



**MANAGEMENT'S DISCUSSION AND ANALYSIS OF  
FINANCIAL CONDITION AND RESULTS OF OPERATIONS  
FOR THE THREE AND TWELVE-MONTH PERIODS ENDED DECEMBER 31, 2017**

*The following management's discussion and analysis of financial condition and results of operations ("MD&A"), dated February 20, 2018, of Supremex Inc. ("Supremex" or the "Company") should be read together with the accompanying audited consolidated financial statements and related notes of the Company for the year ended December 31, 2017. These consolidated financial statements of the Company have been prepared by management in accordance with International Financial Reporting Standards ("IFRS"). The fiscal year of the Company ends on December 31. The Company's reporting currency is the Canadian dollar. Per share amounts are calculated using the weighted average number of shares outstanding for the three and twelve-month periods ended December 31, 2017.*

*The Company's shares are traded on the Toronto Stock Exchange under the symbol SXP. Additional information on Supremex may be found on SEDAR at [www.sedar.com](http://www.sedar.com) and on the Company's website at [www.supremex.com](http://www.supremex.com).*

*This MD&A contains forward-looking information. Please see "Forward-Looking Information" for a discussion of the risks, uncertainties and assumptions relating to these statements. This MD&A contains certain other non-IFRS financial measures. Terms by which non-IFRS financial measures are identified include, but are not limited to, "Adjusted EBITDA", "Adjusted net earnings" and "net indebtedness to Adjusted EBITDA ratio". Non-IFRS financial measures are used to provide management and investors with additional measures of performance. However, non-IFRS financial measures do not have standard meanings prescribed by IFRS and therefore may not be directly comparable to similar measures used by other companies and should not be viewed as alternatives to measures of financial performance prepared in accordance with IFRS. See "Definition of EBITDA, Adjusted EBITDA, Adjusted Net Earnings and non-IFRS measures" and "Reconciliation of Net Earnings to EBITDA to Adjusted EBITDA" and "Reconciliation of Net Earnings to Adjusted Net Earnings".*

## **Business Overview**

Supremex is a leading North American manufacturer and marketer of envelopes and a growing provider of packaging and specialty products. Supremex operates ten facilities across seven provinces in Canada and three facilities in the United States employing approximately 820 people. Supremex' growing footprint allows it to efficiently manufacture and distribute paper and packaging solutions designed to the specifications of major national and multinational corporations, resellers, government entities, SMEs and solutions providers.

The Company manufactures a broad range of stock and custom envelopes in an array of styles, shapes and colours, which allows it to offer its customers a high degree of flexibility and customization. It also manufactures and distributes a diverse range of packaging and specialty products, including corrugated boxes primarily for the food packaging and delivery market and high quality folding carton packaging for leading multinational customers in the cosmetics, personal care and pharmaceutical markets. Other packaging and specialty products include the Conformer Products®, polyethylene bags for courier applications, bubble mailers, Enviro-logiX and Tyvek and other related products such as protective envelopes, X-ray envelopes, medical and file folders, repositionable notes, membership cards as well as labelling products.

## **Growth and Diversification Strategy**

To sustain long-term revenue and profitability growth, Supremex has been actively pursuing a three-pronged diversification strategy. First, strengthening its market-leading position in the Canadian envelope market by leveraging its footprint through capacity allocation and consolidation opportunities. Second, by pursuing growth opportunities in the U.S. envelope market both organically and through acquisitions, focusing on a large and attractive market in the Northeast and Midwest. And third, by building Supremex' packaging capabilities organically and through acquisitions, with the objective of significantly growing its revenues from this attractive growth market.

The growing use of digital alternatives to traditional mail adversely affects the envelope market. Conversely, the growth in e-commerce and changes in consumer behaviour have been significant growth drivers for the packaging, labels and related products markets. In 2016, the Company acquired Durabox Paper Inc. (“Durabox”), a manufacturer and distributor of corrugated paper boxes and, in 2017, acquired Stuart Packaging Inc. (“Stuart Packaging”), a manufacturer of specialty folding carton packaging solutions. These two acquisitions in the paper packaging market represent an important building block of the Company’s diversification strategy.

When Supremex first introduced this strategy in 2014, its revenues from the Canadian envelope market represented 81.4% of total revenues, the U.S. envelope market accounted for 11.2% of revenues and the packaging market, 7.4%. At the end of 2017, close to half of the Company’s revenues now come from a combination of the U.S. envelope market and the packaging market, the latter reaching 19.3% of revenues.

#### **Fourth Quarter Financial Performance Highlights**

- Revenue increased by 13.8% year-over-year, to \$49.4 million.
- Adjusted EBITDA<sup>1</sup> increased by 2.3% to \$8.0 million, compared with \$7.8 million.
- Net earnings decreased by 51.3%, to \$2.3 million (or \$0.08 per share) compared with \$4.6 million (or \$0.16 per share).
- Adjusted Net Earnings<sup>2</sup> decreased by 4.8%, to \$4.4 million (or \$0.16 per share), compared with \$4.6 million (or \$0.16 per share).
- Maintained strong financial flexibility with a net indebtedness to Adjusted EBITDA<sup>1</sup> ratio of 1.5 times.
- Approved a quarterly dividend of \$0.065 per share, equivalent to the last quarter and up 8.3% year-over-year.

#### **Fiscal Year Financial Performance Highlights**

- Revenue increased by 11.5% year-over-year, reaching \$179.1 million compared with \$160.6 million.
- Adjusted EBITDA<sup>1</sup> decreased by 2.7% to \$26.7 million compared with \$27.4 million.
- Net earnings decreased by 15.1% to \$12.4 million (or \$0.43 per share) compared with \$14.6 million (or \$0.51 per share).
- Adjusted Net Earnings<sup>2</sup> increased by 1.0%, to \$14.7 million (or \$0.52 per share), compared with \$14.6 million (or \$0.51 per share).
- Declared a total of \$0.245 per share in dividends, an increase of 8.9% over the prior year.
- Purchased a total of 205,882 common shares for cancellation under the NCIB, for total consideration of \$938,759.

#### **Fiscal Year Operational, Business Highlights and Subsequent Events**

##### **Key Acquisition in Packaging**

On July 20, 2017, the Company announced the acquisition of Stuart Packaging, a leading eco-friendly provider of premium quality folding carton packaging for the consumer market with \$18.0 million of revenues in the last year at the time of the acquisition. Stuart Packaging offers packaging and finishing solutions for some of the largest multinational companies operating in the cosmetics, nutraceutical, fragrance and pharmaceutical industries. The transaction was concluded for total cash consideration of \$17.9 million on a cash-free and debt-free basis. In addition, an amount of up to \$2.1 million is estimated to be payable in 24 months subject to the realization of certain pre-established financial targets over that period. This acquisition represents a key building block of Supremex’ diversification strategy.

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<sup>1</sup> Refer to the reconciliation of Net Earnings to EBITDA to Adjusted EBITDA and to the definition of EBITDA, Adjusted EBITDA, Adjusted Net Earnings and Non-IFRS Measures.

<sup>2</sup> Refer to the reconciliation of Net Earnings to Adjusted Net Earnings and to the definition of EBITDA, Adjusted EBITDA, Adjusted Net Earnings and Non-IFRS Measures.

## **Printer Gateway**

On January 22, 2018, the Company closed its Printer Gateway Inc. (“Printer Gateway”) operations. After a challenging post-acquisition transition, it was determined that this business required disproportionate management attention and resources to achieve acceptable profitability. Given the subsequent acquisition of Stuart Packaging and its other more profitable and growing operations, a swift decision was made to close this business and dedicate the Company’s resources to further grow its packaging operations, which are at the core of the growth and diversification strategy.

Printer Gateway was acquired on December 23, 2016, as a complimentary addition to the Company’s product offering and customer base. The Company purchased the principal net assets of Printer Gateway for an initial cash consideration of \$2.9 million. This purchase price was reduced by a subsequent settlement with the previous owner in the amount of \$0.5 million.

The EBITDA loss attributable to this business during fiscal 2017 was \$1.4 million, and represented \$0.4 million during the fourth quarter ended December 31, 2017. Closing this operation will not affect continuing operations and will improve the Company’s operational profitability going forward. Costs to shut down including the impairment of the non-core assets amounted to \$2.2 million and they were accounted for on the fourth quarter Company’s consolidated financial statements ended December 31, 2017.

## **Renewal and Execution of Normal Course Issuer Bid (“NCIB”)**

On August 1, 2017, the Company announced the renewal of its Normal Course Issuer Bid after its approval by the TSX, to purchase for cancellation, up to 500,000 of its common shares, representing approximately 1.75% of its 28,482,611 issued and outstanding common shares as of July 31, 2017 for a period of twelve months, ending on August 2, 2018. During 2017, the Company purchased for cancellation under the NCIB programs in effect, a total of 205,882 common shares, for total considerations of \$938,759.

## **Increased Credit Facility**

Effective July 31, 2017, the Company increased its credit facility, from \$50 million to \$60 million. This facility bears interest at a floating rate based on the Canadian prime rate plus an applicable margin that varies between 0% and 0.25% or bankers’ acceptance rates, plus an applicable margin that varies between 1.5% and 1.75%.

## **Corporate Developments**

On November 27, 2017, the Company announced that its Chief Financial Officer and Corporate Secretary, Bertrand Jolicoeur, was leaving the Company to pursue other opportunities, effective December 15, 2017. Supremex is currently in the recruitment process for this position. Lyne Bégin is acting as Interim Vice-President of Finance. Ms. Bégin has been with the Company since 2014 and is a seasoned executive, having been involved in every aspect of Supremex’ financial reporting, treasury management, planning and analysis.

Subsequent to year-end, the Company strengthened its executive team with two key nominations. Effective January 1, 2018, Joe Baglione was appointed Vice-President and General Manager, Supremex USA. Mr. Baglione has over 25 years of sales and management experience at Supremex within the Canadian and U.S. operations. Mr. Islem Yezza was appointed Vice-President, Strategic Growth & Business Development, Packaging Division to support Supremex’ continued growth from packaging. Mr. Yezza will work across the packaging platforms to support profitable growth and collaboration. Mr. Yezza has 10 plus years of progressive experience in the paper and packaging business and holds a degree in Chemical Engineering and a Ph.D in Bioprocess Engineering. He will join Supremex on March 1, 2018.

## **Declaration of Dividend**

On February 20, 2018, the Board of Directors declared a quarterly dividend of \$0.065 per common share, payable on April 13, 2018, to the shareholders of record at the close of business on March 29, 2018. This dividend is designated as an “eligible” dividend for the purpose of the Income Tax Act (Canada) and any similar provincial legislation.

## Summary of Financial Information and Non-IFRS Measures

### Selected Consolidated Financial Information

(In thousands of dollars, except for per share amounts)

	Three-month periods ended December 31,		Twelve-month periods ended December 31,	
	2017	2016	2017	2016
<b>Revenue</b>	<b>49,350</b>	43,374	<b>179,072</b>	160,570
Operating expenses	<b>36,115</b>	30,612	<b>130,325</b>	114,447
Selling, general and administrative expenses	<b>5,805</b>	4,935	<b>22,920</b>	18,740
<b>Operating earnings before amortization, loss on disposal of property, plant and equipment and shutdown of non-core operations of Printer Gateway</b>	<b>7,430</b>	7,827	<b>25,827</b>	27,383
Amortization of property, plant and equipment	<b>1,025</b>	777	<b>3,713</b>	4,520
Amortization of intangible assets	<b>497</b>	316	<b>1,682</b>	1,917
Loss on disposal of property, plant and equipment	<b>40</b>	3	<b>115</b>	27
Shutdown of non-core operations of Printer Gateway	<b>2,192</b>	—	<b>2,192</b>	—
<b>Operating earnings</b>	<b>3,676</b>	6,731	<b>18,125</b>	20,919
Financing charges, net	<b>399</b>	202	<b>1,078</b>	852
<b>Earnings before income taxes</b>	<b>3,277</b>	6,529	<b>17,047</b>	20,067
Income tax expense	<b>1,015</b>	1,886	<b>4,656</b>	5,474
<b>Net earnings</b>	<b>2,262</b>	4,643	<b>12,391</b>	14,593
Basic and diluted net earnings per share	<b>0.08</b>	0.16	<b>0.43</b>	0.51
Dividend declared per share	<b>0.065</b>	0.060	<b>0.245</b>	0.225

### Revenue Information

(In millions of dollars)

	Three-month periods ended December 31,		Twelve-month periods ended December 31,	
	2017	2016	2017	2016
<b>Canadian envelope</b>	<b>\$25.5</b>	\$28.0	<b>\$102.1</b>	\$110.0
Volume variation	<b>-11.3%</b>	-7.1%	<b>-7.7%</b>	-1.3%
Average selling price variation	<b>2.5%</b>	3.9%	<b>0.6%</b>	4.4%
Total variation	<b>-9.1%</b>	-3.5%	<b>-7.2%</b>	3.0%
<b>U.S. envelope</b>	<b>\$11.0</b>	\$11.1	<b>\$42.4</b>	\$38.4
Volume variation	<b>5.4%</b>	20.5%	<b>12.6%</b>	46.0%
Average selling price variation (in CAD)	<b>-6.5%</b>	0.8%	<b>-1.9%</b>	5.0%
Total variation	<b>-1.5%</b>	21.5%	<b>10.4%</b>	53.3%
<b>Packaging &amp; specialty products</b>				
Canada & U.S.	<b>\$12.9</b>	\$4.3	<b>\$34.6</b>	\$12.2
Total variation	<b>204.1%</b>	36.5%	<b>184.0%</b>	16.4%
<b>Total revenue</b>	<b>\$49.4</b>	\$43.4	<b>\$179.1</b>	\$160.6
Revenue variation	<b>13.8%</b>	5.1%	<b>11.5%</b>	12.8%

## Reconciliation of Net Earnings to EBITDA to Adjusted EBITDA

(In thousands of dollars)

	Three-month periods ended December 31,		Twelve-month periods ended December 31,	
	2017	2016	2017	2016
<b>Net earnings</b>	<b>2,262</b>	4,643	<b>12,391</b>	14,593
Income tax expense	1,015	1,886	4,656	5,474
Financing charges, net	399	202	1,078	852
Loss on disposal of property, plant and equipment	40	3	115	27
Amortization of property, plant and equipment	1,025	777	3,713	4,520
Amortization of intangible assets	497	316	1,682	1,917
<b>EBITDA<sup>(1)</sup></b>	<b>5,238</b>	7,827	<b>23,635</b>	27,383
Shutdown of non-core operations of Printer Gateway	2,192	—	2,192	—
Provision for contingent remuneration related to business combinations	577	—	827	—
<b>Adjusted EBITDA<sup>(1)</sup></b>	<b>8,007</b>	7,827	<b>26,654</b>	27,383

<sup>(1)</sup> Refer to "Definition of EBITDA, Adjusted EBITDA, Adjusted Net Earnings and Non-IFRS measures"

## Reconciliation of Net Earnings to Adjusted Net Earnings

(In thousands of dollars)

	Three-month periods ended December 31,		Twelve-month periods ended December 31,	
	2017	2016	2017	2016
<b>Net earnings</b>	<b>2,262</b>	4,643	<b>12,391</b>	14,593
Adjustments				
Plus: Shutdown of non-core operations of Printer Gateway, net of income taxes	1,620	—	1,620	—
Plus : Provision for contingent remuneration related to business combinations	538	—	722	—
<b>Adjusted Net Earnings<sup>(1)</sup></b>	<b>4,420</b>	4,643	<b>14,733</b>	14,593

<sup>(1)</sup> Refer to "Definition of EBITDA, Adjusted EBITDA, Adjusted Net Earnings and Non-IFRS measures"

## Results of Operations

### **Three-month period ended December 31, 2017 compared with the three-month period ended December 31, 2016.**

#### *Revenue*

Revenue for the three-month period ended December 31, 2017, increased by 13.8% or \$6.0 million reaching \$49.4 million compared with \$43.4 million during the three-month period ended December 31, 2016. Revenue growth results from the Company's strategy to diversify into the packaging market.

Revenue from the Canadian envelope market stood at \$25.5 million, a decrease of 9.1% or \$2.5 million from \$28.0 million recorded during the fourth quarter of 2016. The reduction in volume of 11.3%, primarily the results of industry-wide secular decline combined with the effects of timing and ebbs and flows on customer movement, was partially compensated by an increase in average selling prices of 2.5%.

Revenue from the U.S. envelope market stood at \$11.0 million, a decrease of 1.5% from revenue of \$11.1 million recorded during the fourth quarter of 2016. The volume of units sold increased by 5.4% and average selling prices decreased by 6.5% primarily from the effect of a stronger Canadian dollar when compared with the equivalent period of last year and a modest change in product mix.

