

Our place. Our time.



SECOND QUARTER REPORT 2003

Our number of cellular customers grew 13.2 per cent during the past year thanks to the efforts of Aliant employees like Shawn Amirault, manager of advertising and customer retention.  
*(see page 9)*

# Earnings per share rise 4.4 per cent; share buyback planned



We recorded a number of significant accomplishments in the second quarter. We sold several companies that were not part of our core telecommunications business. We opened the door to future value creation opportunities in our IT operation. We made decisions about how best to deploy cash that is currently not required in our operations. And we did it all while posting a solid financial performance.

## Earnings per share up 4.4 per cent

Second quarter consolidated revenue from continuing operations was \$665.5 million, up 1.9 per cent from \$653.3 million in the same quarter last year. Net income and earnings per share from continuing operations for the quarter were \$65.3 million and \$0.47 respectively. Net income from continuing operations increased by 4.5 per cent and earnings per share by 4.4 per cent from the same period last year after excluding from the year ago quarter \$36.0 million of net income, or \$0.26 per share, resulting largely from dilution and foreign exchange gains.

Free cash flow from operations of continuing businesses for the second quarter was \$102.5 million, up from \$22.0 million in the same quarter last year, bringing the total for the year-to-date to \$262.4 million, up \$190.0 million from the first half of last year. This significant increase in free cash flow from operations on a year-to-date basis includes the receipt of a \$55.0 million tax claim, a reduction of \$65.9 million in capital spending, and \$30.0 million

resulting from stronger working capital management.

## Non-core businesses sold

During the second quarter we completed the sale of our interest in iMagicTV to Alcatel and our interest in Prexar, an Internet service provider based in Maine, to United System Access. AMI Offshore arrived at an agreement with Rutter Technologies for the sale of two of its holdings, NewTech Instruments and SEA Systems.

## Changes at xwave to save \$20 million annually

During the quarter we continued to search for a business partner and buyer for our information technology business, xwave, based on four criteria we believe are necessary to ensure success for all stakeholders:

- 1) A price representing full value;
- 2) A suitable go-to-market partner to serve our information technology and telecommunications customers;
- 3) An environment that provides personal and professional growth for xwave employees; and
- 4) A suitable partner to meet our own IT needs.

After extensive discussions with a number of companies and a thorough analysis of our options we concluded the greatest benefit for our customers, employees and shareholders would be achieved by retaining xwave within the Aliant family.

In making our decision we acknowledged the need to re-engineer xwave's organizational structure and business model. The new model must reflect the realities of the current business environment. In the few short weeks

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## Financial highlights<sup>1</sup>

For the period ending June 30 (millions of dollars except per share amounts)	Three months		Six months	
	2003	2002	2003	2002
Operating revenues	\$ 665.5	\$ 653.3	\$ 1,308.6	\$ 1,279.2
Net income applicable to common shares	\$ 65.3	\$ 98.5	\$ 106.4	\$ 151.4
Free cash flow from operations <sup>2</sup>	\$ 102.5	\$ 22.0	\$ 262.4	\$ 71.8
Earnings per average common share (basic)	\$ 0.47	\$ 0.71	\$ 0.77	\$ 1.09

<sup>1</sup> Financial highlights represent the results from continuing operations

<sup>2</sup> Free cash flow from operations is defined as cash and cash equivalents from (used in) continuing operations, less capital investments.

since the decision we have taken the necessary first steps to help xwave achieve greater operational effectiveness and profitability, including the creation of a new and streamlined regional operating model, a smaller more condensed management structure, and a downsized supporting structure that will increasingly share resources with Aliant member companies. We are reducing the size of the workforce at xwave by approximately 10%. During the third quarter we will take a charge of \$15.5 million to cover the costs of reorganization that will contribute approximately \$20.0 million in annual pre-tax savings.

As we continue to develop our technology and service offerings we will combine our IT skills and our networks to offer customers a path of technology and application advancement that includes IT-based services and solutions. We will layer on top of our traditional telecommunications services IT-based services to create a one-stop technology solution for customers.

### **Working with the regulator**

The telecommunications industry continues to operate in a challenging regulatory environment. We have been working with the CRTC to ensure they understand our desire to provide our customers with the products and services they want, at a price they are willing to pay. We have also been working to ensure the CRTC considers three key issues when making decisions that relate to the Atlantic Canadian marketplace.

- 1) The market in Atlantic Canada is already very competitive.
- 2) The complexity and cost of operating in a region that has a dispersed and largely rural population is high.
- 3) Our ability to plan for future capital investments is dependent upon understanding the CRTC's definition of the end state for the market.

### **Share buyback**

In keeping with our commitment to enhance shareholder value, we intend to purchase up to 6,925,000, or 5 per cent, of our issued common shares. We believe that buying back shares is in the best interest of shareholders and the best way to deploy cash that is not currently required in our operations. The buyback plan, which requires the approval of the Toronto Stock Exchange, will allow us to purchase shares on the open market commencing August 6, 2003 and ending on August 5, 2004. All shares

*The strength in our operations and the financial stability we have carefully built over the past 18 months have prepared us well for the future. We are positioned to capitalize on opportunities that will no doubt arise from new technologies.*

purchased will be cancelled. (Subsequent to writing this letter, the Toronto Stock Exchange approved the plan.)

The share buyback plan is in addition to a recently completed buyback plan, concluded on July 21, that saw the purchase of 1,600,000 common shares for an average price of \$27.65 per share.

### **Dividend declared**

Our Board of Directors declared a common share dividend of \$0.275 per common share payable on September 30, 2003 to shareholders of record on September 15, 2003. The Board also declared a preferred share dividend of \$0.340625 per preference share, payable on September 30, 2003 to shareholders of record on September 15, 2003.

### **Looking ahead**

The strength in our operations and the financial stability we have carefully built over the past 18 months have prepared us well for the future. We are in a strong position to capitalize on opportunities that will no doubt arise from new technologies, including exciting advancements like voice-over IP that allow the Internet to carry regular voice communications. As IP technologies unfold we see ourselves focusing on the management of local- and wide-area networks, desktops and servers and on providing a full range of support applications to help integrate, manage and simplify the array of communications tools we use today. This is an exciting prospect and one that can hold significant added value for our customers and a potential source of new revenue for our company.



Jay Forbes  
*President and chief executive officer*  
July 24, 2003

# MD&A

*This is a discussion and analysis of the financial condition and results of operations of Aliant Inc. ("Aliant" or "the Company") for the second quarter and the first six months of 2003. This document should be read in conjunction with Aliant's unaudited interim consolidated financial statements and accompanying notes for the period ended June 30, 2003, and with the Company's audited annual consolidated financial statements and management's discussion and analysis for the year ended December 31, 2002.*

*This document contains certain statements and information about potential future circumstances and developments. Such forward-looking statements and information are qualified by any of the inherent risks and uncertainties surrounding future expectations generally and may differ materially from Aliant's actual future experience. Reference is made to the "Consolidated risk assessment" and "Forward-looking statements" sections below for further discussion about the inherent risks and uncertainties surrounding future expectations. Aliant disclaims any intention or obligation to update or revise any forward-looking statements or information, whether as a result of new information, future events or otherwise.*

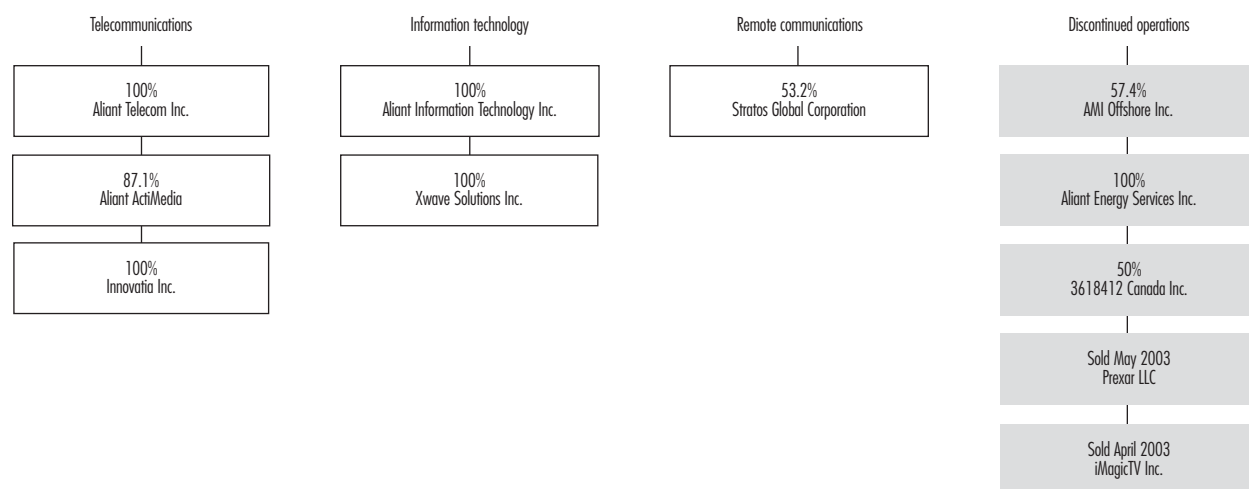
*The Company defines and uses certain terms that are not measures of financial performance under Canadian generally accepted accounting principles (Canadian GAAP) to provide readers with additional measures of the Company's financial performance including: EBITDA, normalized earnings per common share from continuing operations, free cash flow from operations and days sales outstanding in accounts receivable. These terms do not have any standardized meaning prescribed by Canadian GAAP and are therefore not necessarily comparable to similarly titled measures used by other companies.*

## OVERVIEW OF ALIANT'S LEGAL AND OPERATING STRUCTURE

The operating structure of Aliant Inc. ("Aliant" or "the Company") has been simplified during the first six months of 2003. Aliant is now comprised of three main lines of business: Telecommunications, Information Technology and Remote Communications.

The accompanying chart reflects the Company's lines of business and discontinued operations, and the main corporate entities or partnerships in each of these segments for the first six months of 2003. This chart also shows the

### Aliant Inc.



percentage of voting securities or partnership interests that Aliant currently holds, directly or indirectly, in these entities. As a result of recent divestitures the structure has become significantly more streamlined, simplified, and more operationally integrated than before.

## **BUSINESS OF THE COMPANY**

Aliant is an Atlantic Canadian based communications company that carries out various types of operations through its core lines of business. Telecommunications provides a full range of voice and data communications services including local, long distance, Internet and other wireline and wireless services. Information Technology provides IT fulfillment and consulting services to client's in several industry and geographic markets, including Telecommunications. Remote Communications offers mobile and fixed remote communication solutions to a global customer base through a combination of its own satellite and microwave telecommunications facilities and the distribution of services of other network operators.

## **RECENT DEVELOPMENTS**

A fourth segment, Emerging Business, existed until January 1, 2003. At that time Aliant transferred Innovatia Inc. ("Innovatia") from the Emerging Business segment to the Telecommunications segment for operating and reporting purposes, while the remaining companies of the former Emerging Business segment were either disposed of during the second quarter or are in the process of being disposed of. In April 2003, Aliant's 29.3 per cent interest in iMagicTV Inc. ("iMagicTV") was sold and the sale of Prexar LLC ("Prexar") closed in May 2003. At the end of June 2003, the sale of Aliant's 57.4 per cent interest in AMI Offshore Inc. ("AMI") was in progress. These businesses are now classified as discontinued operations.

Other non-core investments that Aliant is in the process of winding down or selling include the operations of Aliant Energy Services Inc. ("AES") and its 50 per cent interest in 3618412 Canada Inc. ("SableCom"). Consequently, these entities are now classified as discontinued operations.

On January 24, 2003, Aliant announced that the Company would seek a partner and buyer for its Information Technology business, Xwave Solutions Inc. ("xwave"). In order for this transaction to proceed, Aliant determined that the following conditions would need to be met:

- agree upon a transaction price representing the full value for the xwave business;
- find a suitable go-to-market partner to serve information technology and telecommunications customers;

- provide an environment to provide personal and professional growth for xwave employees; and
- operate in partnership with the new owner to satisfy Aliant's internal information technology requirements.

During this process Aliant held discussions with several companies; however, none were able to satisfy all of Aliant's conditions. Aliant concluded that it was better for its customers, employees and shareholders to retain xwave, as announced on June 19, 2003.

By leveraging xwave's expertise, knowledge and abilities Aliant expects to strengthen its position in the market and to contribute to the future growth of Aliant and the Atlantic Canadian economy. A formal restructuring plan for this segment will be actioned in the third quarter.

## **ALIAN INC. CONSOLIDATED OPERATING RESULTS**

The following is a summarized discussion of the consolidated operating results for the periods ended June 30, 2003. A more detailed discussion of the items that impact earnings before interest, taxes, depreciation and amortization (EBITDA)<sup>1</sup> is included in the "Operating results by line of business" section.

### **Operating revenues**

Aliant had consolidated operating revenues of \$1,308.6 million for the six months ended June 30, 2003 growing \$29.4 million from the same period in 2002. For the second quarter of 2003, revenues were \$665.5 million, an increase of \$12.2 million from the same period in 2002. Within the quarterly result, Remote Communications revenues grew \$22.7 million due to new contracts and high levels of military activity in the Middle East, and Telecommunications' total revenue grew \$4.3 million due mainly to the contribution from wireless and Internet customer growth. However, these gains were offset by a decrease of \$16.9 million in Information Technology revenues, due to weak economic conditions affecting the Information Technology industry.

### **Cost of operating revenues**

Costs of operating revenues for the second quarter and six months ended June 30, 2003 are relatively unchanged over the same periods in 2002 as revenue growth has been primarily derived from services causing minimal incremental direct cost.

### **Operating expenses**

Operating expenses increased \$36.8 million for the six months ended June 30, 2003 and \$8.2 million for the

<sup>1</sup> EBITDA is defined by the Company as operating income plus depreciation and amortization expense. EBITDA is not a measure of financial performance under Canadian GAAP and is not necessarily comparable to similarly titled measures used by other companies. The Company has included information concerning EBITDA because it believes that it is used by certain investors as one measure of the Company's financial performance. EBITDA should not be construed as an alternative to operating income or to cash flows from operating activities (as determined in accordance with Canadian GAAP) as a measure of liquidity.

second quarter compared to the same periods in 2002. The increase in Telecommunications' pension expense was \$9.2 million for the quarter. In addition, increases to salary and benefits and other expenses due to inflationary pressures, the costs of the Aliant brand campaign and amortization of wireless commissions and subsidies were partially offset by the results of productivity gains, savings from continued close working relationships with Bell and cost reduction initiatives in all lines of business.

