FOCUS

BCRC

British Columbia Railway Company Annual Report 2002

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FOCUS – OUR VISION, MISSION AND VALUES

On Our Vision

Our vision is to act as a valuable strategic advantage for our customers in moving their goods to market.

On Our Mission

Our mission is to build a safe, reliable, cost-effective, self-sustaining, freight railway Company.

On Our Values

- A safe and healthy work environment
- A customer-focused, market-driven approach to business
- A creative, resourceful and entrepreneurial spirit
- Continuous improvement and innovation
- Operate profitably and achieve business targets
- Treat everyone in an honest, fair and respectful manner
- Reward and recognize achievements of individuals and teams

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CORPORATE PROFILE

Corporate Profile

The British Columbia Railway Company (BCRC) is a commercial Crown corporation with all of its business activities operating in competition with the private sector. It is mandated to operate without any government subsidies. For the 2002 year it was comprised of three principal business units:

- BC Rail, an industrial freight railway;
- BCR Marine, which operates Canadian Stevedoring, Casco Terminals and Vancouver Wharves; and
- BCR Properties, which manages the railway's real estate portfolio.

BC Rail

BC Rail is Canada's third largest railway as measured by revenue and continuous track. It operates exclusively within British Columbia and has inter-line connections to all rail-served points within North America. The BC Rail network consists of 2,315 route-kilometres and 740 kilometres of industrial, yard and track sidings throughout the province.

The rail network consists of a 1,577 kilometre mainline from North Vancouver to Fort Nelson, plus branchlines to Mackenzie, Dawson Creek, Tumbler Ridge, Fort St. James and Takla.

In addition, BC Rail owns the 37 kilometre Port Subdivision line, connecting three major railways (Burlington Northern Santa Fe – BNSF; Canadian National Railway – CN; and Canadian

BRITISH COLUMBIA RAILWAY COMPANY ROUTE MAP

Pacific Railway – CP) to the important port terminals at Roberts Bank. BC Rail does not operate any of its own trains over the Port Subdivision, but maintains the track and manages all train operations over the subdivision and into port terminals for the user railways (BNSF, CN and CP) on a shared cost basis.

BC Rail is driven by a commitment to customer service and ongoing improvement to the business. Each year, advances in technology and productivity enhance existing methods of service in all areas of the business.

BC Rail plays an important role in the export economy of British Columbia as almost all of the railway's customers sell their commodities outside the province. More than 80 per cent of BC Rail's total revenue is generated by the transport of commodities such as forest products, energy and agricultural products. Car hire revenue – money earned from BC Rail cars when they travel off-line – as well as income from the operations of Roberts Bank and switching charges account for the remaining revenue.

BCR Marine

BCR Marine consists of Canadian Stevedoring, Casco Terminals and Vancouver Wharves. Canadian Stevedoring is the largest supplier of stevedoring services on Canada's west coast, serving 22 ports throughout the province. It also operates the Fairview Terminal in Prince Rupert. Casco Terminals is located on the south shore of Vancouver Harbour and handles containers, pulp, packaged lumber and general cargo. Vancouver Wharves, based in North Vancouver, handles mineral concentrates, pulp, canola oil, sulphur, and agriproducts.

On March 28, 2002 the Company announced its intent to sell BCR Marine. The Company operated Canadian Stevedoring and Casco Terminals until the businesses were sold on February 25, 2003. The Company continues to operate, and pursue the sale of, Vancouver Wharves.

BCR Properties

BCR Properties manages all of the Company's real estate assets, the majority of which are required for BC Rail operations. It also owns lands in the railway's important industrial parks, most of which are leased to major, long-term tenants and railway customers. In addition, BCR Properties owns and manages a smaller number of income-generating properties (lands and buildings), which it manages for income.

"The Company realized a 103 per cent increase in operating income from continuing operations in 2002"

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MESSAGE FROM THE CHAIRMAN OF THE BOARD AND THE CHIEF EXECUTIVE OFFICER

2002 was a very important year for the British Columbia Railway Company. Over the past twelve months the Board and management have worked together to make a number of important decisions that have refined our strategic business model and focused the company on its core strength – operating an industrial freight railway. As a result, the Company has exited a number of non-core, unprofitable businesses, which are referred to in the Annual Report as discontinued operations. Our strategic focus for our continuing operations is to manage the Railway's real estate portfolio and to be a safe, self-sufficient industrial freight railway serving as a key transportation link for many of British Columbia's export-oriented companies.

This year was a very successful year for our continuing operations. Our commitment to achieving cost reductions and maximizing operating revenue has had a significant impact on our financial results for 2002. Revenues from continuing operations improved by $11 million to $313 million in 2002, and costs were significantly lower – $25 million less in 2002 than in 2001, which is a nine per cent reduction in overall operating costs on continuing operations.

The benefits of exiting money losing or non-rail operations that would have required significant capital investment are clear in our 2002 financial results. The Company realized a 103 per cent increase in operating income from continuing operations in 2002 over 2001, or $71 million dollars as compared to $35 million in the previous year.

BC Rail, like other industrial railways, uses the operating ratio as a measure of efficiency and cost-effectiveness.

MESSAGE FROM THE CHAIRMAN OF THE BOARD AND THE CHIEF EXECUTIVE OFFICER

"The Company announced its intent to sell BCR Marine on March 28, 2002"

The combination of an increase in revenue and a reduction in operating expenses resulted in an operating ratio of 78 per cent in 2002, an improvement of 14 points year over year.

The Company also realized significant improvements in a number of operating areas including safety. The proactive approach by our employees to derailment mitigation and occupational health and safety initiatives translates into one of the safest years on record. This had a significant impact on reducing operating costs.

Once the strategic decision was made to discontinue several lines of business – including BCR Marine, Passenger Rail Services, Finlay Navigation, and Intermodal ToFC (Trailer-on-Flatcar) services – for accounting purposes the Company was required to write down the value of many of those assets, which resulted in the Company reporting a net loss of $84 million for 2002.

The Company discontinued Intermodal ToFC services in February 2002. ToFC was uncompetitive and was losing almost $2 million annually. Furthermore, ToFC was in need of $14 million in capital upgrade, money that BCRC could simply not afford.

The Company announced its intent to sell BCR Marine on March 28, 2002 and indicated that it was looking for a buyer who would take a long-term view of the value of these assets. The sale of Casco Terminals and Canadian Stevedoring to P & O Ports, a subsidiary of Peninsular and Oriental Steam Navigation Company, was completed on February 25, 2003.

P & O Ports is one of the world's largest container terminal operators and developers and is exactly the match the Board of Directors was looking for to unlock the full potential of our marine assets. P & O Ports has the capital resources to allow Casco Terminals and Canadian Stevedoring to fulfill that mandate.

We are confident that the employees at Casco Terminals and Canadian Stevedoring will have an exciting future as part of P & O Ports, and we thank them for their contribution to the success of these companies.

The Company is continuing the process to sell Vancouver Wharves and will continue to operate the business until the sale is complete.

The Company also discontinued the Whistler Northwind luxury tour train and the Pacific Starlight Dinner Train at the end of their 2002 seasons, in September and October respectively. Also in October, the Cariboo Prospector service concluded, which completed BCRC's exit from passenger service. That business unit lost almost $6 million from operations in 2002. The Company recognized a gain on the sale of some of the passenger services equipment.

Having exited unprofitable, tourism focused passenger services in 2002, the communities between D'Arcy and Lillooet, which are considered rail-dependent, still required rail service. BC Rail worked with the Seton Lake Indian Band to develop a solution for the rail-dependent communities between D'Arcy and Lillooet. We are very proud of the unique agreement reached with the Band for the

MESSAGE FROM THE CHAIRMAN OF THE BOARD AND THE CHIEF EXECUTIVE OFFICER

operation of a rail shuttle service that runs along Anderson and Seton Lakes. The Rail Shuttle Management Agreement, which was signed in July 2002, was reached quickly and equitably, and is the first co-management agreement between BC Rail and one of its First Nations neighbours.

A final element in our strategy to focus on our core industrial freight operations will be the sale of Finlay Navigation, which operates freight barge operations on Williston and Babine Lakes. We expect the transaction to be completed in 2003.