Revenue from packaging and specialty products was \$12.9 million, an increase of 204.1% or \$8.6 million compared to the prior year, primarily due to the acquisition of Stuart Packaging on July 20, 2017 and, to a lesser extent, to the

acquisition of Durabox concluded on November 28, 2016 combined with continued growth in the Company's e-commerce packaging business.

#### *Operating Expenses*

Operating expenses for the three-month period ended December 31, 2017, were \$36.1 million compared with \$30.6 million for the same period in 2016, an increase of \$5.5 million or 18.0%. The increase is mainly attributable to the acquisition of Stuart Packaging and to a lesser extent, of Durabox and Printer Gateway. These additional expenses were partially offset by lower operating costs in Canada on lower volumes of envelope sold.

#### *Selling, General and Administrative Expenses*

Selling, general and administrative expenses totalled \$5.8 million for the three-month period ended December 31, 2017, compared with \$4.9 million for the same period in 2016, representing an increase of \$0.9 million or 17.6% primarily due to the 2017 business acquisition and to a lesser extent, to the two smaller business acquisitions concluded during the fourth quarter of 2016. In addition, the Company incurred a \$0.6 million earn-out expense related to the achievement of certain financial targets on two acquisitions. The original purchase price for both acquisitions included an earn-out provision and both acquisitions are on track for their financial targets. The provision related to the Durabox acquisition is now complete and accounted for. The final provision related to the Stuart Packaging acquisition will be accounted for over the remainder of the earn-out period. The resulting provision for contingent remuneration was partially compensated by the reversal of a provision for executive compensation, but still adversely affects this quarter's SG&A expenses.

#### *Adjusted EBITDA and Adjusted EBITDA Margins*

Adjusted EBITDA was at \$8.0 million, compared with \$7.8 million in the fourth quarter of 2016, an increase of \$0.2 million or 2.3%. After quarter-end, Supremex closed its Printer Gateway operations to focus its efforts on its core diversification strategy. The EBITDA loss attributable to this operation was \$0.4 million in the fourth quarter of 2017. Excluding this loss, adjusted EBITDA would have been \$8.4 million including the positive contribution of Stuart Packaging acquired in the third quarter of 2017, an improvement of \$0.6 million compared with \$7.8 million in the fourth quarter of 2016. Accordingly, adjusted EBITDA margins would have been 17.1% of revenues excluding Printer Gateway' sales compared with 18.0% in the fourth quarter of 2016.

#### *Amortization*

Aggregate amortization expense for the three-month period ended December 31, 2017 amounted to \$1.5 million, compared with the prior quarter's amortization expense of \$1.1 million. The higher amortization of property, plant and equipment and intangible assets relates to the 2017 acquisition.

#### *Shutdown of Non-Core Operations of Printer Gateway*

On January 22, 2018, the Company closed its Printer Gateway operations to concentrate on its core diversification strategy. The Company provisioned, in the fourth quarter of 2017, a total of \$0.2 million of non-recurring expenses related to the shutdown of this operation. Additionally, an impairment totaling \$2.0 million was also recorded in connection with the write down of the carrying amounts of the goodwill, customer relation, intangibles and property, plant and equipment.

#### *Financing Charges*

Financing charges for the three-month period ended December 31, 2017, were \$0.4 million, compared to \$0.2 million during the same quarter of the prior year. The increase is related mainly to higher debt used to finance the acquisition of Stuart Packaging in July 2017.

### *Earnings before Income Taxes*

Due to the fluctuation in revenue and expenses described above, earnings before income taxes decreased to \$3.3 million during the three-month period ended December 31, 2017 compared to \$6.5 million for the same period in 2016.

### *Provision for Income Taxes*

The Company recorded a provision for income taxes of \$1.0 million during the three-month period ended December 31, 2017, compared with \$1.9 million recorded in the equivalent quarter of last year mainly due to decreased earnings before income taxes.

### *Net Earnings and Adjusted Net Earnings*

Net earnings were at \$2.3 million (or \$0.08 per share) for the three-month period ended December 31, 2017, compared with \$4.6 million (or \$0.16 per share) for the equivalent period in 2016. The closure of the Printer Gateway operations resulted in non-recurring expenses totaling \$2.2 million - asset impairment charges and other closing expenses in the fourth quarter of 2017. Excluding these non-cash items of \$1.6 million net of tax and the provision for contingent remuneration of \$0.5 million, after tax, Adjusted Net Earnings would have been \$4.4 million (or \$0.16 per share) for the three-month period ended December 31, 2017, compared with \$4.6 million (or \$0.16 per share) for the equivalent period in 2016

### *Other Comprehensive Income*

The discount rate used to calculate the accrued plan benefit obligations decreased to 3.4% as at December 31, 2017 from 3.8% as at September 30, 2017. This decrease generated a pre-tax actuarial loss of \$5.2 million on pension liabilities. This loss was reduced by a pre-tax gain of \$3.6 million on pension assets as a result of higher than expected returns.

### ***Twelve-month period ended December 31, 2017 compared with the twelve-month period ended December 31, 2016.***

#### *Revenue*

Revenue for the year ended December 31, 2017, increased by 11.5% or \$18.5 million to \$179.1 million compared with \$160.6 million during the year ended December 31, 2016. This increase was primarily the result of the Company's diversification strategy into the packaging and U.S. envelope markets.

Revenue from the Canadian envelope market stood at \$102.1 million down by \$7.9 million or 7.2% from fiscal 2016. The decline is mainly to a 7.7% reduction in volume combined with a slight increase in average selling prices when compared with last year. A vast majority of the volume variation is attributable to the secular decline in the envelope market. For comparison, Canada Post's most recently available information<sup>3</sup> indicates Transactional Mail volume was down 5.7% in the first three quarters of 2017 compared to the same period in 2016.

Revenue from the U.S. envelope market grew to \$42.4 million, representing an increase of 10.4%. The majority of this increase is attributable to the acquisition of Bowers Envelope Inc. located in the Midwestern United States and concluded on August 29, 2016. The number of units sold increased by 12.6% and average selling prices were slightly lower due to the effect of a stronger Canadian dollar and a modest change in product mix.

Revenue from packaging and specialty products reached \$34.6 million, an increase of 184.0%. This increase is mainly attributable to the acquisition of Stuart Packaging concluded in July 2017, to the acquisition of Durabox in the fourth quarter of 2016 and to a lesser extent, continued growth of the company's legacy e-commerce packaging business.

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<sup>3</sup> Canada Post Corporation, November 24, 2017, Q3 2017 [Results Press Release](#) for the period ended December 31, 2017

### *Operating Expenses*

Operating expenses for the year ended December 31, 2017, were \$130.3 million compared with \$114.4 million for the same period in 2016, an increase of \$15.9 million or 13.9%. The increase is mainly attributable to the 2017 and 2016 business acquisitions previously mentioned and partially offset by lower operating costs in Canada, in line with the lower volume of envelopes sold.

### *Selling, General and Administrative Expenses*

Selling, general and administrative expenses totalled \$22.9 million for the year ended December 31, 2017, compared with \$18.7 million for the same period in 2016, representing an increase of \$4.2 million or 22.3% primarily due to the fiscal 2017 and 2016 business acquisitions. The total provision for contingent remuneration for the year ended December 31, 2017 relating to the acquisitions of Stuart Packaging and Durabox amounted to \$0.8 million.

### *Adjusted EBITDA and Adjusted EBITDA Margins*

Adjusted EBITDA was at \$26.7 million for the year ended December 31, 2017, compared with \$27.4 million for the same period in 2016, a decrease of \$0.7 million or 2.7%. The EBITDA loss attributable to the now closed Printer Gateway operations was \$1.4 million during fiscal 2017. Excluding this EBITDA loss, Adjusted EBITDA would have been \$28.1 million including the positive contribution from Stuart Packaging acquired in the third quarter of 2017, compared to \$27.4 million in 2016, an improvement of \$0.7 million. Additionally, Adjusted EBITDA margins would have been at 15.9% of revenues excluding Printer Gateway's sales, compared to 17.1% last year.

### *Amortization*

Aggregate amortization expense for the year ended December 31, 2017, amounted to \$5.4 million compared with \$6.4 million for the comparable period of 2016, representing a decrease of \$1.0 million or 16.2% mainly explained by the lower amortizable intangible assets given that certain customer relationships have now been fully amortized, 10 years after the initial public offering in 2006.

### *Shutdown of Non-Core Operations of Printer Gateway*

On January 22, 2018, the Company closed its Printer Gateway operations to concentrate on its core diversification strategy. The EBITDA loss attributable to the now closed operations was \$1.4 million in 2017. The Company provisioned, in the fourth quarter of 2017, a total of \$0.2 million of non-recurring expenses related to the shutdown of this operation. Additionally, an impairment totaling \$2.0 million was also recorded in connection with the write-off of the carrying amount of the goodwill, customer relations, intangibles and property, plant and equipment in the fourth quarter of 2017.

### *Financing Charges*

Financing charges for the year ended December 31, 2017 increased to \$1.1 million compared with \$0.9 million in the prior year, given the higher debt used to finance the acquisition of Stuart Packaging.

### *Earnings before Income Taxes*

Due to the fluctuation in revenue and expenses described herein, earnings before income taxes were \$17.0 million during the year ended December 31, 2017, a decrease of 15.1% from \$20.1 million in 2016.

### *Provision for Income Taxes*

During the year ended December 31, 2017, the Company recorded a provision for income taxes of \$4.7 million, down from \$5.5 million recorded for the year ended December 31, 2016 mainly due to decreased earnings before income taxes.



### Net Earnings and Adjusted Net Earnings

Net earnings were \$12.4 million (or \$0.43 per share) for the year ended December 31, 2017, compared with \$14.6 million (or \$0.51 per share) for the equivalent period in 2016. The closure of the Printer Gateway operations resulted in non-recurring expenses totaling \$2.2 million - asset impairment charges and other closing expenses in the fourth quarter of 2017. Excluding these non-cash items of \$1.6 million net of tax and the provision for contingent remuneration of \$0.7 million, after tax, Adjusted Net Earnings would have been \$14.7 million (or \$0.52 per share) for the year ended December 31, 2017, compared to \$14.6 million (or \$0.51 per share) during the equivalent period in 2016.

### Other Comprehensive Income

The discount rate used to calculate the accrued plan benefit obligations decreased to 3.4% as at December 31, 2017 from 3.8% as at December 31, 2016. This decrease generated a pre-tax actuarial loss of \$6.0 million on pension liabilities. This loss was offset by a pre-tax gain of \$6.9 million on pension assets as a result of higher than expected returns.

### Segment Information

The Company currently operates in one business segment: the manufacturing and sale of envelopes, packaging and specialty products. The Company's non-current assets amounted to \$99.7 million in Canada and \$11.1 million in the United States as at December 31, 2017, compared with \$77.1 million and \$12.8 million respectively as at December 31, 2016.

During the fourth quarter of 2017, the Company's revenue in Canada was \$33.1 million, an increase of 6.0% from \$31.2 million in the equivalent period of 2016, and was \$16.3 million in the United States, up by 33.9% from \$12.1 million in the equivalent period of last year.

For the year ended December 31, 2017, the Company's revenue in Canada was \$124.8 million, an increase of 4.7% compared with \$119.1 million in the equivalent period of 2016, and was \$54.3 million in the United States, up by 31.0% from \$41.4 million in the equivalent period of last year.

During the fourth quarter of 2017, the Company's revenue from envelopes was \$36.5 million, a decrease of 6.9% compared with \$39.1 million in the equivalent period of 2016, and was \$12.9 million from packaging and specialty products, up by 204.1% from \$4.3 million in the equivalent period of last year.

For the year ended December 31, 2017, the Company's revenue from envelopes was \$144.5 million, a decrease of 2.6% compared with \$148.4 million in the equivalent period of 2016, and was \$34.6 million from packaging and specialty products, up by 184.0% from \$12.2 million in the equivalent period of last year.

### Summary of Quarterly Operating Results from January 1, 2016 to December 31, 2017

(In thousands of dollars, except for per share amounts)

	Dec. 31, 2017	Sept. 30, 2017	June 30, 2017	Mar. 31, 2017	Dec. 31, 2016	Sept. 30, 2016	June 30, 2016	Mar. 31, 2016
Revenue	49,350	43,424	41,147	45,151	43,374	36,514	39,420	41,262
Adjusted EBITDA <sup>(1)</sup>	8,007	6,355	5,397	6,895	7,827	5,508	6,903	7,145
Earnings before income taxes	3,277	4,238	4,017	5,514	6,529	3,826	5,264	4,448
Net earnings	2,262	3,214	2,833	4,081	4,643	2,832	3,890	3,228
Net earnings per share	0.08	0.11	0.10	0.14	0.16	0.10	0.14	0.11

<sup>(1)</sup> Refer to "Definition of EBITDA, Adjusted Net Earnings, Adjusted Net Earnings and non-IFRS measures"

## Seasonality

Supremex' revenue is subject to the seasonal advertising and mailing patterns of its customers. The number of envelopes sold by Supremex is generally higher during fall and winter mainly due to the higher number of mailings related to events including the return to school, fund-raising, the holidays and tax seasons. The number of envelopes sold by Supremex is generally lower during spring and summer in anticipation of a slowdown in mailing activities of businesses during the summer. As a result, Supremex' revenue and financial performance for any single quarter may not be indicative of revenue and financial performance which may be expected for the full year. To maintain production efficiencies, Supremex uses warehouse capabilities to stock envelopes as required and thereby counter predictable seasonal variations in sales volume.

## Financial Position and Capital Resources

### Financial Position

(In thousands of dollars)

	December 31, 2017	December 31, 2016
Working capital	25,020	20,442
Total assets	157,924	132,539
Secured credit facility	42,831	26,894
Total equity	86,519	82,337

For the three-month period ended December 31, 2017, cash decreased by \$0.4 million when compared to September 30, 2017. For the twelve-month period ended December 31, 2017, cash decreased by \$1.3 million compared to the prior year-end.

### Summary of Cash Flows

(In thousands of dollars)

	Three-month periods ended December 31,		Twelve-month periods ended December 31,	
	2017	2016	2017	2016
Operating activities	5,739	9,096	15,932	21,622
Investing activities	(332)	(8,017)	(25,000)	(14,313)
Financing activities	(5,821)	(334)	8,085	(8,825)
Net foreign exchange difference	24	110	(275)	(53)
Net change in cash	(390)	855	(1,258)	(1,569)

### Cash Flows from Operating Activities

Cash flows generated from operating activities were \$15.9 million during the year ended December 31, 2017, compared with \$21.6 million during the same period in 2016. Working capital used in operations amounted to a use of \$3.4 million for the year period ended December 31, 2017 compared with cash inflows of \$0.3 million in the equivalent period of 2016. This variation as well as the lower profitability explains the reduction in cash flows generated from operations.

### Cash Flows used in Investing Activities

Net cash flows used in investing activities were \$25.0 million during the year ended December 31, 2017, compared to \$14.3 million in 2016, an increase of \$10.7 million mainly attributable to the acquisition of Stuart Packaging as well as higher capital expenditures due to initial investments in packaging equipment to increase production capacity at Stuart Packaging, to the acquisition of a building in Mississauga, Ontario where the Printer Gateway and the Ontario operations of Premier Envelope were both moved to during the third quarter.

### *Cash Flows from Financing Activities*

Net cash flows from financing activities were \$8.1 million during the year ended December 31, 2017, compared with cash flows used in financing activities of \$8.8 million in the comparable period, an increase of \$16.9 million, almost entirely due to a net increase in the use of the secured credit facility. Supremex remains focused on maintaining low net debt ratios and maximizing shareholder returns while maintaining its financial flexibility.

### *Financial Position and Capital Resources Summary*

The Company's ability to generate cash flows from operations combined with its availability under existing credit facilities are expected to provide sufficient liquidity to meet anticipated needs for existing and future projects.

### **Contractual Obligations and Off-Balance Sheet Arrangements**

The following chart outlines the Company's contractual obligations as at December 31, 2017.

*(in thousands of dollars)*

	Payments due by fiscal year			2020 and thereafter
	Total	2018	2019	
Secured credit facility	43,020	—	—	43,020
Operating leases	16,583	3,603	3,304	9,676
Total	59,603	3,603	3,304	52,696

The Company has no other off-balance sheet arrangements.

### **Financing**

As at December 31, 2017, the Company had a five-year committed \$60 million senior secured revolving facility agreement maturing on October 6, 2020. No principal repayments are required prior to maturity. This facility bears interest at a floating rate based on the Canadian prime rate plus an applicable margin that ranges between 0% and 0.25% or bankers' acceptance rates, plus an applicable margin that ranges between 1.50% and 1.75%.

The secured credit facility is used for working capital, capital expenditure and other general corporate purposes. It is collateralized by hypothec and security interests covering all assets of the Company and its subsidiaries and is subject to certain covenants, which the Company is required, among other conditions, to meet. The Company was in compliance with these covenants during 2017.