### Depreciation and amortization

Depreciation and amortization expense increased by \$4.0 million in the second quarter and by \$6.8 million in the first six months compared to the same periods in 2002. The investment in recent years in broadband and wireless assets, which have depreciable lives as short as three years, is the principal reason.

### Other income (expenses)

Other income (expenses) changed from income of \$30.0 million in the second quarter of 2002 to a \$0.2 million expense in the second quarter of 2003, accounting for

most of the \$29.4 million change in the first six months of 2003 compared to the same period in 2002. During the second quarter of 2002 Aliant realized a \$32.5 million dilution gain with its reduction in ownership interest in Stratos Global Corporation ("Stratos"), not repeated this year. At the same time, a \$5.6 million write-down on portfolio investments was taken, partially offsetting the Stratos dilution gain. This year, the main components of other income (expenses) consist primarily of interest income offset by other miscellaneous charges.

### Gain on foreign exchange

A gain on foreign exchange was incurred in relation to Stratos in the first six months of 2002. Commencing July 1, 2002, Stratos qualified as a self-sustaining operation as discussed under the "Accounting policy changes" section of the Company's 2002 annual management's discussion and analysis. As a result, gains and losses on foreign exchange are no longer recorded in earnings after that date.

### Interest charges

Consolidated interest expense for the second quarter of

## Consolidated statements of income

For the period ended June 30 (thousands of dollars except per share amounts)	Three months			Six months		
	2003	2002	% change	2003	2002	% change
Operating revenues	\$ 665,474	\$ 653,272	1.9	\$ 1,308,593	\$ 1,279,165	2.3
Cost of operating revenues	164,807	167,747	(1.8)	346,692	347,516	(0.2)
Net operating revenues	500,667	485,525	3.1	961,901	931,649	3.2
Operating expenses	246,920	238,760	3.4	493,811	456,998	8.1
EBITDA <sup>1</sup>	253,747	246,765	2.8	468,090	474,651	(1.4)
Depreciation and amortization	108,777	104,796	3.8	217,969	211,193	3.2
Operating income	144,970	141,969	2.1	250,121	263,458	(5.1)
Other income (expenses)	(228)	29,955	—	(492)	28,868	—
Gain on foreign exchange	—	24,402	(100.0)	—	23,944	(100.0)
Interest charges	26,268	32,239	(18.5)	53,428	65,777	(18.8)
Income taxes	45,416	50,164	(9.5)	74,684	75,999	(1.7)
Non-controlling interest	5,423	13,083	(58.5)	10,346	18,276	(43.4)
Net income from continuing operations	67,635	100,840	(32.9)	111,171	156,218	(28.8)
Net income (loss) from discontinued operations	2,931	(16,338)	—	(1,717)	(18,263)	(90.6)
Net income	70,566	84,502	(16.5)	109,454	137,955	(20.7)
Preferred share dividends	2,385	2,385	—	4,769	4,769	—
Net income applicable to common shares	\$ 68,181	\$ 82,117	(17.0)	\$ 104,685	\$ 133,186	(21.4)
Basic and diluted earnings per common share, from continuing operations	\$ 0.47	\$ 0.71	(33.8)	\$ 0.77	\$ 1.09	(29.4)
Basic and diluted earnings per common share, from discontinued operations	0.02	(0.12)	—	(0.02)	(0.13)	84.6
Basic and diluted earnings per common share	\$ 0.49	\$ 0.59	(16.9)	\$ 0.75	\$ 0.96	(21.9)

<sup>2</sup> The 2002 results have been reclassified to reflect the impact of discontinued operations as required under Canadian GAAP to conform to the presentation adopted in the current year.

2003 decreased by \$6.0 million and \$12.3 million for the first six months compared to the same period in 2002. Most of this reduction, \$5.6 million for the second quarter and \$11.5 million for the first six months, was in Remote Communications where an equity issue of CDN\$148.0 million by Stratos in May of 2002 resulted in a significant reduction of debt in that operation and 1 per cent lower interest rates under its renewed credit facility. The average monthly debt in Remote Communications in the first six months of 2003 amounted to \$288.9 million compared to \$465.0 million for the first six months of 2002.

### Income taxes

Aliant's consolidated income tax provision for the second quarter and first six months decreased \$4.7 million and \$1.3 million compared to the same periods in 2002. The effective tax rate for the second quarter and first six months in 2003 was 38.3 per cent and 38.1 per cent compared to 2002 effective tax rates of 30.6 per cent and 30.3 per cent respectively. The 2002 effective rates were reduced by several non-recurring items including a reduction of the tax provision by \$6.8 million as a result of the recognition of tax benefits relating to the tax loss carry forward from Aliant's Remote Communications business in the first quarter of 2002. As well, in the second quarter of 2002 net income included non-taxable foreign exchange gains of \$24.4 million and a taxable dilution gain of \$32.5 million, thereby reducing the effective rate. In 2003 there are no unusual items effecting the tax provision thus with the reduction in net income for the second quarter and first six months, the tax provision has decreased and the effective tax rate is at a more normal level for 2003.

### Non-controlling interest

The non-controlling interest expense has decreased by \$7.7 million in the second quarter compared to the second quarter of 2002 representing most of the \$7.9 million decrease in the first six months of 2003 compared to the same period in 2002. The absence of foreign exchange gains from Stratos' net income in 2003, as discussed previously has resulted in a decrease in

net income for that segment as compared to last year.

### Net income (loss) from discontinued operations

As previously noted, Aliant has been exiting its non-core businesses and accordingly, the current and prior period results of the companies included as discontinued operations have been classified as such. The financial results from discontinued operations for the second quarter of 2003, including the gains or losses on the sale of the businesses, has improved over the same period in the prior year. The sale of Aliant's interest in iMagicTV realized a gain on sale, net of taxes, of \$10.9 million while the loss on the sale of Prexar was not material. The gain (loss) on the sale or wind up of AMI, SableCom and AES, which are not expected to be material, will be recorded when completed in 2003.

### EARNINGS PER COMMON SHARE ANALYSIS

Although earnings per common share from continuing operations for the three months and six months ended June 30, 2003 has declined from the same period in 2002, the main reason for the decline is due to results of activities outside of the normal operations of the Company, as outlined in the "Earnings per common share analysis" on the following page.

### OPERATING RESULTS BY LINE OF BUSINESS

#### Telecommunications operating results

Telecommunications' operating revenues increased by \$4.3 million in the second quarter and \$14.7 million in the first six months of 2003 compared to the same periods in 2002. As discussed more fully below, this revenue growth is attributable mainly to wireless and Internet, but partially offset by year over year revenue decreases in local, long distance and other revenues.

#### Local

Local revenues are earned through the provision of voice and data network access, telephone set rentals, enhanced service features and from the telecommunications industry-financed National Contribution Fund which supports

### Results of discontinued operations

	Three months		Six months	
	2003	2002	2003	2002
<i>For the period ended June 30 (thousands of dollars)</i>				
AMI	\$ (2,147)	\$ 406	\$ (3,581)	\$ 632
Prexar	(3,135)	(6,892)	(4,384)	(8,008)
iMagicTV	9,319	(9,696)	7,564	(10,000)
SableCom	(172)	(169)	(337)	(338)
Aliant Energy Services	(934)	13	(979)	(549)
Net income (loss) from discontinued operations	\$ 2,931	\$ (16,338)	\$ (1,717)	\$ (18,263)

local service in high-cost service areas. Local revenues decreased by \$5.0 million in the second quarter and \$7.0 million in the first six months compared to the same periods in 2002. This decrease is partly a reflection of the changing regulatory and competitive environment. A prior year CRTC ruling resulted in contribution regime changes that lowered the contribution rate and related revenue. In addition, the 2002 price caps decision decreased competitor payment rates and data access revenues. The remainder of the decrease in local revenues is attributable to reduced terminal rentals, as more customers are deciding to purchase, and lower consumer service charges, consistent with lower consumer network access services (NAS).

NAS volumes declined 0.8 per cent, as higher business NAS was more than offset by lower consumer NAS.

Despite this decrease in volumes local NAS revenue remains relatively unchanged for the second quarter and first six months of 2003 compared to the same periods in 2002, due to the higher percentage of total NAS from business. Business NAS is growing due to the small to medium sized business segment while consumer NAS is declining due to a combination of competition, cannibalization to wireless solutions and migration from dial-up to high-speed Internet.

Revenue from the provision of enhanced service features, such as call waiting and call display, grew 2.5 per cent in the second quarter and 4.7 per cent in the first six months compared to the same periods in 2002.

#### *Long distance*

Long distance revenues are derived from toll service,

### Earnings per common share analysis

For the period ended June 30	Three months			Six months		
	2003	2002	\$ change	2003	2002	\$ change
Earnings per common share from continuing operations	<b>\$ 0.47</b>	<i>(reclassified)<sup>2</sup></i> \$ 0.71	\$ (0.24)	<b>\$ 0.77</b>	<i>(reclassified)<sup>2</sup></i> \$ 1.09	\$ (0.32)
Gain on dilution on reduction of ownership interest in Stratos, net of tax	—	(0.19)	0.19	—	(0.19)	0.19
Gain on sale of investments, net of tax	—	(0.01)	0.01	—	(0.01)	0.01
Gain on foreign exchange, net of non-controlling interest	—	(0.09)	0.09	—	(0.09)	0.09
Investment write-downs, net of tax	—	0.03	(0.03)	—	0.03	(0.03)
Tax benefit recognized from loss carry forwards	—	—	—	—	(0.05)	0.05
Normalized earnings per common share from continuing operations <sup>3</sup>	<b>\$ 0.47</b>	\$ 0.45	\$ 0.02	<b>\$ 0.77</b>	\$ 0.78	\$ (0.01)

### Telecommunications operating results

For the period ended June 30 (thousands of dollars)	Three months			Six months		
	2003	2002	% change	2003	2002	% change
Local	<b>\$ 188,473</b>	\$ 193,514	(2.6)	<b>\$ 376,496</b>	\$ 383,473	(1.8)
Long distance	<b>97,799</b>	101,539	(3.7)	<b>198,603</b>	203,084	(2.2)
Wireless	<b>80,485</b>	67,404	19.4	<b>153,646</b>	128,628	19.4
Internet	<b>26,463</b>	22,439	17.9	<b>51,849</b>	44,287	17.1
Innovatia	<b>6,641</b>	6,181	7.4	<b>12,211</b>	11,304	8.0
Other revenues	<b>64,212</b>	68,712	(6.5)	<b>101,129</b>	108,420	(6.7)
Total operating revenues	<b>464,073</b>	459,789	0.9	<b>893,934</b>	879,196	1.7
Cost of operating revenues	<b>39,565</b>	49,182	(19.6)	<b>81,274</b>	95,169	(14.6)
Net operating revenues	<b>424,508</b>	410,607	3.4	<b>812,660</b>	784,027	3.7
Operating expenses	<b>201,091</b>	190,510	5.6	<b>401,522</b>	368,770	8.9
EBITDA	<b>\$ 223,417</b>	\$ 220,097	1.5	<b>\$ 411,138</b>	\$ 415,257	(1.0)
EBITDA as % of revenue	<b>48.1%</b>	47.9%		<b>46.0%</b>	47.2%	

<sup>3</sup> Normalized earnings per common share from continuing operations is defined by the Company as basic earnings per common share from continuing operations adjusted for items considered not to be in the normal course of operations. Normalized earnings per common share from continuing operations is not a measure of financial performance under Canadian GAAP and is not necessarily comparable to similarly titled measures used by other companies. The Company has included information concerning normalized earnings per common share from continuing operations because it believes that it is used by certain investors as one measure of the Company's financial performance. Normalized earnings per common share from continuing operations should not be construed as an alternative to earnings per common share from continuing operations.

data network services and long distance settlement. Long distance revenues have declined by \$3.7 million in the second quarter and \$4.5 million in the first six months compared to the same periods in 2002. The decline is due to decreased per minute settlement rates paid by other telecommunications carriers for calls terminating in Aliant's region.

Aliant's second quarter minute volumes decreased by 3.7 per cent over the same period in 2002, bringing the year-to-date increase in minute volumes to 1.7 per cent compared to the same period in 2002. Business long distance minutes have increased in Atlantic Canada, in part due to growth in the small to medium sized business segment but consumer minutes are lower as a result of changes in customer calling patterns. Aliant's market share of approximately 86.6 per cent of the long distance market in Atlantic Canada has decreased slightly due to certain short-term competitor promotions which, for the most part, were discontinued on June 30, 2003. Aliant continues to have focused price awareness and service oriented marketing campaign in the long distance market. Although minute volumes have decreased, the average revenue per minute has increased \$0.01 per minute to \$0.09, the first increase in eighteen months, as a result of changes to consumer pricing.

#### *Wireless*

Wireless revenues are earned through the provision of cellular, paging and mobile radio services. Aliant's wireless revenues increased \$13.1 million for the second quarter and \$25.0 million for the first six months compared to the same periods in 2002. This is driven by continued new demand for wireless services and increased average revenue per customer (ARPC). The number of Aliant's cellular customers at June 30, 2003 grew 13.2 per cent compared to June 30, 2002, including a 62.0 per cent increase in digital subscribers. Currently, 58.0 per cent of all cellular customers are digital compared to 40.5 per cent for the same period in 2002. Aliant maintains an industry leading position with market share of approximately 75 per cent for cellular services and churn of 1.4 per cent.

Part of the growing demand for cellular services is due to growth in new digital services and digital coverage expansion. At June 30, 2003 approximately 72 per cent of Atlantic Canada's population had access to digital cellular service, which is expected to increase to 83 per cent by the end of 2003. This growth in digital service, which carries higher monthly ARPC than analog, helped produce an ARPC of \$44.77 for the second quarter of 2003 compared with \$41.26 for the same period last year, an 8.5 per cent increase. This positive ARPC change is the result of growth

in the digital subscriber base, a 12.3 per cent increase in minutes of use and select pricing action. Currently, Aliant has the highest postpaid customer mix in Canada at 86.1 per cent of total cellular customers. This represents postpaid growth of 14.6 per cent from June 30, 2002 to June 30, 2003. For postpaid customers, which carry a higher ARPC than prepaid customers, average monthly revenue was \$51.04 for the second quarter of 2003 compared to \$47.53 during the same period in 2002, an increase of 7.4 per cent. Prepaid customer monthly ARPC has increased almost 17 per cent in the second quarter of 2003 to \$6.77 as a result of recent price increases and program changes.