The Company still faces a number of competitive challenges and we must remain focused on our goals. The challenges ahead include:

- Closing of the Bullmoose mine which signals the end of the north-eastern coal traffic;
- High dependence on the forest products industry which, after the end of coal traffic, will represent 78 per cent of our traffic;
- No expectation of any major new freight traffic sources and no new significant shippers coming to market in BC along BC Rail's lines;
- Difficulty growing market share in an increasingly competitive market; and
- Continued pressure on revenue yields from other rail carriers and truckers.

Debt continues to be a major challenge for BC Rail. The Company has reduced its debt load to $592 million, as of December 31, 2002 by aggressively executing our new focused business strategy. However the Company will still be burdened with debt of $502 million after the completion of the sale of Casco Terminals and Canadian Stevedoring.

The successes we have achieved this year have been due in part to the results of labour and management working together on a number of initiatives. BC Rail's collective agreements with the Council of Trade Unions expired on December 31, 2002. We hope that, as a result of our efforts to improve relations with our unionized workforce, the negotiations will end in mutually satisfactory results.

As we look back, it has been a tremendously challenging and exciting year for all our employees and we have achieved a great deal. Our employees have worked hard to reduce operating costs as we continue to work towards an operating ratio of less than 75 per cent, and they have also made significant improvements in overall safety this year. Thank you.

Thank you to our customers and our communities who have worked with us to find innovative and mutually agreeable solutions as we work to achieve our goals.

BOARD OF DIRECTORS AND OFFICERS

BRITISH COLUMBIA RAILWAY COMPANY

DIRECTORS

John R. McLernon, Chair (2)
Anne M. Stewart (2)
Bev A. Briscoe (1)
Brian G. Kenning (1)
Len S. Marchand (2)
Patrick W. Rorison (3)
Jim F. Shepard (3)
Jim R. Yeates (1)
Gerry Offet (4)

OFFICERS

Robert L. Phillips,
Group President and
Chief Executive Officer

Robert P. Pirooz,
Group Vice President and
General Counsel / Corporate Secretary

Peter M. Ballachey,
Vice President Finance and
Chief Financial Officer

(1) Member of Audit, Finance and Risk Management Committee
(2) Member of Human Resources, Governance and Nominating Committee
(3) Member of Environment and Safety Committee
(4) Appointed February 2003

It has also been a challenging year for the Board of Directors who had to deal with a number of difficult decisions along the way. It has also been rewarding, as we start to see the benefits of the changes we initiated. We also want to welcome Mr. Gerry Offet, who joined the Board in February 2003. Thank you to our Board for your service and dedication.

Subsequent to our year-end, the government reiterated that continued change is required to further improve our province's rail transportation system. A new initiative is being launched by the province to seek input on ways to make these much-needed improvements a reality, while still maintaining public ownership of BC Rail's land and rail bed assets

As the government pursues its initiative we will continue to work with our customers, employees and community stakeholders in the year ahead to maintain our focus on building a safe, reliable, cost-effective, self-sustaining, freight railway company.

John McLernon
Chairman of the Board
British Columbia Railway Company

Bob Phillips
Chief Executive Officer
British Columbia Railway Company

"The Company went through one of the biggest restructuring programs in its history."

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THE YEAR IN REVIEW

FOCUS ON OUR CORE BUSINESS

2002 was about focusing on what the Company does best – operating a safe, reliable, cost-effective and efficient industrial freight railway company. To achieve this, the Company went through one of the biggest restructuring programs in its history. The need for change was made more pressing by the reality that the Company began 2002 facing a debt load of $646 million. This year, while major business process improvements were made to the core freight rail business, non-core ventures were sold or discontinued.

Our core values have been the drivers of our success this year and the Company and its employees have every reason to be proud of our achievements in 2002.

As a result of our focus, we have:

- Improved income from continuing operations, before special charges, by $51million;
- Increased earnings before interest, taxes, depreciation and amortization (EBITDA) by almost $29 million;
- Reduced operating expenses by $25 million; and
- Reduced short and long-term debt by over $54 million.

THE YEAR IN REVIEW: FOCUS ON OUR CORE BUSINESS

The year also demonstrated our core value to be a customer-focused, market-driven business, for all customers, but in particular with our forest products customers. BC Rail had originally forecast a decline in lumber volumes in 2002 as a result of the US-imposed softwood lumber tariffs. However, lumber revenues were 17 per cent higher than budgeted and lumber volumes remained ahead of our forecast throughout the year as Canadian producers and specifically BC Rail's customers refocused their lumber sales strategies to maximize production in an effort to reduce unit-operating costs.

The readjustment of our customers' lumber sales strategies meant an unexpected increase in demand for rail cars. The Company worked throughout the spring to bring on additional rolling stock and, over the course of 2002, leased an additional 540 centre-beam lumber cars to meet demand. At the same time, the overall fleet was reduced by 180 cars as the Railway continued to size its fleet. Rolling stock for high yield revenue requirements remains a priority.

Improving customer service is of paramount importance and the Company continually works with our customers to improve our services and find more effective and efficient ways to move goods to market. Transit compliance improved to 95 per cent in 2002, and the customer service centre has been successful in fulfilling committed requirements on a weekly basis since the implementation of the new lumber car allocation policy in March 2002.

Continuous improvement and innovation are other core values of this Company and innovation was a key success factor in reducing costs on a number of other fronts in 2002. One of the strategies included the continuing implementation of Beltpack technology. This system allows switching crews to remotely control a yard locomotive, thereby reducing the size of the crew. Implementation began in Prince George in 2001 and, since then, 40 employees have been certified as Beltpack operators and approximately 950-yard shifts have operated with this technology. Beltpack has not only improved productivity, but has resulted in a dramatic reduction in switching incidents and personal injuries, exceeding management's expectations. BC Rail will continue to implement Beltpack technology across the Company.

Another continuous improvement strategy has been the fuel conservation recovery program. Launched in 2000, it continues to pay dividends in terms of reducing fuel use and reducing environmental impacts. Fuel efficiencies in 2002 lowered costs by 18 per cent and realized a four per cent improvement in consumption of locomotive diesel fuel. The good weather conditions experienced in 2002 also played a role in reducing fuel expenses this year.

This year the Company also continued the consolidation of terminal operations in North Vancouver, Squamish and Prince George, as well as several other smaller locations. In Prince George, the Company moved from nine buildings to three. The consolidation was not without its challenges, but both customers and employees have noticed a number of improvements.

THE YEAR IN REVIEW: FOCUS ON OUR CORE BUSINESS

“This year the Company achieved an improvement in personal safety with a 25 per cent improvement over 2001”

Safety

One of our core values is to be the safest railway in Canada. The Railway work environment presents considerable challenges to safety. Ensuring a safe and healthy work environment requires the commitment of everyone in the Company and improvements only come when every employee makes workplace safety their personal responsibility. The work of BC Rail's Occupational Health and Safety Committee has been critically important in the significant reduction in personal injuries, derailments and yard incidents.

The Derailment Task Force and the Occupational Health and Safety Committee, both joint union-management efforts to identify unsafe practices and conditions, have implemented technology changes and training programs, which have had a significant impact over the last two years. This year the Company achieved an improvement in personal safety with a 25 per cent improvement over 2001 in lost time due to injuries. There was also an improvement of 22 per cent in corresponding days lost.

Our proactive approach to derailment mitigation produced dramatic improvements, with only two derailments in 2002 versus six in 2001. The Railway's mishap costs were primarily due to rock and landslides caused by extreme weather conditions.

“The Rail Shuttle Management Agreement ...is the first co-management agreement between BCRC and one of its First Nations neighbours.”

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ABORIGINAL AFFAIRS

BC Rail continued to build on successful partnerships with neighbouring First Nations communities in 2002. The Company’s goal is to maintain open, two-way information exchanges with the 25 First Nations who live along BC Rail’s right of way, recognizing that relationships take time to develop and are built on trust and understanding.

The Rail Shuttle Management Agreement, which was signed in July 2002, is the first co-management agreement between BCRC and one of its First Nations neighbours. The agreement reached with the Seton Lake Indian Band provides for the operation of a rail shuttle service between D’Arcy and Lillooet. Under this agreement, BC Rail provides the equipment and personnel for the service and the Seton Lake Indian Band is responsible for the booking system and day-to-day management.