As at December 31, 2017, The Company had outstanding letter of credit for a total of \$10,000 compared with \$60,000 as at December 31, 2016.

### **Capitalization**

As at February 20, 2018, the Company had 28,405,469 common shares outstanding, a decrease of 205,882 shares following the repurchase made under the Normal Course Issuer Bid programs since January 1, 2017.

### **Financial Instruments**

#### *Interest rate and foreign exchange risk*

The Company's credit facility bear interest at a floating rate which gives rise to the risk that its earnings and cash flows may be adversely affected by fluctuations in interest rates.

The Company operates in Canada and the United States, which exposes its earnings and cash flows to fluctuations in the exchange rate between the U.S. and Canadian dollar. A portion of Supremex' revenue is earned in U.S. dollars while a large portion of its expenses, including most of its paper and other raw materials costs as well as certain capital expenditures, are incurred in U.S. dollars. Supremex also derives a portion of its revenue from Canadian dollar

sales to certain customers for whom the selling price is sensitive to U.S. competition (see “Risk Factors”). Cash, accounts receivable, accounts payable and accrued liabilities include balances denominated in U.S. dollars at the end of the year.

#### *Fair value*

The fair value of the Company’s financial instruments is indicated in note 22 to the Company’s audited consolidated financial statements for the year ended December 31, 2017.

#### **Disclosure Controls and Internal Controls over Financial Reporting (“ICFR”)**

In accordance with National Instrument 52-109 – Certification of Disclosure in Issuers’ Annual and Interim Filings, the Company has filed certifications signed by the President and Chief Executive Officer and the Interim Vice-President, Finance, that, among other things, report on the design and effectiveness of disclosure controls and procedures, and the design and effectiveness of internal control over financial reporting.

Management has designed disclosure controls and procedures to provide reasonable assurance that material information relating to the Company is made known to the President and Chief Executive Officer and the Interim Vice-President, Finance, particularly during the period in which annual filings are being prepared. The President and Chief Executive Officer and the Interim Vice-President, Finance, evaluated the effectiveness of the Company’s disclosure controls and procedures and concluded, based on its evaluation, that such disclosure controls and procedures were effective as of December 31, 2017.

Management has also designed internal control over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS. The President and Chief Executive Officer and the Interim Vice-President, Finance, evaluated the effectiveness of the Company’s internal control over financial reporting and concluded, based on its evaluation, that such internal control over financial reporting was effective as of December 31, 2017. In making its evaluation, the President and Chief Executive Officer and the Interim Vice-President, Finance, used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control – Integrated Framework.

Finally, there has been no change in the Company’s internal control over financial reporting during the year ended December 31, 2017, that materially affected, or is likely to materially affect, the Company’s internal control over financial reporting.

The Company expects that its 2017 business acquisition will be covered by its certification of ICFR under National Instrument 52-109 by the third quarter of 2018.

#### **Significant accounting policies and estimates**

The Company prepares its financial statements in conformity with IFRS, which requires management to make estimates and assumptions that management believes are reasonable based upon the information available. These estimates and assumptions affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Significant areas requiring the use of management estimates relate to intangible assets and goodwill, employee future benefits and income taxes. Management bases its estimates on historical experience and other assumptions, which it believes are reasonable under the circumstances. Management also assesses its estimates on an ongoing basis. The effect on the financial statements of changes in such estimates in future periods could be material and would be accounted for in the period a change occurs.

The significant accounting policies of the Company are described in note 2 to the Company’s audited consolidated financial statements for the year ended December 31, 2017.

The policies the Company believes are most critical to assist in fully understanding and evaluating its reported results include the following:

## **Intangible assets and goodwill**

Intangible assets and goodwill arise out of business combinations for which the Company has applied the acquisition method of accounting. The acquisition method involves the allocation of the cost of an acquisition to the underlying net assets acquired based on their respective estimated fair value. As part of this allocation process, the Company must identify and attribute values and estimated lives to the intangible assets acquired. These determinations involve significant estimates and assumptions regarding cash flow projections, economic risk and weighted average cost of capital ("WACC").

These estimates and assumptions determine the amount allocated to other identifiable intangible assets and goodwill as well as the amortization period for identifiable intangible assets with finite lives. If future events or results differ adversely from these estimates and assumptions, the Company could record increased amortization or impairment charges in the future.

As at December 31, 2017, the Company performed a goodwill impairment test for both of its cash generating units using the discounted cash flows method based upon management's best estimates which reflect the Company's planned course of action in light of market conditions. The Company concluded that there was no impairment in the carrying amount of its goodwill. The Company will continue to monitor the resulting impact of market changes.

### *Valuation technique*

The Company uses the discounted cash flows ("DCF") method to determine the value in use of its cash-generating unit and has not made any changes to the valuation methodology used to assess goodwill impairment since the last annual impairment test.

### *Significant assumptions*

The income approach is predicated upon the value of the future cash flows that a business will generate going forward. The DCF method which was used as at December 31, 2017, involves projecting cash flows and converting them into a present value equivalent through discounting. The discounting process uses a rate of return that is commensurate with the risk associated with the business or asset and the time value of money. This approach requires assumptions about revenue growth or decline rates, operating margins, tax rate and discount rates.

### *Growth or Decline of Revenue*

The assumptions used were based on the Company's internal budget. The Company projected revenue, operating margins and cash flows for a period of four years for each CGU. Specific assumptions are used for each CGU. Forecasts for Envelope CGU considered a lower demand in the Canadian and US envelope markets and applied a perpetual long-term decline rate for the period thereafter. Forecasts for Packaging CGU considered a perpetual long-term growth for this value-added market. In arriving at its forecasts, the Company considered past experience, recent acquisitions, economic trends as well as industry and market trends.

### *Discount Rate*

The Company assumed a pre-tax discount rate to calculate the present value of its projected cash flows. The discount rate represented a weighted average cost of capital ("WACC") for comparable companies operating in a similar industry. The WACC is an estimate of the overall required rate of return on an investment for both debt and equity owners and serves as the basis for developing an appropriate discount rate. Determination of the WACC requires separate analysis of the cost of equity and debt, and considers a risk premium based on an assessment of risks related to the projected cash flows.

The key assumptions used in performing the impairment test were as follows:

	2017		2016
	Envelopes	Packaging	
Pre-tax discount rate	16.7%	16.8%	16.6%
Tax rate	26.1%	26.5%	26.1%
Perpetual (decline) growth rate	(3.0%)	2.0%	(3.0%)

#### *Sensitivity*

In the most recent impairment test performed for the Envelopes CGU, if the pre-tax discount rate had increased to 19.5% or the perpetual decline rate had increased to 8.0%, the recoverable amount of the cash generating unit would have then equaled the carrying amount as at December 31, 2017. If the pre-tax discount rate had increased to 18.3% or the perpetual growth rate had decreased to (0.2%), the recoverable amount of the Packaging CGU would have then equaled the carrying amount as at December 31, 2017.

#### **Employee future benefits**

The Company sponsors defined benefit plans to provide pension and other post-employment benefits to covered employees. The determination of expense and obligations associated with employee future benefits requires the use of assumptions such as the discount rate to measure obligations, the expected mortality, the expected retirement age, the expected rate of future compensation increase and the expected healthcare cost trend rate. Because the determination of the cost and obligations associated with employee future benefits requires the use of various assumptions, there is measurement uncertainty inherent in the actuarial valuation. Actual results will differ from estimated results which are based on assumptions.

#### *Significant assumptions:*

Discount rate for accrued benefit obligation	3.40%
Discount rate for net pension costs	3.80%
Rate of compensation increase	2.50%
Mortality assumption	CPM Private

#### *Discount rate*

As at December 31, 2017, we used the *Fiera Capital's CIA Method Accounting Discount Rate Curve* which follows the methodology suggested in the CIA Education Note on *Accounting Discount Rate Assumption for Pension and Post-employment Benefit Plans*.

#### *Sensitivity analysis*

For the Company, a 0.25% increase or decrease in the discount rate would have decreased or increased the defined benefit liability by approximately \$3.3 million as at December 31, 2017. A 0.25% increase or decrease in the rate of compensation would have increased or decreased the pension benefit liability by approximately \$0.4 million as at December 31, 2017. An increase of one year in the life expectancy of plan members as at December 31, 2017 results in an increase of \$3.2 million in total projected defined benefit obligation of pension plans. The sensitivity analysis has been determined based on a method that determines the impact on the defined benefit liability of a 0.25% change in the key assumptions. There have been no changes in the methods and assumptions used to determine the sensitivity analysis from the comparative year.

#### *Rate of compensation*

Future salary increases are based on expected future inflation rates.

## **Income taxes**

The Company computes an income tax provision in each of the jurisdictions in which it operates. However, the actual amount of the income tax expense becomes final only upon filing and acceptance of the tax return by the relevant authorities, which take place subsequent to the issuance of the financial statements. Additionally, estimation of income taxes includes evaluating the recoverability of deferred tax assets based on an assessment of the ability to use the underlying future tax deductions against future taxable income before they expire. The assessment is based upon existing tax laws and estimates of future taxable income. To the extent estimates differ from the final tax return, earnings would be affected in a subsequent period.

The Company is subject to taxation in multiple jurisdictions. There are many transactions and calculations for which the ultimate tax determination is uncertain during the normal course of business. The Company maintains provisions for uncertain tax positions that it believes appropriately reflects its risk with respect to tax matters under active discussion, audit, dispute or appeal with tax authorities, or which are otherwise considered to involve uncertainty. These provisions are made using the best estimate of the amount expected to be paid based on a qualitative assessment of all relevant factors. The Company reviews the adequacy of these provisions at the end of the reporting period. However, it is possible that at some future date an additional liability could result from audits by taxing authorities. Where the final outcome of these tax-related matters is different from the amounts that were initially recorded, such differences will affect the tax provisions in the period in which such determination is made.

The Company's 2017 effective tax rate was 26.1% of earnings before income tax.

## **Future Changes of Accounting Policies**

### **IFRS 9, Financial instruments**

IFRS 9, Financial Instruments ("IFRS 9") which replaces IAS 39, Financial Instruments: Recognition and Measurement, establishes principles for the financial reporting of financial assets and financial liabilities that will present relevant and useful information to users of financial statements for their assessment of the amounts, timing and uncertainty of an entity's future cash flows.

IFRS 9 is effective as of January 1, 2018.

The Company has assessed its financial instruments and does not expect the standard to have a material impact on its financial statements.

### **IFRS 15, Revenue from contracts with customers**

In May 2014, the International Accounting Standards Board (IASB) issued a revenue recognition standard, IFRS 15 Revenue from Contracts with Customers, which replaces IAS 18 Revenue and IAS 11 Construction Contracts and all existing IFRS revenue interpretations. IFRS 15 establishes a five-step model that will apply to revenue earned from a contract with a customer (with limited exceptions), regardless of the type of revenue transaction or the industry. The standard's requirements will also apply to the recognition and measurement of gains and losses on the sale of some non-financial assets that are not an output of the entity's ordinary activities (e.g., sales of property, plant and equipment or intangibles). In April 2016, the International Accounting Standards Board (IASB) issued the amendments to IFRS 15. The amendments provide clarification in order to assist companies with implementing the new revenue standard.

IFRS 15 is effective for annual periods beginning on or after January 1, 2018.

The Company has undertaken a comprehensive review of its significant contracts in accordance with the five-step model in IFRS 15 to determine the impact on the timing and measurement on its revenue recognition. Based on this review, the Company does not expect the standard to have a material impact on its financial statements.

## **IFRS 16, Leases**

IFRS 16, Leases is required to be applied retrospectively for annual periods beginning on or after January 1, 2019, with early adoption permitted provided that IFRS 15 has been applied or is applied at the same time as IFRS 16.

IFRS 16 replaces IAS 17 Leases and related interpretation. Under this new standard, which provides a single model for leases abolishing the current distinction between finance leases and operating leases, most leases will be recognized in the statement of financial position. Certain exemptions will apply for short-term leases of low-value assets. The Company anticipates that the adoption of IFRS 16 will have a material impact on its statement of financial position and its statement of earnings as nearly all operating leases will be capitalized with a corresponding liability, while the rent expense will be replaced by the amortization of the right to use the related assets, and interest accretion expense from the liabilities will be recorded.

The Company is currently still assessing the impact of this new standard on its consolidated financial statements.

## **Recent Event**

On February 20, 2018, the Board of Directors declared a quarterly dividend of \$0.065 per common share, payable on April 13, 2018, to shareholders of record at the close of business on March 29, 2018.

## **Risk Factors**

The results of operations, business prospects and financial condition of Supremex are subject to a number of risks and uncertainties, and are affected by a number of factors outside the control of Supremex' management.

### *Decline in Envelope Consumption*

Supremex' envelope manufacturing business is highly dependent upon the demand for envelopes sent through the mail. Supremex may compete with product substitutes, which can impact demand for its products. Usage of the Internet and other electronic media continues to grow. Consumers use these media to purchase goods and services, and for other purposes such as paying invoices. Advertisers use the Internet and electronic media for targeted campaigns directed at specific electronic user groups. Large and small businesses use electronic media to conduct business, send invoices and receive payments.

The North American envelope manufacturing and mailing industries are expected to continue to decline in the foreseeable future, due to a general progressive reduction in the use of traditional paper-based products. The business depends on transactional mail and direct mail activities. Transactional mail volumes are thought to have declined in the last few years due in part to the increasing use of non-traditional means of communication and information transfer, such as electronic mail and the Internet. There is no assurance that the direct mail industry will remain at its current levels. As a result, there can be no assurance that Supremex will be able to grow or even maintain historical sales levels.

To reduce this risk, the Company continually strives to improve operational efficiency and develop and acquire new products such as the packaging directed toward e-commerce fulfillment and other applications.

The majority of envelopes consumed in Canada and the United States are mailed and as a result, any strike or other work stoppage by unionized postal workers would result in a temporary suspension of the mail activities of most of Supremex' customers and could have a material adverse effect on Supremex. In the summer of 2011, there was a work stoppage at Canada Post that lasted about 3 weeks. Further labour negotiations threatened a work stoppage at Canada Post in the summer of 2016. However an agreement was reached and work disruptions were averted. During both periods, envelope shipments to customers were slightly affected and some direct mail orders were cancelled. Adoption of e-billing also increased during that period. Many large corporations used the work stoppage at Canada Post to promote the advantages of e-billing. It is impossible to quantify the impact of the work stoppage due to its long-term potential effect.



In addition, postal rates are a significant factor affecting envelope usage and any increases in postal rates, relative to changes in the cost of alternative delivery means or advertising media, could result in reductions in the volume of mail sent. To that effect, in December 2013, Canada Post announced a Five-Point action plan by which, notably:

- Over the next five years, the one third of Canadian households that receive their mail at their door will be converted to community mailbox delivery (since suspended by the Trudeau government);
- A new pricing structure for Letter Mail mailed within Canada will be introduced in March 2014 (increases from 14.75% for machineable standard letter mail to 35% for individual stamps);
- The retail network will be strengthened by opening more franchise postal outlets in stores across Canada;
- Changes to internal operations to obtain a more efficient flow of parcels and mail through the network and to the customers; and
- Changes to the business model, which will require fewer employees.

No assurance can be provided that future increases in postal rates will not have a negative effect on the level of mail sent or the volume of envelopes purchased.

Finally, from time to time, there has been talk of “do-not-mail” legislation in the U.S. with respect to the direct mail industry, primarily around the distribution of non-targeted advertising mail and the environment. “Do-not-mail” legislation is instituted at the state level. While such activities have generally not been successful, if such legislation were to be passed, it would have a negative impact on the Company’s sales volume.

#### *Customer relationships*

Supremex typically does not enter into long-term, written agreements with customers. As a result, there is a risk that customers may, without notice or penalty, terminate their relationship with Supremex at any time. In addition, even if customers decide to continue their relationship with Supremex, there can be no guarantee that they will purchase the same amount as in the past, or that purchases will be on similar terms.

#### *Competition*

Despite Supremex’ leading market position in Canada in the envelope business, new entrants into the Canadian envelope market may have an impact on sales and margins. During the 2008-2011 period, the strengthening of the Canadian dollar against the U.S. dollar created an incentive for US-based competitors to increase market penetration in Canada in the five years preceding 2013. U.S. envelope manufacturers may use their excess capacity to penetrate the Canadian envelope market. As long as the U.S. market stays oversupplied, there will be pricing pressure in the Canadian market. However, the costs of freight, coupled with delivery inefficiencies are barriers to servicing any significant customer volume from a distance. Since the second half of 2012, the Canadian dollar started weakening against the U.S. dollar, a general trend that still continues

In the current market, the Canadian envelope manufacturers are more aggressive on pricing in order to generate new sales to replace their sales lost to secular decline. Given the Company’s large market share in Canada, most of the gains by smaller competitors in Canada are made at the expense of Supremex’ accounts.