#### *Internet*

Continued customer growth and a higher ARPC have resulted in an increase in Internet services revenue of \$4.0 million for the second quarter and \$7.6 million for the first six months compared to the same periods in 2002. During the second quarter of 2003 Aliant's high-speed customers increased by 24.1 per cent while the number of dial-up customers declined by 2.5 per cent, over the second quarter of 2002. The migration of high-speed customers from introductory to regular pricing and pricing changes have increased consumer high-speed ARPC by 12.9 per cent from the second quarter of 2002 to \$34.54 in the second quarter of 2003. As well, the effect of increased pricing in the business high-speed market has resulted in an increase of 12.5 per cent from the second quarter in 2002 to \$93.44 in the second quarter of 2003. As at June 30, 2003 Aliant's high-speed Internet services passed 63 per cent of the homes in Atlantic Canada. Aliant is aggressively managing an Internet churn of 2.1 per cent through new contract offers and increased customer contact.

Internet growth is anticipated as result of Aliant's launch of ultra high-speed Internet in selected areas during the third quarter of 2003 and a focused marketing program.

#### *Innovatia*

Revenues from Innovatia increased by \$0.5 million in the second quarter and \$0.9 million in the first six months compared to the same periods in 2002, as a result of new TeleWeb sales operations delivered in relationship with Marketbridge.

#### *Other revenues*

Other revenues decreased \$4.5 million for the second quarter and \$7.3 million for the first six months of 2003 compared to the same periods in 2002. Increased directory and product revenues were offset primarily due to the absence of Internet help desk revenue for the first six months, as the Information Technology segment now provides that service.

### Cost of operating revenues

Cost of operating revenues decreased by \$9.6 million in the second quarter and by \$13.9 million in the first six months of 2003 compared to the same periods in 2002. This decrease is attributable to lower per minute settlement rates and decreased Internet help desk costs as discussed above, offset by higher cost of goods sold associated with increased product sales.

### Operating expenses

Operating expenses increased by \$10.6 million in the second quarter and by \$32.8 million for the first six months of 2003 compared to the same periods in 2002 due primarily to increased pension expense. Pension expense increases contributed \$9.2 million and \$19.5 million to the quarterly and six month increases in operating expenses, respectively. Approximately \$10.8 million of the year-to-date increase in pension expense is attributable to a change in certain pension accounting assumptions (as discussed under "Significant accounting policies"). The remainder of the increase in pension expense in the first half of 2003 compared to 2002 relates to the increase in amortization of accumulated actuarial losses of prior years, an increasing pension obligation, a lower value for pension plan assets after capital market losses in recent years and higher pensionable earnings for employees.

Operating expenses also increased in the first six months by \$10.8 million for salaries and benefits as a result of cost of living increases and to support Aliant's focus on superior customer service, \$4.7 million increase in amortization of

wireless commissions and subsidies due to a higher base of deferred costs and \$1.5 million of costs related to the Aliant brand campaign underway in 2003. For the second quarter, these expenses increased \$7.4 million over the second quarter in 2002. These and other operating expense increases have been partially offset by various ongoing productivity and cost reduction initiatives, such as the consolidation of server platforms across the four Atlantic Provinces to reduce maintenance costs, advertising campaigns and market research in co-ordination with Bell, contact centre integration and the use of various workforce management tools.

### Information Technology operating results

Aliant's Information Technology revenues decreased \$16.9 million in the second quarter and \$30.4 million in the first six months of 2003 compared to the same periods in 2002. The company continues to feel the effects of the current economic slowdown on system integration service revenues and product revenues. Cost of sales decreased in correlation with reduced product sales. Year-to-date operating expenses increased as a result of a \$5.5 million charge relating to downsizing activities initiated in the first quarter. The second quarter saw the results of the reduced headcount and other cost containment strategies with a decrease in operating expenses.

On June 19, 2003, Aliant announced its decision to retain, restructure and operate xwave. xwave provides high quality information technology services to clients in several industry and geographic markets. Leveraging xwave's

### Other revenues

For the period ended June 30 (thousands of dollars)	Three months			Six months		
	2003	2002	% change	2003	2002	% change
Product sales	\$ 26,678	\$ 24,663	8.2	\$ 51,303	\$ 43,395	18.2
Directory revenues	26,113	25,339	3.1	27,876	27,053	3.0
Internet help desk	—	5,168	(100.0)	—	11,199	(100.0)
Other miscellaneous	11,421	13,542	(15.7)	21,950	26,773	(18.0)
	\$ 64,212	\$ 68,712	(6.5)	\$ 101,129	\$ 108,420	(6.7)

### Information Technology operating results

For the period ended June 30 (thousands of dollars)	Three months			Six months		
	2003	2002	% change	2003	2002	% change
Operating revenues	\$ 86,718	\$ 103,655	(16.3)	\$ 194,777	\$ 225,181	(13.5)
Cost of operating revenues	27,115	35,430	(23.5)	73,868	90,690	(18.5)
Net operating revenues	59,603	68,225	(12.6)	120,909	134,491	(10.1)
Operating expenses	57,757	59,390	(2.7)	120,598	117,076	3.0
EBITDA	\$ 1,846	\$ 8,835	(79.1)	\$ 311	\$ 17,415	(98.2)
EBITDA as % of revenue	2.1%	8.5%		0.2%	7.7%	

talents and realigning its strategy with Aliant's will require restructuring activities that will focus on various elements of the business, including leadership, processes, systems and organizational structure. This restructuring plan will be formalized in the third quarter and will impact less than 10 per cent of xwave's current workforce. As a result of the restructuring, xwave's third quarter results will include a charge of approximately \$15.5 million that will contribute approximately \$20.0 million in annual pre-tax savings.

### Remote Communications operating results

Aliant's Remote Communications line of business is represented by its 53.2 per cent ownership of Stratos Global Corporation, a publicly traded company (TSX:SGB). This section should be read in conjunction with Stratos Global Corporation's "Management's Discussion and Analysis of Financial Condition and Results of Operations for the six months ended June 30, 2003". Readers should note that Stratos reports its results in U.S. dollars thus it is necessary for Aliant to convert those results to Canadian dollars for its presentation. Accordingly, financial results may vary due to foreign exchange rate fluctuations. As well, Stratos and Aliant have different definitions of EBITDA. As a result, US\$1.9 million (CDN\$2.6 million) of other costs have been excluded from EBITDA on Stratos' financial statements but recorded in operating expenses on Aliant's financial statements and thus included in EBITDA.

Stratos' revenue increased \$22.7 million in the second quarter and \$40.2 million for the first six months of 2003 compared to 2002. The corporation's mobile satellite business continues to benefit from new contract awards and ongoing military presence in the Middle East. Cost of sales increased largely in accordance with revenue growth and in part due to changes in product mix. Operating

expenses for the first six months are relatively unchanged from the same period in the prior year despite the growth of the business. These results contributed to EBITDA growth of \$9.2 million for the second quarter and \$10.7 million for the first six months of 2003.

### FINANCIAL AND CAPITAL MANAGEMENT

Aliant's free cash flow from operations<sup>4</sup> continues to show significant increase over the first quarter and six months of 2002. This improvement is attributable to prudent management of working capital and reduced capital spending.

Aliant has US\$20.0 million in long-term debt that is due to be paid under the Stratos credit facilities within the remainder of 2003 and currently has no plans for major acquisitions in 2003.

Refer to the "Summary of consolidated cashflows" on the following page for more detailed information.

### Operating activities

Cash generated from operating activities was \$180.4 million for the second quarter and \$417.0 million for the first six months. This represents a significant increase of \$43.7 million and \$124.7 million respectively over the same periods in 2002 and is due to a continued focus on reducing the investment in working capital. This focus has resulted in a \$68.8 million reduction in working capital since June 30, 2002 with \$5.3 million of the reduction since March 31, 2003. Similarly, days sales outstanding in accounts receivable<sup>5</sup> decreased by 10.3 days to 65.5 days at June 30, 2003 compared to June 30, 2002 with 4.8 days reduction since March 31, 2003. Also contributing to cash from operations in 2003 was \$55.0 million of tax refunds received during the first quarter of 2003. The one time

### Remote Communications operating results

For the period ended June 30 (thousands of dollars)	Three months			Six months		
	2003	2002	% change	2003	2002	% change
Operating revenues	\$ 151,406	\$ 128,749	17.6	\$ 295,462	\$ 255,289	15.7
Cost of operating revenues	98,136	83,305	17.8	191,550	161,902	18.3
Net operating revenues	53,270	45,444	17.2	103,912	93,387	11.3
Operating expenses	20,898	22,300	(6.3)	38,659	38,830	(0.4)
EBITDA	\$ 32,372	\$ 23,144	39.9	\$ 65,253	\$ 54,557	19.6
EBITDA as % of revenue	21.4%	18.0%		22.1%	21.4%	

<sup>4</sup> Free cash flow from operations is defined as cash and cash equivalents from (used in) operating activities, less capital investments. Free cash flow from operations is not a measure of financial performance under Canadian GAAP and is not necessarily comparable to similarly titled measures used by other companies. The Company has included information concerning free cash flow from operations because it believes that it is used by certain investors as one measure of the Company's financial performance. Free cash flow from operations should not be construed as an alternative measure of liquidity.

<sup>5</sup> Day sales outstanding in accounts receivable is defined as accounts receivable divided by annualized sales including sales tax. Day sales outstanding in accounts receivable is not a measure of financial performance under Canadian GAAP and is not necessarily comparable to similarly titled measures used by other companies. The Company has included information concerning days sales outstanding in accounts receivable because it believes that it is used by certain investors as one measure of the Company's financial performance.

tax refunds resulted from implementation of tax planning strategies as well as the settlement of prior years' claims for Scientific Research and Experimental Development investment tax credits.

### Capital investments

Aliant's consolidated capital investments declined by \$36.8 million in the second quarter and by \$65.9 million in the first six months compared to the same periods in 2002.

#### Telecommunications

Telecommunications' capital asset additions in the second quarter and first six months in 2003 are lower compared to the same periods for 2002 due to significantly lower investment in the new products and service introduction, wireline voice and data network and broadband infrastructure. Aliant continues to work closely with Bell to leverage their new product and services investment. The significant expenditures relating to the wireline voice and data network in 2002 provided capacity for 2003

growth and as such no similar expenditures will be made in the current year. Following the completion of the 2002 investment of the broadband infrastructure, Digital Subscriber Line, most of the required infrastructure build-out for this service was in place.

The latest major infrastructure build-out programs in wireless and broadband have been largely completed. Telecommunications' continues to make capital investments in its networks principally to maintain current levels of capacity and capability as existing assets are retired, and in response to customer demand forecasts. Expansion in broadband infrastructure and wireless digital coverage is being carried out where the opportunities are economically justified. Additionally, Aliant is now placing greater focus on increasing the utilization of the infrastructure capacity already in place.

#### Information Technology

Information Technology's capital investments for the quarter

### Summary of consolidated cash flows

For the period ended June 30 (thousands of dollars)	Three months			Six months		
	2003	2002	% change	2003	2002	% change
Cash and cash equivalents from (used in):		(reclassified) <sup>2</sup>			(reclassified) <sup>2</sup>	
Operating activities:						
Net income from continuing operations	\$ 67,635	\$ 100,840	(32.9)	\$ 111,171	\$ 156,218	(28.8)
Other operating activities	112,792	35,870	214.4	305,795	136,089	124.7
	180,427	136,710	32.0	416,966	292,307	42.6
Capital investments	(77,915)	(114,704)	(32.1)	(154,569)	(220,458)	(29.9)
<b>Free cash flow from operations<sup>4</sup></b>	<b>102,512</b>	<b>22,006</b>	<b>365.8</b>	<b>262,397</b>	<b>71,849</b>	<b>265.2</b>
Financing activities	(143,716)	(68,422)	110.0	(281,264)	(18,155)	—
Other investing activities	(27,906)	(7,635)	265.5	(23,966)	6,259	—
Continuing operations	(69,110)	(54,051)	27.9	(42,833)	59,953	—
Discontinued operations	18,284	4,926	271.2	19,043	4,296	343.3
Effect of exchange rate changes on cash	(2,291)	—	—	(4,926)	—	—
Cash and short-term investments, beginning of period	285,576	243,678	17.2	261,175	130,304	100.4
<b>Cash and short-term investments, end of period</b>	<b>\$ 232,459</b>	<b>\$ 194,553</b>	<b>19.5</b>	<b>\$ 232,459</b>	<b>\$ 194,553</b>	<b>19.5</b>

### Capital investments

For the period ended June 30 (thousands of dollars)	Three months			Six months		
	2003	2002	% change	2003	2002	% change
Telecommunications	\$ 71,379	\$ 103,098	(30.8)	\$ 141,169	\$ 193,622	(27.1)
Information Technology	633	3,367	(81.2)	1,141	4,313	(73.5)
Remote Communications	5,082	8,004	(36.5)	11,100	22,197	(50.0)
Other	821	235	249.4	1,159	326	255.5
Total capital investments	\$ 77,915	\$ 114,704	(32.1)	\$ 154,569	\$ 220,458	(29.9)

and six months ended June 30, 2003 are significantly less than the investments made during the same periods in 2002. In particular spending in the second quarter of 2002 was higher as a result of investment made in xwave's internal financial and business systems and related implementation work. In the current year, tight controls were maintained over Information Technology's capital investments in order to bring the business model in line with the current and projected information technology market conditions. The information technology industry is not highly capital intensive and capital needs are driven largely by growth in the employee base and in the data processing business.

#### *Remote Communications*

Remote Communications' capital spending for the quarter ended June 30, 2003 has decreased compared to the second quarter of 2002 when land earth stations in England and New Zealand were upgraded. This activity combined with network upgrades required to support a U.S. Navy contract contributed to the higher capital investment activity in the first six months of 2002 as compared to 2003.

### **Financing activities**

#### *Telecommunications*

The most recent debt issue by Aliant Telecom Inc. ("Aliant Telecom") was on January 15, 2002, when it issued \$100.0 million of 5-year notes bearing interest at 5.35 per cent under its shelf prospectus for the issue of new Medium Term Notes (MTNs) in the Canadian market. The shelf prospectus expired in May 2003 and was not renewed at that time, as management does not foresee

### **Outstanding share information as of July 23, 2003:**

#### *Authorized*

Unlimited number of preference shares, issuable in series.

Unlimited number of common shares, without par value.