The Company continues to break new ground in the implementation of BC Rail’s integrated vegetation management plan with First Nations.

Last year there were six successful First Nations candidates from BC Rail’s vegetation management training program. In total, nine First Nations members have successfully completed this course and are now certified pesticide applicators (industrial vegetation).

Last year the Company’s Aboriginal Affairs group met with 20 of 25 First Nations whose traditional territories border on BC Rail’s right of way. One of the highlights and outcomes in 2002 was the resolution of right of way access and land overlap issues with Xaxli’p First Nation. The agreement settles a long-standing dispute and allows BC Rail access to Xaxli’p lands in order to stabilize slide areas.

In addition, the Company signed two new protocol agreements in 2002, with the Tl’azt’en Nation in August and with the Gitxsan Hereditary Chiefs of the Sustat in September.

BC RAIL'S REGIONAL RAILWAY STATUS

“BC Rail faces significant difficulties increasing its market share”

In spite of the progress made in 2002 to restructure the business and focus on becoming a self-sustaining industrial freight railway company, BC Rail still faces a number of competitive challenges, not the least of which is that it is a regional railway with the cost structure of a Class 1 or national railway. BC Rail does not have the economies of scale or opportunities to generate significant new business. BC Rail is highly dependent on the forest products industry, which in 2003 will comprise approximately 78 per cent of the Company's traffic mix. The Railway competes directly with two national railways, numerous short-line carriers and trucking firms for this business. As demands on the forest products industry continue, BC Rail's forest products customers will be looking at ways to achieve cost savings and put pressure on their suppliers, which will make it difficult to increase revenue yields.

As a regional railway, BC Rail faces significant difficulties increasing its market share. With no new major shippers in BC, the Company must compete with other transportation operators for a greater piece of existing shipping business.

Despite these challenges, the Company is committed to and will remain focused on becoming a self-sustaining, industrial freight railway, delivering outstanding customer service and ensuring a safe and healthy working environment.

SERVICE PLAN

"Today, BCRC is fundamentally an industrial freight railway company, conducting business through its principal operating subsidiary, BC Rail"

The British Columbia Railway Company is a commercial Crown corporation operating in a deregulated environment in full competition with the private sector without government subsidies. As a commercial business competing in the private sector, the risks of disclosing commercially sensitive information or financial data are significant. Therefore, the Company's Annual Report only publishes consolidated historical results. Releasing other types of information to the public could seriously undermine the Company's competitive position.

When the 2002–2004 Service Plan was tabled in the legislature in February 2002, the Board and management had made a number of significant decisions to refine its strategic business model and focus on its core strength – operating an industrial freight railway. The Company believes that the decisions made in 2002 will ensure the long-term sustainability of the industrial freight railway.

Today, BCRC is fundamentally an industrial freight railway company, conducting business through its principal operating subsidiary, BC Rail. It is anticipated that all divestitures will be completed in 2003 and are now, therefore, considered discontinued businesses.

The Company's 2003 – 2005 Service Plan was tabled in the legislature in February 2003. The full text of this document can be viewed on the Company's website.

Looking ahead at the 2003 – 2005 Service Plan, the Company will be focused on four goals representing the traditional pillars of a balanced strategic plan:

1. Revenue and yield improvement;

2. Productivity improvement and cost reduction;

3. Customer service; and

4. Safe, healthy and productive work environment.

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FINANCIALS

MANAGEMENT DISCUSSION AND ANALYSIS

Overview

The British Columbia Railway Company is a competitive, commercial Crown corporation owned by the Province of British Columbia. Since 1993, when BC Rail began a strategy of diversification, it operated as two distinct operating business units: BC Rail and BCR Marine. BC Rail is the historic founding company and includes the industrial freight railway and the Real Estate Division.

BCR Marine consists of Vancouver Wharves, Casco Terminals, and Canadian Stevedoring – providing diversification into the marine terminal business. A new strategy for the organization was set in 2002: a return to the core rail operations and the divestiture and/or discontinuation of non-core transportation businesses and services.

In 2001, the Company set forth its 2002-2004 strategic service plan, which resulted in significant changes to the organization. The primary result of the new strategy and goals was to divest and/or discontinue the following non-core transportation businesses and services:

- Vancouver Wharves
- Casco Terminals
- Canadian Stevedoring
- passenger services
- Finlay Navigation
- ToFC Intermodal service

Therefore, the Company will return to its main business of operating a freight railway service connecting northern BC to the Port of Vancouver and its connecting carriers in Prince George and the Lower Mainland.

The Real Estate division, which manages all of the Railway's real estate assets, has been retained. The majority of the land holdings are those required for BC Rail operations (rights-of-way, yards, terminal facilities, etc.) and lands in the Railway's important industrial parks, which are leased to railway customers and other tenants. In addition, the Real Estate division owns a smaller number of properties (lands and buildings), which it manages for income. As this source of funds has become increasingly important to supporting the overall cash flow requirements of the organization, it was decided to retain the portfolio of income-producing property.

BC Rail still faces many challenges. The effects of a deregulated Canadian transportation industry, which encourages competition among transportation modes, combined with the ongoing trend of mergers and consolidations amongst major North American railways have caused downward pressure on BC Rail's freight rates. The resulting challenge for the Company is to provide competitive freight rates to its customers while still attaining its profitability goals.

Another significant challenge is the restructuring and reduction of the Company's debt. Due to its Crown ownership, the Company is not able to source any new equity capital nor will it be able to access any new debt. Therefore, all capital requirements must be financed through operational cash flow.
A large portion of BC Rail's debt was incurred in 1983 through BC Rail's involvement in northeast coal developments. Unfortunately, the anticipated returns did not materialize as coal volumes and revenues fell far short of expectations. Coal traffic will completely cease by the spring of 2003. Therefore, the value of all coal-related assets was written down significantly in 2001. The debt, however, still remains.

The proceeds from the sale of the previously-mentioned non-core businesses will be used to repay the debt, thus providing some relief. Still, the challenge for management remains to restructure BC Rail to ensure its economic viability on an independent, stand-alone basis.

Other difficulties faced by the Railway include limited new freight traffic sources, increased dependence on the forest products sector, increased competition for market share, and the always challenging physical operating environment in British Columbia.

The 2002-2004 strategic service plan was developed to achieve the Company's current vision *"to act as a valuable strategic advantage for our customers in moving their goods to market"* and mission *"to build a safe, reliable, cost effective, self-sustaining, freight railway company"* and to overcome the challenges currently being faced. It is founded on four goals:

1. Revenue and yield improvement
2. Productivity improvement and cost reduction
3. Customer service
4. Safe, healthy, and productive work environment

The main objective of the first goal is to improve yield and net contribution from the freight business by evaluating the contribution of new and existing traffic. The second goal relates to improving operational productivity which the Company believes will be achieved via the divestiture / discontinuation of non-core transportation services as discussed above, improved fleet and infrastructure utilization, and the reduction of overhead costs. The benchmark of success for both of these goals is the reduction of the operating ratio below 75 per cent.

The third goal covers the challenges associated with increased competition and limited new traffic sources. Overall, the objective is to protect current rail traffic revenues by improving service reliability and consistency while still implementing cost reduction initiatives. Further, the Company intends to integrate business systems and processes between customers and BC Rail to build loyalty and provide mutual value.

The fourth goal relates to the work environment and employee safety and productivity. The belief is that a healthy, well-informed work force will be more productive and supportive of the long-term strategy of the Company, resulting in overall success for the organization.

BRITISH COLUMBIA RAILWAY COMPANY

MANAGEMENT DISCUSSION AND ANALYSIS
For the Year Ended December 31, 2002

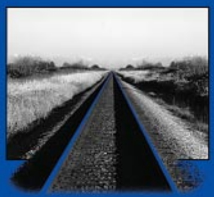
2002 Results

The year, although challenging, has had positive financial results. The consolidated net income from continuing operations for 2002 was $56 million, a significant increase from the net income from continuing operations (before special charges) of $5 million in 2001. Operating results from those business units that have been or will be discontinued as well as any expected loss on sale of those operations have been grouped and classified as discontinued operations. They include the BCR Marine division (i.e. Vancouver Wharves, Casco Terminals and Canadian Stevedoring), Finlay Navigation, and passenger services. The positive financial results in 2002 of the continuing operations confirm the economic benefits that the Company had anticipated and re-affirm its commitment to the strategic plan.