Over the last several years, the U.S. envelope market has been undergoing structural changes and pricing pressure resulting from an oversupplied environment. On February 2, 2018, the industry’s largest manufacturer filed for Chapter 11 bankruptcy protection<sup>4</sup>. Although there can be no assurance of such an outcome, management believes that Supremex, through its U.S. operations, is well positioned to capture additional market share.

#### *Growth by Acquisitions*

The Company plans to grow both organically and through acquisitions. In the recent years, the Company has grown through acquisitions and should reasonably and in large part rely on new acquisitions to pursue its growth. The ability to properly evaluate the fair value of the businesses being acquired, to properly devote the time and human resources required to successfully integrate their activities with those of the Company as well as the capability to realize synergies, improvements and the expected profit and to achieve anticipated returns constitute inherent risks related to

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<sup>4</sup> [Envelope Maker, Comic Book Printer Cenveo Files for Bankruptcy Protection](#), Reuters, February 2, 2018.

acquisitions. The company may also be subject to potential liabilities from past acquisitions that it may not discover in conducting its due diligence.

#### *Economic Cycles*

A significant risk that Supremex faces and over which it has no control is related to economic cycles. In a soft economy, the market most affected at Supremex is its direct mail market. There is a direct correlation between growth/decline in the gross domestic product and direct mail volume. As a result of the soft economic conditions faced recently, the industry has experienced a significant direct mail volume decline. The effects of this decline are limited for Supremex, since direct mail represents less than 20% of Supremex' total annual volume, but a decline does put pressure on the overall market. For transactional mail, which represents about 50% of Supremex' annual volume, economic cycles have a lesser impact than on direct mail since businesses must still mail out invoices to their customers, although the online billing penetration is growing in this segment. In the long term, transactional mail volume has been declining.

#### *Reliance on Key Personnel*

Supremex' senior executives and employees have extensive experience in the industry and with the business, suppliers, products and customers. The loss of management knowledge, expertise and technical proficiency as a result of the loss of one or more members of the core management team could result in a diversion of management resources or a temporary executive gap, and negatively affect the Company's ability to develop and pursue other business strategies, which could materially adversely affect its business and financial results. Also, the expertise pertaining to envelope manufacturing is rare and the loss of key executives heading those functions could have a material adverse effect on the Company's ability to continue to offer a compelling product offering to its customers, which in turn would materially adversely affect its business and financial results.

#### *Raw Material*

The primary raw materials the Company uses are paper and paper-based substrates, window material, glue and ink. Fluctuations in raw material and energy prices affect operations.

While paper costs were generally a pass through in the past, an increase in the price of paper can negatively affect our operations if it changes the purchasing habits of customers, especially in the current economic conditions. Moreover, an increase in the price of paper negatively affects Supremex' profitability if the increases cannot be passed on to the customer. To mitigate this risk, the Company does not rely on any one supplier and is generally disciplined in passing on any raw material increases to its customers. The availability of suitable quality recycled board within a reasonable distance of the Company's packaging divisions is also a risk. Finally, fluctuations in the price of oil, a core ingredient in the composition of window material, glue and ink has a direct impact on their price. An increase in the price of oil can have a negative effect on operations if it changes the purchasing habits of customers.

#### *Exchange Rate*

A portion of Supremex' revenue is earned in U.S. dollars while a large portion of its expenses, including most of its paper and other raw materials costs as well as certain capital expenditures are incurred in U.S. dollars. Supremex also derives a portion of its revenue from Canadian dollar sales to certain customers for whom selling price is sensitive to U.S. competition.

Net exposure to the U.S. dollar continues to decrease as the Company's growing revenues in the U.S. envelope market, compensates for the volume of raw materials it currently purchases in USD. Revenue generated from customers in the United States represented 30.3% of consolidated revenue in fiscal 2017, up from 25.8% in fiscal 2016.

## *Environment*

The Company operates in an industry which uses large quantities of paper in its day-to-day operations. With society's mounting concern over the protection of the environment and sustainable development, Supremex' products and services are under pressure to be more environmentally friendly. For instance, the growing concern over the environment could change the consumption habits of consumers and new regulations could force the Company to use more expensive environmentally friendly materials in its production process. To mitigate this risk, the Company tries to be at the forefront of its industry in terms of commitment to the environment and, in collaboration with its suppliers, seeks on an ongoing basis to reduce its impact on the environment. Supremex is also a leader in the Canadian envelope market in the marketing of environmentally friendly products, such as 100% recycled paper.

## *Availability of Capital*

In 2015, the Company entered into a Five-Year Committed \$50 million Senior Secured Revolving Facility Agreement with Bank of Montreal maturing on October 6, 2020. This facility was increased to \$60 million in July 2017. Although the Company carried out this modification to its line of credit successfully, there is no guarantee that additional funds will be available in the future, and if they are, that they will be provided in a timeframe and under conditions acceptable to the Company.

## *Credit*

The Company is exposed to credit risk with respect to trade receivables. A specific credit limit is established for each customer and periodically reviewed by the Company. No single customer accounts for more than 10% of consolidated accounts receivable. Supremex' customer base is solidly diversified and consists mainly of large national customers, such as large Canadian corporations, nationwide resellers and governmental bodies, as well as paper merchants and solution and process providers. Historically, the level of bad debt has been low given the nature of the customers. As at December 31, 2017, the maximum credit risk exposure for receivables corresponds to their carrying value.

## *Interest Rate*

The Company is exposed to market risks related to interest rate fluctuations. Floating-rate debt bears interest based on Canadian prime rate, plus an applicable margin that ranges between 0% and 0.25% or bankers' acceptance rates, plus an applicable margin, which ranges from 1.50% to 1.75%. As at February 20, 2018, the Company assessed that the cost of entering into an interest swap outweighed its benefits.

## *Litigation*

Supremex, like other manufacturing and sales organizations, is subject to potential liabilities connected with its business operations, including expenses associated with product defects, performance, reliability or delivery delays. Supremex is from time to time threatened with, or named as a defendant in, legal proceedings, including lawsuits based on product liability, personal injury, breach of contract and lost profits or other consequential damages claims, in the ordinary course of conducting its business. A significant judgment against Supremex or the imposition of a significant fine or penalty, as a result of a finding that Supremex failed to comply with laws or regulations, or being named as a defendant on multiple claims could have a material adverse effect on Supremex' business, financial condition, results of operations and cash available for distributions.

## *Employee Future Benefits*

The Company maintains four registered defined benefit pension plans substantially covering all of its employees. Three of these plans are hybrids and included a defined contribution component. In the third quarter of 2012, the Company converted, for future services, its defined benefit pension plans into defined-contribution plans. In the past, the Company has also provided post-retirement and post-employment benefits, including health care, dental care and life insurance, to a limited number of employees.

The level of the contributions may vary depending on the realized return on the pension fund asset and the discount rate of the future liabilities, which could affect the financial condition of Supremex.

## **Forward-Looking Information**

This MD&A contains “forward-looking information” within the meaning of applicable Canadian securities laws, including (but not limited to) statements about the EBITDA and future performance of Supremex and similar statements or information concerning anticipated future results, circumstances, performance or expectations. Forward-looking information may include words such as anticipate, assumption, believe, could, expect, goal, guidance, intend, may, objective, outlook, plan, seek, should, strive, target and will. Such information relates to future events or future performance and reflects current assumptions, expectations and estimates of management regarding growth, results of operations, performance, business prospects and opportunities, Canadian economic environment and liability to attract and retain customers. Such forward-looking information reflects current assumptions, expectations and estimates of management and is based on information currently available to Supremex as at the date of this MD&A. Such assumptions, expectations and estimates are discussed throughout the MD&A for the year ended December 31, 2017.

Forward-looking information is subject to certain risks and uncertainties, and should not be read as a guarantee of future performance or results and actual results may differ materially from the conclusion, forecast or projection stated in such forward-looking information. These risks and uncertainties include but are not limited to the following: economic cycles, availability of capital, decline in envelope consumption, increase of competition, exchange rate fluctuations, raw material increases, credit risks with respect to trade receivables, increases in funding requirements of pension plans, postal services deficiencies, interest rates fluctuations and potential risk of litigation. Such risks and uncertainties are discussed throughout this MD&A for the year ended December 31, 2017 and, in particular, in “Risk Factors”. Consequently, we cannot guarantee that any forward-looking information will materialize. Readers should not place any undue reliance on such forward-looking information unless otherwise required by applicable securities legislation. The Company expressly disclaims any intention and assumes no obligation to update or revise any forward-looking information, whether as a result of new information, future events or otherwise

## **Definition of EBITDA, Adjusted EBITDA, Adjusted Net Earnings and Non-IFRS Measures**

References to “EBITDA” are to earnings before financing charges, income tax expense, amortization of property, plant and equipment and of intangible assets, gain or loss on disposal of property, plant and equipment. Supremex believes that EBITDA is a measurement commonly used by readers of financial statements to evaluate a company’s operational cash-generating capacity and ability to discharge its financial obligations. References to “Adjusted EBITDA” are to EBITDA adjusted to remove the expenses related to the shutdown of non-core operations of Printer Gateway as well as the effect of removing remuneration expense related to the accounting of contingent considerations in connection with business combinations as these charges are considered non-recurring. References to “Adjusted Net Earnings” are to net earnings adjusted to remove the expenses related to the shutdown of non-core operations of Printer Gateway as well as the effect of removing remuneration expense related to the accounting of contingent considerations in connection with business combinations, net of income taxes, as these charges are considered non-recurring.

EBITDA, Adjusted EBITDA or Adjusted Net Earnings are not recognized earnings measures under IFRS and do not have a standardized meaning prescribed by IFRS. Therefore, EBITDA, Adjusted EBITDA or Adjusted Net Earnings may not be comparable to similar measures presented by other entities. Investors are cautioned that EBITDA, Adjusted EBITDA or Adjusted Net Earnings should not be construed as an alternative to net earnings determined in accordance with IFRS as an indicator of the Company’s performance. Non-IFRS measures include net indebtedness to Adjusted EBITDA ratio (with Adjusted EBITDA including the recently acquired company’s last-twelve-month EBITDA). This ratio is calculated in accordance with the definition in the Company’s credit agreement as total debt net of cash divided by Adjusted EBITDA.

## **Additional Information**

Additional information relating to the Company, including the Company’s annual information form, is available on SEDAR at [www.sedar.com](http://www.sedar.com).

Consolidated Financial Statements

**Supremex Inc.**

December 31, 2017 and 2016

All amounts expressed in Canadian dollars

## Independent auditors' report

To the shareholders of  
**Supremex Inc.**

We have audited the accompanying consolidated financial statements of **Supremex Inc.**, which comprise the consolidated statements of financial position as at December 31, 2017 and 2016, and the consolidated statements of earnings, comprehensive income, changes in equity and cash flows for the years then ended, and a summary of significant accounting policies and other explanatory information.

### Management's responsibility for the consolidated financial statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

### Auditors' responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

### Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of **Supremex Inc.** as at December 31, 2017 and 2016, and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards.

*Ernst & Young LLP<sup>1</sup>*

Montreal, Canada  
February 20, 2018

<sup>1</sup> CPA auditeur, CA, permis de comptabilité publique n° A121006

Supremex Inc.

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

As at December 31	Notes	2017 \$	2016 \$
<b>ASSETS</b>			
<b>Current assets</b>			
Cash		706,190	1,964,947
Accounts receivable	6	25,977,010	21,237,321
Income tax receivable		524,520	472,886
Inventories	7	18,917,859	16,042,550
Prepaid expenses		1,026,896	647,541
<b>Total current assets</b>		<b>47,152,475</b>	<b>40,365,245</b>
Property, plant and equipment	8,10	34,329,207	27,404,026
Accrued pension benefit asset	9	3,876,907	2,305,107
Intangible assets	10,11	14,796,056	9,377,021
Goodwill	10,12	57,769,363	53,088,016
<b>Total assets</b>		<b>157,924,008</b>	<b>132,539,415</b>
<b>LIABILITIES AND EQUITY</b>			
<b>Current liabilities</b>			
Accounts payable and accrued liabilities	5,13	19,994,984	17,881,807
Dividend payable	19	1,846,355	1,716,681
Provisions	14	290,864	324,236
<b>Total current liabilities</b>		<b>22,132,203</b>	<b>19,922,724</b>
Secured credit facility	15	42,830,886	26,893,914
Deferred income tax liabilities	16	5,808,186	3,186,717
Other long term liability	5	427,000	—
Other post-retirement benefit obligations	9	206,600	199,000
<b>Total liabilities</b>		<b>71,404,875</b>	<b>50,202,355</b>
<b>Equity</b>			
Share capital	17	9,695,439	9,765,711
Contributed surplus	17	278,111,408	278,979,895
Deficit		(200,939,855)	(207,043,901)
Foreign currency translation reserve		(347,859)	635,355
<b>Total equity</b>		<b>86,519,133</b>	<b>82,337,060</b>
<b>Total liabilities and equity</b>		<b>157,924,008</b>	<b>132,539,415</b>

Commitments, contingencies and guarantees [note 20]

Subsequent event [note 25]

See accompanying notes

On behalf of the Directors:

By: signed (Robert B. Johnston) \_\_\_\_\_  
Director

By: signed (Mathieu Gauvin) \_\_\_\_\_  
Director

Supremex Inc.

CONSOLIDATED STATEMENTS OF EARNINGS

Years ended December 31	Notes	2017 \$	2016 \$
<b>Revenue</b>		<b>179,072,759</b>	160,570,353
Operating expenses	7, 9, 18	130,325,375	114,447,567
Selling, general and administrative expenses	9, 18	22,920,182	18,740,282
<b>Operating earnings before amortization, loss on disposal of property, plant and equipment and shutdown of non-core operations of Printer Gateway</b>		<b>25,827,202</b>	27,382,504
Amortization of property, plant and equipment	8	3,713,196	4,519,575
Amortization of intangible assets	11	1,682,702	1,916,581
Loss on disposal of property, plant and equipment		114,533	26,766
Shutdown of non-core operations of Printer Gateway	8, 10, 11, 12	2,191,765	—
<b>Operating earnings</b>		<b>18,125,006</b>	20,919,582
Financing charges, net	15	1,078,191	852,029
<b>Earnings before income taxes</b>		<b>17,046,815</b>	20,067,553
Income tax expense	16	4,655,987	5,474,809
<b>Net earnings</b>		<b>12,390,828</b>	14,592,744
<b>Basic and diluted net earnings per share</b>		<b>0.4348</b>	0.5094
<b>Weighted average number of shares outstanding</b>		<b>28,495,406</b>	28,645,053

See accompanying notes



## Supremex Inc.

## CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

Years ended December 31	Notes	2017 \$	2016 \$
<b>Net earnings</b>		<b>12,390,828</b>	14,592,744
<b>Other comprehensive (loss) income</b>			
<i>Other comprehensive loss to be reclassified to earnings in subsequent periods</i>			
Foreign currency translation adjustments		(983,214)	(201,156)
Net other comprehensive loss to be reclassified to earnings in subsequent periods		(983,214)	(201,156)
<i>Items not to be reclassified to earnings in subsequent periods</i>			
Recognized actuarial gain on defined benefit pension plans, net of income tax expense of \$244,822 [2016 – \$847,190]	9	692,878	2,401,910
Recognized actuarial (loss) gain on other post-retirement benefit, net of income tax recovery of \$1,775 [2016 – expense of \$6,962]	9	(5,025)	19,738
Net other comprehensive income not being reclassified to earnings in subsequent periods		687,853	2,421,648
Other comprehensive (loss) income		(295,361)	2,220,492
<b>Total comprehensive income</b>		<b>12,095,467</b>	16,813,236

See accompanying notes

## Supremex Inc.

## CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

Years ended December 31

	Share capital \$	Contributed surplus \$	Deficit \$	Foreign currency translation reserve \$	Total equity \$
As at December 31, 2015	9,813,365	279,601,180	(217,615,887)	836,511	72,635,169
Net earnings	—	—	14,592,744	—	14,592,744
Other comprehensive income (loss)	—	—	2,421,648	(201,156)	2,220,492
Total comprehensive income	—	—	17,014,392	(201,156)	16,813,236
Dividends declared [note 19]	—	—	(6,442,406)	—	(6,442,406)
Shares repurchased and cancelled [note 17]	(47,654)	(621,285)	—	—	(668,939)
<b>As at December 31, 2016</b>	<b>9,765,711</b>	<b>278,979,895</b>	<b>(207,043,901)</b>	<b>635,355</b>	<b>82,337,060</b>
Net earnings	—	—	12,390,828	—	12,390,828
Other comprehensive income (loss)	—	—	687,853	(983,214)	(295,361)
Total comprehensive income	—	—	13,078,681	(983,214)	12,095,467
Dividends declared [note 19]	—	—	(6,974,635)	—	(6,974,635)
Shares repurchased and cancelled [note 17]	(70,272)	(868,487)	—	—	(938,759)
<b>As at December 31, 2017</b>	<b>9,695,439</b>	<b>278,111,408</b>	<b>(200,939,855)</b>	<b>(347,859)</b>	<b>86,519,133</b>

