainly due to a change in traffic mix, an increase in the average length of haul, and the translation impact of the stronger Canadian dollar.

### Grain and fertilizers

| *Year ended December 31,* | 2003 | 2002 | % Δ |
|---|---|---|---|
| Revenues *(millions)* | $ 938 | $ 986 | (5%) |
| RTMs *(millions)* | 35,556 | 35,773 | (1%) |
| Revenue/RTM *(cents)* | 2.64 | 2.76 | (4%) |

Revenues for the year ended December 31, 2003 decreased by $48 million, or 5%, from 2002. The decrease was mainly due to the translation impact of the stronger Canadian dollar and a decrease in Canadian export wheat shipments due to the smaller 2002/2003

Canadian crop. Partially offsetting these decreases were increased Canadian canola shipments and strong U.S. corn shipments to North American markets. Revenue per revenue ton mile decreased by 4% from 2002 as the translation impact of the stronger Canadian dollar was partially offset by a decrease in the average length of haul.

**Intermodal**

| *Year ended December 31,* | 2003 | 2002 | *% Δ* |
|---|---|---|---|
| Revenues *(millions)* | $ 1,101 | $ 1,052 | 5% |
| RTMs *(millions)* | 31,168 | 29,257 | 7% |
| Revenue/RTM *(cents)* | 3.53 | 3.60 | (2%) |

Revenues for the year ended December 31, 2003 increased by $49 million, or 5%, from 2002. The increase was mainly due to increased import volumes, the higher fuel surcharge in 2003 to offset the significant increase in fuel costs and new traffic through the Port of Vancouver. Partially offsetting these gains was reduced traffic in the domestic segment due to the closure of smaller terminal facilities in the U.S. Revenue per revenue ton mile decreased by 2% from 2002 due to the translation impact of the stronger Canadian dollar and an increase in the average length of haul, partially offset by the higher fuel surcharge.

**Automotive**

| *Year ended December 31,* | 2003 | 2002 | *% Δ* |
|---|---|---|---|
| Revenues *(millions)* | $ 525 | $ 591 | (11%) |
| RTMs *(millions)* | 3,225 | 3,281 | (2%) |
| Revenue/RTM *(cents)* | 16.28 | 18.01 | (10%) |

Revenues for the year ended December 31, 2003 decreased by $66 million, or 11%, from 2002. The decrease was primarily due to the translation impact of the stronger Canadian dollar, weaker North American vehicle sales and production, and a change in shipping patterns for a significant customer. Revenue per revenue ton mile decreased by 10% from 2002 mainly due to the translation impact of the stronger Canadian dollar and a significant increase in the average length of haul.

**Operating expenses**

Operating expenses amounted to $4,516 million in 2003 compared to $5,012 million in 2002. The decrease was mainly due to the charges recorded in the fourth quarter of 2002 for personal injury and other claims and workforce reductions, and the translation impact of the stronger Canadian dollar on U.S. dollar denominated expenses. Partly offsetting these decreases were higher casualty and other expenses and higher fuel costs.

| *In millions* *Year ended December 31,* | | 2003 | | | 2002 | |
|---|---|---|---|---|---|---|
| | | Amount | % of revenue | | Amount | % of revenue |
| Labor and fringe benefits | $ | 1,929 | 32.8% | $ | 2,069 | 33.9% |
| Purchased services and material | | 879 | 15.0% | | 908 | 14.9% |
| Depreciation and amortization | | 472 | 8.0% | | 499 | 8.1% |
| Fuel | | 471 | 8.0% | | 459 | 7.5% |
| Equipment rents | | 299 | 5.1% | | 353 | 5.8% |
| Casualty and other | | 466 | 7.9% | | 724 | 11.8% |
| *Total* | $ | 4,516 | 76.8% | $ | 5,012 | 82.0% |

*Labor and fringe benefits:* Labor and fringe benefits expenses in 2003 decreased by $140 million, or 7%, as compared to 2002. The decrease was mainly due to the workforce reduction charge of $120 million recorded in the fourth quarter of 2002, the effects of a reduced workforce and the translation impact of the stronger Canadian dollar. Higher wages and employee benefits, including increased costs for pensions resulting from a change in management's assumption for the expected long-term rate of return on pension plan assets from 9% to 8%, partly offset the decrease.

In 2002, the Company had recorded a workforce reduction charge of $120 million in a renewed drive to improve productivity across all its corporate and operating functions. Reductions relating to this initiative and the 2001 workforce reduction charge of $98 million were completed in 2003. The charges included payments for severance, early retirement incentives and bridging to early retirement to be made to affected employees.

*Purchased services and material:* Purchased services and material expenses in 2003 decreased by $29 million, or 3%, as compared to 2002. The decrease was mainly due to lower expenses for consulting and professional services, lower discretionary spending (courier, communication charges, occupancy costs, etc.), reflecting the Company's continued focus on cost containment, and the translation impact of the stronger Canadian dollar. Higher repair expenses for rolling stock partly offset the decrease.

*Depreciation and amortization:* Depreciation and amortization expenses in 2003 decreased by $27 million, or 5%, as compared to 2002, mainly due to the translation impact of the stronger Canadian dollar.

*Fuel:* Fuel expense in 2003 increased by $12 million, or 3%, as compared to 2002. The increase was mainly due to a higher average price per gallon, net of the impact of the hedging program, and higher volumes. These increases were partly offset by the translation impact of the stronger Canadian dollar.

*Equipment rents:* Equipment rents in 2003 decreased by $54 million, or 15%, as compared to 2002. The decrease was due to the Company's continued focus on asset utilization, which resulted in lower lease expense for freight cars and locomotives and a reduction in net car hire expense. Also contributing to the decrease was the translation impact of the stronger Canadian dollar and a reduction in intermodal car hire rates.

*Casualty and other:* Casualty and other expenses in 2003 decreased by $258 million, or 36%, as compared to 2002, which included a fourth quarter charge of $281 million to increase the provision for U.S. personal injury and other claims. Excluding this charge, the increase was mainly due to higher expenses for personal injury claims and increased insurance premiums. Partly offsetting the increase were lower travel-related expenses and lower provincial capital taxes.

Other

*Interest expense:* Interest expense decreased by $36 million to $317 million for the year ended December 31, 2003 as compared to 2002. The decrease was mainly due to the translation impact of the stronger Canadian dollar and lower interest rates on new debt to replace matured debt.

*Other income:* In 2003, the Company recorded other income of $21 million compared to $76 million in 2002. The decrease was mainly due to lower right of way fees due to the termination of a contract in late 2002, lower income from the Company's equity investments, and realized foreign exchange losses in 2003.

*Income tax expense:* The Company recorded income tax expense of $338 million for the year ended December 31, 2003 compared to $268 million in 2002. The effective tax rate for the year ended December 31, 2003 was 31.5% compared to 32.6% in 2002. The decrease was mainly due to net favorable adjustments relating to the resolution of matters pertaining to prior years' income taxes of $44 million and lower corporate income tax rates in Canada. Partly offsetting the decrease was a $33 million deferred income tax expense recorded in the fourth quarter of 2003 resulting from the enactment of higher corporate tax rates in the province of Ontario.