Revenues

Consolidated revenues from continuing operations for 2002 were $313.3 million, an increase of $11.5 million or 3.8 per cent from 2001. With the return to the core business of freight rail transport, revenue from freight traffic represents 95 per cent of total revenues. The balance is derived from the Real Estate division. Freight revenues were $297.6 million for 2002, up $10.1 million or 3.5 per cent from 2001.

($ thousands)	2002	2001
Forest products	$ 171,331	$ 161,730
Coal	16,973	12,884
Sulphur	20,694	21,180
Other bulk products	29,611	31,295
Car hire	43,993	37,501
Other	14,978	22,930
Total freight revenues	297,580	287,520
Real Estate division revenues	15,675	14,244
Total revenues	$ 313,255	$ 301,764



Forest Products

Revenue from forest products was up $9.6 million or 6 per cent from 2001 and was primarily responsible for the increase in freight revenues in 2002.

Lumber traffic was particularly strong this year. During the first half of the year, shippers moved significantly higher volumes over the border before the imposition of the US Softwood Lumber duties at the end of May. Traffic volumes continued to be strong through the third and fourth quarters due to the strategy of major shippers to counter the impact of the US duties by producing and shipping higher volumes, thereby lowering their per unit production costs. Furthermore, increased housing starts had a positive impact on lumber shipments throughout the year.

Woodpulp revenue continued to be negatively impacted by the decline in the world pulp market and the corresponding decline in export shipments followed by extensive mill curtailments and/or shutdowns.

Revenue from Logs and Poles increased in 2002 mainly due to increased volumes from the Takla region. The Takla saw an extended winter logging season due to the cold weather through the Spring of 2002 and increased volumes from the summer logging program.

Finally, Other Forest Products including Newsprint, Oriented Strand Board (OSB), Plywood, Veneer, and other miscellaneous commodities, experienced a 14 per cent increase in 2002. The positive variance was caused by stronger results across all commodity groups with the exception of Newsprint. Increased housing starts impacting lumber also had a positive affect on panel products (i.e. plywood and OSB).

Bulk Products

Revenue from bulk products was slightly better than the prior year mostly due to improved revenue from coal. Overall revenue from bulk products increased from $65.4 million in 2001 to $67.3 million in 2002, an increase of $1.9 million or 3 per cent.

Revenue from coal increased significantly in 2002, growing from $12.9 million in 2001 to $17.0 million in 2002 – an increase of $4.1 million or 32 per cent. During the year the Company moved to longer 125-car trains from the Bullmoose mine, thereby increasing the number of cars provided to reduce stockpiles at the mine. Furthermore, the average rate-per-car was higher as a result of improved strip ratios and exchange rates.

Sulphur revenue was down from 2001 caused primarily by lower traffic volumes from Alberta. Improved prices in the world market for sulphur offset some of the negative impact of the reduced traffic levels.

Grain traffic was also down in 2002. The negative variance began during the first quarter of the year when export sales by the Canadian Wheat Board were very slow. Volumes rebounded slightly through the second quarter, and then slowed again through the third and fourth quarters due to poor crop conditions in the Peace Region and the impact of the grain-handlers strike at the Port of Vancouver.

Finally, Other Bulk Products including Concentrates, Petroleum products, Liquified Petroleum Gas (LPG) products, and other miscellaneous bulk commodities, experienced a slight decrease in 2002. The negative variance is due to slightly poorer results across many of the commodities within the group with Chemicals and LPG's having the larger variances.

Other Freight Revenue

The most significant component of other freight revenue is Car Hire revenues – rent earned on offline BC Rail equipment. Car Hire revenues grew significantly in 2002, up $6.5 million or 17 per cent mostly due to increased lumber shipments.

Intermodal revenue decreased significantly in 2002 as the business unit services were reduced to include a Reload centre only. As part of the 2002-2004 strategic plan it was decided that effective February 1, 2002 Trailer-on-Flatcar (ToFC) and Highway Services would be discontinued. This was part of the overall plan to return to core rail service and a push towards higher yield traffic. The decrease in revenues in 2002 is completely due to the elimination of ToFC and Highway Services.

Expenses

Consolidated expenses from continuing operations were $241.9 million for 2002, down $24.6 million or 9 per cent from 2001. With the return to the core rail operations, expenses consist primarily (about 97 per cent) of costs associated with the operations of the Railway. The balance is associated with the Real Estate division. Consolidated labour costs decreased by $5.7 million or 5 per cent and material costs decreased by $3.7 million or 16 per cent. The reductions are due to efficiencies gained in both manpower and the consolidation of maintenance shops. Also, fuel costs decreased by $6.7 million or 21 per cent due to lower average fuel prices and lower consumption due to more efficient operations.

Freight expenses, being the majority of operating costs incurred in 2002, were $233.9 million down from $258.0 million in 2001.

($ thousands)	2002	2001
Operating expenses		
Maintenance	$ 62,615	$ 71,349
Operations	70,479	79,624
Fuel	22,050	26,909
Mishaps	4,653	6,502
Intermodal	1,888	12,803
Other	1,543	3,238
	163,228	200,425
Administrative overhead	33,401	16,318
Amortization expense	37,243	41,281
Total freight expenses	233,872	258,024
Real Estate division expenses	8,068	8,559
Total expenses	$ 241,940	$ 266,583

Operating expenses were down significantly from 2001, dropping $37.2 million or almost 19 per cent. An overall focus on efficiency and higher yield traffic, consistent with the 2002-2004 strategic goals, caused the reduction in expenses. Specifically, maintenance and operations saw the largest reductions.

The decrease in operations costs was mainly due to lower labour costs as a result of fewer freight trains and relief trains operated, and fewer yard shifts required compared to 2001. Furthermore, 2002 saw lower running trades training due to the heavy trainmen and enginemen training initiative in 2001.

The decrease in maintenance is related to two areas: Engineering and Mechanical. Engineering saw a reduction in expenses of $4.4 million as a result of the change in scope of the tie replacement program. Mechanical saw a reduction of $3.0 million as a result of savings in several areas including lower cost of locomotive servicing, lower labour and material used in freight car repair, and lower shop costs primarily in the locomotive area due to decreased utilities and shop activities resulting from the effort in 2001 to consolidate shops and manpower.

The reduction in operating fuel costs was equally due to positive volume and price variances. During 2002, fuel prices fluctuated significantly. However the Company's fuel hedging program was successful in hedging approximately one third of its fuel consumption. The Railway's focus on fuel conservation resulted in additional savings.

Consistent with the revenues, Intermodal costs are down due to the elimination of the ToFC and Highway Services early in 2002.

Administrative overhead expenses in 2002 were more than double the expense for 2001. The increase is primarily due to the pension plan credit, which is calculated annually, based on the actuarial valuation of the Company's pension plan. In 2001, income of $11.7 million was recorded compared to the current year's expense of $0.5 million. Also, insurance premiums increased in 2002 following the events of September 11, 2001.

Amortization expense decreased in 2002 primarily due to the sale of Intermodal equipment during the year. Also, there were certain information systems that were written off in 2002 as part of the 2002-2004 strategic initiative to replace and improve internal information systems and therefore were not amortized in 2002.

Discontinued Operations

The results of discontinued operations relate to those business units that were disposed of during the year or for which there was a formal plan of disposal. They include:

- Casco Terminals
- Canadian Stevedoring
- Vancouver Wharves
- Finlay Navigation
- passenger services

Revenues from the operations of Casco Terminals and Canadian Stevedoring declined $2.6 million or 3.3 per cent from $79.2 million in 2001 to $76.6 million in 2002. In August 2002, the Grainworkers in Vancouver were locked out by their employers, which negatively affected the stevedoring operations. In 2001, grain stevedoring accounted for 12.5 per cent of the stevedoring sales while in 2002 it accounted for 6.7 per cent of stevedoring sales. Revenue at Casco Terminals increased 8.0 per cent over 2001 as a result of a new customer that was signed up in late 2001. Profitability of container operations declined in 2002 due to tighter operating margins and increased amortization related to the terminal expansion completed in early 2002.