See accompanying notes

## CONSOLIDATED STATEMENTS OF CASH FLOWS

Years ended December 31	Notes	2017 \$	2016 \$
<b>OPERATING ACTIVITIES</b>			
Net earnings		12,390,828	14,592,744
Non-cash adjustment to reconcile net earnings to net cash flows			
Amortization of property, plant and equipment	8	3,713,196	4,519,575
Amortization of intangible assets	11	1,682,702	1,916,581
Amortization of deferred financing costs	15	68,628	68,628
Loss on disposal of property, plant and equipment		114,533	26,766
Shutdown of non-core operations of Printer Gateway	10	2,191,765	—
Deferred income tax recovery	16	(629,423)	(474,488)
Change in employees benefits		19,700	676,754
		<b>19,551,929</b>	<b>21,326,560</b>
Working capital adjustments			
Variation in accounts receivable		(1,855,105)	2,394,651
Variation in inventories		(1,107,192)	1,180,850
Variation in prepaid expenses		(222,221)	44,309
Variation in accounts payable and accrued liabilities		(61,565)	(1,959,958)
Variation in provisions	14	(33,372)	(8,703)
Variation in income tax payable		(114,786)	(1,308,132)
Change in employee benefits		(653,000)	(47,400)
Change in other long term liability	5	427,000	—
<b>Net cash flows from operating activities</b>		<b>15,931,688</b>	<b>21,622,177</b>
<b>INVESTING ACTIVITIES</b>			
Business combinations, net of cash acquired	5	(17,930,008)	(11,983,435)
Adjustments to considerations paid for previous business combinations		463,533	—
Acquisition of property, plant and equipment	8	(8,062,692)	(1,635,186)
Acquisition of intangibles assets	11	(373,835)	(770,446)
Proceeds from sale of property, plant and equipment		903,127	75,982
<b>Net cash flows used in investing activities</b>		<b>(24,999,875)</b>	<b>(14,313,085)</b>
<b>FINANCING ACTIVITIES</b>			
Increase (repayment) of secured credit facility		15,868,344	(1,848,735)
Dividends paid	19	(6,844,961)	(6,307,029)
Purchase of share capital for cancellation	17	(938,759)	(668,939)
<b>Net cash flows from (used in) financing activities</b>		<b>8,084,624</b>	<b>(8,824,703)</b>
Net change in cash		(983,563)	(1,515,611)
Net foreign exchange difference		(275,194)	(53,359)
Cash, beginning of period		1,964,947	3,533,917
<b>Cash, ending of period</b>		<b>706,190</b>	<b>1,964,947</b>
<b>Supplemental information <sup>(1)</sup></b>			
Interest paid		1,149,003	887,660
Interest received		12,670	6,555
Income taxes paid		5,593,141	7,503,602
Income taxes received		388,038	388,672

<sup>(1)</sup> Amounts paid and received for interest and for income taxes were reflected as cash flows from operating activities in the consolidated statements of cash flows.

See accompanying notes

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017 and 2016

### 1. CORPORATE INFORMATION

Supremex Inc. (the "Company" or "Supremex") was incorporated on March 31, 2006 under the *Canadian Business Corporation Act*. The common shares of the Company are listed on the Toronto Stock Exchange ("TSX") under the symbol SXP. The Company's registered office is located at 7213 Cordner Street in LaSalle, Quebec.

Supremex is a leading North American manufacturer and marketer of envelopes and a growing provider of packaging and specialty products. Supremex' revenue is subject to the seasonal advertising and mailing patterns of its customers. The number of envelopes sold by Supremex is generally higher during fall and winter mainly due to the higher number of mailings related to events including the return to school, fund-raising, the holidays and tax seasons. The number of envelopes sold by Supremex is generally lower during spring and summer in anticipation of a slowdown in mailing activities of businesses during the summer.

These consolidated financial statements were approved by the Company's Board of Directors on February 20, 2018.

### 2. SIGNIFICANT ACCOUNTING POLICIES

#### Basis of preparation and statement of compliance

These consolidated financial statements were prepared in accordance with International Financial Reporting Standards ("IFRS"). These consolidated financial statements were prepared on a going concern basis, under the historical cost convention.

#### Principles of consolidation

The consolidated financial statements comprise the financial statements of Supremex Inc. and its wholly-owned subsidiaries, Stuart Packaging Inc., Supremex Midwest Inc., SXP Packaging Inc., Buffalo Envelope Inc. and Classic Envelope Inc.

Subsidiaries are fully consolidated from the date of acquisition, being the date on which the Company obtains control, and continue to be consolidated until the date that such control ceases. The financial statements of the subsidiaries are prepared for the same reporting period as the parent company, using consistent accounting policies. All intra-group balances, income and expenses, unrealized gains and losses and dividends resulting from intra-group transactions are eliminated in full.

#### Business combinations and goodwill

Business combinations are accounted for using the acquisition method. The cost of an acquisition is measured as the aggregate of the consideration transferred, measured at the fair value at the date of the acquisition. Acquisition costs incurred are expensed and included in administrative expenses.

Goodwill is initially measured at cost, being the excess of the aggregate of the consideration transferred over the Company's net identifiable assets acquired and liabilities assumed. If this consideration is lower than the fair value of the net assets of the subsidiary acquired, the difference is recognized in profit or loss.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017 and 2016

### 2. SIGNIFICANT ACCOUNTING POLICIES [Cont'd]

After initial recognition, goodwill is measured at cost less any accumulated impairment losses.

Goodwill is allocated as at the date of a business combination to a cash-generating unit ("CGU") for purpose of impairment testing [See note 2 (*Impairment testing of goodwill*)]. The allocation is made to the CGU or group of CGUs expected to benefit from the synergies of the business acquisitions.

#### **Segment reporting**

The Company operates in one reporting segment: the manufacturing and sale of a broad range of standard and custom envelopes, packaging and specialty products.

#### **Foreign currency translation**

Supremex' consolidated financial statements are presented in Canadian dollars, which is also its functional currency. Supremex and its subsidiaries each determine their own functional currency and items included in each of their financial statements are measured using that functional currency.

#### ***Transactions and balances***

Transactions in foreign currencies are initially recorded by the entities at their respective functional currency rates prevailing at the date of the transaction.

Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency spot rate of exchange ruling at the reporting date. All differences are taken to the consolidated statement of earnings.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions.

#### ***Subsidiaries***

The assets and liabilities of foreign operations are translated into Canadian dollars at the rate of exchange prevailing at the reporting date and their statements of earnings are translated at average exchange rates of the period. The exchange differences arising on translation are recognized in other comprehensive income (loss). On disposal of a foreign operation, the component of other comprehensive income (loss) relating to that particular foreign operation is recognized in the consolidated statement of earnings.

#### **Revenue recognition**

Revenue is measured at the fair value of the consideration received or receivable, net of estimated returns and discounts, and after eliminating intercompany sales.

Revenue from the sale of goods is recognized when the following criteria are met:

- The risks and rewards of ownership, including managerial involvement, have been transferred to the buyer;
- The amount of revenue can be measured reliably;
- The receipt of economic benefits is probable; and
- Costs incurred or to be incurred can be measured reliably.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017 and 2016

### 2. SIGNIFICANT ACCOUNTING POLICIES [Cont'd]

In addition to the above general principles, the Company applies specific revenue recognition for bill and hold transactions. When customers request a bill and hold, revenue is recognized when the customer is invoiced for goods that have been produced, packaged and made ready for shipment. These goods are shipped within a specified period of time and are segregated from other inventory, the risk of ownership of the goods is assumed by the customer, and the terms and collection experience on the related billings are consistent with all other sales.

#### Taxation

Tax expense comprises current and deferred tax. Tax is recognized in the consolidated statement of earnings except to the extent it is related to items recognized in other comprehensive loss or directly in equity.

##### *Current tax*

Current tax expense is based on the results for the year as adjusted for items that are not taxable or not deductible. Current tax is calculated using tax rates and laws that were enacted or substantively enacted at the end of the reporting period. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. Provisions are established where appropriate on the basis of amounts expected to be paid to the tax authorities.

##### *Deferred tax*

Deferred tax is recognized, using the liability method, on temporary differences at the reporting date arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated statement of financial position. Deferred tax is calculated using tax rates and laws that have been enacted or substantively enacted at the end of the reporting period, and which are expected to apply when the related deferred income tax asset is realized or the deferred income tax liability is settled.

##### *Deferred tax liabilities:*

- Are generally recognized for all taxable temporary differences;
- Are recognized for taxable temporary differences arising on investments in subsidiaries, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future; and
- Are not recognized on temporary differences that arise from goodwill which is not deductible for tax purposes.

##### *Deferred tax assets:*

- Are recognized to the extent it is probable that taxable profits will be available against which the deductible temporary differences (carry-forward of unused tax credits and unused tax losses) can be utilized ; and
- Are reviewed at the end of the reporting period and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017 and 2016

### 2. SIGNIFICANT ACCOUNTING POLICIES [Cont'd]

Deferred tax assets and liabilities are not recognized in respect of temporary differences that arise on initial recognition of assets and liabilities acquired other than in a business combination and the transaction does not affect accounting profit or taxable profit upon completion. The carrying amount of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilized. Unrecognized deferred tax assets are reassessed at each reporting date and are recognized to the extent that it has become probable that future taxable profits will allow the deferred tax asset to be recovered.

#### *Sales tax*

Revenues, expenses and assets are recognized net of the amount of sales tax, except:

- Where the sales tax incurred on a purchase of assets or services is not recoverable from the taxation authority, in which case the sales tax is recognized as part of the cost of acquisition of the asset or as part of the expense item as applicable;
- For accounts receivables and trade payables that are stated with the amount of sales tax included.

The net amount of sales tax recoverable from, or payable to, the taxation authority is included as part of the accounts payable and accrued liabilities in the consolidated statement of financial position.

#### **Employee future benefits**

The Company maintains four defined benefit pension plans, three of which are hybrid as they also have a defined contribution component, covering substantially all of its employees. In the third quarter of 2012, the Company converted its defined benefit pension plans into defined contribution plans for future services. All defined benefit pension plans are funded.

For defined benefit pension plans and other post-employment benefits, the net periodic pension expense is actuarially determined on an annual basis by independent actuaries using the projected unit credit method. The past service cost is recognized in the consolidated statement of earnings on the earlier of the date of the plan amendment or curtailment, and the date the Company recognizes pension plan restructuring related costs.

The asset or liability recognized in the consolidated statement of financial position is the present value of the defined benefit obligation at the end of the reporting period less the fair value of plan assets and the effect of the ceiling, if any. The present value of the defined benefit obligation for service accrued at year-end is determined by discounting the estimated future cash outflows using interest rates of high-quality corporate bonds that are denominated in the currency in which the benefits will be paid and that have terms to maturity approximating the terms of the related pension liability. All actuarial gains and losses, the effect of the asset ceiling and the return on plan assets, excluding net interest, are recognized immediately in other comprehensive income (loss). For funded plans, surpluses are recognized only to the extent that the surplus is considered recoverable taking into account future contributions for unfunded liability. Recoverability is primarily based on the extent to which the Company can unilaterally reduce future contributions to the plan. The interest expense of defined benefit obligation is calculated by applying the prior year's discount rate to the beginning balance of the accrued pension benefit liability and to the year's cash inflows. It is recognized in the financing charges of the consolidated statements of earnings. All the other administrative defined benefit plan expense components are recognized in the selling, general and administrative expenses of the consolidated statement of earnings.

Payments to defined contribution plans are expensed as incurred, i.e., as the related employee service is rendered.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017 and 2016

### 2. SIGNIFICANT ACCOUNTING POLICIES [Cont'd]

#### Termination benefits

Termination benefits are generally payable when employment is terminated before the normal retirement date or whenever an employee accepts voluntary redundancy in exchange for these benefits. The Company recognizes termination benefits when it is demonstrably committed to either terminating the employment of current employees according to a detailed formal plan without realistic possibility of withdrawal or providing termination benefits as a result of an offer made to encourage voluntary redundancy.

#### Basic and diluted net earnings per share

The Company presents basic net earnings per share for its common shares, calculated by dividing the net earnings attributable to common shareholders of the Company by the weighted average number of common shares outstanding during the year.

#### Inventories

Inventories are stated at the lower of cost and net realizable value. Cost is determined using the first-in, first-out method. The cost of finished goods and work-in-progress comprises raw materials, direct labour, other direct costs and related production overheads. Net realizable value is the estimated selling price in the normal course of business, less applicable variable selling expenses.

#### Property, plant and equipment

Property, plant and equipment are recorded at cost. Amortization is calculated using the straight-line method over the following estimated useful lives:

Buildings	10 to 40 years
Leasehold improvements	Lease term
Machinery and equipment	Seven to 15 years
Office equipment	Three to five years
Computer equipment	Three years

Residual values, method of amortization and useful lives are reviewed annually prior to year-end and adjusted if appropriate.

#### Intangible assets

Upon acquisition, identifiable intangible assets are recorded at fair value if they result from a business acquisition, if not, at cost and are carried at cost less accumulated amortization. Intangible assets acquired are comprised of mainly customer relationships and non-compete agreements which are amortized on a straight-line basis over ten years. Software is amortized on a straight line basis over seven to ten years.

#### Impairment of non-financial assets

Impairments are recorded when the recoverable amount of assets are less than their carrying amounts. The recoverable amount is the higher of an asset's fair value less cost to sell or its value in use. Impairment losses, other than those relating to goodwill, are evaluated for potential reversals when events or changes in circumstances warrant such consideration.



## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017 and 2016

### 2. SIGNIFICANT ACCOUNTING POLICIES [Cont'd]

The carrying values of all intangible assets and property, plant and equipment are reviewed for impairment whenever events or changes in circumstances indicate that their carrying amount may not be recoverable. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash inflows. The Company bases its impairment calculation on detailed budgets and forecast calculations, which generally cover a period of four years.

#### **Impairment testing of goodwill**

Goodwill is tested for impairment annually as at December 31 or more often if events or changes in circumstances indicate that it might be impaired. The impairment test consists of a comparison of the recoverable amount of the cash-generating unit to which goodwill is assigned with its carrying amount. Any impairment loss in the carrying amount compared with the fair value is charged to earnings in the period in which the impairment occurs.

#### **Provisions**

Provisions are recognized when the Company has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and the amount can be reliably estimated. Provisions are measured at the present value of the expected expenditures to settle the obligation using a discount rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognized as a financing charge.

#### **Leases**

Leases are classified as either operating or finance, based on the substance of the transaction at the inception of the lease. Classification is re-assessed if the terms of the lease are changed.

#### ***Operating lease***

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments under an operating lease are recognized in the consolidated statement of earnings on a straight-line basis over the period of the lease.

#### **Financial instruments**

The Company classifies its financial assets in the following categories: at fair value through earnings or loans and receivables. The classification depends on the purpose for which the financial assets were acquired. The Company determines the classification of its financial assets at initial recognition. Financial liabilities are classified as other financial liabilities. For assets and liabilities that are recognized in the consolidated financial statements on a recurring basis, the Company determines whether transfers have occurred between levels of fair value hierarchy at the end of each reporting period.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017 and 2016

### 2. SIGNIFICANT ACCOUNTING POLICIES [Cont'd]

#### ***Fair value through earnings***

##### *Classification*

Financial assets are classified at fair value through earnings if acquired principally for the purpose of selling in the short-term, such as financial assets held for trading, or if so designated by the Company. Assets in this category include cash.

##### *Recognition and measurement*

Financial assets carried at fair value through earnings are initially recognized, and subsequently carried, at fair value, with changes recognized in the consolidated statement of earnings. Transaction costs are expensed.

#### ***Loans and receivables***

##### *Classification*

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets, except for maturities greater than 12 months after the end of the reporting period. These are classified as non-current assets. The Company's loans and receivables comprise accounts receivable in the consolidated statement of financial position.

##### *Recognition and measurement*

Loans and receivables are initially recognized at fair value plus transaction costs and subsequently carried at amortized cost using the effective interest method.

#### ***Impairment of financial assets***

At the end of each reporting period, the Company assesses whether there is objective evidence that a financial asset is impaired. Impairments are measured as the excess of the carrying amount over the fair value and are recognized in the consolidated statement of earnings.