### Summary of quarterly financial data - unaudited

| *In millions, except per share data* | 2004 | | | | 2003 | | | |
|---|---|---|---|---|---|---|---|---|
| | **Fourth** | **Third** | **Second** | **First** | Fourth | Third | Second | First |
| Revenues | **$ 1,736** | **$ 1,709** | **$ 1,665** | **$ 1,438** | $ 1,512 | $ 1,413 | $ 1,463 | $ 1,496 |
| Operating income | **$ 620** | **$ 609** | **$ 592** | **$ 409** | $ 363 | $ 329 | $ 335 | $ 341 |
| Net income | **$ 373** | **$ 367** | **$ 338** | **$ 219** | $ 169 | $ 208 | $ 177 | $ 180 |
| Basic earnings per share | **$ 1.31** | **$ 1.28** | **$ 1.19** | **$ 0.77** | $ 0.60 | $ 0.73 | $ 0.62 | $ 0.61 |
| Diluted earnings per share | **$ 1.28** | **$ 1.26** | **$ 1.17** | **$ 0.76** | $ 0.59 | $ 0.72 | $ 0.61 | $ 0.61 |
| Dividend declared per share | **$ 0.195** | **$ 0.195** | **$ 0.195** | **$ 0.195** | $ 0.167 | $ 0.167 | $ 0.167 | $ 0.167 |

The volume of goods and commodities transported by the Company during the year is influenced by seasonal weather conditions, general economic conditions, cyclical demand for rail transportation, and competitive forces in the transportation marketplace. Operating expenses reflect the impact of freight volumes, seasonal weather conditions, labor costs, fuel prices, and the Company's productivity initiatives.

The Company's quarterly results include items that affect the quarter-over-quarter comparability of the results of operations. The Company's results of operations for 2004 included GLT as of May 10, 2004 and BC Rail as of July 14, 2004. First-quarter 2004 results were affected by the month-long CAW strike, which negatively impacted operating income and net income by $35 million and $24 million, respectively. Fourth-quarter 2003 included a deferred income tax expense of $33 million resulting from the enactment of higher corporate tax rates in the province of Ontario. Also affecting comparability was the significant appreciation in the Canadian dollar relative to the U.S. dollar which has impacted the conversion of the Company's U.S. dollar denominated revenues and expenses and resulted in a reduction in net income of approximately $45 million for 2004, particularly in the first quarter.

### Liquidity and capital resources

The Company's principal source of liquidity is cash generated from operations. The Company also has the ability to fund liquidity requirements through its revolving credit facility, the issuance of debt and/or equity, and the sale of a portion of its accounts receivable through a securitization program. In addition, from time to time, the Company's liquidity requirements can be supplemented by the disposal of surplus properties and the monetization of assets.

*Operating activities:* Cash provided from operating activities was $2,139 million for the year ended December 31, 2004 compared to $1,500 million for 2003. Net cash receipts from customers and others were $6,501 million for the year ended December 31, 2004 compared to $6,022 million in 2003. In 2004, payments for employee services, suppliers and other expenses were $3,628 million, a decrease of $108 million when compared to 2003. Also consuming cash in 2004 were payments for interest, workforce reductions and personal injury and other claims of $282 million, $93 million and $106 million, respectively, compared to $327 million, $155 million and $126 million, respectively, in 2003. In 2004, pension contributions and payments for income taxes were $161 million and $92 million, respectively, compared to $92 million and $86 million, respectively, in 2003. The Company increased the level of accounts receivable sold under its accounts receivable securitization program by $12 million in 2004 and $132 million in 2003. Payments in 2005 for workforce reductions are expected to be $90 million while pension contributions are expected to be approximately $120 million.

As at December 31, 2004, the Company had outstanding information technology service contracts of $18 million.

*Investing activities:* Cash used by investing activities in 2004 amounted to $2,411 million compared to $599 million in 2003. The Company's investing activities in 2004 included $984 million related to the acquisition of BC Rail and $547 million related to the acquisition of GLT, net proceeds of $141 million from the EWS capital reorganization and $52 million from the sale of its Canac Inc. and Beltpack subsidiaries. Net capital expenditures for the year ended December 31, 2004 amounted to $1,072 million, an increase of $489 million over 2003, mainly resulting from the change in property capitalization. The following table details capital expenditures for 2004 and 2003.

| *In millions* | *Year ended December 31,* | **2004** | 2003 |
|---|---|---|---|
| Rail infrastructure | | **$ 769** | $ 373 |
| Rolling stock | | **253** | 97 |
| Information technology and other | | **210** | 160 |
| | | **1,232** | 630 |
| Less: capital leases | | **160** | 47 |
| Net capital expenditures | | **$ 1,072** | $ 583 |

The Company expects that its capital expenditures will increase in 2005 due to the acquisition of rolling stock and increased expenditures required for ongoing renewal of the basic plant and other acquisitions and investments required to improve the Company's operating efficiency and customer service.

As at December 31, 2004, the Company had commitments to acquire railroad ties, rail, freight cars, locomotives and other equipment at an aggregate cost of $194 million ($211 million at December 31, 2003).

*Dividends:* During 2004, the Company paid dividends totaling $222 million to its shareholders at the quarterly rate of $0.195 per share compared to $191 million at the rate of $0.167 per share, in 2003.

### Free cash flow

The Company generated $1,025 million of free cash flow for the year ended December 31, 2004, compared to $578 million in 2003. Free cash flow does not have any standardized meaning prescribed by GAAP and may, therefore, not be comparable to similar measures presented by other companies. The Company believes that free cash flow is a useful measure of performance as it demonstrates the Company's ability to generate cash after the payment of capital expenditures and dividends. The Company defines free cash flow as cash provided from operating activities, excluding changes in the level of accounts receivable sold under the securitization program, less investing activities and dividends paid, and adjusted for significant acquisitions as they are not indicative of normal day-to-day investments in the Company's asset base, calculated as follows:

| *In millions* | *Year ended December 31,* | **2004** | 2003 |
|---|---|---|---|
| Cash provided from operating activities | | **$ 2,139** | $ 1,500 |
| ***Less:*** | | | |
| Investing activities | | **(2,411)** | (599) |
| Dividends paid | | **(222)** | (191) |
| Cash provided (used) before financing activities | | **(494)** | 710 |
| ***Adjustments:*** | | | |
| Change in accounts receivable sold | | **(12)** | (132) |
| Acquisition of BC Rail & GLT | | **1,531** | - |
| **Free cash flow** | | **$ 1,025** | **$ 578** |

*Financing activities:* Cash provided from financing activities totaled $511 million for the year ended December 31, 2004 compared to cash used by financing activities of $605 million in 2003. In July 2004, the Company issued U.S.$300 million (Cdn$395 million) of 4.25% Notes due 2009 and U.S.$500 million (Cdn$658 million) of 6.25% Debentures due 2034. In March 2004, the Company had repaid U.S.$266 million (Cdn$355 million) of

7.00% 10-year Notes with cash on hand and the proceeds received from the issuance of commercial paper. In May 2003, the Company had repaid U.S.$150 million (Cdn$207 million) of 6.625% 10-year Notes and U.S.$100 million (Cdn$138 million) of 6.75% 10-year Notes with the proceeds received in March 2003 from the issuance of U.S.$400 million (Cdn$586 million) 4.40% Notes due 2013. In 2004 and 2003, issuances and repayments of long-term debt related principally to the Company's commercial paper and revolving credit facility.

In 2004, the Company used $273 million to repurchase 4.0 million common shares under its current share repurchase program whereas in 2003, the Company used $656 million to repurchase the remaining 15.0 million common shares under its previous share repurchase program initiated in 2002.

During 2004, the Company recorded $160 million in capital lease obligations ($47 million in 2003) related to new equipment and the exercise of purchase options on existing equipment.

The Company has access to various financing arrangements:

*Revolving credit facility*

The Company has a U.S.$1,000 million three-year revolving credit facility expiring in December 2005, which it intends to renew before such date. The credit facility provides for borrowings at various interest rates, including the Canadian prime rate, bankers' acceptance rates, the U.S. federal funds effective rate and the London Interbank Offer Rate, plus applicable margins. The credit facility agreement contains customary financial covenants, based on U.S. GAAP, including limitations on debt as a percentage of total capitalization and maintenance of tangible net worth above pre-defined levels, with which the Company has been in compliance. The Company's borrowings of U.S.$180 million (Cdn$233 million) outstanding at December 31, 2003 at an average interest rate of 1.49% were entirely repaid in the first quarter of 2004. As at December 31, 2004, the Company had borrowings under its revolving credit facility of U.S.$90 million (Cdn$108 million) at an average interest rate of 2.77% and letters of credit drawn of $342 million.