#### *Issued*

(thousands of dollars)

	<i>July 23, 2003</i>	
	Number of shares	Value
Preference shares, series 2	7,000,000	\$ 172,264
Common shares	138,516,323	1,035,551
		\$ 1,207,815

A summary of the Company's stock option plan is presented below:

	<i>July 23, 2003</i>	
	Number of options	Weighted average exercise price
Options outstanding	2,682,904	\$ 29.62
Options exercisable	1,926,844	\$ 29.81

any need for new borrowings in the capital markets for at least the remainder of 2003.

A \$65.0 million Aliant Telecom bond matured on June 16, 2003 and was repaid. Aliant Telecom has notified holders of \$7.5 million in first mortgage bonds maturing in July 2008 that these bonds will be redeemed on their July 28, 2003 call date.

Aliant Telecom maintains bank operating lines of credit totaling \$42.0 million, which remain undrawn at June 30, 2003.

#### *Information Technology*

xwave has reduced its operating and acquisition lines of credit from \$75.0 million at December 31, 2002 to an operating line of credit for \$15.0 million at June 30, 2003. The amount outstanding at June 30, 2003 on this line was \$7.2 million, a reduction of \$31.5 million since December 31, 2002. In addition, xwave receives internal financing from Aliant. At December 31, 2002 the balance owing to Aliant was \$26.4 million. In the first quarter, an additional \$44.1 million was advanced to xwave, with repayments of \$20.6 million made to Aliant to June 30, 2003 leaving a balance outstanding of \$49.9 million.

#### *Remote Communications*

In the second quarter of 2003, Stratos repaid US\$10.0 million of debt in accordance with its repayment schedule and US\$11.3 million in additional repayments for total repayments in the first six months of US\$31.3 million.

These payments were split equally between bridge and term facilities. As a result of Stratos reducing its bridge facility in 2003, the amount guaranteed by Aliant has been reduced from US\$28.0 million at the end of 2002 to US\$12.4 million at the end of June 2003.

#### *Corporate*

Aliant issued \$4.6 million in common equity during the second quarter by way of its common shareholder dividend reinvestment and stock purchase plan, and the exercise of options under its employee stock option plan. Shares were purchased on the open market to fulfill the requirements of the Company's employees' stock savings plan.

On July 18, 2002, Aliant announced acceptance by the Toronto Stock Exchange of notice of intention to purchase, from time to time, up to 1,600,000 of its outstanding common shares on the Toronto Stock Exchange pursuant to a Normal Course Issuer Bid (NCIB). This limit represented approximately 1.1 per cent of the issued and outstanding common shares of Aliant as of that date, being 139,567,382 common shares. Under the NCIB, the Company acquired, from time to time, its common shares at market price through the facilities of the Toronto Stock Exchange. Purchases of common shares could be made during the twelve month period commencing July 22, 2002 and ending on July 21, 2003. During 2002 Aliant purchased and cancelled 264,300 shares for an aggregate price of \$7.2 million. By June 30, 2003, Aliant had completed the purchase of all 1,600,000 shares permitted under this NCIB, purchasing and cancelling the balance of 1,335,700 common shares during the first six months of 2003 for an aggregate price of \$37.1 million.

On July 24, 2003 Aliant announced it will file with the Toronto Stock Exchange (TSX) a notice of Aliant's intention to purchase, from time to time, up to 6,925,000 of its issued and outstanding common shares. These shares represent 5.0 per cent of the total issued and outstanding shares which total 138,516,323 as at July 23, 2003. The application to the TSX includes provisions to enable Bell Canada, Aliant's majority shareholder, to participate

on a pro-rata basis in the bid process to the extent that it decides to do so. Bell Canada's participation is subject to regulatory and Board approval. Under the NCIB the Company would be able to acquire, from time to time, its common shares for cash at the market price through the facilities of the Toronto Stock Exchange at a pace and in an amount which will be at the company's discretion, subject to the rules of the Toronto Stock Exchange. The Board of Directors of Aliant believes that such purchases are in the best interest of Aliant and a desirable use of corporate funds. It is anticipated that purchases of shares under the renewal bid will be made during the twelve month period commencing August 6, 2003 and ending on August 5, 2004. All common shares of Aliant purchased pursuant to the NCIB will be cancelled.

Total dividends paid by Aliant to its common shareholders in the first half of 2003 increased by \$11.5 million over 2002 levels, despite the lower number of shares outstanding. Based on Aliant's demonstrated financial strength, its Board of Directors approved an increase in the quarterly dividend of 2.5 cents per common share in the third quarter of 2002. In addition, the Board of Directors has since approved another 2.5 cent increase to the quarterly dividend effective with the June 30, 2003 dividend, raising the annual rate to \$1.10 per common share.

Aliant paid preferred shareholder dividends of \$2.4 million for the second quarter of 2003, consistent with the amount paid in the second quarter of 2002.

Aliant maintains lines of credit totaling \$460.0 million in aggregate with its bankers, of which \$350.0 million is a committed facility supporting the Company's commercial paper program and \$110.0 million is the total of Aliant's uncommitted operating lines. There were no balances outstanding on these lines of credit as at June 30, 2003.

#### **Consolidated capital structure**

The percentage of debt to total capital was 42.0 per cent at June 30, 2003 compared to 45.2 per cent at December 31, 2002. The reduction in this ratio is due

#### **Consolidated capital structure**

*(thousands of dollars)*

	<b>June 30, 2003</b>		<b>December 31, 2002</b>	
			<i>(reclassified)<sup>2</sup></i>	
Common equity	<b>\$ 1,472,563</b>	<b>47.5%</b>	\$ 1,498,311	44.7%
Preferred equity	<b>172,264</b>	<b>5.6%</b>	172,264	5.2%
Non-controlling interest	<b>151,361</b>	<b>4.9%</b>	164,886	4.9%
Long-term debt, including current portion	<b>1,246,795</b>	<b>40.3%</b>	1,402,769	41.8%
Short-term debt, including bank indebtedness and interest payable	<b>53,804</b>	<b>1.7%</b>	113,719	3.4%
	<b>\$ 3,096,787</b>	<b>100.0%</b>	\$ 3,351,949	100.0%

to the reduction in debt outstanding held by Aliant Telecom and Stratos being greater than the net reduction in Aliant's common equity as a result of the repurchase and cancellation of common shares under the NCIB.

### **Other financial arrangements**

#### *Use of off-balance sheet arrangements*

Aliant uses a transfer of receivables arrangement whereby it sells certain accounts receivable to a securitization trust. The terms of the purchase and sale arrangement and accounting policy followed by Aliant are described in notes 2 and 4 to the unaudited interim consolidated financial statements for the period ended June 30, 2003.

The Company's retained interest in accounts receivable as at June 30, 2003 is \$28.7 million and is included in deferred charges. This retained interest equals the amount of overcollateralization in the receivables transferred, calculated as the excess of amounts transferred of \$158.7 million over the cash proceeds of \$130.0 million. A reduction in the amount of receivables eligible for sale to the trust caused a \$5.0 million net reduction in the proceeds to Aliant during the second quarter of 2003.

Aliant's subsidiaries also enter into various operating leases for equipment, satellite capacity and other network infrastructure. The amounts of estimated future minimum lease payments are detailed in note 16 to the unaudited interim consolidated financial statements for the period ended June 30, 2003.

#### *Use of derivative financial instruments*

Aliant's subsidiaries use certain derivative financial instruments in the management of foreign currency and interest rate exposures. Further information concerning Aliant's policy and use of derivative financial instruments is contained in note 2 to the unaudited interim consolidated financial statements for the period ended June 30, 2003.

The following derivative financial instruments were outstanding at June 30, 2003:

- Interest rate swap agreements involving the exchange of LIBOR floating interest rate on US\$160.0 million of Stratos' long-term debt obligations for fixed interest rates of 5.43 per cent in order to manage the associated interest rate exposure. Changes in the LIBOR floating interest rate since the swap commenced would have resulted in a payment of US\$9.1 million to the financial institution had the agreement been cancelled at the option of Stratos at June 30, 2003.
- Interest rate swaption agreements involving the monetization of call options are embedded in certain long-term debt obligations of Aliant Telecom. \$5.4 million

in unamortized premium income is recorded as a deferred credit on Aliant's balance sheet at June 30, 2003 related to the swaption. Since inception of the agreements, interest rates have changed such that cancellation of the swaptions at June 30, 2003 would have required a payment of \$25.3 million to the financial institution.

#### *Pension obligations*

Aliant performs a valuation on its non-contributory defined benefit plans at least every three years to determine the actuarial present value of the accrued pension and other employment benefits. The Company is currently in the process of conducting a full actuarial valuation of its pension plans in 2003. Aliant anticipates that these plans will require significant levels of funding in 2003, largely due to the negative equity market returns since the last valuation of its pension plans. In advance of receiving the results of the 2003 actuarial valuation, Aliant has estimated that pension funding requirements for 2003 will be at least \$30.0 million. Based on this estimation Aliant began making additional contributions to each plan in the first half of 2003. Contributions for the six months ended June 30, 2003 total \$15.6 million. Upon completion of the 2003 valuation the Company will adjust its year-to-date contributions to reflect new current service rates, and will make special deficit-funding payments if required. Aliant will also review the current pension expense including the amortization of actuarial losses to ensure the appropriate provisions are being made.

### **CONSOLIDATED RISK ASSESSMENT**

While management is confident about the Company's long-term prospects, the risks and uncertainties noted below could have a negative effect on the financial condition or results of operations of Aliant or its subsidiaries. The risks noted may not be all inclusive as there may be others that Aliant is currently unaware of or presently considers insignificant to its consolidated operations.

#### **General economic conditions**

Changes in general economic conditions, consumer confidence and spending affect the demand for Aliant's communications products and services. In particular, the performance of Aliant's Information Technology and components of the Telecommunications business have been negatively affected. Weak industry and economic conditions could lead to:

- lower than anticipated demand for system integration consulting and information technology products;
- lower than expected growth in data revenue, because of softer demand from enterprises and wholesale customers;

- lower than anticipated long distance and wireless revenues due to decrease in tourists visiting region as a result of the strengthening of the Canadian dollar and incidences of SARS in Canada; and
- increased credit risk of customers thus increasing the provisions for uncollectible receivables.

The existence of these conditions or the emergence of new conditions could reduce revenues or increase costs, negatively impacting results. The Company constantly monitors the economic conditions and implements strategies to mitigate risks or adjust assumptions used in recording the effects of these risks on the Company's results.

### **Changing technology**

Aliant operates in an industry that experiences constant technological change, driven by industry standards, customer demands and short product life cycles. While a timely response to changing technology presents Aliant with the opportunity to obtain gains in new high growth revenue areas, failure to respond in a timely and effective manner could result in current products or services becoming unmarketable or cause prices to fall which could result in reduced net income due to inventory write-offs and decreased revenues. The Company is responding to the fast-pace of technological change by embracing new service development with strategic partners, accelerating new service introduction and developing an integrated growth plan to become the next generation services provider.

### **Increasing competition**

Atlantic Canada is one of the most competitive regions for telecommunications services in North America. Competition for local service consists of national telecommunications competitors and regional cable companies and the entry of other competitors is considered a possibility. Cable companies and independent Internet service providers have increased Internet competition to such a degree that pricing in Atlantic Canada is amongst the lowest in North America. The wireless industry is also highly competitive. Aliant competes locally with a number of national wireless carriers. Competition is expected to intensify through the development of new technologies, products and services and through consolidations in the industry. The threat of new competitors or an increased presence of existing competitors is always a possibility. Competition could affect pricing strategies and market share thus lowering revenues and net income. Aliant is constantly monitoring this situation and is making continuous efforts to ensure superior quality of service and product offerings that are responsive to market demands and simple for the customer to access and use.

### **Changing regulations**

The CRTC continues to focus on ensuring that there is a competitive Canadian environment for certain telecommunications services through continued regulation of incumbent local exchange carriers such as Aliant Telecom. In the past year, Aliant's profitability has been negatively impacted by regulatory changes concerning price caps, contribution regime and bundling. The restrictions on pricing and packaging of Aliant Telecom's products and services make it increasingly difficult to respond to competition. The CRTC is also giving consideration to eliminating the Telecom foreign ownership restrictions which may result in increased competition from foreign companies with greater access to capital. Changing CRTC regulation may impact Aliant's ability to compete and as a result negatively impact net operating revenues. Aliant will continue its dialogue with the CRTC in an attempt to increase bi-lateral understanding of key business and regulatory initiatives.

### **Improving productivity and cost reductions**

The Company has and will continue to implement productivity and cost reduction initiatives. Many of these initiatives result from Aliant's continued focus on alignments with strategic partners, business process improvements and restructuring activities. In the upcoming quarters Aliant will be undertaking significant initiatives to improve the profitability of the Information Technology segment. There could be a negative impact on the Company's profitability if productivity and cost reduction initiatives are unsuccessful.

### **Renegotiating labour agreements**

Aliant's employees play an integral role in the Company's ability to provide a competitive advantage based on quality of service. The Council of Atlantic Telecommunications Unions (CATU) represents many of Aliant's unionized employees. These employees have been without a collective agreement since December 31, 2001. Management has been involved in negotiations with CATU since March 4, 2002 and will continue bargaining into the third quarter of 2003. Renegotiating collective agreements could result in higher labour costs or work disruptions thus affecting the operating results and financial condition of Aliant.

### **SIGNIFICANT ACCOUNTING POLICIES**

Aliant's consolidated financial statements have been prepared in accordance with Canadian GAAP. Greater detail on the significant accounting policies used by the Company is provided in note 1 to the consolidated financial statements for the year ended December 31, 2002 and note 2 to the unaudited interim consolidated financial statements for the period ended June 30, 2003.

The accounting policies and methods used are consistent with those in effect in the most recent annual audited financial statements except as explained under stock-based compensation and other stock-based payments.

The preparation of financial statements in conformity with Canadian GAAP requires Aliant to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses and the disclosure of contingent assets and liabilities in the financial statements. Aliant constantly evaluates these estimates and assumptions.

Aliant bases its estimates and assumptions on past experience and other factors that are deemed reasonable under the circumstances. This involves varying degrees of judgment and uncertainty, thus the amounts currently reported in the financial statements could prove to be inaccurate in the future.

Aliant considers the estimates and assumptions described in this section to be an important part in understanding the financial statements. These estimates and assumptions rely heavily on management's judgment, are based on factors that are inherently uncertain and thus are subject to change.

The following describes key assumptions and estimates used in significant accounting policies and changes in the accounting standards implemented during the period.