Revenues at Vancouver Wharves declined $1.9 million or 3.9 per cent from $49.9 million in 2001 to $47.9 million in 2002. In 2002 Vancouver Wharves recorded a loss of $12.4 million as compared to a loss of $1.8 million in 2001. The decline in operating results is largely attributable to a 9.0 per cent decrease in volumes through the terminal and an increase to the environmental provision recorded during the year.

The sale of the operations and assets of Canadian Stevedoring and Casco Terminals was completed in February 2003. The sale of the assets to P&O Ports for proceeds of $105 million will result in a net gain on sale of approximately $36 million. The sale of Vancouver Wharves is in progress and is expected to be completed during 2003. A write-down of $123.7 million was recorded against the Company's investment in Vancouver Wharves in 2002.

The sale of Finlay Navigation began in September 2002 and is expected to complete during the second quarter of 2003. Passenger services equipment, consisting mainly of a fleet of cars, is in the process of being disposed of. A significant portion of the Passenger equipment had been sold by the end of 2002.

BRITISH COLUMBIA RAILWAY COMPANY

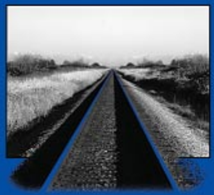
MANAGEMENT DISCUSSION AND ANALYSIS
For the Year Ended December 31, 2002

Looking Forward

The plan for 2003-2005 is to remain on track with the strategic plan and focus on the four main goals of the plan. Particularly, the Company is continuing to look for more efficient ways of using its resources in order to reduce operating costs and still provide competitive, reliable, and consistent service to customers.

Overall revenues are expected to decrease slightly in 2003 as compared to 2002, mostly due to the loss of coal shipments. Expenses for 2003, despite an effort to reduce costs and improve efficiencies, will likely remain at similar levels as 2002. The high yield on coal traffic is proving difficult to replace and/or absorb through operational efficiencies. Company management is targeting operating income from continuing operations in 2003 to be in line with 2002.

The Company's current plans for 2004 to 2007 project an operating ratio in the 75 per cent to 80 per cent range. Furthermore, it is forecasting that, after the proceeds from sales of the non-core businesses have been applied against outstanding debt, cash from operations (after interest and taxes) will be more than sufficient to cover the capital spending required to sustain the business. The long-term goal remains to operate the Railway as efficiently and reliably as possible, moving traffic at the highest yields possible.



REPORT OF MANAGEMENT

The accompanying consolidated financial statements of British Columbia Railway Company and all other information contained in the Annual Report are the responsibility of management. The consolidated financial statements were prepared in conformity with generally accepted accounting principles appropriate in the circumstances in a manner consistent with the previous year and, accordingly, include some amounts based on management's best judgments and estimates. The financial information contained elsewhere in this Annual Report is consistent with that in the consolidated financial statements.

Management is responsible for maintaining a system of internal accounting controls and procedures to provide reasonable assurance, at an appropriate cost/benefit relationship, that assets are safeguarded and transactions are authorized, recorded and reported properly. The internal accounting control system is augmented by a program of internal audits and appropriate reviews by management, written policies and guidelines and a written Code of Business Conduct adopted by the Board of Directors, applicable to all employees of the Company. Management believes that the Company's internal accounting controls provide reasonable assurance that assets are safeguarded against material loss from unauthorized use or disposition and that the financial records are reliable for preparing financial statements and other data and maintaining accountability for assets.

The Audit, Finance and Risk Management Committee of the Board of Directors meets with the independent auditors, management and internal auditors periodically to discuss internal accounting controls, auditing and financial reporting matters. The committee reviews with the independent auditors the scope and results of the audit effort. The committee also meets with the independent auditors without management present to ensure that the independent auditors have free access to the committee. The committee reviews the consolidated annual financial statements and recommends their approval by the Board of Directors.

The independent auditors, KPMG LLP Chartered Accountants, are appointed by the Minister of Finance to examine the financial statements of British Columbia Railway Company and conduct such tests and related procedures as they deem necessary in conformity with generally accepted auditing standards. The opinion of the independent auditors, based upon their examination of the financial statements, is contained in this Annual Report.

R. L. Phillips
President and Chief Executive Officer
British Columbia Railway Company

Peter M. Ballachey
Vice President Finance & CFO
British Columbia Railway Company

AUDITOR'S REPORT

To the Lieutenant Governor in Council
Province of British Columbia

We have audited the consolidated balance sheet of British Columbia Railway Company as at December 31, 2002 and the consolidated statement of income and deficit and cash flows for the year then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2002 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

KPMG LLP

Chartered Accountants

Vancouver, Canada

February 19, 2003

CONSOLIDATED BALANCE SHEET

(in thousands of dollars)

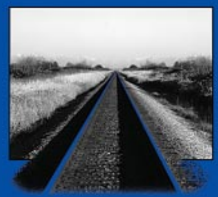
December 31	2002	2001 Restated (Note 2)
ASSETS		
Current		
Cash and cash equivalents	$ 21,046	$ 21,095
Accounts receivable	48,295	57,166
Inventories and other items	20,795	25,537
Future income taxes	14,000	–
Discontinued operations – Note 2	22,558	23,548
	126,694	127,346
Property and equipment – Note 3	880,921	883,384
Other assets – Note 4	78,580	68,274
Discontinued operations – Note 2	120,723	250,730
	$ 1,206,918	$ 1,329,734
LIABILITIES AND SHAREHOLDER'S EQUITY		
Current		
Accounts payable and accrued liabilities	$ 116,634	$ 113,077
Short-term notes payable to the Province	41,517	86,471
Current obligations on long-term debt – Note 6	7,405	7,497
Discontinued operations – Note 2	23,817	17,131
	189,373	224,176
Other liabilities – Note 5	94,371	119,863
Long-term debt – Note 6	553,668	539,925
Discontinued operations – Note 2	34,188	26,254
	871,600	910,218
Shareholder's equity		
Share capital – Note 7	257,688	257,688
Contributed surplus	277,547	277,547
Deficit	(199,917)	(115,719)
	335,318	419,516
	$ 1,206,918	$ 1,329,734

Commitments – Note 8
Contingent liabilities – Note 9
Subsequent event – Note 16
See accompanying notes to the consolidated financial statements.

On behalf of the Board

John McLernon,
Director

Brian G. Kenning,
Director

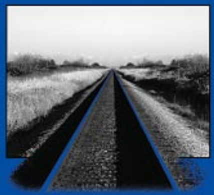


CONSOLIDATED STATEMENT OF INCOME AND DEFICIT

(in thousands of dollars)

For the years ended December 31	2002	2001
		Restated (Note 2)
Revenues	$ 313,255	$ 301,764
Expenses		
Labour costs	103,388	109,102
Amortization of property and equipment	38,843	46,462
Purchased services and other	27,411	24,821
Lease expense	23,405	24,044
Materials and supplies	19,583	23,260
Fuel	24,529	31,229
Capital and operating taxes	4,781	7,665
	241,940	266,583
Operating income	71,315	35,181
Non-operating expenses (income)		
Net interest expense – Note 11	29,270	29,734
Income tax expense (recovery) – Note 12	(13,993)	12
Income from continuing operations before special charges	56,038	5,435
Special charges		
Restructuring costs – Note 10	–	79,777
Income (loss) from continuing operations	56,038	(74,342)
Loss from discontinued operations – Note 2	(140,236)	(32,565)
Net loss	(84,198)	(106,907)
Deficit, beginning of year	(115,719)	(8,812)
Deficit, end of year	$ (199,917)	$ (115,719)

See accompanying notes to the consolidated financial statements.