*Commercial paper*

The Company has a commercial paper program, which is backed by a portion of its revolving credit facility, enabling it to issue commercial paper up to a maximum aggregate principal amount of $800 million, or the U.S. dollar equivalent. As the revolving credit facility will mature within the next twelve months and the refinancing has not been renegotiated, the outstanding balance of U.S.$211 million (Cdn$254 million) of commercial paper at an average interest rate of 2.37% has been included in the current portion of long-term debt at December 31, 2004. The Company had no commercial paper outstanding at December 31, 2003.

*Shelf registration statement*

On July 9, 2004, the Company issued U.S.$300 million (Cdn$395 million) of 4.25% Notes due 2009 and U.S.$500 million (Cdn$658 million) of 6.25% Debentures due 2034. The debt offering was made under the Company's shelf prospectus and registration statement filed in October 2003. Accordingly, the amount available under the shelf prospectus and registration statement has been reduced to U.S.$200 million. The Company used the net proceeds of U.S.$790 million to finance a portion of the acquisition costs of BC Rail and GLT.

The Company's access to current and alternate sources of financing at competitive costs is dependent on its credit rating. The Company is not currently aware of any adverse trend, event or condition that would affect the Company's credit rating.

**Contractual obligations**

In the normal course of business, the Company incurs contractual obligations. The following table sets forth the Company's contractual obligations for the following items as at December 31, 2004:

| *(In millions)* | Total | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 & thereafter |
|---|---|---|---|---|---|---|---|
| Long-term debt obligations (a) | **$ 4,403** | $ 497 | $ 308 | $ 60 | $ 207 | $ 363 | $ 2,968 |
| Capital lease obligations (b) | **1,103** | 113 | 106 | 130 | 52 | 93 | 609 |
| Operating lease obligations | **992** | 206 | 194 | 146 | 116 | 90 | 240 |
| Purchase obligations (c) | **212** | 191 | 10 | 5 | 3 | 3 | - |
| **Total obligations** | **$ 6,710** | **$ 1,007** | **$ 618** | **$ 341** | **$ 378** | **$ 549** | **$ 3,817** |

(a) Presented net of unamortized discounts, of which $838 million relates to non-interest bearing notes due in 2094 assumed as part of the BC Rail acquisition and excludes capital lease obligations of $761 million which are included in "Capital lease obligations."

(b) Includes $342 million of imputed interest on capital leases at rates ranging from approximately 2.23% to 13.13%.

(c) Includes commitments for railroad ties, rail, freight cars, locomotives and other equipment and outstanding information technology service contracts.

For 2005 and the foreseeable future, the Company expects cash flow from operations and from its various sources of financing to be sufficient to meet its debt repayments and future obligations, and to fund anticipated capital expenditures.

**Acquisitions**

*BC Rail*

In November 2003, the Company entered into an agreement with British Columbia Railway Company, a corporation owned by the Government of the Province of British Columbia (Province), to acquire all the issued and outstanding shares of BC Rail Ltd. and all the partnership units of BC Rail Partnership (collectively BC Rail), and the right to operate over BC Rail's roadbed under a long-term lease, for a purchase price of $1 billion.

On July 2, 2004, the Company reached a consent agreement with Canada's Competition Bureau, allowing for the closing of the transaction, whereby the Company reaffirmed its commitment to share merger efficiencies with BC Rail shippers and assure them competitive transportation options through its Open Gateway Rate and Service Commitment. The consent agreement also maintains competitive rates and service for grain shippers in the Peace River region.

On July 14, 2004, the Company completed its acquisition of BC Rail and began a phased integration of the companies' operations. The acquisition was financed by debt and cash on hand.

The Company accounted for the acquisition using the purchase method of accounting as required by Section 1581, "Business Combinations," and Section 3062, "Goodwill and Other Intangible Assets," of the CICA. As such, the consolidated financial statements of the Company include the assets, liabilities and results of operations of BC Rail as of July 14, 2004, the date of acquisition. The Company's cost to acquire BC Rail of $991 million includes purchase price adjustments and transaction costs. The preliminary purchase price allocation, based on the fair value of BC Rail's assets acquired, owned and leased, and liabilities assumed at acquisition, as presented in Note 3 – Acquisitions, of the Company's Annual Consolidated Financial Statements, is subject to a final valuation, the impact of which is not expected to have a material effect on the results of operations.

*Great Lakes Transportation LLC's Railroads and Related Holdings*

In October 2003, the Company, through an indirect wholly owned subsidiary, entered into an agreement for the acquisition of GLT for a purchase price of U.S.$380 million.

As of April 2004, the Company received all necessary regulatory approvals, including the U.S. Surface Transportation Board (STB) ruling rendered on April 9, 2004.

On May 10, 2004, the Company completed its acquisition of GLT and began a phased integration of the companies' operations. The acquisition was financed by debt and cash on hand.

The Company accounted for the acquisition using the purchase method of accounting. As such, the consolidated financial statements of the Company include the assets, liabilities and results of operations of GLT as of May 10, 2004, the date of acquisition. The Company's cost to acquire GLT of U.S.$395 million (Cdn$547 million) includes purchase price adjustments and transaction costs. The preliminary purchase price allocation, based on the fair value of GLT's assets acquired and liabilities assumed at acquisition, as presented in Note 3 – Acquisitions, of the Company's Annual Consolidated Financial Statements, is subject to a final valuation, the impact of which is not expected to have a material effect on the results of operations.

These acquisitions involve the integration of two previously independent businesses to provide shippers enhanced rail services over a coordinated network. There can be no assurance that CN will be able to integrate its business with that of either BC Rail or GLT without encountering operational difficulties or experiencing the loss of key employees or customers, or that the rail service levels and other efficiencies or synergies expected from these acquisitions will be attained.

**Investment in English Welsh and Scottish Railway (EWS) – Capital reorganization**

On January 6, 2004, EWS shareholders approved a plan to reduce the EWS share capital to enable cash to be returned to the shareholders by offering them the ability to cancel a portion of their EWS shares. For each share cancelled, EWS shareholders would receive cash and 8% notes due in 2009, redeemable in whole or in part at any time by EWS, at their principal amount together with accrued but unpaid interest up to the date of repayment.

The Company elected to have the maximum allowable number of shares cancelled under the plan, thereby reducing its ownership interest of EWS to approximately 31% on a fully diluted basis (13.7 million shares) compared to approximately 37% on a fully diluted basis (43.7 million shares) prior to the capital reorganization. In the first quarter of 2004, the Company received £57.7 million (Cdn$141 million) in cash and a note receivable of £23.9 million (Cdn$58 million) from EWS.

**Off balance sheet arrangements**

*Accounts receivable securitization program*

The Company has an accounts receivable securitization program, expiring in June 2006, under which it may sell, on a revolving basis, a maximum of $450 million of eligible freight trade and other receivables outstanding at any point in time, to an unrelated trust. The Company has a contingent residual interest of approximately 10% of receivables sold, which is recorded in Other current assets.

The Company is subject to customary reporting requirements for which failure to perform could result in termination of the program. In addition, the trust is subject to customary credit rating requirements, which if not met could also result in termination of the program. The Company monitors these reporting and credit rating requirements for any trends, events or conditions that could cause such termination.

The accounts receivable securitization program provides the Company with readily available short-term financing for general corporate uses. In the event the program is terminated before its scheduled maturity, the Company expects to meet its future payment obligations through its various sources of financing, including its revolving credit facility and commercial paper program, and/or access to capital markets.