#### **Post employment benefits**

Aliant and its subsidiaries provide certain pension plans and other non-pension post employment benefits to qualified employees. The amounts reported in the financial statements in relation to these benefits are determined using actuarial calculations that are based on assumptions. Significant actuarial assumptions include the discount rate, expected long-term rate of return on plan assets, rate of compensation increase, and the per capita cost of covered health care benefits. These assumptions are disclosed in note 10 to the consolidated financial statements for the year ended December 31, 2002. The Company reviews the appropriateness of its assumptions on an annual basis. Aliant reduced the assumed rate of return on pension assets from 9.0 per cent to 7.5 per cent and lowered the discount rate used to calculate pension liabilities from 7.0 per cent to 6.75 per cent, commencing December 31, 2002. Management believes that these assumptions are appropriate; but variances between assumptions and actual results could impact the accrued benefit obligation and related expense. Management disclosed the sensitivity of its key assumptions in note 10 to the consolidated financial statements for the year ended December 31, 2002.

The change in pension assumptions adopted December 31, 2002 translates into increased pension expense and reduced pre-tax earnings for the quarter and six months ended June 30, 2003 of \$5.4 million and \$10.8 million respectively, with an anticipated annual pre-tax increase of approximately \$21.7 million. The impact of this, along with the increase in amortization of accumulated actuarial losses of prior years, an increasing pension obligation, a lower value for pension plan assets after capital market losses in recent years and higher pensionable earnings for employees will contribute to an anticipated annual pre-tax cost of approximately \$37.0 million in relation to pension expenses.

Aliant reported unamortized net actuarial losses totaling \$372.3 million in its pension plans at the end of 2002. Canadian GAAP prescribes how this unamortized loss is to be recognized as additional pension expense and recognizes that future investment returns on plan assets and actuarial changes in the plans can influence the amount of the loss and can even reverse it over time. Based on these accounting principles, Aliant estimates that amortization of past actuarial losses will contribute \$5.8 million to pension expense in 2003, which is included in the \$37.0 million increase in pension expense previously noted. Amortization of \$2.9 million has been expensed in the first half of 2003. The impact of prior year unamortized pension fund losses on future pension expense cannot be determined with certainty because it will be influenced by experience in the current and future years. However, it is expected that pension expense will remain at least at the current level for the next few years.

#### **Impairment of long-lived assets**

The Company annually reviews the value associated with the goodwill of all its reporting units to ensure that the fair value is greater than, or equal to, the carrying value. In addition, events or changes in circumstances throughout the year may indicate that the carrying value of goodwill or other long-lived assets may not be recoverable in which case an impairment provision is recorded. Any impairment to the value of these assets is charged to income in the period such impairment is determined.

Aliant uses the projected discounted cash flow method to measure impairment. The Company believes that its estimates of future cash flows and fair value are reasonable. The assumptions are based on internal planning and reflect the Company's best estimates. These assumptions are subject to inherent uncertainties that are beyond management's control, hence the results of the impairment test could be different if there is a change in assumptions or conditions. Aliant is unable to predict whether an event

that triggers impairment will occur, when it will occur or how it will affect the asset values that have been reported.

### **Legal and regulatory contingencies**

Aliant may become involved in various litigation and regulatory proceedings in the normal course of its business. Pending litigation, regulatory initiatives or regulatory proceedings represent potential financial loss. The Company accrues potential losses if they believe the loss is probable and can be reasonably estimated. Estimates of loss are based on consultation with legal counsel and involve analyzing potential outcomes and assuming various litigation and settlement strategies. If the resolution of a legal or regulatory matter results in a judgment against Aliant that has not been accrued, it could have a significant and adverse effect on our results of operations, cash flows and financial position in the period in which the judgment or settlement occurs.

### **Stock-based compensation and other stock-based payments**

The accounting standard issued by the Canadian Institute of Chartered Accountants (“CICA”) on stock-based compensation in late 2001 encouraged, but did not require, the use of the fair value method to account for stock-based awards, other than direct awards of stock, stock appreciation rights and similar awards with a cash settlement feature. In recognition of the demands of the financial community and the fact that standard setters in Canada and the United States are moving towards the adoption of mandatory fair value accounting, Aliant began expensing stock-based awards issued to employees subsequent to December 31, 2002 using the fair value approach. Previously, this cost was estimated and disclosed in the notes to the financial statements but not recognized as an expense in the financial statements themselves. This accounting change resulted in a related expense for the three months and six months ended June 30, 2003 of \$0.2 million and \$0.4 million. The cumulative expected negative impact on pre-tax income for fiscal 2003 is \$1.0 million.

The fair value of each option granted is estimated on the date of grant using the Black-Scholes option-pricing model based on the weighted average assumptions for dividend yield, expected volatility, risk-free interest rate

and expected life as disclosed in note 14 of the unaudited interim consolidated financial statements for the period ended June 30, 2003.

### **FORWARD-LOOKING STATEMENTS**

Certain statements contained in this document and in particular the statements contained in the “Consolidated risk assessment” and “Significant accounting policies” sections, constitute forward-looking statements. These forward-looking statements relate to future financial condition and results of operations of Aliant. These statements are based on current expectations and estimates about the markets in which Aliant operates and management’s beliefs and assumptions regarding these markets. In some cases forward-looking statements may be identified by words such as “anticipate”, “believe”, “could”, “expect”, “plan”, “seek”, “may”, “intend”, “will”, “target”, “goal” and similar expressions. These statements are subject to important risks and uncertainties which are difficult to predict and assumptions which may prove to be inaccurate. Some of the factors which could cause results or events to differ materially from current expectations include but are not limited to those factors identified in the “Consolidated risk assessment” section, many of which are beyond the control of Aliant. Should any of these factors impact the Company in an unexpected manner, or should assumptions underlying the forward-looking statements prove incorrect, the results or events predicted in management’s discussion and analysis may differ materially from actual results or events. Consequently, all of the forward-looking statements made in this document and the documents referred to within are qualified by these cautionary statements, and there can be no assurance that the results or developments anticipated by Aliant will be realized or, even if substantially realized, that they will have the expected consequences for Aliant. Readers should also consult the Annual Information Form for the year ended December 31, 2002 for Aliant Inc., Aliant Telecom Inc., and Stratos Global Corporation. Readers should not place undue reliance on any forward-looking statements. Further, Aliant disclaims any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events, or any other occurrence.

# Statements (unaudited)

## CONSOLIDATED BALANCE SHEETS

<i>(thousands of dollars)</i>	As at June 30, 2003	As at December 31, 2002 <i>(note 3)</i>
<b>Assets</b>		
Current assets		
Cash and short-term investments	\$ 232,459	\$ 261,175
Accounts receivable (note 4)	398,377	410,485
Inventory	27,360	27,770
Prepayments	67,171	41,228
Income tax receivable	11,774	55,536
Current assets held for sale (note 3)	22,175	24,148
	<b>759,316</b>	<b>820,342</b>
Capital investments (note 5)	<b>2,214,826</b>	<b>2,313,793</b>
Other assets		
Long-term investments (note 6)	32,884	37,640
Deferred charges	117,430	118,868
Future income tax asset	45,581	18,885
Goodwill (note 7)	319,712	365,740
Non-current assets held for sale (note 3)	2,654	20,448
	<b>518,261</b>	<b>561,581</b>
<b>Total assets</b>	<b>\$ 3,492,403</b>	<b>\$ 3,695,716</b>
<b>Liabilities and shareholders' equity</b>		
Current liabilities		
Notes payable and bank advances (note 8)	\$ 35,667	\$ 95,591
Payables and accruals (note 9)	264,797	223,446
Income tax payable	20,048	10,939
Future income tax liability	12,211	12,658
Long-term debt due within one year (note 10)	52,463	140,278
Current liabilities held for sale (note 3)	19,721	19,143
	<b>404,907</b>	<b>502,055</b>
Long-term debt (note 10)	1,194,332	1,262,491
Accrued benefit obligation	76,158	73,873
Deferred credits	12,246	12,834
Non-current liabilities held for sale (note 3)	8,572	9,002
	<b>1,696,215</b>	<b>1,860,255</b>
Non-controlling interest (note 11)	<b>151,361</b>	<b>164,886</b>
Shareholders' equity		
Capital stock (note 12)	1,207,575	1,237,650
Contributed surplus	69,320	69,320
Retained earnings	385,913	354,080
Cumulative translation adjustment	(17,981)	9,525
	<b>1,644,827</b>	<b>1,670,575</b>
<b>Total liabilities and shareholders' equity</b>	<b>\$ 3,492,403</b>	<b>\$ 3,695,716</b>

See accompanying notes to the consolidated financial statements  
Signed on behalf of the Board of Directors



Charles White  
Chairman



Edward Reevey  
Director

## CONSOLIDATED FINANCIAL STATEMENTS

## CONSOLIDATED STATEMENTS OF INCOME

	Three months		Six months	
	2003	2002	2003	2002
<i>For the period ended June 30 (thousands of dollars except per share amounts)</i>				
		(note 3)		(note 3)
Operating revenues (note 13)	\$ 665,474	\$ 653,272	\$ 1,308,593	\$ 1,279,165
Expenses				
Cost of operating revenues	164,807	167,747	346,692	347,516
Operating expenses	246,920	238,760	493,811	456,998
Depreciation and amortization	108,777	104,796	217,969	211,193
	520,504	511,303	1,058,472	1,015,707
Operating income	144,970	141,969	250,121	263,458
Other income (expenses)				
Gain on foreign exchange (note 2)	—	24,402	—	23,944
Other income (expenses)	(228)	29,955	(492)	28,868
	(228)	54,357	(492)	52,812
Interest charges				
Interest on long-term debt	26,043	32,371	52,911	65,556
Other interest expense (income)	225	(132)	517	221
	26,268	32,239	53,428	65,777
Income before underlisted items	118,474	164,087	196,201	250,493
Income taxes	45,416	50,164	74,684	75,999
Income before non-controlling interest	73,058	113,923	121,517	174,494
Non-controlling interest	5,423	13,083	10,346	18,276
<b>Net income from continuing operations</b>	<b>\$ 67,635</b>	<b>\$ 100,840</b>	<b>\$ 111,171</b>	<b>\$ 156,218</b>
<b>Net income (loss) from discontinued operations (note 3)</b>	<b>\$ 2,931</b>	<b>\$ (16,338)</b>	<b>\$ (1,717)</b>	<b>\$ (18,263)</b>
<b>Net income</b>	<b>\$ 70,566</b>	<b>\$ 84,502</b>	<b>\$ 109,454</b>	<b>\$ 137,955</b>
<b>Earnings per common share (note 14)</b>				
Basic from continuing operations	\$ 0.47	\$ 0.71	\$ 0.77	\$ 1.09
Basic from discontinued operations	0.02	(0.12)	(0.02)	(0.13)
Basic	\$ 0.49	\$ 0.59	\$ 0.75	\$ 0.96
Diluted from continuing operations	\$ 0.47	\$ 0.71	\$ 0.77	\$ 1.09
Diluted from discontinued operations	0.02	(0.12)	(0.02)	(0.13)
Diluted	\$ 0.49	\$ 0.59	\$ 0.75	\$ 0.96

See accompanying notes to the consolidated financial statements

## CONSOLIDATED STATEMENTS OF RETAINED EARNINGS

	2003	2002
<i>For the six months ended June 30 (thousands of dollars)</i>		
Retained earnings, beginning of period	\$ 354,080	\$ 317,988
Net income	109,454	137,955
Preferred share dividends	(4,769)	(4,769)
Common share dividends	(72,852)	(61,319)
<b>Retained earnings, end of period</b>	<b>\$ 385,913</b>	<b>\$ 389,855</b>

See accompanying notes to the consolidated financial statements

## CONSOLIDATED STATEMENTS OF CASH FLOWS

For the period ended June 30 (thousands of dollars)	Three months		Six months	
	2003	2002 <i>(note 3)</i>	2003	2002 <i>(note 3)</i>
Cash and cash equivalents from (used in) operations				
Net income from continuing operations	\$ 67,635	\$ 100,840	\$ 111,171	\$ 156,218
Add (deduct) non-cash items:				
Depreciation and amortization	108,777	104,796	217,969	211,193
Gain on foreign exchange	—	(24,402)	—	(23,944)
(Gain) loss on disposal of assets	379	(29,774)	427	(29,928)
Future income taxes	(476)	15,650	(26,692)	(1,877)
Deferred pension costs	11,659	2,907	23,319	5,815
Non-controlling interest share of income	5,423	13,083	10,346	18,276
Other non-cash items	(420)	(49)	(297)	(103)
	192,977	183,051	336,243	335,650
Change in non-cash working capital balances related to operations	(12,550)	(46,341)	80,723	(43,343)
	180,427	136,710	416,966	292,307
Cash and cash equivalents from (used in) financing				
Repurchase of accounts receivable	(5,000)	(5,000)	(5,000)	(15,000)
Net proceeds (repayments) of notes payable and bank advances	7,822	22,508	(59,924)	(9,391)
Proceeds from long-term debt	—	—	—	100,000
Repayments of long-term debt	(92,962)	(190,883)	(108,783)	(191,415)
Increase in non-controlling interest	138	109,917	138	108,162
Proceeds from issue (repurchase) of common shares	(15,614)	9,165	(34,649)	18,499
Preferred share dividends	(2,385)	(2,385)	(4,769)	(4,769)
Common share dividends	(35,715)	(11,744)	(68,277)	(24,241)
	(143,716)	(68,422)	(281,264)	(18,155)
Cash and cash equivalents from (used in) investing				
Capital investments	(77,915)	(114,704)	(154,569)	(220,458)
Proceeds on sale of investments	374	7,703	2,481	8,676
Increase in investments	(14)	(800)	(14)	(1,051)
Increase in deferred credits	(28,266)	(14,538)	(26,433)	(1,366)
	(105,821)	(122,339)	(178,535)	(214,199)
Cash and short-term investments from (used in) continuing operations	(69,110)	(54,051)	(42,833)	59,953
Cash and short-term investments from (used in) discontinued operations (note 3)	18,284	4,926	19,043	4,296
Cash and short-term investments, beginning of period	285,576	243,678	261,175	130,304
Effect of exchange rate changes on cash	(2,291)	—	(4,926)	—
<b>Cash and short-term investments, end of period</b>	<b>\$ 232,459</b>	<b>\$ 194,553</b>	<b>\$ 232,459</b>	<b>\$ 194,553</b>
Supplementary disclosure				
Interest paid	\$ 33,997	\$ 42,078	\$ 55,458	\$ 63,658
Income taxes paid	\$ 47,626	\$ 40,454	\$ 61,623	\$ 88,992

See accompanying notes to the consolidated financial statements

# Statement notes

## 1 INTERIM FINANCIAL STATEMENTS

The accounting policies and methods followed for interim reporting purposes are consistent with those in effect for the most recent annual financial statements for the year ended December 31, 2002, except as explained in note 2

under accounting changes. These unaudited interim financial statements should be read in conjunction with the Company's audited financial statements for the year ended December 31, 2002.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### Consolidated financial statements

The consolidated financial statements include the accounts of Aliant Inc. ("the Company") and all entities that are controlled by the Company and its proportionate share of jointly controlled entities.