#### ***Financial liabilities***

Accounts payable and accrued liabilities, dividend payable, provisions and secured credit facilities are classified as other financial liabilities. They are initially recognized at fair value, net of directly attributable transaction costs, and are subsequently carried at amortized cost using the effective interest method.

### 3. SIGNIFICANT ACCOUNTING ESTIMATES

The preparation of the Company's consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities, and the disclosure of contingent liabilities at the end of the reporting period. However, uncertainty about these assumptions and estimates could result in outcomes that require a material adjustment to the carrying amount of the asset or liability affected in future periods.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017 and 2016

### 3. SIGNIFICANT ACCOUNTING ESTIMATES [Cont'd]

The key assumptions concerning the future and other key sources of estimation uncertainty at the reporting date that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below:

#### **Intangible assets and goodwill**

Intangible assets and goodwill arise out of business combinations for which the Company has applied the acquisition method of accounting. The acquisition method involves the allocation of the cost of an acquisition to the underlying net assets acquired based on their respective estimated fair value. As part of this allocation process, the Company must identify and attribute values and estimated lives to the intangible assets acquired. These determinations involve significant estimates and assumptions regarding cash flow projections, economic risk and weighted average cost of capital ("WACC").

These estimates and assumptions determine the amount allocated to other identifiable intangible assets and goodwill as well as the amortization period for identifiable intangible assets with finite lives. If future events or results differ adversely from these estimates and assumptions, the Company could record increased amortization or impairment charges in the future [see note 5]. The Company used also other estimates and assumptions related to the impairment test of goodwill [see note 12].

#### **Employee future benefits**

The Company sponsors defined benefit plans providing pension and other post-employment benefits to covered employees. The determination of expense and obligations associated with employee future benefits requires the use of assumptions such as the discount rate to measure obligations, the expected mortality, the expected retirement age, the expected rate of future compensation increase and the expected healthcare cost trend rate. Because the determination of the cost and obligations associated with employee future benefits requires the use of various assumptions, there is measurement uncertainty inherent in the actuarial valuation process [see note 9]. Actual results will differ from estimated results which are based on assumptions.

#### **Income taxes**

The Company computes an income tax provision in each of the jurisdictions in which it operates. However, actual amounts of income tax expense only become final upon filing and acceptance of the tax return by the relevant authorities, which occur subsequent to the issuance of the financial statements. Additionally, estimation of income taxes includes evaluating the recoverability of deferred tax assets based on an assessment of the ability to use the underlying future tax deductions against future taxable income before they expire. The assessment is based upon existing tax laws and estimates of future taxable income. To the extent estimates differ from the final tax return, earnings would be affected in a subsequent period.

The Company is subject to taxation in multiple jurisdictions. There are many transactions and calculations for which the ultimate tax determination is uncertain during the normal course of business. The Company maintains a provision for uncertain tax positions that it believes appropriately reflect its risk with respect to tax matters under active discussion, audit, dispute or appeal with tax authorities, or which are otherwise considered to involve uncertainty. These provisions are made using the best estimate of the amount expected to be paid based on a qualitative assessment of all relevant factors. The Company reviews the adequacy of these provisions at the end of the reporting period. However, it is possible that, at some future date, an additional liability could result from audits by taxing authorities.

Where the final outcome of these tax-related matters is different from the amounts that were initially recorded, such differences will affect the tax provisions in the period in which such determination is made.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017 and 2016

### 4. RECENT ACCOUNTING PRONOUNCEMENTS

Certain new standards, interpretations, amendments and improvements to existing standards were recently issued. The standards impacted that are applicable to the Company are as follows:

- IFRS 9, *Financial Instruments*  
IFRS 9, *Financial Instruments* ("IFRS 9") which replaces IAS 39, *Financial Instruments: Recognition and Measurement*, establishes principles for the financial reporting of financial assets and financial liabilities that will present relevant and useful information to users of financial statements for their assessment of the amounts, timing and uncertainty of an entity's future cash flows.

IFRS 9 is effective as of January 1, 2018.

The Company has assessed its financial instruments and does not expect the standard to have a material impact on its financial statements.

- IFRS 15, *Revenue from Contracts with Customers*  
In May 2014, the International Accounting Standards Board (IASB) issued a revenue recognition standard, IFRS 15 *Revenue from Contracts with Customers*, which replaces IAS 18 *Revenue* and IAS 11 *Construction Contracts* and all existing IFRS revenue interpretations. IFRS 15 establishes a five-step model that will apply to revenue earned from a contract with a customer (with limited exceptions), regardless of the type of revenue transaction or the industry. The standard's requirements will also apply to the recognition and measurement of gains and losses on the sale of some non-financial assets that are not an output of the entity's ordinary activities (e.g., sales of property, plant and equipment or intangibles). In April 2016, the International Accounting Standards Board (IASB) issued the amendments to IFRS 15. The amendments provide clarification in order to assist companies with implementing the new revenue standard.

IFRS 15 is effective for annual periods beginning on or after January 1, 2018.

The Company has undertaken a comprehensive review of its significant contracts in accordance with the five-step model in IFRS 15 to determine the impact on the timing and measurement on its revenue recognition. Based on this review, the Company does not expect the standard to have a material impact on its financial statements.

- IFRS 16, *Leases*  
IFRS 16, *Leases* is required to be applied retrospectively for annual periods beginning on or after January 1, 2019, with early adoption permitted provided that IFRS 15 has been applied or is applied at the same time as IFRS 16.

IFRS 16 replaces IAS 17 *Leases* and related interpretation. Under this new standard, which provides a single model for leases abolishing the current distinction between finance leases and operating leases, most leases will be recognized in the statement of financial position. Certain exemptions will apply for short-term leases of low-value assets. The Company anticipates that the adoption of IFRS 16 will have a material impact on its statement of financial position and its statement of earnings as nearly all operating leases will be capitalized with a corresponding liability, while the rent expense will be replaced by the amortization of the right to use the related assets, and interest accretion expense from the liabilities will be recorded.

The Company is currently still assessing the impact of this new standard on its consolidated financial statements.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017 and 2016

## 5. BUSINESS COMBINATIONS

On July 20, 2017, the Company acquired all of the outstanding shares of Stuart Packaging Inc. ("Stuart Packaging") for a cash consideration of \$18,639,950. Stuart Packaging is a leading provider of premium quality folding carton packaging for the consumer based in Montreal, Quebec. In addition to the consideration paid, the Company has a contingent consideration payable to the previous owner on the realization of certain financial targets 24 months after the acquisition date. The contingent consideration of up to \$2,050,000 is considered as remuneration and is accounted for over the services period.

This acquisition aligns with the Company's long-term strategy to extend its core products in key markets.

The purchase price allocation is based on initial estimates of fair values at the dates of acquisition and is subject to change until the business valuation is final. The Company expects to complete the purchase price allocation as soon as it has gathered all the significant information available and considered necessary in order to finalize this allocation. The effect may be to transfer an amount to or from the assets acquired, liabilities assumed and goodwill.

The following table presents a preliminary summary of the estimated fair value of assets acquired and liabilities assumed at the acquisition date that occurred during the year ended December 31, 2017:

	Stuart Packaging \$
<b>Net assets acquired</b>	
Cash	709,942
Accounts receivable	2,948,043
Inventories	1,851,164
Prepaid expenses	163,648
<b>Total current assets</b>	<b>5,672,797</b>
Property, plant and equipment	4,411,294
Customer relationships	7,600,000
Goodwill	6,002,328
<b>Total assets</b>	<b>23,686,419</b>
Accounts payable and accrued liabilities	2,022,678
Income tax payable	63,152
Deferred income tax liabilities	2,960,639
<b>Net assets acquired</b>	<b>18,639,950</b>
<b>Cash consideration, net of cash acquired</b>	<b>17,930,008</b>
Acquisition-related costs recognized as an expense	83,877

The Company's consolidated statement of earnings for the period ended December 31, 2017 includes the Stuart Packaging's revenue of \$7,721,717 since the acquisition date. The fair value of the receivables acquired of \$2,948,043 of which no amount was considered uncollectible at the acquisition date, is included in the current asset in the accounting of the business acquisition.

If the acquisition had occurred on January 1, 2017 revenue for the full year from Stuart Packaging would have been approximately \$18,000,000.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017 and 2016

### 5. BUSINESS COMBINATIONS [Cont'd]

There is no goodwill deductible for tax purposes. The goodwill related to the acquisition is composed of expected growth and operational synergies.

#### 2016 business combinations

On December 23, 2016, the Company purchased the principal net assets of Printer Gateway Inc. ("Printer Gateway") for an initial cash consideration of \$2,900,000. During the year ended December 31, 2017, the Company reduced its consideration paid by \$484,371 for the December 2016 acquisition of Printer Gateway Inc. after reaching a settlement with the previous owner. The Company revised the purchase price allocation and adjustments are mainly related to the revised assessment of the acquisition-date fair value of property, plant and equipment and customer relationships.

On November 28, 2016, the Company purchased the principal net assets of Durabox Paper Inc. ("Durabox Paper") for a final cash consideration of \$4,435,341. Durabox Paper is a manufacturer of specialty corrugated paper boxes based in Lachine, Quebec. In addition to the consideration paid, the Company has a contingent consideration payable to the previous owner on the realization of certain financial targets 18 months after the acquisition date. The contingent consideration of \$400,000 is considered as remuneration and is included under the caption of "Accounts payable and accrued liabilities".

On August 29, 2016, the Company purchased the principal net assets of Bowers Envelope Company, Inc. ("Bowers Envelope") for a final cash consideration of \$4,668,932 (\$3,585,419 US). Bowers Envelope is a growing manufacturer and printer of envelopes based in Indianapolis, Indiana.

These two acquisitions are part of the Company's long-term strategy to extend its core products in key markets.

The Company completed its final assessment of the fair value of assets acquired and liabilities assumed of Durabox Paper and Bowers Envelope.

There was no significant adjustment required to the initial purchased price allocations and therefore the prior year was not retroactively adjusted.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017 and 2016

## 5. BUSINESS COMBINATIONS [Cont'd]

The following table presents a summary of the fair value of assets acquired and liabilities assumed at the acquisition date that occurred during the year ended December 31, 2016. The adjustments of net assets acquired of Printer Gateway are included in the following table.

	Bowers Envelope Company, Inc. \$	Durabox Paper Inc. \$	Printer Gateway Inc. \$	Total before adjustments \$	Adjustments \$	Total \$
<b>Net assets acquired</b>						
Accounts receivable	1,196,611	891,764	184,771	2,273,146	(54,051)	2,219,095
Inventories	918,617	608,400	132,770	1,659,787	(67,377)	1,592,410
Prepaid expenses	18,713	—	19,557	38,270	16,092	54,362
<b>Total current assets</b>	<b>2,133,941</b>	<b>1,500,164</b>	<b>337,098</b>	<b>3,971,203</b>	(105,336)	<b>3,865,867</b>
Property, plant and equipment	1,740,098	1,064,946	946,541	3,751,585	(323,666)	3,427,919
Software	—	—	546,207	546,207	—	546,207
Customer relationships	898,518	2,313,311	290,000	3,501,829	113,000	3,614,829
Goodwill	1,102,989	15,736	1,159,550	2,278,275	(4,959)	2,273,316
<b>Total assets</b>	<b>5,875,546</b>	<b>4,894,157</b>	<b>3,279,396</b>	<b>14,049,099</b>	(320,961)	<b>13,728,138</b>
Accounts payable and accrued liabilities	900,429	414,225	379,396	1,694,050	(12,999)	1,681,051
Deferred income tax liabilities	355,878	15,736	—	371,614	155,571	527,185
<b>Net assets acquired</b>	<b>4,619,239</b>	<b>4,464,196</b>	<b>2,900,000</b>	<b>11,983,435</b>	(463,533)	<b>11,519,902</b>
<b>Cash consideration</b>	<b>4,619,239</b>	<b>4,464,196</b>	<b>2,900,000</b>	<b>11,983,435</b>	(463,533) <sup>1</sup>	<b>11,519,902</b>
Acquisition-related costs recognized as an expense	149,501	115,336	39,612	—	—	304,449

<sup>1</sup> The adjustments are mainly related to Printer Gateway business combination.

The Company's consolidated statement of earnings for the year ended December 31, 2016 includes the operating results of Bowers Envelope, Durabox Paper and Printer Gateway, since their acquisition dates; including additional revenue of \$4,382,555. The fair value of the receivables acquired of \$2,219,095 of which no amount was considered uncollectible at the acquisition date, is included in the current assets in the accounting of the business acquisition.

If the acquisition had occurred on January 1, 2016, revenue for the full year from Bowers Envelope, Durabox Paper and Printer Gateway would have been approximately \$22,800,000.

Goodwill deductible for tax purposes amounts to \$2,073,495. The goodwill related to the acquisitions is composed of expected growth and operational synergies.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017 and 2016

## 6. ACCOUNTS RECEIVABLE

	December 31, 2017 \$	December 31, 2016 \$
Trade receivables	24,796,841	20,721,591
Less: Allowance for doubtful accounts	(230,835)	(185,693)
Trade receivables - net	24,566,006	20,535,898
Other receivables	1,411,004	701,423
	<b>25,977,010</b>	<b>21,237,321</b>

Trade receivables are non-interest bearing and are generally on 30-60 days terms.

The aging analysis of trade receivables at each reporting date was as follows:

	December 31, 2017 \$	December 31, 2016 \$
Current	13,560,351	13,431,999
31 – 60 days	7,532,980	5,079,123
61 – 90 days	2,769,781	1,241,245
91 – 120 days	593,914	620,508
Over 120 days	339,815	348,716
	<b>24,796,841</b>	<b>20,721,591</b>

**Allowance for doubtful accounts**

The changes in the allowance for doubtful accounts were as follows:

	December 31, 2017 \$	December 31, 2016 \$
Balance, beginning of year	185,693	87,757
Business combinations	66,125	31,406
(Recovery) charge for the year	(530)	121,007
Utilized	(20,778)	(49,552)
Impact of foreign exchange losses (gains)	325	(4,925)
<b>Balance, end of year</b>	<b>230,835</b>	<b>185,693</b>

The Company is exposed to normal credit risk with respect to its accounts receivable and maintains provisions for potential credit losses. Potential for such losses is mitigated because there is no significant exposure to any single customer and because customer credit worthiness is evaluated before credit is extended.



## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017 and 2016

## 7. INVENTORIES

	December 31, 2017 \$	December 31, 2016 \$
Raw materials	5,895,409	5,234,234
Work in progress	696,612	279,212
Finished goods	12,325,838	10,529,104
	<b>18,917,859</b>	<b>16,042,550</b>

The cost of inventories recognized as an expense and included in operating expenses, including the related amortization of property, plant and equipment allocated to cost of inventories, during the year ended December 31, 2017 is \$133,708,713 [2016 - \$118,765,333].

## 8. PROPERTY, PLANT AND EQUIPMENT

	Lands, buildings and leasehold improvements \$	Machinery and equipment \$	Office and computer equipment \$	Total \$
<b>Cost:</b>				
At December 31, 2015	15,427,327	44,962,943	1,917,435	62,307,705
Acquisition	192,276	1,096,728	346,182	1,635,186
Business combinations [note 5]	108,331	3,573,179	70,075	3,751,585
Adjustments for previous year's business combinations [note 5]	—	(66,765)	—	(66,765)
Disposals	(115,896)	(505,752)	(18,507)	(640,155)
Translation adjustment	2,490	(111,010)	(2,532)	(111,052)
At December 31, 2016	15,614,528	48,949,323	2,312,653	66,876,504
Acquisition	3,818,631	4,128,540	115,521	8,062,692
Business combinations [note 5]	282,892	3,788,024	340,378	4,411,294
Adjustments for previous year's business combinations [note 5]	—	(323,666)	—	(323,666)
Disposals	(19,662)	(1,793,029)	(250,356)	(2,063,047)
Translation adjustment	(8,143)	(497,553)	(7,705)	(513,401)
<b>At December 31, 2017</b>	<b>19,688,246</b>	<b>54,251,639</b>	<b>2,510,491</b>	<b>76,450,376</b>
<b>Amortization:</b>				
At December 31, 2015	3,811,442	30,081,836	1,624,036	35,517,314
Amortization	436,628	3,953,210	129,737	4,519,575
Disposals	(115,896)	(421,511)	—	(537,407)
Translation adjustment	(442)	(23,869)	(2,693)	(27,004)
At December 31, 2016	4,131,732	33,589,666	1,751,080	39,472,478
Amortization	509,421	2,952,903	250,872	3,713,196
Impairment from shutdown of Printer Gateway [note 10]	—	113,733	25,388	139,121
Disposals	(19,662)	(779,601)	(246,124)	(1,045,387)
Translation adjustment	(1,641)	(150,422)	(6,176)	(158,239)
<b>At December 31, 2017</b>	<b>4,619,850</b>	<b>35,726,279</b>	<b>1,775,040</b>	<b>42,121,169</b>
<b>Net book value:</b>				
At December 31, 2016	11,482,796	15,359,657	561,573	27,404,026
<b>At December 31, 2017</b>	<b>15,068,396</b>	<b>18,525,360</b>	<b>735,451</b>	<b>34,329,207</b>

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017 and 2016

## 9. EMPLOYEE DEFINED BENEFIT PLANS

## (a) Pension Plans

The Company maintains four defined benefit pension plans covering substantially all of salaried and hourly employees. Three of these pension plans are hybrid because they also have a defined contribution component. All defined benefit pension plans are funded. Two of these plans are governed by the *Pension Benefits Act of Ontario*. The benefits of one of these plans are based on the average earnings of the best three years and on the final average earnings of the five consecutive years for the other plan. The other two plans are governed under the *Supplemental Pension Plans Act of the Régie des rentes du Québec*. The benefits of one of these plans are based on the average earning of the best three years where the maximum salary was reached and on the average earnings of the best five consecutive years for the other plan. During the third quarter of 2012, the Company converted, for future service, its defined benefit pension plans into defined contributions plans.