At December 31, 2004, pursuant to the agreement, $445 million had been sold compared to $448 million at December 31, 2003.

*Guarantees and indemnifications*

In the normal course of business, the Company, including certain of its subsidiaries, enters into agreements that may involve providing certain guarantees or indemnifications to third parties and others, which extend over the term of the agreement. These include, but are not limited to, residual value guarantees on operating leases, standby letters of credit and surety bonds, and indemnifications that are customary for the type of transaction or for the railway business.

Effective January 1, 2003, the Company is required to disclose its obligations undertaken in issuing certain guarantees on the date the guarantee is issued or modified. Where the Company expects to make a payment in respect of a guarantee, a liability will be recognized to the extent that one has not yet been recognized.

The nature of these guarantees or indemnifications, the maximum potential amount of future payments and the nature of any recourse provisions are disclosed in Note 19 – Major commitments and contingencies of the Company's Annual Consolidated Financial Statements.

**Financial instruments**

The Company has limited involvement with derivative financial instruments and does not use them for trading purposes. Collateral or other security to support financial instruments subject to credit risk is usually not obtained. While the Company is exposed to counterparty credit risk in the event of non-performance, the credit standing of counterparties or their guarantors is regularly monitored, and losses due to counterparty non-performance are not anticipated.

*Fuel*

To mitigate the effects of fuel price changes on its operating margins and overall profitability, the Company has a systematic hedging program which calls for regularly entering into swap positions on crude and heating oil to cover a target percentage of future fuel consumption up to two years in advance. However, in the fourth quarter of 2004, the Company did not enter into any swap positions on crude and heating oil. At December 31, 2004, the Company had hedged approximately 50% of the estimated 2005 fuel consumption, representing approximately 203 million U.S. gallons at an average price of U.S.$0.74 per U.S. gallon, and 17% of the estimated 2006 fuel consumption, representing 69 million U.S. gallons at an average price of U.S.$0.89 per U.S. gallon.

Realized gains from the Company's fuel hedging activities were $112 million, $49 million and $3 million for the years ended December 31, 2004, 2003 and 2002, respectively.

As a result of fuel hedging activities, the Company had an unrealized gain of $92 million at December 31, 2004 compared to $38 million at December 31, 2003.

*Interest rate*

In the first quarter of 2004, in anticipation of future debt issuances, the Company had entered into treasury lock transactions for a notional amount of U.S.$380 million to fix the treasury component on these future debt issuances. Upon expiration in June 2004, these treasury rate locks were rolled into new contracts expiring in September 2004, at an average locked-in rate of 5.106%. The Company settled these treasury locks at a gain of U.S.$9 million (Cdn$12 million) upon the pricing of the U.S.$500 million 6.25% Debentures due 2034, subsequently issued on July 9, 2004 and recorded the gain immediately into income, as a reduction of interest expense.

**Common stock**

*Share repurchase program*

On October 26, 2004, the Board of Directors of the Company approved a share repurchase program which allows for the repurchase of up to 14.0 million common shares between November 1, 2004 and October 31, 2005 pursuant to a normal course issuer bid, at prevailing market prices. As at December 31, 2004, 4.0 million common shares have been repurchased for $273 million, at an average price of $68.31 per share.

*Common stock split*

On January 27, 2004, the Board of Directors of the Company approved a three-for-two common stock split which was effected in the form of a stock dividend of one-half additional common share of CN payable for each share held. The stock dividend was paid on February 27, 2004, to shareholders of record on February 23, 2004. All equity-based benefit plans were adjusted to reflect the issuance of additional shares or options due to the declaration of the stock split. All share and per share data has been adjusted to reflect the stock split.

*Outstanding share data*

As at January 25, 2005, the Company had 283.1 million common shares outstanding.

**Critical accounting policies**

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of revenues and expenses during the period, the reported amounts of assets and liabilities, and the disclosure of contingent assets and liabilities at the date of the financial statements. On an ongoing basis, management reviews its estimates, including those related to personal injury and other claims, environmental claims, depreciation, pensions and other post-retirement benefits, and income taxes, based upon currently available information. Actual results could differ from these estimates. The following accounting policies require management's more significant judgments and estimates in the preparation of the Company's consolidated financial statements and as such, are considered to be critical. The following information should be read in conjunction with the Company's Annual Consolidated Financial Statements and notes thereto.

Management has discussed the development and selection of the Company's critical accounting estimates with the Audit, Finance and Risk Committee of the Company's Board of Directors and the Audit, Finance and Risk Committee has reviewed the Company's related disclosures herein.

**Personal injury and other claims**

In the normal course of its operations, the Company becomes involved in various legal actions, including claims relating to personal injuries, occupational disease and damage to property.

In Canada, employee injuries are governed by the workers' compensation legislation in each province whereby employees may be awarded either a lump sum or future stream of payments depending on the nature and severity of the injury. Accordingly, the Company accounts for costs related to employee work-related injuries based on actuarially developed estimates of the ultimate cost associated with such injuries, including compensation, health care and administration costs. For all other legal actions, the Company maintains, and regularly updates on a case-by-case basis, provisions for such items when the expected loss is both probable and can be reasonably estimated based on currently available information.

Assumptions used in estimating the ultimate costs for Canadian employee injury claims consider, among others, the discount rate, the rate of inflation, wage increases and health care costs. The Company periodically reviews its assumptions to reflect currently available information. Over the past three years, the Company has not changed any of these assumptions. For all other legal claims in Canada, estimates are based on case history, trends and judgment.

In the United States, employee work-related injuries, including occupational disease claims, are compensated according to the provisions of the Federal Employers' Liability Act (FELA) and represent a major expense for the railroad industry. The FELA system, which requires either the finding of fault through the U.S. jury system or individual settlements, has contributed to the significant increase in the Company's personal injury expense in recent years. In view of the Company's growing presence in the United States and the increase in the number of occupational disease claims over the past few years, an actuarial study was conducted in 2002, and in the fourth quarter of 2002 the Company changed its methodology for estimating its liability for U.S. personal injury and other claims, including occupational disease claims and claims for property damage, from a case-by-case approach to an actuarial-based approach. Consequently, and as discussed in Note 2 to the Annual Consolidated Financial Statements, the Company recorded a charge of $281 million ($173 million after tax) to increase its provision for these claims.

Under the actuarial-based approach, the Company accrues the expected cost for personal injury and property damage claims and asserted occupational disease claims, based on actuarial estimates of their ultimate cost. A liability for the minimum amount of unasserted occupational disease claims is also accrued to the extent they can be reasonably estimated. The amount recorded reflects a 25-year horizon as the Company expects that a large majority of these cases will be received over such period.

For the U.S. personal injury and other claims liability, historical claim data is used to formulate assumptions relating to the expected number of claims and average cost per claim (severity) for each year. Changes in any one of these assumptions could materially affect Casualty and other expense as reported in the Company's results of operations. For example, a 5% change in the number of claims or severity would have the effect of changing the provision by approximately $23 million and the annual expense by approximately $8 million.

In 2004, the Company's expenses for personal injury and other claims, net of recoveries, were $149 million ($127 million in 2003 and $393 million in 2002) and payments for such items were $106 million ($126 million in 2003 and $156 million in 2002). As at December 31, 2004, the Company had aggregate reserves for personal injury and other claims of $642 million ($590 million at December 31, 2003).

**Environmental claims**

*Regulatory compliance*

A risk of environmental liability is inherent in railroad and related transportation operations; real estate ownership, operation or control; and other commercial activities of the Company with respect to both current and past operations. As a result, the Company incurs significant compliance and capital costs, on an ongoing basis, associated with environmental regulatory compliance and clean-up requirements in its railroad operations and relating to its past and present ownership, operation or control of real property. Environmental expenditures that relate to current operations are expensed unless they relate to an improvement to the property.