CONSOLIDATED STATEMENT OF CASH FLOWS

(in thousands of dollars)

For the years ended December 31	2002	2001 Restated (Note 2)
Operating activities		
Income (loss) from continuing operations	$ 56,038	$ (74,342)
Adjustment for items not involving cash		
Loss (gain) on sale of assets	(2,231)	110
Amortization of property and equipment	38,843	46,462
Amortization of other assets and liabilities	65	1,275
Pension and post employment benefit income – Note 13	3,656	(9,176)
Pension and post employment benefit contributions – Note 13	(3,328)	(1,998)
Future income taxes – Note 12	(14,000)	–
Restructuring costs – Note 10	–	79,777
Net change in non-cash working capital – Note 14	(1,385)	(7,425)
Cash provided by operating activities	77,658	34,683
Investing activities		
Purchase of property and equipment	(39,941)	(47,834)
Proceeds on sale of property and equipment, net of selling costs	7,599	13,263
Mortgage repayments received	7,025	692
Change in insurance deposits	(3,417)	1,448
Additions to other assets	(3,120)	(1,878)
Cash used in investing activities	(31,854)	(34,309)
Financing activities		
Short-term notes advanced from the Province	(44,954)	35,875
Payments and interest earned on sinking funds	(6,838)	(6,188)
Repayment of long-term debt	(2,579)	(3,175)
Cash provided by (used in) financing activities	(54,371)	26,512
Increase (decrease) in cash and cash equivalents from continuing operations	(8,567)	26,886
Cash provided by (used in) discontinued operations	8,518	(24,316)
Cash and cash equivalents, beginning of year	21,095	18,525
Cash and cash equivalents, end of year	$ 21,046	$ 21,095

See accompanying notes to the consolidated financial statements

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

British Columbia Railway Company is owned by the Province of British Columbia (the "Province") and was incorporated under the British Columbia Railway Act.

The Company provides industrial freight rail transportation and terminal services within British Columbia (including rail, deep-sea terminals and stevedoring). During 2002, the Company began a significant restructuring of its business in which it plans to dispose of or discontinue its deep-sea terminals, stevedoring operations and other non-core activities.

1. SIGNIFICANT ACCOUNTING POLICIES

These consolidated financial statements are expressed in Canadian dollars and have been prepared in accordance with Canadian generally accepted accounting principles.

Basis of consolidation

These consolidated financial statements include the accounts of British Columbia Railway Company and all of its subsidiaries. In these notes, "Company" refers to British Columbia Railway Company, its subsidiaries and partnerships. All significant inter-company transactions have been eliminated.

Use of estimates

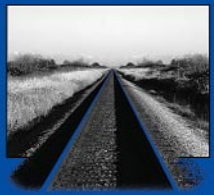
The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Significant areas requiring the use of management estimates relate to the determination of net recoverable value of assets, useful lives for amortization and provisions for post employment benefits, contingencies, restructuring and environmental matters. Actual amounts may ultimately differ from these estimates.

Cash and cash equivalents

Cash and cash equivalents include cash and those short-term money market instruments with initial terms to maturity of three months or less.

Inventories

Inventories of material and supplies are valued at the lower of average cost and net realizable value.



NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. SIGNIFICANT ACCOUNTING POLICIES (cont'd)

Property and equipment

Road property is recorded at cost, net of government grants. Abandoned or relocated sections are removed at average unit costs. Track materials installed during planned programs are recorded at cost. However, labour costs for programmed replacements are expensed as incurred. Repairs and non-programmed replacements of track structure are charged against current operations. Betterments and major track relocations are capitalized.

During the year, the Company early adopted CICA Handbook Section 3063 "Impairment of Long-Lived Assets". The new section requires a determination of impairment for assets held for use under a two-step process: the first step determines when impairment is recognized using undiscounted cash flows, and the second step measures the amount of the impairment using fair value.

In accordance with generally accepted accounting practices for railways in Canada, property and equipment is amortized on a straight-line basis over the estimated useful lives of the assets. The cost of assets retired or disposed, less salvage value, is charged against accumulated amortization in accordance with the group method of amortization. No gain or loss on retirements, other than on accidental destruction of rolling stock and on disposal of land and commercial property, is included in income. The original cost of assets less estimated salvage value is amortized over the following number of years:

	Number of Years
Road and buildings:	
Tunnels	150
Grade	100
Bridges	30 - 80
Rail, ties and ballast	25 - 35
Wharves and buildings	10 - 40
Equipment:	
Locomotives	25
Freight cars	15 - 33
Handling and other equipment	3 - 20

Equipment under capital lease is amortized over its lease term.

1. SIGNIFICANT ACCOUNTING POLICIES (cont'd)

Revenue recognition

Rail freight revenues and associated movement costs are recognized as the service is performed.

Foreign exchange

Transactions denominated in a foreign currency are translated at exchange rates prevailing on the date of transactions. Assets and liabilities denominated in a foreign currency at the balance sheet date are translated to equivalent Canadian amounts at the exchange rate in effect on that date.

Post employment benefits

The Company accrues its obligations under employee benefit plans and the related costs as benefits are earned, net of returns on plan assets. The Company policies are as follows:

i) The cost of retirement benefits earned by employees is actuarially determined using the projected benefit method pro-rated on service and management's best estimate of expected plan investment performance, salary escalation, retirement ages of employees and expected health care costs.

ii) The expected interest cost on any prior service obligation is calculated using management's estimate for the long-term rate of return.

iii) The expected return on plan assets is calculated at a market-related value for the assets.

iv) Past service costs from plan amendments, experience gains and losses and any changes in assumptions are amortized on a straight-line basis over the expected average remaining service period of active employees and included in the pension expense for the year.

Income taxes

The Company follows the asset and liability method of accounting for income taxes. Under this method, changes in future tax asset and liability balances are included in income. These balances are determined using enacted tax rates expected to apply to taxable income in the years in which temporary differences are expected to be recovered or settled.

Derivative financial instruments

Derivative financial instruments are utilized by the Company to manage its exposure to market risks relating to fuel prices. The Company's policy is to formally designate each derivative financial instrument as a hedge of anticipated fuel purchases. The Company believes the derivative financial instruments are effective as hedges, both at inception and over the term of the instrument, as it is certain that fuel consumption will be greater than the amount of fuel contracted for in the derivative financial instruments. Unrealized gains and losses on derivative instruments used as hedges are deferred and recognized in income in the period that the hedged exposure is recognized in income, which is the same period the instrument is settled.

1. SIGNIFICANT ACCOUNTING POLICIES (cont'd)

The Company also uses foreign currency swaps to manage foreign exchange risks related to debt denominated in foreign currencies (Note 6).

Environmental expenditures and liabilities

Environmental expenditures that relate to current operations are expensed as part of operating activities or capitalized as appropriate. Expenditures that relate to an existing condition caused by past operations and which are not expected to contribute to current or future operations are expensed. Environmental liabilities related to environmental assessment and/or remedial efforts are accrued when the expenditures are considered likely and the costs can be reasonably estimated.

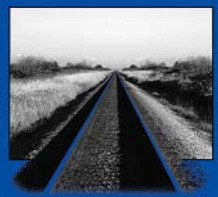
2. DISCONTINUED OPERATIONS

In December 2001, the Company approved its 2004 Strategic Plan to reorganize its operations. Part of this plan was the sale or discontinuation of non-strategic lines of business. In accordance with this plan, the Company decided to sell BCR Marine and Finlay Navigation and to discontinue its Passenger Services operations.

The Company's Board of Directors approved the sale of BCR Marine (including the operations of Vancouver Wharves, Casco Terminals and Canadian Stevedoring) in March 2002. The Company expects to complete the sale of the assets of Canadian Stevedoring Company Limited ("CSCL", which includes the operations of Casco Terminals and Canadian Stevedoring) on February 25, 2003 (Note 16). The Company is proceeding with the sale of Vancouver Wharves, which is expected to be completed during 2003.

The Company entered into a formal plan of disposal for Finlay Navigation in September 2002. The Company is currently working with a prospective purchaser to complete the sale of this operation. A sale is expected to occur in early 2003.

The Company entered into a formal plan to discontinue its Passenger Services operations in March 2002. The Company ceased the operations of its passenger lines over the course of 2002, with the final run of this service occurring in October 2002. The sale of assets from this business is continuing.



NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(tabular amounts in thousands of dollars)

2. DISCONTINUED OPERATIONS (cont'd)

The Company's results for 2001 have been restated to reflect these discontinued operations.