The key risks pension plans are exposed to include interest rate risks, investment risks and change in the life expectancy for pensioners.

The defined benefit and defined contribution plans expenses included in operating, selling, general and administrative expenses are as follows:

	2017	2016
	\$	\$
<b>Defined benefit plans</b>		
Administration expenses	195,200	246,400
Past service gains	(88,100)	—
Defined benefit plans expense	107,100	246,400
Defined contribution plan expense	1,320,200	1,373,300
<b>Pension plans expense [note 18]</b>	<b>1,427,300</b>	<b>1,619,700</b>

Interest (income) expense on pension defined benefit plan obligation of (\$94,800) [2016 – \$29,400] is included in the financing charges in the consolidated statement of earnings [see note 15].

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017 and 2016

## 9. EMPLOYEE DEFINED BENEFIT PLANS [Cont'd]

The following table presents the changes in the accrued benefit obligation and the fair value of plan assets, as well as the funded status of the defined benefit plans.

	December 31, 2017 \$	December 31, 2016 \$
<b>Change in accrued benefit obligation</b>		
Benefit obligation, beginning of the year	93,391,800	92,221,800
Interest cost	3,463,800	3,504,900
Employees contribution	88,100	1,600
Actuarial loss from change in financial assumptions	5,311,900	1,291,600
Actuarial loss from experience	680,600	1,076,600
Benefits paid	(4,480,900)	(4,704,700)
Past service gains	(88,100)	—
<b>Benefit obligation, end of year</b>	<b>98,367,200</b>	<b>93,391,800</b>
<b>Change in plan assets</b>		
Fair value of plan assets, beginning of the year	95,696,907	91,920,461
Interest income on plan assets	3,558,600	3,475,500
Actuarial gains	6,930,200	5,617,300
Employer contribution	646,400	25,200
Employees contribution	88,100	1,600
Use of surplus to pay for employer defined contributions	—	(392,054)
Benefits paid	(4,480,900)	(4,704,700)
Plan administration expenses	(195,200)	(246,400)
<b>Fair value of plan assets, end of year</b>	<b>102,244,107</b>	<b>95,696,907</b>
<b>Net amount recognized as accrued pension benefit asset</b>	<b>3,876,907</b>	<b>2,305,107</b>

The defined benefit plans amount recognized in other comprehensive income (loss), before taxation, is as follows:

	2017 \$	2016 \$
Total actuarial gains	937,700	3,249,100
	<b>937,700</b>	<b>3,249,100</b>

The cumulative amount of actuarial losses recognized in the consolidated statement of comprehensive income is \$1,736,300 as at December 31, 2017 [2016 – \$2,674,000].

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017 and 2016

## 9. EMPLOYEE DEFINED BENEFIT PLANS [Cont'd]

The key assumptions used in computing the benefit obligation and net pension cost were as follows:

	2017 %	2016 %
Discount rate for accrued benefit obligation	3.40	3.80
Discount rate for net pension cost	3.80	3.90
Rate of compensation increase	2.50	2.50
Mortality assumption <sup>1</sup>	CPM Private	CPM Private

The weighted average allocation of plan assets as at December 31 is as follows:

	2017 %	2016 %
Equity securities		
Canadian	29.9	30.2
Oil & Gas	1.6	6.9
Financial services	5.9	6.6
Communications & media	1.1	3.5
Industrial products	2.5	4.0
Other	8.9	9.2
Preferred Shares Funds <sup>(1)</sup>	9.9	—
Foreign Global Equity Funds	31.2	27.4
	<b>61.1</b>	<b>57.6</b>
Fixed income funds		
Canadian <sup>(1)</sup>	37.6	37.6
Cash and short-term securities		
Canadian	1.3	4.8
<b>Total</b>	<b>100.0</b>	<b>100.0</b>

<sup>(1)</sup> In 2016, the Preferred Shares Funds were classified in under Canadian Fixed Income Funds.

All financial equity instruments and investment funds are classified as Level 1 fair value hierarchy (quoted prices in active markets).

The pension plans have an investment policy with the following target asset allocations: 60% in equity securities and 40% in fixed income securities [2016 – 50% in equity securities and 50% in fixed income securities]. As at December 31, 2017 and 2016, the pension plans were in compliance with the investment policy allocations.

As of December 31, 2017 and 2016, there were no Supremex shares held in the Company's pension plans.

The average duration of the defined benefit plan obligation is 14.0 years as at December 31, 2017 [2016 – 14.0 years].

<sup>1</sup> CPM 2014 Private Sector Mortality table projected generationally using CPM improvement scale B with no size adjustment

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017 and 2016

## 9. EMPLOYEE DEFINED BENEFIT PLANS [Cont'd]

*Sensitivity analysis*

For the Company, a 0.25% increase or decrease in the discount rate would have decreased or increased the defined benefit liability by approximately \$3.3 million as at December 31, 2017. A 0.25% increase or decrease in the rate of compensation would have increased or decreased the pension benefit liability by approximately \$0.4 million as at December 31, 2017. An increase of one year in the life expectancy of plan members as at December 31, 2017 results in an increase of \$3.2 million in total projected defined benefit obligation of pension plans. The sensitivity analysis has been determined based on a method that determines the impact on the defined benefit liability of a 0.25% change in the key assumptions. There have been no changes in the methods and assumptions used to determine the sensitivity analysis from the comparative year.

## (b) Post-retirement benefits other than pension

The following table provides a reconciliation of the change in the accrued benefit obligation of the plans.

	December 31, 2017 \$	December 31, 2016 \$
<b>Change in accrued benefit obligation</b>		
Benefit obligation, beginning of year	199,000	239,000
Interest cost [ <i>note 15</i> ]	7,400	8,900
Actuarial loss (gain) from change in financial assumption	6,800	(26,700)
Benefits paid	(6,600)	(22,200)
<b>Benefit obligation, end of year</b>	<b>206,600</b>	<b>199,000</b>

Post-employment and other retirement benefits plans are not funded.

The other post-retirement benefits amount recognized in other comprehensive income (loss), before taxation, consists of actuarial losses (gains) of \$6,800 [2016 – (\$26,700)]. The cumulative amount of actuarial losses recognized in the consolidated statement of comprehensive income is \$412,900 as at December 31, 2017 [2016 - \$406,100].

The assumptions used in the measurement of the Company's other post-retirement benefit cost were as follows:

	2017 %	2016 %
<b>Weighted-average assumptions</b>		
Discount rate for benefit obligation	3.40	3.80
Discount rate for net periodic benefit cost	3.80	3.90

As at December 31, 2017, no coverage is provided to retirees for healthcare and dental. The average duration of the other post-retirements obligation is 7.0 years as at December 31, 2017 and 2016.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017 and 2016

## 10. SHUTDOWN OF NON-CORE OPERATIONS OF PRINTER GATEWAY

On January 22, 2018, the Company closed its Printer Gateway operation to concentrate on its core diversification strategy. The Company provisioned, in the fourth quarter of 2017, a total of \$0.2 million of non-recurring expenses related to the shutdown of this operation. Additionally, an impairment loss totaling \$2.0 million was also recorded in connection with the write-down of the carrying amounts of goodwill, customer relations, intangibles and property, plant and equipment.

## 11. INTANGIBLE ASSETS

	Customer relationships \$	Non-compete agreements \$	Software \$	Total \$
<b>Cost</b>				
At December 31, 2015	64,249,784	755,000	1,238,996	66,243,780
Additions	—	—	770,446	770,446
Business combinations [note 5]	3,501,829	—	546,207	4,048,036
Translation adjustment	(24,205)	—	—	(24,205)
At December 31, 2016	67,727,408	755,000	2,555,649	71,038,057
Additions	—	—	373,835	373,835
Business combinations [note 5]	7,600,000	—	—	7,600,000
Adjustments for previous year's business combinations [note 5]	113,000	—	—	113,000
Translation adjustment	(167,474)	—	—	(167,474)
<b>At December 31, 2017</b>	<b>75,272,934</b>	<b>755,000</b>	<b>2,929,484</b>	<b>78,957,418</b>
<b>Accumulated amortization:</b>				
At December 31, 2015	59,006,776	736,332	—	59,743,108
Amortization	1,816,971	18,668	80,942	1,916,581
Translation adjustment	1,347	—	—	1,347
At December 31, 2016	60,825,094	755,000	80,942	61,661,036
Amortization	1,385,084	—	297,618	1,682,702
Impairment from shutdown of Printer Gateway [note 10]	362,700	—	478,177	840,877
Translation adjustment	(23,253)	—	—	(23,253)
<b>At December 31, 2017</b>	<b>62,549,625</b>	<b>755,000</b>	<b>856,737</b>	<b>64,161,362</b>
<b>Net book value:</b>				
At December 31, 2016	6,902,314	—	2,474,707	9,377,021
<b>At December 31, 2017</b>	<b>12,723,309</b>	<b>—</b>	<b>2,072,747</b>	<b>14,796,056</b>

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017 and 2016

## 12. GOODWILL

	\$
<b>Cost</b>	
At December 31, 2015	50,765,024
Business combinations [note 5]	2,278,275
Adjustments for previous year's business combinations [note 5]	120,557
Translation adjustment	(75,840)
At December 31, 2016	53,088,016
Business combinations [note 5]	6,002,328
Adjustments for previous business combinations [note 5]	(4,959)
Impairment from shutdown of Printer Gateway [note 10]	(999,020)
Translation adjustment	(317,002)
<b>At December 31, 2017</b>	<b>57,769,363</b>

The net carrying amount of goodwill as of December 31, 2017 was allocated to the following significant CGU groups:

	\$
<b>CGU groups</b>	
Envelopes <sup>1</sup>	51,595,728
Packaging	6,173,635
<b>Total</b>	<b>57,769,363</b>

<sup>1</sup> Includes the packaging and specialty products from legacy envelope businesses.

The packaging CGU was newly created in 2017 following two recent acquisitions; Stuart Packaging acquired on July 20, 2017 and Durabox Paper acquired on November 28, 2016.

**Impairment test of goodwill**

The Company conducted its annual impairment test as at December 31, 2017, in accordance with its policy described in note 2. The recoverable amount of each of the cash-generating unit exceeded its carrying values. As a result, no goodwill impairment was recorded.

**Valuation technique**

The Company uses the discounted cash flows ("DCF") method to determine the value in use of each of its cash-generating unit and has not made any changes to the valuation methodology used to assess goodwill impairment since the last annual impairment test.

**Significant assumptions**

The income approach is predicated upon the value of the future cash flows that a business will generate going forward. The DCF method, which was used as at December 31, 2017, involves projecting cash flows and converting them into a present value equivalent through discounting. The discounting process uses a rate of return that is commensurate with the risk associated with the business or asset and the time value of money. This approach requires assumptions about revenue growth or decline rates, operating margins, tax rate and discount rate.

*Growth or decline of revenue*

The assumptions used were based on the Company's internal budget. The Company projected revenue, operating margins and cash flows for a period of four years for each CGU. Specific assumptions are used for

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017 and 2016

## 12. GOODWILL [Cont'd]

each CGU. Forecasts for Envelopes CGU considered a lower demand in the Canadian and U.S. envelope markets and a perpetual long-term decline rate for the periods thereafter. Forecasts for Packaging CGU considered a perpetual long-term growth for this value-added market. In arriving at its forecasts, the Company considered past experience, recent acquisitions, economic trends as well as industry and market trends.

*Discount rate*

The Company assumed a pre-tax discount rate in order to calculate the present value of its projected cash flows. The discount rate represented a weighted average cost of capital ("WACC") for comparable companies operating in a similar industry. The WACC is an estimate of the overall required rate of return on an investment for both debt and equity owners and serves as the basis for developing an appropriate discount rate.

Determination of the WACC requires separate analysis of the cost of equity and debt, and considers a risk premium based on an assessment of risks related to the projected cash flows.

The key assumptions used in performing the impairment test were as follows:

	2017		2016
	Envelopes	Packaging	
Pre-tax discount rate	16.7%	16.8%	16.6%
Tax rate	26.1%	26.5%	26.1%
Perpetual (decline) growth rate	(3.0%)	2.0%	(3.0%)

*Sensitivity*

In the most recent impairment test performed for the Envelopes CGU, if the pre-tax discount rate had increased to 19.5% or the perpetual decline rate had increased to 8.0%, the recoverable amount of the cash generating unit would have then equaled the carrying amount as at December 31, 2017. If the pre-tax discount rate had increased to 18.3% or the perpetual growth rate had decreased to (0.2%), the recoverable amount of the Packaging cash generating unit would have then equaled the carrying amount as at December 31, 2017.

## 13. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

	December 31, 2017	December 31, 2016
	\$	\$
Trade payables	10,033,787	8,833,102
Accrued liabilities	9,961,197	9,048,705
	<b>19,994,984</b>	<b>17,881,807</b>

Trade payables are non-interest bearing and are normally settled on 20 to 60 day terms.



## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017 and 2016

## 14. PROVISIONS

In connection with the previous years' restructuring plans, the Company recognized a provision for severance, relocation and exit costs relating to certain employees and facilities. As at December 31, 2017, the amount of the remaining accrued restructuring provision was \$0.3 million [\$0.3 million as at December 31, 2016]. This amount is related to deferred severance for employees on long-term disability and is payable on demand.

The following is a summary of amounts accrued and paid relating to restructuring expenses.

	December 31, 2017 \$	December 31, 2016 \$
Balance, beginning of year	324,236	332,939
Cash payments	(33,372)	(8,703)
<b>Balance, end of year</b>	<b>290,864</b>	<b>324,236</b>

## 15. SECURED CREDIT FACILITY

As at December 31, 2017, the Company had a five-year committed \$60 million senior secured revolving facility agreement maturing on October 6, 2020. No principal repayments are required prior to maturity. This facility bears interest at a floating rate based on the Canadian prime rate, plus an applicable margin that ranges between 0% and 0.25% or bankers' acceptance rates, plus an applicable margin that ranges between 1.50% and 1.75%.

The secured credit facility is used for working capital, capital expenditure and other general corporate purpose. It is collateralized by hypothec and security interests covering all assets of the Company and its subsidiaries and is subject to certain covenants, which the Company is required, among other conditions, to meet. The Company was in compliance with these covenants during 2017.

Amounts owed under secured credit facility are as follows:

	December 31, 2017 \$	December 31, 2016 \$
Revolving credit facility	43,019,609	27,151,265
Less: deferred financing costs, net	(188,723)	(257,351)
<b>Long-term portion of secured credit facility</b>	<b>42,830,886</b>	<b>26,893,914</b>

The Company had outstanding letters of credit for a total of \$10,000 as at December 31, 2017, [2016 – \$60,000].

The effective interest rate on the secured credit facility was 3.09% as at December 31, 2017 [2.43% as at December 31, 2016].