Expenditures that relate to an existing condition caused by past operations and which are not expected to contribute to current or future operations are expensed.

*Known existing environmental concerns*

The Company is subject to environmental clean-up and enforcement actions. In particular, the Federal Comprehensive Environmental Response, Compensation and Liability Act of 1980 (CERCLA), also known as the Superfund law, as well as similar state laws generally impose joint and several liability for clean-up and enforcement costs on current and former owners and operators of a site without regard to fault or the legality of the original conduct. The Company has been notified that it is a potentially responsible party for study and clean-up costs at approximately 17 Superfund sites for which investigation and remediation payments are or will be made or are yet to be determined and, in many instances, is one of several potentially responsible parties.

The ultimate cost of known contaminated sites cannot be definitely established, and the estimated environmental liability for any given site may vary depending on the nature and extent of the contamination, the available clean-up technique, the Company's share of the costs and evolving regulatory standards governing environmental liability. As a result, liabilities are recorded based on the results of a four-phase assessment conducted on a site-by-site basis. Cost scenarios established by external consultants based on extent of contamination and expected costs for remedial efforts are used by the Company to estimate the costs related to a particular site. A liability is initially recorded when environmental assessments and/or remedial efforts are likely, and when costs, based on a specific plan of action in terms of the technology to be used and the extent of the corrective action required, can be reasonably estimated. Adjustments to initial estimates are recorded as additional information becomes available. Based on the information currently available, the Company considers its provisions to be adequate.

At December 31, 2004, most of the Company's properties not acquired through recent acquisitions have reached the final assessment stage and therefore costs related to such sites have been anticipated. For properties acquired through recent acquisitions, the Company obtains assessments from both external and internal consultants and a liability has been or will be accrued based on such assessments.

*Unknown existing environmental concerns*

The Company's ongoing efforts to identify potential environmental concerns that may be associated with its properties may lead to future environmental investigations, which may result in the identification of additional environmental costs and liabilities. The magnitude of such additional liabilities and costs cannot be reasonably estimated due to:

(i) the lack of specific technical information available with respect to many sites;
(ii) the absence of any government authority, third-party orders, or claims with respect to particular sites;
(iii) the potential for new or changed laws and regulations and for development of new remediation technologies and uncertainty regarding the timing of the work with respect to particular sites;
(iv) the ability to recover costs from any third parties with respect to particular sites;

and as such, costs related to future remediation will be accrued in the period they become known.

*Future occurrences*

In the operation of a railroad, it is possible that derailments, explosions or other accidents may occur that could cause harm to human health or to the environment. As a result, the Company may incur costs in the future, which may be material, to address any such harm, including costs relating to the performance of clean-ups, natural resource damages and compensatory or punitive damages relating to harm to individuals or property.

In 2004, the Company's expenses relating to environmental matters, net of recoveries, were $10 million ($6 million in both 2003 and 2002) and payments for such items were $8 million ($12 million in 2003 and $16 million in 2002). As at December 31, 2004, the Company had aggregate accruals for environmental costs of $113 million ($83 million as at December 31, 2003). The Company anticipates that the majority of the liability will be paid out over the next five years.

**Depreciation**

Railroad properties are carried at cost less accumulated depreciation including asset impairment write-downs. The Company follows the group method of depreciation for railroad properties and, as such, depreciates the cost of railroad properties, less net salvage value, on a straight-line basis over their estimated useful lives. In addition, under the group method of depreciation, the cost of railroad properties, less net salvage value, retired or disposed of in the normal course of business, is charged to accumulated depreciation.

Assessing the reasonableness of the estimated useful lives of properties requires judgment and is based on currently available information, including periodic depreciation studies conducted by the Company. The Company's U.S. properties are subject to comprehensive depreciation studies conducted by external consultants as required by the STB. Depreciation studies for Canadian properties are not required by regulation and are therefore conducted internally. Studies are performed on specific asset groups on a periodic basis. The studies consider, among others, the analysis of historical retirement data using recognized life analysis techniques, and the forecasting of asset life characteristics. Changes in circumstances, such as technological advances, changes to the Company's business strategy, changes in the Company's capital strategy or changes in regulations can result in the actual useful lives differing from the Company's estimates.

A change in the remaining useful life of a group of assets, or their estimated net salvage, will affect the depreciation rate used to amortize the group of assets and thus affect depreciation expense as reported in the Company's results of operations. A change of one year in the composite useful life of the Company's fixed asset base would impact annual depreciation expense by approximately $12 million.

Depreciation studies are a means of ensuring that the assumptions used to estimate the useful lives of particular asset groups are still valid and where they are not, they serve as the basis to establish the new depreciation rates to be used on a prospective basis. In 2004, the Company conducted a comprehensive study for its Canadian properties and U.S. rolling stock and equipment. The study did not have a significant effect on depreciation expense.

In 2004, the Company recorded total depreciation and amortization expense of $521 million ($478 million in 2003 and $506 million in 2002). At December 31, 2004, the Company had Properties of $16,688 million, net of accumulated depreciation of $6,448 million ($15,158 million in 2003, net of accumulated depreciation of $6,265 million).

**Pensions and other post-retirement benefits**

The Company accounts for pensions and other post-retirement benefits as required by CICA Handbook Section 3461, "Employee Future Benefits." Under this accounting standard, assumptions are made regarding the valuation of benefit obligations and performance of plan assets. Deferred recognition of differences between actual results and those assumed is a guiding principle of these standards. This approach allows for a gradual recognition of changes in benefit obligations and plan performance over the expected average remaining service life of the employee group covered by the plans. The Company has various pension plans, however, the following description pertaining to pensions relates generally to the Company's main pension plan, the CN Pension Plan.

The Canadian plans have a measurement date of December 31 whereas the U.S. plans have a measurement date of September 30. For pensions and other post-retirement benefits, assumptions are required for, among others, the discount rate, the expected long-term rate of return on plan assets, the rate of compensation increase, health care cost trend rates, mortality rates, employee early retirements, terminations or disability. Changes in these assumptions result in actuarial gains or losses which in accordance with CICA Handbook Section 3461, the Company has elected to amortize over the expected average remaining service life of the employee group covered by the plans only to the extent that the unrecognized net actuarial gains and losses are in excess of 10% of the greater of the beginning of year balances of the projected benefit obligation or market-related value of plan assets. The future effect on the Company's results of operations is dependent on economic conditions, employee demographics, mortality rates and investment performance.

The Company sets its discount rate assumption annually to reflect the rates available on high-quality, fixed-income debt instruments with a duration of approximately 12 years, which is expected to match the timing and amount of expected benefit payments. High quality debt instruments are corporate bonds with a rating of AA or better. A discount rate of 5.75%, based on bond yields prevailing at December 31, 2004, was considered appropriate by the Company and is supported by reports issued by third party advisors. A one-percentage-point decrease in the discount rate would cause annual net periodic benefit cost to increase by approximately $33 million whereas a one-percentage-point increase would not have a material change in net periodic benefit cost as the Company amortizes actuarial gains and losses over the expected average remaining service life of the employee group covered by the plans, only to the extent they are in excess of 10% of the greater of the beginning of year balances of the projected benefit obligation or market-related value of plan assets.