At June 30, 2003, the principal subsidiaries of the Company include: Aliant Telecom Inc., Innovatia Inc., Aliant ActiMedia, Aliant Information Technology Inc., Xwave Solutions Inc., and Stratos Global Corporation.

The following subsidiaries have been classified as discontinued operations: AMI Offshore Inc., Prexar LLC, Aliant Energy Services Inc., 3618412 Canada Inc. ("SableCom"), as discussed in note 3.

### Use of accounting estimates

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results may differ from those estimates.

### Regulation

Aliant Telecom Inc., the Company's major telecommunications subsidiary, is subject to regulation by the Canadian Radio-

television and Telecommunications Commission ("CRTC"). On May 30, 2002 the CRTC released its Decision 2002-34 ("price cap decision"), which includes prescribed new rules effective for a four year period to determine the rates charged for certain telecommunications services. In 2003, the expected impact of the decision on the Company may change following further analysis and clarification from the CRTC on the deferral account mechanism as discussed in note 17.

### Cash and short-term investments

Cash and short-term investments consist of cash on hand and balances with banks, and investments in money market instruments with original maturity of less than 90 days that are readily convertible to known amounts of cash and are subject to an insignificant risk of change in fair value.

### Transfer of receivables

The Company entered into a Purchase and Sale Agreement under which it sells its interest in a pool of present and future eligible accounts receivable to a securitization trust that issues securities to investors. These transactions are accounted for as sales when the Company is considered to have surrendered control over the transferred accounts receivable and receives proceeds from the trust, other than a beneficial interest in the assets sold. Losses or gains on these transactions are recognized as other expenses or income and are dependent in part on the previous carrying amount of the accounts receivable transferred, which is allocated between the accounts receivable sold and the

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

retained interest, based on their relative value at the date of the transfer. The Company determines fair value based on the present value of future expected cash flows using management's best estimates of key assumptions such as discount rates, weighted average life of accounts receivable and credit loss ratios.

### Inventory

Inventory is valued at the lower of cost and net realizable value.

### Income taxes

The Company follows the liability method of accounting for income taxes. Under this method future income tax assets and liabilities are determined based on the differences between the financial reporting and tax bases of assets and liabilities and are measured using substantively enacted tax rates and laws that are expected to be in effect in the periods in which the future tax assets or liabilities are expected to be realized or settled. The effect of a change in substantively enacted income tax rates on future income tax assets and liabilities is included in income in the period that the change occurs.

### Capital investments

Capital investments are recorded at cost. Depreciation is computed on a straight-line basis (outlined in the table below) over the useful lives of the assets.

<i>Asset</i>	<i>Method</i>	<i>Rate</i>
Buildings and towers	Straight line	10 – 40 years
Telecommunications facilities and equipment	Straight line	4 – 40 years
Application software and other equipment	Straight line	3 – 15 years

Depreciation is not recorded on capital under construction that is not yet operational.

Gains and losses on the disposal of identifiable capital investments are included in income in the period they occur.

### Long-term investments

The Company accounts for its investments in affiliated companies over which it has significant influence using the equity method of accounting, whereby the investments are initially recorded at cost, and subsequently adjusted to recognize the Company's share of earnings or losses of the investee companies and reduced by dividends received.

Portfolio investments are accounted for at cost. Declines in market value below cost are recognized when such declines are considered to be other than temporary.

### Deferred charges

Deferred charges include debt issue costs, which are amortized on a straight-line basis over the term of the related debt, cellular dealer commissions and hardware subsidies, which are amortized over the length of customer contracts, as well as Internet commissions, which are amortized over a defined customer relationship period. Also included in deferred charges is the Company's retained interest in accounts receivable transferred to a securitization trust.

### Goodwill

Goodwill represents the excess, at the dates of acquisition, of the costs over the fair values of the net amounts assigned to identifiable assets acquired and liabilities assumed. The Company annually reviews the goodwill of all its reporting units to ensure that its fair value remains greater than, or equal to, carrying value. Any impairment in the value of goodwill is charged to income in the period such impairment is determined.

### Derivative financial instruments

Derivative financial instruments are used by the Company in the management of its foreign currency and interest rate exposures. The Company's policy is not to utilize derivative financial instruments for trading or speculative purposes.

The Company's policy is to formally designate each derivative financial instrument as a hedge of specific assets and liabilities on the balance sheet or to specific firm commitments. The Company believes the derivative financial instruments are effective as hedges, both at inception and over the term of the instrument, as the term to maturity and the (notional) principal amount match the terms of the instrument or transaction being hedged.

Foreign exchange forward contracts may be used periodically by the Company to manage its exposure to fluctuations in currency exchange rates. Foreign exchange forward contracts are accounted for as hedges to the extent that they are designated as, and are effective as, hedges of firm foreign currency commitments. Gains and losses on foreign exchange forward contracts are recognized in income in the same period as gains and losses on the underlying hedged transactions are recognized.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

The Company has entered into interest rate swap and swaption agreements in order to manage the interest rate exposure associated with certain long-term debt obligations. Amounts payable or receivable under interest rate swap agreements are recognized as adjustments to interest expense. In addition, premiums received or paid, if any, under interest rate swaption agreements are amortized as an adjustment to interest expense over the period from receipt, or payment, of the premium income to maturity of the underlying debt obligation.

Realized and unrealized gains or losses associated with derivative instruments, which have been terminated or cease to be effective prior to maturity, are deferred and reported under deferred charges on the balance sheet and recognized in income in the period in which the underlying hedged transaction is recognized. In the event a designated hedged item is sold, extinguished or matures prior to the termination of the related derivative instrument, any realized or unrealized gain or loss on such derivative instrument is recognized in income.

### **Post employment benefits**

The Company and its subsidiaries provide certain pension plans and other non-pension post employment benefits to qualified employees. These include contributory defined contribution pension plans, non-contributory defined benefit final average pension plans and other retirement benefits such as life insurance and health care plans.

The Company accrues its obligations under employee benefit plans and the related costs, net of plan assets. The Company has adopted the following policies for its defined benefit pension plans and other post employment benefits:

- (a) The cost of pensions and other post employment benefits earned by employees is actuarially determined using the projected benefit method pro rated on service and management's best estimate of expected plan investment performance, salary escalation, retirement ages of employees and expected health care costs.
- (b) For the purpose of calculating the expected return on plan assets, those assets are valued at market-related value.
- (c) Past service costs from plan amendments are amortized on a straight-line basis over the average remaining service period of employees active at the date of amendment.
- (d) The excess of the net actuarial gain (loss) over 10 per cent of the greater of the benefit obligation and the market-related value of plan assets is amortized over the average remaining service period of active employees being 16 years at June 30, 2003 (December 31, 2002 – 16 years).

- (e) When the restructuring of a benefit plan gives rise to both a curtailment and a settlement of obligations, the curtailment is accounted for prior to the settlement.
- (f) A valuation is performed at least every three years to determine the actuarial present value of the accrued pension and other non-pension post employment benefits.

Defined contribution plan costs are recognized as employees render services during the year.

### **Earnings per common share**

Earnings per common share is based on the average number of common shares outstanding for the period. Diluted earnings per share is computed in accordance with the treasury stock method and based on the average number of common shares and dilutive common share equivalents.

### **Stock-based compensation plan**

The Company has a stock-based compensation plan for executives and certain senior managers, which is described in note 15. For stock-based awards granted after January 1, 2003, compensation expense recognition commences when stock options are issued, with full recognition over the three year vesting period. Compensation expense is also recognized for the Company's contributions to the employees' stock savings plan.

A subsidiary of the Company has a stock-based compensation plan specific to its own shares. A participant in this plan may elect to cash settle the options in lieu of exercising them. The company records a liability and compensation expense in connection with these awards based on their intrinsic value at the date of grant. Subsequent changes in the amount of the liability due to stock price changes are recorded as compensation expense.

### **Foreign currency translation**

Effective July 1, 2002, the economic facts and circumstances surrounding the Company's foreign operations changed such that operations that were previously classified as integrated are now reported as self-sustaining. This change is the result of a significant reduction in the Company's financial guarantee provided to the foreign operation's lender along with strong evidence in the first two quarters of 2002 of the foreign operations ability to meet its debt servicing obligation with the lender thus limiting the Company's exposure related to the remaining guarantee. As a result, the translation method used has changed from the temporal to the current rate method.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

Assets and liabilities of the Company's self-sustaining foreign operations are translated using the current rate method at exchange rates prevailing at the balance sheet date, which was US\$1.00=Canadian \$1.35 at June 30, 2003 (US\$1.00=Canadian\$1.58 at December 31, 2002). Resulting unrealized gains or losses are deferred and included in shareholders' equity as a cumulative translation adjustment. The change in the cumulative translation adjustment account reflects changes due to fluctuations in exchange rates during the period. Revenues and expenses are translated at the average exchange rate prevailing during the period.

### Accounting changes

As permitted under the CICA accounting standard for Stock-Based Compensation and Other Stock-Based Payments, the Company does not record compensation expense upon issuance of stock options to employees

under its own stock option plan for awards granted prior to January 1, 2003. However, as required by the standard, the Company is disclosing the pro-forma net income and pro-forma earnings per share using the fair value method of accounting for stock-based compensation awards. The pro-forma information is presented in note 14. In addition, a subsidiary of the Company follows this method of accounting.

For stock-based compensation awards granted by the Company after January 1, 2003, the Company has changed its accounting policy to record compensation expense upon issuance of stock options to employees calculated using the fair value method. This accounting change resulted in an increase in expense of \$0.2 million and \$0.4 million respectively for the three and six months ended June 30, 2003.

## 3 DISCONTINUED OPERATIONS

Effective January 1, 2003, Innovatia Inc., which was previously reported under the Emerging business segment, has been transferred to the Telecommunications segment. The remaining assets of the Emerging business segment, which include AMI Offshore Inc., Prexar LLC, and iMagicTV Inc., were either sold or are being held for sale.

In April 2003, the investment in iMagicTV Inc. was sold and the sale of Prexar LLC closed in May 2003. At the end of June 2003, the sale of AMI Offshore Inc., and SableCom were in progress, and Aliant Energy Services Inc., was being wound up. These are expected to

be completed by the end of the year.

For reporting purposes, the results of operations of, AMI Offshore Inc., Prexar LLC, iMagicTV Inc., Aliant Energy Services Inc., and SableCom have been presented as discontinued operations. Accordingly, prior period financial statements, including segmented information as disclosed in note 13, have been reclassified to reflect this change.

The summarized statements of income for the discontinued operations are as follows:

<i>(thousands of dollars)</i>	Three months		Six months	
	2003	2002	2003	2002
Operating revenues	\$ 10,264	\$ 16,837	\$ 22,578	\$ 36,591
Expenses	14,767	18,111	30,075	39,329
Other expenses	4,558	17,986	6,831	18,423
Gain on disposal	10,858	—	10,858	—
Interest on long-term debt	116	152	280	310
Income taxes (recovery)	(783)	(3,431)	(1,387)	(4,052)
Non-controlling interest share of income (loss)	(467)	357	(646)	844
Net income (loss) from discontinued operations	\$ 2,931	\$ (16,338)	\$ (1,717)	\$ (18,263)

## 4 TRANSFER OF RECEIVABLES

Under an agreement dated December 13, 2001, the Company sells certain accounts receivable to a securitization trust. The excess of amounts transferred over the cash proceeds represents the Company's retained interest and the amount of overcollateralization in the receivables transferred and is included in deferred charges. The Company remains exposed to certain risks of default on the amount of receivables under securitization. It has provided various credit enhancements in the form of overcollateralization and subordination of its retained interests. The purchaser and its investors have no recourse to the Company's other assets for failure of the obligator to pay the amounts when due.

Under the agreement receivables are sold on a fully serviced basis, so that the Company continues to administer

the collection of such receivables. The Purchaser will re-invest the funds from collections in the purchase of additional interests in the Company's accounts receivable until the expiration of the agreement on December 13, 2006.

As at June 30, 2003, the Company had sold \$130.0 million (December 31, 2002 – \$135.0 million) of accounts receivable and transferred \$158.7 million (December 31, 2002 – \$164.9 million) of receivables to the trust. Included in deferred charges is the Company's retained interest of \$28.7 million (December 31, 2002 – \$29.9 million).

During the six months ended June 30, 2003, the Company recognized a pre-tax loss of approximately \$2.3 million (December 31, 2002 – \$3.7 million) on the transfer of receivables.

## 5 CAPITAL INVESTMENTS

(thousands of dollars)

	June 30, 2003		
	Cost	Accumulated depreciation	Net book value
Land	\$ 15,125	\$ —	\$ 15,125
Buildings and towers	340,566	169,171	171,395
Telecommunications facilities and other equipment	4,273,000	2,702,239	1,570,761
Application software and other equipment	905,585	499,821	405,764
Capital under construction	42,463	—	42,463
Materials and supplies	9,318	—	9,318
	<b>\$ 5,586,057</b>	<b>\$ 3,371,231</b>	<b>\$ 2,214,826</b>

(thousands of dollars)

	December 31, 2002		
	Cost	Accumulated depreciation	Net book value
Land	\$ 15,568	\$ —	\$ 15,568
Buildings and towers	339,975	165,285	174,690
Telecommunications facilities and other equipment	4,242,723	2,616,912	1,625,811
Application software and other equipment	928,655	462,875	465,780
Capital under construction	22,690	—	22,690
Materials and supplies	9,254	—	9,254
	<b>\$ 5,558,865</b>	<b>\$ 3,245,072</b>	<b>\$ 2,313,793</b>

## 6 LONG-TERM INVESTMENTS

(thousands of dollars)

	June 30, 2003	December 31, 2002
Investments subject to significant influence	\$ (153)	\$ —
Portfolio investments	<b>33,037</b>	37,640
	<b>\$ 32,884</b>	\$ 37,640

## 7 GOODWILL

(thousands of dollars)

	June 30, 2003	December 31, 2002
Goodwill, at cost	\$ 406,538	\$ 456,154
Cumulative impairment provision	<b>(50,000)</b>	(50,000)
Accumulated amortization	<b>(36,826)</b>	(40,414)
	<b>\$ 319,712</b>	\$ 365,740

Changes in the cost of goodwill and accumulated amortization are a result of foreign exchange fluctuations.