The Company's share of the assets, liabilities and revenues and expenses of its discontinued operations for the years ended December 31, 2002 and 2001 are as follows:

	CSCL		Vancouver Wharves		Passenger Services		Other		Total	
	2002	2001	**2002**	2001	**2002**	2001	**2002**	2001	**2002**	2001
Balance Sheet										
Current assets	**$ 12,753**	$ 15,282	**$ 8,088**	$ 5,975	**$ 50**	$ 890	**$ 1,667**	$ 1,401	**$ 22,558**	$ 23,548
Capital assets and other	**61,787**	53,961	**47,482**	178,811	**3,206**	5,406	**8,248**	12,552	**120,723**	250,730
Current liabilities	**(8,776)**	(10,630)	**(7,367)**	(5,073)	**(84)**	(768)	**(7,590)**	(660)	**(23,817)**	(17,131)
Other liabilities	**(4,252)**	(88)	**(27,812)**	(23,844)	**–**	–	**(2,124)**	(2,322)	**(34,188)**	(26,254)
Net assets of discontinued operations	**$ 61,512**	$ 58,525	**$ 20,391**	$ 155,869	**$ 3,172**	$ 5,528	**$ 201**	$10,971	**$ 85,276**	$230,893
Statement of income										
Revenues	**$ 76,604**	$ 79,218	**$ 47,937**	$ 49,867	**$ 8,254**	$ 9,127	**$ 9,120**	$ 7,202	**$ 141,915**	$145,414
Expenses	**75,215**	79,976	**60,295**	51,626	**14,146**	18,771	**7,658**	7,383	**157,314**	157,756
Restructuring costs – Note 10	**–**	–	**–**	–	**–**	11,726	**–**	8,497	**–**	20,223
Gain on disposal of assets	**–**	–	**–**	–	**(7,472)**	–	**–**	–	**(7,472)**	–
Estimated loss on disposal	**–**	–	**125,309**	–	**–**	–	**7,000**	–	**132,309**	–
	$ 1,389	$ (758)	**$ (137,667)**	$ (1,759)	**$ 1,580**	$ (21,370)	**$ (5,538)**	$ (8,678)	**$ (140,236)**	$ (32,565)

The revenues and expenses in the above table include the results of the discontinued operations for the entire year. The results of operations before adoption of the formal plans of disposition ("measurement dates") was a loss of $4.1 million (2001 - $32.6 million). Subsequent to the measurement dates, the net loss from discontinued operations (including the estimated loss on disposal) was $136.2 million (2001- $nil).

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(tabular amounts in thousands of dollars)

3. PROPERTY AND EQUIPMENT

($ millions)	2002 Cost	2002 Accumulated Amortization	2002 Net	2001 Cost	2001 Accumulated Amortization	2001 Net
Road and buildings	$ 1,624,074	$ 1,009,496	$ 614,578	$ 1,581,563	$ 977,921	$ 603,642
Equipment	395,307	157,303	238,004	410,945	172,452	238,493
Equipment under capital lease	31,226	24,548	6,678	31,384	24,346	7,038
Construction in progress	21,661	–	21,661	34,211	–	34,211
	$ 2,072,268	$ 1,191,347	$ 880,921	$ 2,058,103	$ 1,174,719	$ 883,384

Interest of $254,000 (2001 - $604,000) has been capitalized during the year. During 2001, the Company entered into two agreements with the Province and the Squamish Nation for the exchange of parcels of land. Under these agreements, the Company exchanged land, development costs and cash for a total value of $4.4 million for land, timber rights and cash with a fair value of $4.7 million. The Company recognized a gain of $300,000 on the transaction, which was recorded at market value.

During 2002, the Company sold land near Prince George, including timber and gravel on site, to its tenant, Carrier Lumber Ltd. This transaction was part of a larger transaction between the Province and Carrier in which the Province paid the Company $2.6 million for the above assets on behalf of Carrier. The Company recorded a gain of $2.5 million on the sale.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(tabular amounts in thousands of dollars)

4. OTHER ASSETS

	2002	2001
Accrued benefit asset – Note 13	$ 28,741	$ 27,233
Insurance deposits	26,441	23,024
Foreign currency contract – Note 6	10,842	–
Deferred system costs	3,889	1,987
Mortgages receivable	373	7,398
Other	8,294	8,632
	$ 78,580	$ 68,274

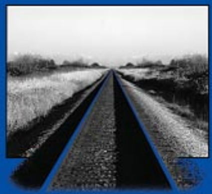
Insurance deposits are funds required to be put on deposit as part of the Company's self-insurance program, calculated as the excess of the premiums paid over the actual losses incurred, plus investment income.

Deferred system costs include costs incurred to develop information systems, which are being amortized over their expected useful lives of 3 to 7 years.

5. OTHER LIABILITIES

	2002	2001
Accrued non-pension benefit obligation – Note 13	$ 43,237	$ 41,400
Restructuring costs – Note 10	18,754	35,032
Workers' compensation	16,337	16,125
Environmental liability accrual – Note 9	9,000	8,000
Future income tax liability	5,965	5,965
Foreign currency contract – Note 6	–	12,226
Other	1,078	1,115
	$ 94,371	$ 119,863

(tabular amounts in thousands of dollars)



6. LONG-TERM DEBT

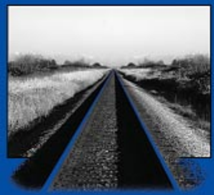
(a) Long-term debt outstanding, less current maturities, consists of the following:

		2002	2001
Sinking fund bonds, notes and debentures payable to the Province of British Columbia:			
8.00 %	due August 2005	$ 44,000	$ 44,000
10.99 %	due August 2005	24,490	24,490
6.00 %	due June 2008	50,000	50,000
6.377 %	due July 2009	160,842	137,774
8.00 %	due June 2026	50,000	50,000
6.15 %	due November 2027	25,000	25,000
5.70 %	due June 2029	175,000	175,000
5.75 %	due January 2039	50,000	50,000
		579,332	556,264
Capital lease obligations		12,036	14,365
Other long-term notes payable		–	250
		591,368	570,879
Less:			
Sinking funds		30,295	23,457
Current portion		7,405	7,497
		553,668	539,925
Foreign currency contract – Note 6 (d)		(10,842)	12,226
Net long-term debt outstanding after hedging		$ 542,826	$ 552,151

(b) The sinking fund bonds, notes and debentures payable to the Province of British Columbia are unsecured.

(c) Sinking fund requirements for the next five years are as follows:

2003	$ 4,918
2004	4,918
2005	4,918
2006	3,862
2007	3,862



NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(tabular amounts in thousands of dollars)

6. LONG-TERM DEBT (cont'd)

(d) The 6.377% note is a French franc 636,959,470 note subject to swap agreements which hedge the Company against foreign exchange changes arranged by the Company's fiscal agent on the Company's behalf. The French franc has a fixed conversion rate to the euro of 6.55957 (1 euro = 6.55957 French francs). The note is included in long-term debt at the closing exchange rate as at the balance sheet date. The note after hedging is valued at C$150 million.

(e) Effective interest rates for assets under capital leases recorded in the property and equipment accounts as at December 31, 2002 range from 5.60% to 13.13%. The future minimum lease payments are as follows:

2003	**$ 3,955**
2004	**1,965**
2005	**1,965**
2006	**1,965**
2007	**1,965**
Thereafter	**10,695**
Total minimum lease payments	**22,510**
Less:	
Maintenance costs	**4,098**
Imputed interest	**6,376**
Net liability	**$ 12,036**

7. SHARE CAPITAL

Authorized: 10,000,000 shares with a par value of $100 each.

Issued and outstanding: 2,576,885 shares held by the Province.

As all of the common shares of the Company are held by the Province, earnings per share data has not been provided.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(tabular amounts in thousands of dollars)

8. COMMITMENTS

The following is a schedule of future minimum payments at December 31, 2002, required under non-cancelable operating leases:

2003	**$ 20,139**
2004	**15,372**
2005	**10,467**
2006	**4,831**
2007	**2,354**
Thereafter	**366**
Total minimum lease payments	**$ 53,529**

At December 31, 2002, the Company had outstanding commitments to acquire material and equipment amounting to $8 million (2001 - $18 million).

9. CONTINGENT LIABILITIES

(a) The Company is contingently liable with respect to pending litigation and claims arising in the normal course of business. In the opinion of management, any liability that may arise would not have a material adverse effect on future income as sufficient provisions have been made.

(b) The risk of environmental liability is inherent in the operation of railways, terminal facilities, and property management companies with respect to both current and past operations. As a result, the Company incurs significant costs, on an ongoing basis, associated with environmental regulatory compliance and clean-up requirements.

The Company accrues for both anticipated expenditures on existing environmental remediation programs over a 10 year horizon and contingent liabilities in relation to specific sites where the expected costs can be reasonably estimated.