To develop its expected long-term rate of return assumption used in the calculation of net periodic benefit cost applicable to the market-related value of assets, the Company considers both its past experience and future estimates of long-term investment returns, the expected composition of the plans' assets as well as the expected long-term market returns in the future. The Company has elected to use a market-related value of assets, whereby realized and unrealized gains/losses and appreciation/depreciation in the value of the investments are recognized over a period of five years, while investment income is recognized immediately. The Company follows a disciplined investment strategy, which limits concentration of investments by asset class, foreign currency, sector or company. The Investment Committee of the Board of Directors has approved an investment policy that establishes long-term asset mix targets based on a review of historical returns achieved by worldwide investment markets. Investment managers may deviate from these targets but their performance is evaluated in relation to the market performance of the target mix. The Company does not anticipate the return on plan assets to fluctuate materially from related capital market indices. The Investment Committee reviews investments regularly with specific approval required for major investments in illiquid securities. The policy also permits the use of derivative financial instruments to implement asset mix decisions or to hedge existing or anticipated exposures. The Pension Plan does not invest in the securities of the Company or its subsidiaries. During the last ten years ended December 31, 2004, the CN Pension Plan earned an annual average rate of return of 9.8%. The actual and market-related value rates of return on plan assets for the last five years were as follows:

| Rates of return | 2004 | 2003 | 2002 | 2001 | 2000 |
|---|---|---|---|---|---|
| *Actual* | 11.7% | 9.6% | (0.3)% | (1.4)% | 10.5% |
| *Market-related value* | 6.3% | 7.0% | 7.4% | 10.2% | 13.7% |

For that same period, the Company used a long-term rate of return assumption on the market-related value of plan assets not exceeding 9% to compute net periodic benefit cost. In 2003, the Company had reduced the expected long-term rate of return on plan assets from 9% to 8% to reflect management's view of long-term investment returns. The effect of this change in management's assumption was to increase net periodic benefit cost in 2003 by approximately $50 million.

Based on the fair value of the assets held as at December 31, 2004, the plan assets are comprised of 56% in Canadian and foreign equities, 34% in debt securities, 3% in real estate assets and 7% in other assets. The long-term asset allocation percentages are not expected to differ materially from the current composition.

The rate of compensation increase, 3.75% to determine both the benefit obligation and the net periodic benefit cost, is another significant assumption in the actuarial model for pension accounting and is determined by the Company based upon its long-term plans for such increases. For other post-retirement benefits, the Company reviews external data and its own historical trends for health care costs to determine the health care cost trend rates. For measurement purposes, the projected health care cost trend rate was 15% in the current year, and it is assumed that the rate will decrease gradually to 6% in 2013 and remain at that level thereafter. A one-percentage-point change in either the rate of compensation increase or the health care cost trend rate would not cause a material change to the Company's net periodic benefit cost for both pensions and other post-retirement benefits.

For pension funding purposes, an actuarial valuation is required at least on a triennial basis. However, for the last 15 years, the Company has conducted an annual actuarial valuation to account for pensions. The latest actuarial valuation of the CN Pension Plan was conducted as at December 31, 2003 and indicated a funding excess. Total contributions for all of the Company's pension plans are expected to be approximately $120 million in each of 2005, 2006, and 2007 based on the plans' current position. The assumptions discussed above are not expected to have a significant impact on the cash funding requirements of the pension plans. The Canadian Institute of Actuaries (CIA) has adopted a new standard that will be used to calculate the values that pension plan members are entitled to receive on termination of employment. The new standard will impact the calculation of the pension plan liabilities under a solvency or wind-up scenario when the Company conducts an actuarial valuation for purposes of determining the funding position of the Company's Canadian pension plans. The standard is effective in February 2005 and may significantly impact future funding requirements.

For pension, the Company recorded consolidated net periodic benefit cost of $22 million and $49 million in 2004 and 2003, respectively, and no net periodic benefit cost in 2002. Consolidated net periodic benefit cost for other post-retirement benefits was $29 million, $33 million, and $25 million in 2004, 2003, and 2002, respectively. At December 31, 2004, the Company's accrued benefit cost for post-retirement benefits other than pensions was $309 million ($164 million at December 31, 2003). In addition, at December 31, 2004, the Company's consolidated pension benefit obligation and accumulated post-retirement benefit obligation (APBO) were $13,137 million and $319 million, respectively ($12,020 million and $309 million at December 31, 2003).

The Medicare Prescription Drug, Improvement, and Modernization Act of 2003 (the "Act"), signed into law in the United States in December 2003, provides for prescription drug benefits under Medicare, as well as a federal subsidy to sponsors of retiree health care benefit plans that provide prescription drug benefits that have been concluded to be actuarially equivalent to the Medicare benefit. Pursuant to guidance by the Financial Accounting Standards Board (FASB) in the United States, adopted on July 1, 2004, the Company evaluated and determined the prescription drug benefits provided by its health care plans to be actuarially equivalent to the Medicare benefit under the Act. The Company measured the effects of the Act on the APBO as of January 1, 2004 and, as such, the APBO was reduced by $49 million. Net periodic benefit cost for the year ended December 31, 2004 was reduced by $7 million due to the effects of the Act.

In 2004, with the acquisitions of GLT and BC Rail, the Company assumed two additional defined benefit plans. The following table provides the Company's plan assets by category, benefit obligation at end of year and Company and employee contributions by major pension plan:

| *In millions* *December 31, 2004* | CN Pension Plan | BC Rail Pension Plan | US and Other Plans | Total |
|---|---|---|---|---|
| **Plan assets by category** | | | | |
| Equity securities | $ 6,812 | $ 312 | $ 105 | $ 7,229 |
| Debt securities | 3,888 | 212 | 54 | 4,154 |
| Real estate | 348 | 16 | 1 | 365 |
| Other | 1,208 | 73 | 24 | 1,305 |
| Total | $ 12,256 | $ 613 | $ 184 | $ 13,053 |
| **Benefit obligation at end of year** | $ 12,172 | $ 626 | $ 339 | $ 13,137 |
| **Company contributions in 2004** | $ 74 | $ 20 | $ 71 | $ 165 |
| **Employee contributions in 2004** | $ 55 | $ - | $ - | $ 55 |

**Income taxes**

The Company follows the asset and liability method of accounting for income taxes. Under the asset and liability method, the change in the net deferred income tax asset or liability is included in the computation of net income. Deferred income tax assets and liabilities are measured using substantively enacted income tax rates expected to apply to taxable income in the years in which temporary differences are expected to be recovered or settled. As a result, a projection of taxable income is required for those years, as well as an assumption of the ultimate recovery/settlement period for temporary differences. The projection of future taxable income is based on management's best estimate and may vary from actual taxable income. On an annual basis, the Company assesses its need to establish a valuation allowance for its deferred income tax assets and if it is deemed more likely than not that its deferred income tax assets will not be realized based on its taxable income projections, a valuation allowance is recorded. As at December 31, 2004, the Company expects that its deferred income tax assets will be recovered from future taxable income and therefore, has not set up a valuation allowance. In addition, Canadian and U.S. tax rules and regulations are subject to interpretation and require judgment by the Company that may be challenged by the taxation authorities. The Company believes that its provisions for income taxes are adequate pertaining to any assessments from the taxation authorities.

The Company's deferred income tax assets are mainly composed of temporary differences related to accruals for workforce reductions, personal injury and other claims, environmental and other post-retirement benefits, and losses and tax credit carryforwards. The majority of these accruals will be paid out over the next five years. The Company's deferred income tax liabilities are mainly composed of temporary differences related to properties and prepaid benefit cost for pensions. The reversal of temporary differences is expected at future-substantively enacted income tax rates which could change due to fiscal budget changes and/or changes in income tax laws. As a result, a change in the timing and/or the income tax rate at which the components will reverse, could materially affect deferred income tax expense as recorded in the Company's results of operations. A one-percentage-point change in the Company's reported effective income tax rate would have the effect of changing the income tax expense by $19 million in 2004. In the fourth quarter of 2003, the Company had recorded an increase of $33 million to its net deferred income tax liability resulting from the enactment of higher corporate tax rates in the province of Ontario.