## 8 NOTES PAYABLE AND BANK ADVANCES

At June 30, 2003 the Company has \$nil (December 31, 2002 – \$nil) outstanding under its commercial paper program. The Company has lines of credit available of \$460.0 million (December 31, 2002 – \$535.0 million). These lines consist of \$350.0 million (December 31, 2002 – \$300.0 million) in committed lines supporting the Company's commercial paper program, \$nil

(December 31, 2002 – \$125.0 million) in committed lines supporting a Stratos loan guarantee, and \$110.0 million (December 31, 2002 – \$110.0 million) in uncommitted lines. Certain of the Company's subsidiaries also have lines of credit available totalling \$57.0 million (December 31, 2002 – \$ 125.0 million) for operating and acquisition purposes.

## 9 RESTRUCTURING CHARGE

During 2001, the Company commenced a significant organizational restructuring which resulted in a charge of \$111.2 million against earnings. The action taken in 2001 to effect the restructuring was an acceleration of long-term plans for continued efforts to realize cost savings and efficiencies resulting from the consolidation and integration of its operations.

Costs associated with workforce reduction and operational integration continue to be charged against the restructuring

provision recorded at December 31, 2001. These costs include severance, pension costs and benefits as well as costs to consolidate systems and services, downsize business units, terminate contracts and streamline management and administration functions.

As at June 30, 2003, the balance of this restructuring provision included in payables and accruals totaled \$3.2 million (December 31, 2002 – \$10.0 million). The remaining provision will be drawn down during 2003.

# 10 LONG-TERM DEBT

(thousands of dollars)

	Interest rate	Maturity	June 30, 2003	December 31, 2002
<b>Telecommunications</b>				
Notes	5.35%—6.80%	2004—2011	\$ 600,000	\$ 600,000
Bonds	8.76%—11.45%	2008—2019	192,500	192,500
Debentures	8.30%—11.13%	2013—2025	200,000	265,000
Other			1,100	2,000
			<b>993,600</b>	1,059,500
Present value of obligations under capital leases			5,188	3,526
Total — Telecommunications			<b>998,788</b>	1,063,026
<b>Information technology</b>				
Mortgages	Prime plus 1.00%—1.50%	2012	469	917
Present value of obligations under capital leases			452	429
Total — Information technology			<b>921</b>	1,346
<b>Remote communications</b>				
Term debt	LIBOR + 2.00%	2005	228,267	291,856
Acquisition facility	LIBOR + 2.00%	2004	16,709	44,173
Other	7.59%	Various	1,680	2,368
Present value of obligations under capital leases			430	—
Total — Remote communications			<b>247,086</b>	338,397
Total long-term debt			<b>1,246,795</b>	1,402,769
Less: Portion due within one year			<b>52,463</b>	140,278
			<b>\$ 1,194,332</b>	\$ 1,262,491

On June 16, 2003, a \$65 million 6.40 per cent Debenture NBTel Series AI matured.

# 11 NON-CONTROLLING INTEREST

The non-controlling interest consists of common equity of subsidiary companies held by third parties.

(thousands of dollars)

	June 30, 2003	December 31, 2002
Stratos Global Corporation	\$ 148,070	\$ 161,612
TechKnowledge Inc.	687	839
Atlantic Mobility Products Ltd.	2,604	2,435
	<b>\$ 151,361</b>	\$ 164,886

# 12 CAPITAL STOCK

## Authorized

Unlimited number of preference shares, cumulative redeemable at the price of \$25.00 per share and with a fixed annual dividend rate of \$1.3625 per share. These shares are non-voting, except under certain conditions, and are redeemable at the Company's option on June 30, 2006 or on June 30 each fifth year thereafter. Preference

shareholders (Series 2) may convert Series 2 preference shares to Series 3 shares on June 30, 2006 or on June 30 each fifth year thereafter, provided that the Company has not delivered a notice of redemption.

Unlimited number of common shares, without par value.

## Issued

	June 30, 2003		December 31, 2002	
	Number of shares	Value	Number of shares	Value
Preference shares, series 2	7,000,000	\$ 172,264	7,000,000	\$ 172,264
Common shares	138,505,154	1,035,311	139,513,639	1,065,386
		\$ 1,207,575		\$ 1,237,650

The following table summarizes the changes in issued common shares of the Company:

	June 30, 2003		December 31, 2002	
	Number of shares	Value	Number of shares	Value
Stock option plan (note 15)	221,986	\$ 3,984	437,018	\$ 7,369
Common shareholder dividend reinvestment and stock purchase plan	105,229	2,997	1,373,235	38,335
Employees' stock savings plan (note 15)	—	—	441,539	12,452
Shares purchased for cancellation	(1,335,700)	(37,056)	(264,300)	(7,186)
	(1,008,485)	\$ (30,075)	1,987,492	\$ 50,970

Under the provisions of the Company's common shareholder dividend reinvestment and stock purchase plan and employees' stock savings plan, shareholders purchase additional common shares in lieu of receiving corporate dividends in the form of cash.

During the period, the Company issued shares in relation to the common shareholder dividend reinvestment and stock purchase plan as well as the employees' stock savings plan in lieu of paying cash dividends in the amount of \$4.6 million (December 31, 2002 – \$41.5 million).

On July 18, 2002, Aliant Inc. announced acceptance by the Toronto Stock Exchange of Notice of intention to purchase from time to time up to 1,600,000 of its outstanding common shares on the Toronto Stock

Exchange, representing approximately 1.1 per cent of the issued and outstanding common shares of Aliant Inc. as of that date, being 139,567,382 common shares. Under the bid, the Company would acquire, from time to time, its common shares at the market price from cash through the facilities of the Toronto Stock Exchange. Purchases of common shares may be made during the 12-month period commencing July 22, 2002 and ending on July 21, 2003. Aliant Inc. has purchased and cancelled all of the 1,600,000 shares as of June 2003.

For the six months ended, June 30, 2003, the Company purchased and cancelled 1,335,700 shares (December 31, 2002 – 264,300) for an aggregate price of \$37.1 million (December 31, 2002 – \$7.2 million).

# 13 SEGMENTED INFORMATION

The Company operates through three reportable segments:

*Telecommunications* – provides a full range of telecommunications services in New Brunswick, Nova Scotia, Prince Edward Island and Newfoundland and Labrador. Included in this line of business are Aliant Telecom Inc., Innovatia Inc., and Aliant ActiMedia.

*Information technology* – provides systems integration, application development, local area network installation, wide area network management, data center operations, VAR and information technology planning services. Included in this line of business is Xwave Solutions Inc.

*Remote communications* – provides a full range of satellite communications services to clients in the international marketplace. Included in this line of business are Stratos Global Corporation and its subsidiaries.

Effective January 1, 2003, Innovatia Inc. was transferred to the telecommunications segment with the remaining businesses previously reported under the emerging business segment reported as discontinued operations.

These reportable segments are managed as separate business units as they operate in different industries and require different market strategies and technologies.

The accounting policies of the segments are the same as those described in note 2. The Company evaluates performance based on a number of financial and non-financial indicators including net income, return on equity, and revenue growth.

The Company accounts for intersegment sales and transfers as if the sales or transfers were to third parties, that is, at current market prices.

# 13 SEGMENTED INFORMATION continued

For the three month period ended June 30 (thousands of dollars)

2003

	Telecommunications	Information technology	Remote communications	All others	Eliminations	Consolidated
Revenue from external customers	\$ 458,797	\$ 54,622	\$ 151,406	\$ 649	\$ —	\$ 665,474
Intersegment revenue	5,276	32,096	—	—	(37,372)	—
Operating revenues	464,073	86,718	151,406	649	(37,372)	665,474
Operating expenses	240,656	84,872	119,034	5,739	(38,574)	411,727
Depreciation and amortization	96,042	3,007	10,395	291	(958)	108,777
Gain on foreign exchange	—	—	—	—	—	—
Other income (expenses)	628	54	—	2,642	(3,552)	(228)
Interest charges	20,778	631	5,548	2,863	(3,552)	26,268
Income taxes (recovery)	41,960	(716)	4,802	(1,303)	673	45,416
Non-controlling interest	1	23	5,437	(38)	—	5,423
Net income (loss)						
from continuing operations	\$ 65,264	\$ (1,045)	\$ 6,190	\$ (4,261)	\$ 1,487	\$ 67,635
Net income (loss)						
from discontinued operations	\$ —	\$ —	\$ —	\$ 2,931	\$ —	\$ 2,931
Net income (loss)	\$ 65,264	\$ (1,045)	\$ 6,190	\$ (1,330)	\$ 1,487	\$ 70,566
Total assets	\$ 2,696,330	\$ 168,533	\$ 686,558	\$ 1,960,410	\$ (2,019,428)	\$ 3,492,403
Capital investments	\$ 71,379	\$ 633	\$ 5,082	\$ 821	\$ —	\$ 77,915

For the three month period ended June 30 (thousands of dollars)

2002 (note 3)

	Telecommunications	Information technology	Remote communications	All others	Eliminations	Consolidated
Revenue from external customers	\$ 455,578	\$ 66,872	\$ 128,749	\$ 2,073	\$ —	\$ 653,272
Intersegment revenue	4,211	36,783	—	(417)	(40,577)	—
Operating revenues	459,789	103,655	128,749	1,656	(40,577)	653,272
Operating expenses	239,692	94,820	105,605	4,954	(38,564)	406,507
Depreciation and amortization	91,524	2,945	10,176	151	—	104,796
Gain on foreign exchange	—	—	24,402	—	—	24,402
Other income (expenses)	(327)	43	193	32,965	(2,919)	29,955
Interest charges	22,208	384	11,165	1,401	(2,919)	32,239
Income taxes (recovery)	42,776	2,519	1,017	4,386	(534)	50,164
Non-controlling interest	223	6	12,895	(41)	—	13,083
Net income (loss)						
from continuing operations	\$ 63,039	\$ 3,024	\$ 12,486	\$ 23,770	\$ (1,479)	\$ 100,840
Net income (loss)						
from discontinued operations	\$ —	\$ —	\$ —	\$ (16,338)	\$ —	\$ (16,338)
Net income (loss)	\$ 63,039	\$ 3,024	\$ 12,486	\$ 7,432	\$ (1,479)	\$ 84,502
Total assets	\$ 2,744,134	\$ 246,379	\$ 792,991	\$ 1,990,815	\$ (1,889,756)	\$ 3,884,563
Capital investments	\$ 103,098	\$ 3,367	\$ 8,004	\$ 235	\$ —	\$ 114,704

# 13 SEGMENTED INFORMATION continued

For the six month period ended June 30 (thousands of dollars)

2003

	Telecommunications	Information technology	Remote communications	All others	Eliminations	Consolidated
Revenue from external customers	\$ 883,944	\$ 128,454	\$ 295,462	\$ 733	\$ —	\$ 1,308,593
Intersegment revenue	9,990	66,323	—	—	(76,313)	—
Operating revenues	893,934	194,777	295,462	733	(76,313)	1,308,593
Operating expenses	482,796	194,466	230,209	11,237	(78,205)	840,503
Depreciation and amortization	192,215	5,791	21,397	414	(1,848)	217,969
Gain on foreign exchange	—	—	—	—	—	—
Other income (expenses)	182	(39)	—	5,370	(6,005)	(492)
Interest charges	41,590	1,264	12,073	4,506	(6,005)	53,428
Income taxes (recovery)	69,589	(2,429)	9,398	(2,335)	461	74,684
Non-controlling interest	1	(40)	10,467	(82)	—	10,346
Net income (loss)						
from continuing operations	\$ 107,925	\$ (4,314)	\$ 11,918	\$ (7,637)	\$ 3,279	\$ 111,171
Net income (loss)						
from discontinued operations	\$ —	\$ —	\$ —	\$ (1,717)	\$ —	\$ (1,717)
Net income (loss)	\$ 107,925	\$ (4,314)	\$ 11,918	\$ (9,354)	\$ 3,279	\$ 109,454
Total assets	\$ 2,696,330	\$ 168,533	\$ 686,558	\$ 1,960,410	\$ (2,019,428)	\$ 3,492,403
Capital investments	\$ 141,169	\$ 1,141	\$ 11,100	\$ 1,159	\$ —	\$ 154,569

For the six month period ended June 30 (thousands of dollars)

2002 (note 3)

	Telecommunications	Information technology	Remote communications	All others	Eliminations	Consolidated
Revenue from external customers	\$ 870,606	\$ 150,374	\$ 255,289	\$ 2,896	\$ —	\$ 1,279,165
Intersegment revenue	8,590	74,807	—	(325)	(83,072)	—
Operating revenues	879,196	225,181	255,289	2,571	(83,072)	1,279,165
Operating expenses	463,939	207,766	200,732	11,372	(79,295)	804,514
Depreciation and amortization	184,990	5,800	19,933	470	—	211,193
Gain on foreign exchange	—	—	23,944	—	—	23,944
Other income (expenses)	(1,161)	72	—	35,504	(5,547)	28,868
Interest charges	43,991	757	23,604	2,972	(5,547)	65,777
Income taxes (recovery)	72,779	5,003	(3,462)	2,987	(1,308)	75,999
Non-controlling interest	417	(27)	17,968	(82)	—	18,276
Net income (loss)						
from continuing operations	\$ 111,919	\$ 5,954	\$ 20,458	\$ 20,356	\$ (2,469)	\$ 156,218
Net income (loss)						
from discontinued operations	\$ —	\$ —	\$ —	\$ (18,263)	\$ —	\$ (18,263)
Net income (loss)	\$ 111,919	\$ 5,954	\$ 20,458	\$ 2,093	\$ (2,469)	\$ 137,955
Total assets	\$ 2,744,134	\$ 246,379	\$ 792,991	\$ 1,990,815	\$ (1,889,756)	\$ 3,884,563
Capital investments	\$ 193,622	\$ 4,313	\$ 22,197	\$ 326	\$ —	\$ 220,458