Financing charges are as follows:

	2017 \$	2016 \$
Interest on secured credit facility	1,100,922	739,618
Interest (income) expense on defined benefit plan obligation [note 9]	(94,800)	29,400
Interest on post-retirement benefits [note 9]	7,400	8,900
Other interest (income) expense	(3,959)	5,483
Amortization of deferred financing costs	68,628	68,628
	<b>1,078,191</b>	<b>852,029</b>

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017 and 2016

## 16. INCOME TAXES

## Income tax expense

The major components of income tax expense recognized in the consolidated statement of earnings were as follows:

	2017	2016
	\$	\$
<b>Current income tax:</b>		
Current income tax expense	5,285,410	5,949,297
<b>Deferred income tax:</b>		
Reversal of temporary differences	(629,423)	(474,488)
<b>Income tax expense</b>	<b>4,655,987</b>	<b>5,474,809</b>

Income taxes on items recognized in other comprehensive loss were as follows:

	2017	2016
	\$	\$
Deferred income tax related to items imputed directly to equity during the year:		
Deferred tax expense on recognized actuarial gain on defined benefit pension plans	244,822	847,190
Deferred tax (benefit) expense on recognized actuarial (loss) gain on other post-retirement benefit	(1,775)	6,962
<b>Income tax expense charged to other comprehensive income</b>	<b>243,047</b>	<b>854,152</b>

The income tax expense differs from the expense that would be obtained by applying the combined Canadian income tax (federal and provincial) as follows:

	2017	2016
	\$	\$
Earnings before income taxes	17,046,815	20,067,553
Income tax expense at combined federal and provincial statutory rate of 26.1% [2016 – 26.1%]	4,442,908	5,232,113
Effect of change in enacted tax rates	(588,716)	97
Income tax rate differential for subsidiaries	40,007	11,405
Non-deductible expenses and other	761,788	231,194
<b>Income tax expense</b>	<b>4,655,987</b>	<b>5,474,809</b>

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017 and 2016

## 16. INCOME TAXES [Cont'd]

## Deferred income tax

Deferred income tax relates to the following:

	Consolidated statement of financial position		Consolidated statement of earnings	
	December 31, 2017 \$	December 31, 2016 \$	December 31, 2017 \$	December 31, 2016 \$
<b>Deferred tax assets</b>				
Goodwill	1,025,638	1,253,251	332,358	152,123
Other	219,036	271,796	(64,295)	105,160
Non-capital losses	189,845	186,437	(13,806)	(6,686)
	<b>1,434,519</b>	<b>1,711,484</b>	<b>254,257</b>	<b>250,597</b>
<b>Deferred tax liabilities</b>				
Accrued pension benefit liability	1,012,213	601,048	(166,344)	167,763
Property, plant and equipment	3,693,997	3,509,167	726,720	440,036
Intangible assets	2,324,635	574,222	325,777	122,039
Other	211,860	213,764	(2,473)	(4,753)
	<b>7,242,705</b>	<b>4,898,201</b>	<b>883,680</b>	<b>725,085</b>
<b>Deferred tax recovery</b>			<b>(629,423)</b>	<b>(474,488)</b>
<b>Net deferred income tax liabilities</b>	<b>(5,808,186)</b>	<b>(3,186,717)</b>		

## Reconciliation of net deferred tax liabilities

	2017 \$	2016 \$
Balance – beginning of the year	(3,186,717)	(2,419,291)
Tax recovery during the year recognized in the consolidated statement of earnings	629,423	474,488
Tax benefit recognized in other comprehensive loss	(243,047)	(854,152)
Net deferred tax from business combinations [note 5]	(2,960,639)	(425,406)
Net deferred tax from adjustments for previous year's business combinations [note 5]	(155,571)	—
Translation adjustment on net deferred tax	108,365	37,644
<b>Balance – end of year</b>	<b>(5,808,186)</b>	<b>(3,186,717)</b>

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017 and 2016

## 17. SHARE CAPITAL

An unlimited number of common shares are issuable. Each common share represents a shareholder's proportionate undivided interest in the Company. Each common share confers to its holder the right to one vote at any meeting of shareholders and to participate equally and rateably in any dividends of the Company, if any, and, in the event of any required distribution of all of the property of the Company, in the net assets of the Company remaining after satisfaction of all liabilities.

The change in share capital was as follows:

	Number of common shares	Share capital \$
Balance, as of December 31, 2015	28,750,967	9,813,365
Purchase of share capital for cancellation	(139,616)	(47,654)
Balance, as of December 31, 2016	28,611,351	9,765,711
Purchase of share capital for cancellation	(205,882)	(70,272)
<b>Balance, as of December 31, 2017</b>	<b>28,405,469</b>	<b>9,695,439</b>

During the year ended December 31, 2017, the Company repurchased 205,882 (2016 – 139,616) common shares for cancellation through a normal course issuer bid for a consideration of \$938,759 (2016 - \$668,939). The excess of the purchase price over the carrying value in the amount of \$868,487 (2016- \$621,285) was recorded as a reduction of contributed surplus.

On August 1, 2017, Supremex received approval from the TSX to renew the Company's NCIB program to repurchase up to 500,000 common shares for cancellation during a period of 12 months ending August 2, 2018.

**Deferred Share Unit Plan (DSU)**

On December 15, 2015 the Company adopted a Deferred Share Unit ("DSU") Plan for its members of the Board of Directors. The DSU Plan enables its participants to receive compensation in cash at the termination date, as a member of the Board of Directors, equal to the market price of the Corporation's common share for each DSU.

Each participant in the DSU Plan may elect, each fiscal year, to receive up to 100% of their director's annual retainer fees in DSUs. Such DSUs are expensed on an earned basis and their costs are determined using a valuation model and all issued and outstanding DSUs are measured at each reporting period.

The financial liability resulting from the plan of \$309,251 [2016 - \$113,800] is presented under "*Accounts payable and accrued liabilities*".

The compensation expense for the DSUs during the twelve-month period ended December 31, 2017 amounted to \$125,451 [2016 - \$113,800] and is recognized under selling, general and administrative expenses.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017 and 2016

## 18. OPERATING, SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

	2017	2016
	\$	\$
Wages and salaries	45,662,043	39,702,805
Social security costs	6,840,664	6,235,175
Pension plans expense [see note 9]	1,427,300	1,619,700
Employee benefits expenses	53,930,007	47,557,680
Raw materials and other purchases	73,748,958	63,170,718
Other	25,566,592	22,459,451
	<b>153,245,557</b>	<b>133,187,849</b>

## 19. DIVIDENDS

Dividends declared from January 1, 2017 to December 31, 2017 were as follows:

Declaration date	Record date	Payment date	Per share	Dividend
			\$	\$
February 15, 2017	March 31, 2017	April 14, 2017	0.06	1,714,995
May 4, 2017	June 30, 2017	July 14, 2017	0.06	1,708,957
July 31, 2017	September 30, 2017	October 13, 2017	0.06	1,704,328
November 9, 2017	December 31, 2017	January 16, 2018	0.065	1,846,355
<b>Total</b>				<b>6,974,635</b>

Dividends declared from January 1, 2016 to December 31, 2016 were as follows:

Declaration date	Record date	Payment date	Per share	Dividend
			\$	\$
February 17, 2016	March 31, 2016	April 14, 2016	0.055	1,575,462
May 5, 2016	June 30, 2016	July 14, 2016	0.055	1,575,462
July 28, 2016	September 30, 2016	October 14, 2016	0.055	1,574,801
November 3, 2016	December 30, 2016	January 13, 2017	0.06	1,716,681
<b>Total</b>				<b>6,442,406</b>

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017 and 2016

## 20. COMMITMENTS, CONTINGENCIES AND GUARANTEES

**Operating lease commitments**

The Company has entered into operating leases mainly for buildings.

Future minimum rentals payable under non-cancellable operating leases are as follows:

	December 31, 2017 \$
Within one year	3,603,270
After one year but not more than five years	9,947,140
More than five years	3,032,572
	<u>16,582,982</u>

**Legal claim**

In the normal course of its operations, the Company is exposed to various claims, disputes and legal proceedings. These disputes may involve numerous uncertainties and the outcome of individual cases is unpredictable. According to management, these disputes should not have a significant negative impact on the Company's financial position.

**Guarantees**

In the normal course of business, the Company has entered into agreements that contain features which meet the definition of a guarantee. These agreements may require the Company to compensate counterparties for costs and losses incurred as a result of various events including breaches of representations and warranties, loss of or damages to property, claims that may arise while providing services, and environmental liabilities. These agreements provide for indemnification and guarantees to counterparties as follows:

**Operating leases**

The Company has general indemnity clauses in many of its real estate leases whereby it, as lessee, indemnifies the lessor against liabilities related to the use of leased property. These leases mature at various dates through July 2027 with renewal option for some leases. The nature of these indemnification agreements prevents the Company from estimating the total potential amount it would have to pay to lessors, since these events have not occurred yet. Historically, the Company has not made any significant payments under such agreements, has insurance coverage for certain of the obligations undertaken and, as at December 31, 2017, has not recorded any liability associated with these indemnifications.

## 21. RELATED PARTY TRANSACTIONS

Compensation of key management personnel of Supremex is as follows:

	2017 \$	2016 \$
Short-term employee benefits	1,560,223	1,704,627
Post-employment benefits	74,363	74,575
	<u>1,634,586</u>	<u>1,779,202</u>

The amounts disclosed in the table are the amounts recognized as an expense related to key management personnel during the reporting period.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017 and 2016

## 22. FINANCIAL INSTRUMENTS

## Financial assets and liabilities

Financial assets and liabilities in the statements of financial position were as follows:

December 31, 2017	Loans and receivables \$	Assets at fair value through earnings \$	Other financial liabilities \$	Total \$
Cash	—	706,190	—	706,190
Accounts receivable	25,977,010	—	—	25,977,010
Accounts payable and accrued liabilities excluding sales tax payable	—	—	(18,773,105)	(18,773,105)
Dividend payable	—	—	(1,846,355)	(1,846,355)
Provisions	—	—	(290,864)	(290,864)
Secured credit facility	—	—	(43,019,609)	(43,019,609)
Other long term liability	—	—	(427,000)	(427,000)
<b>Total</b>	<b>25,977,010</b>	<b>706,190</b>	<b>(64,356,933)</b>	<b>(37,673,733)</b>

December 31, 2016	Loans and receivables \$	Assets at fair value through earnings \$	Other financial liabilities \$	Total \$
Cash	—	1,964,947	—	1,964,947
Accounts receivable	21,237,321	—	—	21,237,321
Accounts payable and accrued liabilities excluding sales tax payable	—	—	(16,591,199)	(16,591,199)
Dividend payable	—	—	(1,716,681)	(1,716,681)
Provisions	—	—	(324,236)	(324,236)
Secured credit facilities	—	—	(27,151,265)	(27,151,265)
<b>Total</b>	<b>21,237,321</b>	<b>1,964,947</b>	<b>(45,783,381)</b>	<b>(22,581,113)</b>

## Fair values

The carrying amount of secured credit facilities approximates its fair value given its nature and floating interest rate.

For the secured credit facilities, the Company categorized the fair value measurement in Level 2, as it is primarily derived from observable market inputs, that is, interest rates.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017 and 2016

### 22. FINANCIAL INSTRUMENTS [Cont'd]

#### **Management of risks arising from financial instruments**

In the normal course of business, the Company is exposed to a range of financial risks, which include credit risk, liquidity risk and market risk. To limit the effects of these risks on revenues, expenses and cash flows, the Company can avail itself of various derivative financial instruments. The Company's management is responsible for determining the acceptable level of risk and uses derivative financial instruments only to manage existing or anticipated risks, commitments or obligations based on past experience.

#### **Credit risk**

Credit risk arises from cash and accounts receivable. In order to minimize the credit exposure, the Company's cash is placed with Canadian Schedule 1 banks and their U.S subsidiaries.

Credit risk stems primarily from the potential inability of clients to discharge their obligations. Accounts receivable credit risk is mitigated through established monitoring activities, lack of customer concentration and the Company's diversified customer base. Historically, the Company has never made any significant write-off of accounts receivable. As at December 31, 2017 and 2016, total trade accounts receivable over 90 days past due amounted to less than 5% [see note 6]. The Company does not hold collateral as security.

#### **Liquidity risk**

The Company is exposed to the risk of being unable to honour its financial commitments within the deadlines set out under the terms of such commitments and at a reasonable price. The Company manages liquidity risk by maintaining adequate cash balances and by appropriately using the Company's secured credit facilities. The Company continuously reviews both actual and forecasted cash flows to ensure that it has adequate credit facility capacity. The Company continuously reviews its exposure to interest rate fluctuations and as at February 20, 2018, the Company assessed that the cost of entering into an interest swap outweighed its benefits.



## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017 and 2016

## 22. FINANCIAL INSTRUMENTS [Cont'd]

The table below sets forth the contractual undiscounted cash flows of financial liabilities by maturity based on the remaining period from December 31, to the contractual maturity date.

December 31, 2017	Less than 3 months \$	1 to 5 years \$	Total \$
Accounts payable and accrued liabilities excluding sales tax payable	18,773,105	—	18,773,105
Dividend payable	1,846,355	—	1,846,355
Provisions	290,864	—	290,864
Secured credit facilities	—	43,019,609	43,019,609
Other long term liabilities	—	427,000	427,000
	<b>20,910,324</b>	<b>43,466,609</b>	<b>64,356,933</b>

  

December 31, 2016	Less than 3 months \$	1 to 5 years \$	Total \$
Accounts payable and accrued liabilities excluding sales tax payable	16,591,199	—	16,591,199
Dividend payable	1,716,681	—	1,716,681
Provisions	324,236	—	324,236
Secured credit facilities	—	27,151,265	27,151,265
	<b>18,632,116</b>	<b>27,151,265</b>	<b>45,783,381</b>

**Market risk**

Market risk is the risk that changes in market prices due to foreign exchange rates and interest rates will affect the value of the Company's financial instruments. The objective of market risk management is to mitigate and control exposures within acceptable parameters while optimizing the return on risk.

*Interest rate risk*

The Company is exposed to interest rate fluctuations mainly on its secured credit facility. The Company manages interest rate exposure by maintaining a balanced portfolio of fixed and variable loans and borrowings depending on the level of the Company's exposure. Furthermore, interest rate fluctuations could have an impact on interest expense on its credit facility and on income the Company derives from cash. The Company invests, when applicable, its cash in highly liquid investment instruments to safeguard its capital while generating a reasonable return.

On December 31, 2017, a 25 basis-point rise or fall in interest rates, assuming all other variables remained unchanged, would have resulted, respectively, in a \$193,685 increase or decrease in the Company's net earnings for the year ended December 31, 2017 [2016 - \$44,997].

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2017 and 2016

## 22. FINANCIAL INSTRUMENTS [Cont'd]

*Foreign exchange risk*

The Company is exposed to fluctuations in U.S. exchange rates because a portion of its activities are conducted in the United States and a portion of its purchases and capital expenditures are made in U.S. dollars. The Company continuously reviews its exposure to fluctuations in the U.S. exchange rate and has decided at this time not to enter into derivatives as the net exposure is not significant.

As at December 31, 2017, net financial assets of the Company in Canadian dollars, denominated in U.S. dollars, totalled \$4,793,913 [2016 - \$2,537,766].

On December 31, 2017, a 5% rise or fall in the Canadian dollar against the U.S. dollar on financial instruments held at that date, assuming all other variables remained unchanged, would have resulted, respectively, in a \$239,696 increase or decrease in the Company's net earnings for the year then ended [2016 - \$126,888], whereas other comprehensive income (loss) would have increased or decreased by \$304,434 [2016 - \$332,543].

## 23. CAPITAL MANAGEMENT

The Company's capital consists of equity and secured credit facilities. The Company maintains a capital level that enables it to meet several objectives:

- Assure the longevity of its capital to support continued operations;
- Satisfy certain financial covenants under the secured credit facilities;
- Preserve its financial flexibility to benefit from potential opportunities as they arise; and
- Sustain growth in share value.

The Company continually assesses the adequacy of its capital structure and capacity and makes adjustments in view of the Company's strategy, economic conditions and the risk characteristics of the business to achieve the above objectives. The Company also monitors its capital to ensure full adherence to the "secured credit facility/EBITDA" and "fixed charge coverage" ratios as defined in the credit facilities agreement.

The Company's capital structure is composed of equity and secured credit facilities less cash. The capital structure is as follows:

	December 31, 2017	December 31, 2016
	\$	\$
Secured credit facility	42,830,886	26,893,914
Cash	(706,190)	(1,964,947)
Net debt	42,124,696	24,928,967
Equity	86,519,133	82,337,060

The Company is not subject to any externally imposed capital requirements other than certain restrictions under the terms of its secured credit facilities.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**December 31, 2017 and 2016**

**24. SEGMENTED INFORMATION**

The Company currently operates in one reporting segment: the manufacturing and sale of envelopes, packaging and specialty products. The Company's non-current assets amounted to \$99,656,332 in Canada and \$11,115,201 in the United States as at December 31, 2017 [\$77,092,104 and \$12,776,959, respectively, as at December 31, 2016]. The Company's revenue amounted to \$124,771,855 in Canada and \$54,300,904 in the United States for the year ended December 31, 2017 based on customer location [2016 - \$119,132,897 in Canada and \$41,437,456 in the United States]. The Company's revenue amounted to \$144,472,369 from envelopes and \$34,600,390 from packaging and specialty products based on product classification [2016 - \$148,385,881 from envelopes and \$12,184,472 from packaging and related products].

**25. SUBSEQUENT EVENT**

On February 20, 2018, the Board of Directors declared a quarterly dividend of \$0.065 per common share, payable on April 13, 2018 to shareholders of record at the close of business on March 29, 2018.