For the year ended December 31, 2004, the Company recorded total income tax expense of $631 million ($338 million in 2003 and $268 million in 2002) of which $401 million was for deferred income taxes ($232 million in 2003 and $156 million in 2002). The Company's net deferred income tax liability at December 31, 2004 was $3,198 million ($3,240 million at December 31, 2003).

**Business risks**

Certain information included in this report may be "forward-looking statements" within the meaning of the United States Private Securities Litigation Reform Act of 1995. Such forward-looking statements are not guarantees of future performance and involve known and unknown risks, uncertainties and other factors which may cause the outlook, the actual results or performance of the Company or the rail industry to be materially different from any future results or performance implied by such statements. Such factors include the factors set forth below as well as other risks detailed from time to time in reports filed by the Company with securities regulators in Canada and the United States.

**Competition**

The Company faces significant competition from a variety of carriers, including Canadian Pacific Railway Company (CP) which operates the other major rail system in Canada, serving most of the same industrial and population centers as the Company, long distance trucking companies and, in many markets, major U.S. railroads and other Canadian and U.S. railroads. Competition is generally based on the quality and reliability of services provided, price, and the condition and suitability of carriers' equipment. Competition is particularly intense in eastern Canada where an extensive highway network and population centers, located relatively close to one another, have encouraged significant competition from trucking companies. In addition, much of the freight carried by the Company consists of commodity goods that are available from other sources in competitive markets. Factors affecting the competitive position of suppliers of these commodities, including exchange rates, could materially adversely affect the demand for goods supplied by the sources served by the Company and, therefore, the Company's volumes, revenues and profit margins.

In addition to trucking competition, and to a greater degree than other rail carriers, the Company's subsidiary, Illinois Central Railroad Company (ICRR), is vulnerable to barge competition because its main routes are parallel to the Mississippi River system. The use of barges for some commodities, particularly coal and grain, often represents a lower cost mode of transportation. Barge competition and barge rates are affected by navigational interruptions from ice, floods and droughts, which can cause widely fluctuating barge rates. The ability of ICRR to maintain its market share of the available freight has traditionally been affected by the navigational conditions on the river.

The significant consolidation of rail systems in the United States has resulted in larger rail systems that are able to offer seamless services in larger market areas and accordingly, compete effectively with the Company in certain markets. This requires the Company to consider transactions that would similarly enhance its own service, such as its acquisitions of BC Rail and the GLT carriers. There can be no assurance that the Company will be able to compete effectively against current and future competitors in the railroad industry and that further consolidation within the railroad industry will not adversely affect the Company's competitive position. No assurance can be given that competitive pressures will not lead to reduced revenues, profit margins or both.

**Environmental matters**

The Company's operations are subject to numerous federal, provincial, state, municipal and local environmental laws and regulations in Canada and the United States concerning, among other things, emissions into the air; discharges into waters; the generation, handling, storage, transportation, treatment and disposal of waste, hazardous substances and other materials; decommissioning of underground and aboveground storage tanks; and soil and groundwater contamination. A risk of environmental liability is inherent in railroad and related transportation operations; real estate ownership, operation or control; and other commercial activities of the Company with respect to both current and past operations. As a result, the Company incurs significant compliance and capital costs, on an ongoing basis, associated with environmental regulatory compliance and clean-up requirements in its railroad operations and relating to its past and present ownership, operation or control of real property.

While the Company believes that it has identified the costs likely to be incurred for environmental matters in the next several years, based on known information, the Company's ongoing efforts to identify potential environmental concerns that may be associated with its properties may lead to future environmental investigations, which may result in the identification of additional environmental costs and liabilities.

In railroad and related transportation operations, it is possible that derailments, explosions or other accidents may occur that could cause harm to human health or to the environment. As a result, the Company may incur costs in the future, which may be material, to address any such harm, including costs relating to the performance of clean-ups, natural resource damages and compensatory or punitive damages relating to harm to individuals or property.

The ultimate cost of known contaminated sites cannot be definitely established, and the estimated environmental liability for any given site may vary depending on the nature and extent of the contamination, the available clean-up technique, the Company's share of the costs and evolving regulatory standards governing environmental liability. Also, additional contaminated sites yet unknown may be discovered or future operations may result in accidental releases. For these reasons, there can be no assurance that material liabilities or costs related to environmental matters will not be incurred in the future, or will not have a material adverse effect on the Company's financial position or results of operations in a particular quarter or fiscal year, or that the Company's liquidity will not be adversely impacted by such environmental liabilities or costs.

**Personal injury and other claims**

In the normal course of its operations, the Company becomes involved in various legal actions, including claims relating to personal injuries, occupational disease and damage to property. The Company maintains provisions for such items, which it considers to be adequate for all of its outstanding or pending claims. The final outcome with respect to actions outstanding or pending at December 31, 2004, or with respect to future claims, cannot be predicted with certainty, and therefore there can be no assurance that their resolution will not have a material adverse effect on the Company's financial position or results of operations in a particular quarter or fiscal year.

**Labor negotiations**

*Canadian workforce*

Labor agreements covering approximately 97% of the Company's Canadian unionized workforce expired on December 31, 2003. As of January 2005, the Company has successfully negotiated four collective agreements with the CAW, retroactive to January 1, 2004, covering the Company's shopcraft forces, clerical workers, intermodal yard employees and owner operators. Agreements were also reached with the Company's Rail Traffic Controllers, Toronto Terminal employees and the Canadian Railway Police Association as well as a United Transportation Union (UTU) group that represents employees in the Company's northern Quebec territory (CFIL). In addition, the Company has reached a tentative labor agreement with the United Steelworkers of America, representing approximately 2,250 track, bridges and structures employees, whose agreement also expired on December 31, 2003. The UTU, representing 2,520 brakemen and conductors, the Teamsters Canada Rail Conference (TCRC), which represents 1,750 locomotive engineers, and the 630-member International Brotherhood of Electrical Workers (IBEW), representing close to 40% of the unionized workforce in Canada, filed for conciliation in the fourth quarter and the negotiations have since been conducted with government assistance. On December 29, 2004, the Minister of Labour also referred to the Canadian Industrial Relations Board (CIRB) a question respecting the maintenance of essential services should there be a strike or lockout involving these groups. Until the Board renders its decision, the right to strike or lockout is suspended. In addition to the Board's decision, at least 72 hours' strike or lockout notice would be required prior to any legal strike or lockout.

In the third quarter of 2004, the Company acquired BC Rail. At December 2004, the Company had reached implementing agreements for BC Rail employees with the Council of Trade Unions and its members, representing all unions, regarding the integration of the various collective agreements.

In the first quarter of 2004, the Company's shopcraft forces, clerical workers and intermodal yard employees, represented by the CAW had rejected three tentative agreements signed by the CAW and the Company on January 23, 2004. The strike that ensued lasted one month and disrupted the Company's operations and affected operating income by approximately $35 million in the first quarter of 2004. There can be no assurance that the Company will be able to have all its collective agreements renewed and ratified without any other strikes or lockouts, or that such strikes or lockouts or the resolution of these collective bargaining negotiations will not have a material adverse effect on the Company's financial position or results of operations.

*U.S. workforce*

The general approach to labor negotiations by U.S. Class 1 railroads is to bargain on a collective national basis. Grand Trunk Western (GTW), Duluth, Winnipeg and Pacific (DWP), ICRR, CCP Holdings, Inc. (CCP) and Wisconsin Central Transportation Corporation (WC), have bargained on a local basis rather than holding national, industry wide negotiations because it results in agreements that better address both the employees' concerns and preferences, and the railways' actual operating environment. However, local negotiations may not generate federal intervention in a strike or lockout situation, since a dispute may be localized. The Company believes the potential mutual benefits of local bargaining outweigh the risks.