# 13 SEGMENTED INFORMATION continued

## Revenue from external customers by product and service:

For the period ended June 30 (thousands of dollars)	Three months		Six months	
	2003	2002	2003	2002
Telecommunications				
Local	\$ 188,473	\$ 193,514	\$ 376,496	\$ 383,473
Long distance	92,523	97,836	188,613	195,002
Wireless	80,485	67,404	153,646	128,628
Other telecommunications	97,316	96,824	165,189	163,503
	<b>458,797</b>	455,578	<b>883,944</b>	870,606
Information technology				
Fulfillment	24,937	35,276	72,504	90,180
Services	29,685	31,596	55,950	60,194
	<b>54,622</b>	66,872	<b>128,454</b>	150,374
Remote communications				
Mobile satellite services	116,318	93,590	224,228	184,196
Broadband services	35,088	35,159	71,234	71,093
	<b>151,406</b>	128,749	<b>295,462</b>	255,289
Other	649	2,073	733	2,896
	<b>\$ 665,474</b>	\$ 653,272	<b>\$ 1,308,593</b>	\$ 1,279,165

# 14 EARNINGS PER COMMON SHARE

For the period ended June 30 (thousands of dollars except per share amounts)	Three months		Six months	
	2003	2002	2003	2002
Net income applicable to common shares:				
Net income from continuing operations	\$ 67,635	\$ 100,840	\$ 111,171	\$ 156,218
Preferred share dividends	(2,385)	(2,385)	(4,769)	(4,769)
Net income applicable to common shares from continuing operations	\$ 65,250	\$ 98,455	\$ 106,402	\$ 151,449
Net income (loss) from discontinued operations	2,931	(16,338)	(1,717)	(18,263)
Net income applicable to common shares	\$ 68,181	\$ 82,117	\$ 104,685	\$ 133,186
Basic:				
Average number of common shares outstanding	138,683	138,891	138,976	138,355
Basic earnings per common share from continuing operations	\$ 0.47	\$ 0.71	\$ 0.77	\$ 1.09
Basic earnings per common share from discontinued operations	0.02	(0.12)	(0.02)	(0.13)
Basic earnings per common share	\$ 0.49	\$ 0.59	\$ 0.75	\$ 0.96
Diluted:				
Average number of common shares outstanding	138,683	138,891	138,976	138,355
Impact of outstanding stock options	—	69	—	79
	<b>138,683</b>	138,960	<b>138,976</b>	138,434
Diluted earnings per common share from continuing operations	\$ 0.47	\$ 0.71	\$ 0.77	\$ 1.09
Diluted earnings per common share from discontinued operations	0.02	(0.12)	(0.02)	(0.13)
Diluted earnings per common share	\$ 0.49	\$ 0.59	\$ 0.75	\$ 0.96

# 14 EARNINGS PER COMMON SHARE continued

Common shares issuable under the terms of the Company's stock option plans have not been included in the calculation of diluted earnings per share as their effect is anti-dilutive for 2003.

The table below presents pro-forma net income, earnings per share and diluted earnings per share using the fair

value method of accounting for the stock option plan. The pro-forma adjustments presented below pertain to new awards granted since adoption of the new stock-based compensation standards on January 1, 2002, excluding those granted in 2003 for which compensation was recorded, as described in note 2.

	Three months		Six months	
	2003	2002	2003	2002
<i>For the period ended June 30 (thousands of dollars except per share amounts)</i>				
Pro-forma net income applicable to common shares:				
Net income from continuing operations	\$ 67,635	\$ 100,840	\$ 111,171	\$ 156,218
Preferred share dividends	(2,385)	(2,385)	(4,769)	(4,769)
Pro-forma adjustments	(467)	(1,030)	(923)	(1,328)
Pro-forma net income applicable to common shares from continuing operations	\$ 64,783	\$ 97,425	\$ 105,479	\$ 150,121
Pro-forma net income applicable to common shares from discontinued operations	\$ 2,931	\$ (16,338)	\$ (1,717)	\$ (18,263)
Pro-forma net income applicable to common shares	\$ 67,714	\$ 81,087	\$ 103,762	\$ 131,858
Basic:				
Average number of common shares outstanding	138,683	138,891	138,976	138,355
Pro-forma earnings per common share from continuing operations	\$ 0.47	\$ 0.70	\$ 0.76	\$ 1.09
Pro-forma earnings per common share from discontinued operations	\$ 0.02	\$ (0.12)	\$ (0.02)	\$ (0.13)
Pro-forma earnings per common share	\$ 0.49	\$ 0.58	\$ 0.74	\$ 0.96
Diluted:				
Average number of common shares outstanding	138,683	138,891	138,976	138,355
Impact of outstanding stock options	—	69	—	79
	138,683	138,960	138,976	138,434
Pro-forma earnings per common share from continuing operations	\$ 0.47	\$ 0.70	\$ 0.76	\$ 1.08
Pro-forma earnings per common share from discontinued operations	\$ 0.02	\$ (0.12)	\$ (0.02)	\$ (0.13)
Pro-forma earnings per common share	\$ 0.49	\$ 0.58	\$ 0.74	\$ 0.95

The fair value of each option granted is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions used:

<i>June 30</i>	<i>2003</i>	<i>2002</i>
Dividend yield	3.41%	3.10%
Expected volatility	25.30%	25.30%
Risk-free interest rate	4.33%	5.08%
Expected lives	6.4 years	7.8 years

# 15 STOCK-BASED COMPENSATION PLANS

At June 30, 2003 the Company has the following stock-based compensation plans.

## Stock option plan

Under the stock option plan, the Company may grant options to plan members for up to 7,361,746 shares of common stock, of which 2,698,073 options for the same number of common shares were outstanding as at June 30, 2003 (December 31, 2002 – 2,680,450). The exercise price

of each option equals the market price of the Company's stock on the date of grant and an option's maximum term is ten years. Options vest evenly over three years from the date they are granted under the plan.

A summary of the status of the Company's stock option plan as of June 30, 2003 and December 31, 2002, and changes during the periods ended on those dates are presented below:

	June 30, 2003		December 31, 2002	
	Number of shares	Weighted-average exercise price	Number of shares	Weighted-average exercise price
Options outstanding at beginning of period	2,680,450	\$ 28.94	2,558,275	\$ 26.67
Granted	285,472	26.79	633,049	29.05
Forfeited	(45,863)	30.82	(73,856)	25.48
Exercised	(221,986)	17.95	(437,018)	16.86
Options outstanding at end of period	2,698,073	\$ 29.59	2,680,450	\$ 28.94
Options exercisable at end of period	1,938,013	\$ 29.76	1,668,501	\$ 27.61

The following table summarizes information about stock options outstanding at June 30, 2003:

Range of exercise prices	Options outstanding			Options exercisable	
	Number outstanding	Weighted-average remaining contractual life in years	Weighted-average exercise price	Weighted-Number exercisable	average exercise price
\$10.63 to \$15.72	105,913	3.4	\$14.03	105,913	\$14.03
\$17.56 to \$20.08	151,617	4.6	\$19.84	151,617	\$19.84
\$21.77 to \$25.55	275,741	5.5	\$22.93	275,741	\$22.93
\$26.79 to \$34.90	1,678,019	8.4	\$30.85	1,031,701	\$32.61
\$35.25 to \$38.10	486,783	7.6	\$35.42	373,041	\$35.42
	2,698,073		\$29.59	1,938,013	\$29.76

The Company expects that approximately 95 per cent of the non-vested awards at June 30, 2003 will eventually vest.

## 15 STOCK-BASED COMPENSATION PLANS continued

### **Employees' stock savings plan**

Under the employees' stock savings plan, the Company is authorized to issue up to 3,500,000 shares of common stock to its full-time employees, nearly all of who are eligible to participate.

Under the terms of the plan, employees can choose each year to have a portion of their annual base earnings withheld to purchase the Company's common stock. The Company contributes to the plan on behalf of eligible participants based upon a prescribed formula. The purchase price of the stock is the arithmetic average of the closing price of the shares traded on The Toronto Stock Exchange on the last five days up to, and including, the dividend payment date. Over 80 per cent of eligible employees are participating in the plan.

### **Employee stock option plan of a subsidiary company**

A subsidiary of the Company has a stock option plan specific to its own shares. Under this stock option plan, the subsidiary may grant options to plan members at the discretion of the Board of Directors. The exercise price of each option equals the fair market value price of the company's stock on the date of grant and an option's maximum term is ten years. Options become fully vested at the date they are granted under the plan. A participant in this plan may elect to cash settle the options in lieu of exercising them.

As at June 30, 2003, there were 834,029 (December 31, 2002 – 565,414) options outstanding and exercisable. The weighted average remaining contractual life of the options is 7.0 years (December 31, 2002 – 8.0 years) and the weighted average exercise price is \$9.42 (December 31, 2002 – \$8.00).

## 16 COMMITMENTS AS LESSEE

The estimated future minimum lease payments under operating leases for the next five years and thereafter are as follows: 2003 – \$27.0 million; 2004 – \$45.9 million; 2005 – \$45.3 million; 2006 – \$44.3 million; 2007 – \$46.8 million; and thereafter \$210.3 million.

## 17 CONTINGENCIES

(a) An action has been commenced against the Company by 132 former employees who took early retirement under the 1998 early retirement incentive program. The former employees seek damages which could, in the aggregate, exceed \$9 million, the difference between what they received upon retirement in 1998, and what they would have received had they retired under the 1999 early retirement incentive program. The outcome of this matter is not determinable at this time.

(b) On May 30, 2002 the CRTC released its price cap decision, that prescribed new rules to determine the rates charged for certain telecommunications services provided by incumbent local exchange carriers ("ILECs") for the next four years effective June 1, 2002. The price cap decision, requires the use of a new mechanism, the deferral account, to mitigate the potential adverse effects on competition in the local market, as a result of mandated rate reductions. Certain mandated revenue reductions are accumulated in an interest bearing deferral account. The deferral account will be reduced by one, or a combination of the following:

- Rate reductions for residential local services that are proposed as the result of competitive pressures;
- Certain rate reductions for services provided to competitors;
- The approval of exogenous factors for matters beyond control of the ILECs;
- Rate increases less than the amount by which inflation exceeds productivity;
- Subscriber rebates; and
- Funding of initiatives that would benefit residential customers in other ways.

The Company has calculated its deferral account balance to be \$10.2 million as of June 30, 2003 (\$9.6 million – December 31, 2002). The Company has not recognized the deferral account as a liability in its financial statements because it has made a proposal to the CRTC to approve reductions to the deferral account by means other than rebates or rate reductions. If the CRTC rejects this proposal and requires the Company to reduce rates or issue rebates the amount in the deferral account would be charged to income and recorded as a liability.

## 18 COMPARATIVE FIGURES

The comparative financial information has been reclassified to conform to the presentation adopted for 2003.

# Owning AIT

## We're here to help

To learn more about Aliant, please visit our Web site at [www.aliant.ca](http://www.aliant.ca). Contact Aliant investor relations for additional financial and statistical information, and industry developments.

Phone: 1.877.248.3113 (toll free in Canada and U.S.)

Fax: 1.877.498.2464 (toll free in Canada and U.S.)

Email: [investor.relations@aliant.ca](mailto:investor.relations@aliant.ca)

Mailing address: Aliant Investor Relations  
PO Box 1113, Station Central RPO  
Halifax, NS B3J 2X1

Contact our transfer agent, CIBC Mellon Trust Company, for information about the dividend reinvestment and stock purchase plan (DRP) and for answers to shareholder inquiries.

Phone: 1.800.387.0825 (toll free in Canada and U.S.)

Email: [inquiries@cibcmellon.com](mailto:inquiries@cibcmellon.com)

Web site: [www.cibcmellon.com](http://www.cibcmellon.com)

Mailing address: CIBC Mellon Trust Company

Investor Correspondence  
PO Box 7010, Adelaide Street Postal Station  
Toronto, ON M5C 2W9

## Where we're listed

Our shares are listed on The Toronto Stock Exchange. Aliant's ticker symbol is AIT.

## Direct deposit of dividends

Registered common shareholders may have dividends deposited electronically into their bank account (in Canada only). Contact CIBC Mellon Trust Company.

## Common share dividend dates for 2003\*

<i>Record dates</i>	<i>Payment dates</i>
March 15	March 30
June 15	June 30
September 15	September 30
December 15	December 30

\* Subject to approval by the Board of Directors

## Performance numbers

(as at June 30)

	2003	2002	% change
Network access services — landline	1,513,862	1,526,753	(0.8)
Network access services — cellular	573,412	506,639	13.2
Internet subscribers — high-speed	105,117	84,722	24.1
Internet subscribers — dial-up	188,754	193,554	(2.5)
Long distance conversation minutes	855,955,000	889,156,000	(3.7)

## Dividend reinvestment plan

Registered common shareholders of Aliant may reinvest their dividends, automatically and without fees, in additional shares of the Company. Also, up to \$10,000 in Company shares may be purchased each quarter with optional cash payments. All administration costs are paid by the Company. A brochure containing information on the dividend reinvestment and stock purchase plan may be obtained by calling CIBC Mellon Trust Company.

## Electronic distribution of materials

Registered shareholders can obtain investor information and reports from Aliant electronically rather than through the mail. To access our online enrollment form, go to [www.cibcmellon.com/electronicdelivery](http://www.cibcmellon.com/electronicdelivery) located on our transfer agent's Web site and follow the simple instructions.

## Stock registrar and transfer agent

CIBC Mellon Trust Company

## Bond trustee, registrar and transfer agent

Computershare Investor Services, and CIBC Mellon Trust Company

## Annual information form

The annual information form as filed with the Canadian securities commissions is available upon request. For further information about the Company, institutional investors, brokers and security analysts should contact Aliant investor relations.

## Common share price range\*

	April	May	June
High	\$29.34	\$29.46	\$30.50
Low	\$27.28	\$27.25	\$28.66
Close	\$28.00	\$29.40	\$29.13

\* Toronto Stock Exchange

**About the cover**

Powerful. Dynamic. Enduring. Atlantic Canadians share a common bond: The ocean. It has shaped our history and defined our people. At Aliant, we bring together Atlantic Canadians too – with technology – to help them share the present and build the future.

*Photograph taken at Peggy's Cove, Nova Scotia*

# Our vision

*To be the company with the strongest  
connection to the hearts and minds  
of Atlantic Canadians.*

**Aliant Inc.**  
**1.877.248.3113**  
**investor.relations@aliant.ca**  
**www.aliant.ca**



**here. for you.**