As of January 2005, the Company had in place agreements with bargaining units representing the entire unionized workforce at ICRR, GTW, DWP, CCP and GLT, and 93% of the unionized workforce at WC. Agreements in place have various moratorium provisions, ranging from the end of 2001 to the end of 2005, which preserve the status quo in respect of given areas during the terms of such moratoriums. Several of these agreements are currently under renegotiation and several will open for negotiation in 2005.

Negotiations are ongoing with the bargaining units with which the Company does not have agreements or settlements. Until new agreements are reached or the processes of the Railway Labor Act have been exhausted, the terms and conditions of existing agreements or policies continue to apply. Although the Company does not anticipate work action related to these negotiations while they are ongoing, there can be no assurance that there will not be any such work action and that the resolution of these negotiations will not have a material adverse effect on the Company's financial position or results of operations.

**Regulation**

The Company's rail operations in Canada are subject to regulation as to (i) rate setting and network rationalization by the Canadian Transportation Agency (the Agency) under the Canada Transportation Act (Canada) (the CTA), and (ii) safety by the federal Minister of Transport under the Railway Safety Act (Canada) and certain other statutes. The Company's U.S. rail operations are subject to regulation as to (i) economic regulation by the STB (the successor to the Interstate Commerce Commission) and (ii) safety by the Federal Railroad Administration. As such, various Company business transactions must gain prior regulatory approval, with attendant risks and uncertainties. The Company is also subject to a variety of health, safety, security, labor, environmental and other regulations, all of which can affect its competitive position and profitability.

The CTA Review Panel, which was appointed by the federal government to carry out a comprehensive review of the Canadian transportation legislation, issued its report to the Minister of Transport at the end of June 2001. The report was released to the public on July 18, 2001 and contains numerous recommendations for legislative changes affecting all modes of transportation, including rail. On February 25, 2003, the Canadian Minister of Transport released its policy document *Straight Ahead – A Vision for Transportation in Canada* and tabled in the House of Commons Bill C-26 entitled *An Act to Amend the Canada Transportation Act and the Railway Safety Act, to enact the VIA Rail Canada Act and to make consequential amendments to other Acts*. Bill C-26 died on the Order Paper (was terminated) when Parliament was prorogued on November 12, 2003. No assurance can be given that any future legislative action by the federal government pursuant to the report's recommendations and the policy document, or other future governmental initiatives will not materially adversely affect the Company's financial position or results of operations.

The U.S. Congress has had under consideration for several years various pieces of legislation that would increase federal economic regulation of the railroad industry. In addition, the STB is authorized by statute to commence regulatory proceedings if it deems them to be appropriate. No assurance can be given that any future regulatory initiatives by the U.S. federal government will not materially adversely affect the Company's operations, or its competitive and financial position.

The Company is subject to statutory and regulatory directives in the United States addressing homeland security concerns. These include new border security arrangements, pursuant to an agreement the Company and CP entered into with U.S. Customs and Border Protection (CBP) and the Canada Border Services Agency (CBSA). These requirements include advance electronic transmission of cargo information for U.S.-bound traffic and cargo screening (including gamma ray and radiation screening), as well as U.S. government imposed restrictions on the transportation into the United States of certain commodities. In the fourth quarter of 2003, the CBP issued regulations to extend advance notification requirements to all modes of transportation and the U.S. Food and Drug Administration promulgated interim final rules requiring advance notification by all modes for certain food imports into the United States. The Company has also worked with the Association of American Railroads to develop and put in place an extensive industry-wide security plan. While the Company will continue to work closely with the CBSA, CBP, and other Canadian and U.S. agencies, as above, no assurance can be given that future decisions by the U.S. and/or Canadian governments on homeland security matters, or joint decisions by the industry in response to threats to the North American rail network, will not materially adversely affect the Company's operations, or its competitive and financial position.

In October 2002, the Company became the first North American railroad to gain membership in the U.S. Customs Service's Customs-Trade Partnership Against Terrorism (C-TPAT). C-TPAT is a joint government-business initiative designed to build cooperative relationships that strengthen overall supply chain and border security on goods exported to the U.S. The Company is also designated as a low-risk carrier under the Customs Self-Assessment (CSA) program, a CBSA program designed to expedite the cross-border movement of goods of CSA-accredited importing companies for goods imported into Canada.

The Company's ownership of the former Great Lakes Transportation vessels is subject to regulation by the U.S. Coast Guard and the Department of Transportation, Maritime Administration, which regulate the ownership and operation of vessels operating on the Great Lakes and in U.S. coastal waters. On February 4, 2004, the Maritime Administration and the U.S. Coast Guard issued a Joint Notice of Proposed Rulemaking, proposing modifications to the regulations governing vessel documentation for lease financing for vessels engaged in the coastwise trade. In addition, the U.S. Congress has from time to time considered modifications to the legislation governing the United States coastwise trade. As a result of maritime legislation enacted in 2004, the regulations governing the Company's acquisition of these vessels should not be affected. No assurance can be given that any future legislative or regulatory initiatives by the U.S. federal government will not materially adversely affect the Company's operations, or its competitive and financial position.

**Business prospects and other risks**

In any given year, the Company, like other railroads, is susceptible to changes in the economic conditions of the industries and geographic areas that produce and consume the freight it transports or the supplies it requires to operate. In addition, many of the goods and commodities carried by the Company experience cyclicality in demand. Many of the bulk commodities the Company transports move offshore and are affected more by global rather than North American economic conditions. The Company's results of operations can be expected to reflect these conditions because of the significant fixed costs inherent in railroad operations.

Global, as well as North American trade conditions, including trade barriers on certain commodities, may interfere with the free circulation of goods across Canada and the United States.

Potential terrorist actions can have a direct or indirect impact on the transportation infrastructure, including railway infrastructure in North America, and interfere with the free flow of goods. International conflicts can also have an impact on the Company's markets.

Although the Company conducts its business and receives revenues primarily in Canadian dollars, a growing portion of its revenues, expenses, assets and debt are denominated in U.S. dollars. Thus, the Company's results are affected by fluctuations in the exchange rate between these currencies. Based on the Company's current operations, the estimated annual impact on net income of a year-over-year one-cent change in the Canadian dollar relative to the U.S. dollar is approximately $8 million. Changes in the exchange rate between the Canadian dollar and other currencies (including the U.S. dollar) make the goods transported by the Company more or less competitive in the world marketplace and thereby affect the Company's revenues and expenses.

Should a major economic slowdown or recession occur in North America or other key markets, or should major industrial restructuring take place, the volume of rail shipments carried by the Company is likely to be adversely affected.

In addition to the inherent risks of the business cycle, the Company's operations are occasionally susceptible to severe weather conditions, which can disrupt operations and service for the railroad as well as for the Company's customers. Recent severe drought conditions in western Canada, for instance, significantly reduced bulk commodity revenues, principally grain.

Generally accepted accounting principles require the use of historical cost as the basis of reporting in financial statements. As a result, the cumulative effect of inflation, which has significantly increased asset replacement costs for capital-intensive companies such as CN, is not reflected in operating expenses. Depreciation charges on an inflation-adjusted basis, assuming that all operating assets are replaced at current price levels, would be substantially greater than historically reported amounts.

**Controls and procedures**

The Company's Chief Executive Officer and its Chief Financial Officer, after evaluating the effectiveness of the Company's "disclosure controls and procedures" (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) as of December 31, 2004, have concluded that the Company's disclosure controls and procedures were adequate and effective and designed to ensure that material information relating to the Company and its consolidated subsidiaries would have been made known to them. During the fourth quarter ending December 31, 2004, there was no change in the Company's internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

Additional information, including the Company's 2003 Annual Information Form and Form 40-F, may be found on SEDAR at www.sedar.com and on EDGAR at www.sec.gov/edgar.shtml, respectively.

Montreal, Canada
January 25, 2005