The Company believes it has identified the costs likely to be incurred over the next several years, based on known information. However, ongoing efforts to identify potential environmental concerns associated with the Company's properties may lead to future environmental investigations, which may result in the identification of additional environmental costs and liabilities, the magnitude of which cannot be reasonably estimated.

(c) The Company leases a portion of its property used in its operations in North Vancouver from Canada Lands Company Limited (CLCL). Subsequent to the year end, the Company received a notice of default on its lease from CLCL. The Company is currently assessing whether the allegations in the notice of default are factually correct and has no indication of what outcome or cost will arise as a result of this notice.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(tabular amounts in thousands of dollars)

10. RESTRUCTURING COSTS

During 2001, the Company approved its 2004 Strategic Plan to reorganize its rail operations. The reorganization involves closing redundant offices, eliminating non-strategic lines of business, and implementing changes in systems, personnel, and business processes. The estimated cost of $100 million was fully recorded in the 2001 financial year. In conjunction with discontinued operations reporting, $20.2 million of the restructuring costs have been reclassified to discontinued operations.

As at December 31, 2002, $37 million of the amounts accrued for this restructuring in 2001 remain and will be expended over the next three years. Of this amount, $18.8 million is classified as long term.

11. NET INTEREST EXPENSE

	2002	2001
Interest on long-term debt and short-term notes to the Province	$ 38,930	$ 40,312
Interest on capital lease obligations	1,221	1,370
Other interest expense	1,825	119
	41,976	41,801
Less:		
Sinking fund earnings	1,918	1,265
Interest earned on temporary investments	1,420	2,090
Interest capitalized	254	604
Interest allocated to discontinued operations	9,114	8,108
	12,706	12,067
Net interest expense	$ 29,270	$ 29,734

12. INCOME TAXES

(a) Income tax expense (recovery) is comprised as follows:

	2002	2001
Current	$ 7	$ 12
Future	(14,000)	–
	$ (13,993)	$ 12

Future income taxes of $14 million were recognized as it more likely than not they will be used as a result of the gain on the sale of the assets of CSCL (Note 16).

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(tabular amounts in thousands of dollars)

12. INCOME TAXES (cont'd)

(b) As at December 31, 2002, the Company had available tax losses carried forward aggregating $327 million of which $37 million have been recognized as a future tax asset. The tax losses available to be carried forward expire as follows:

2003	$	42,300
2004		13,500
2005		31,800
2006		44,302
2007		66,000
2008		86,501
2009		42,824
Total	$	327,227

13. EMPLOYEE BENEFITS

(a) The Company has defined benefit and defined contribution pension plans and other retirement and post employment benefit plans which cover most of its employees. The amounts presented in this note are actuarially determined projections.

	Pension Plans		Other Plans	
	2002	2001	**2002**	2001
Reconciliation of accrued benefit asset (liability)				
Opening balance	**$ (484,694)**	$ (426,627)	**$ (35,674)**	$ (30,215)
Current service cost	**(15,607)**	(13,726)	**(763)**	(690)
Benefits paid	**33,744**	22,719	**1,276**	860
Interest cost	**(33,294)**	(31,659)	**(2,516)**	(2,286)
Plan amendments	**(2,624)**	–	**–**	–
Actuarial gains (losses)	**92,240**	(35,401)	**(14,675)**	(3,343)
Ending balance	**(410,235)**	(484,694)	**(52,352)**	(35,674)
Reconciliation of plan assets				
Opening balance	**567,793**	649,912	**–**	–
Actual return on plan assets	**(4,299)**	(60,538)	**–**	–
Employer contributions	**2,052**	1,138	**1,276**	860
Benefits	**(33,744)**	(22,719)	**(1,276)**	(860)
Ending balance	**531,802**	567,793	**–**	–
Fund status – surplus (deficit)	**121,567**	83,099	**(52,352)**	(35,674)
Unamortized transitional asset	**(93,417)**	(103,521)	**–**	–
Unamortized net actuarial loss (gain)	**(2,251)**	47,437	**9,115**	(5,726)
Other	**2,842**	218	**–**	–
Accrued benefit asset (liability)	**$ 28,741**	$ 27,233	**$ (43,237)**	$ (41,400)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(tabular amounts in thousands of dollars)

13. EMPLOYEE BENEFITS (cont'd)

(b) Significant actuarial assumptions adopted in measuring the Company's accrued benefit obligations are as follows as of December 31:

	Pension Plans		Other Plans	
	2002	2001	**2002**	2001
Discount rate for liabilities	**7.25%**	7.0%	**7.25%**	7.0%
Expected long-term rate of return on plan assets	**7.0%**	7.0%	**–**	–
Salary escalation rate	**0% to and including 2005; 3.5% from 2006**	3.0%	**–**	–

The weighted average rate of increase in the per capita cost of future covered health care benefits was assumed to be 6.3% grading down to 4.2% in 2008.

The plan asset portfolio currently comprises equity investments and debt. Equity investments are 50%-70% of the portfolio and include Canadian, International, and Real Estate investments. Debt is 30%-50% of the portfolio and comprises short-term debt, bonds and mortgages. Asset mix is reviewed periodically and may vary in the future.

(c) The Company's net benefit plan expense (income) is as follows:

	Pension Plans		Other Plans	
	2002	2001	**2002**	2001
Current service cost	**$ 15,607**	$ 13,726	**$ 763**	$ 690
Interest cost	**33,294**	31,659	**2,516**	2,286
Expected return on plan assets	**(38,308)**	(44,442)	**–**	–
Amortization of transitional asset	**(10,104)**	(10,104)	**–**	–
Other	**55**	(2,559)	**(167)**	(432)
	$ 544	$ (11,720)	**$ 3,112**	$ 2,544

(tabular amounts in thousands of dollars)

14. STATEMENT OF CASH FLOWS – SUPPLEMENTAL INFORMATION

(a) The components of changes in non-cash working capital balances relating to operations are as follows:

	2002	2001
Accounts receivable	$ 8,871	$ 9,689
Inventories and other items	4,742	1,275
Accounts payable and accrued liabilities	(14,998)	(18,389)
	$ (1,385)	$ (7,425)

(b) The following interest was paid (received) in the current year:

	2002	2001
Interest paid to third parties	$ 40,715	$ 41,658
Interest received from third parties	(3,123)	(3,321)
	$ 37,592	$ 38,337

(c) The following non-cash transactions were recorded during the year:

	2002	2001
Future income taxes – Note 12	$ 14,000	$ –
Other assets and fixed assets	–	2,040
Restructuring costs – Note 10	–	100,000
	$ 14,000	$ 102,040

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(tabular amounts in thousands of dollars)

15. FINANCIAL INSTRUMENTS

(a) Fair Values

The Company's financial instruments include cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities, short-term notes, long-term debt, and foreign currency contracts. The carrying amounts approximate fair value due to their immediate or short-term maturity, except as disclosed in the following table:

	2002		2001	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Bonds, notes and debentures	$ (579,332)	$ (669,651)	$ (556,264)	$ (626,211)
Sinking funds	30,295	31,794	23,457	23,760
Foreign currency contracts	10,842	11,576	(12,226)	(15,695)

(b) The Company has no unrecognized losses in relation to its fuel hedging instruments as at December 31, 2002.

16. SUBSEQUENT EVENT

The Company expects to complete the sale of the assets of CSCL to P&O Ports Canada Inc. on February 25, 2003 for proceeds of $105.1 million. The Company estimates that a pre-tax gain of $36 million will arise on the sale. The proceeds will be used to reduce a portion of the Company's long-term debt through defeasance and to repay a portion of short-term debt.

17. COMPARATIVE FIGURES

The presentation of the 2001 consolidated financial statements has been restated to conform with that of the current year.

STATEMENT OF CORPORATE GOVERNANCE

Sound corporate governance principles are essential to the success of every commercial enterprise. British Columbia Railway Company ("BCRC") is committed to these principles to foster its continued success.

A Code of Conduct for all BCRC employees, officers, agents and directors was introduced in 1995 and remains in effect today. The Code emphasizes the importance of honesty, fair dealing, faithful performance of contract and integrity. In 1999, the Board of Directors adopted Standards of Ethical Conduct for Directors and Officers ("Standards"). The Standards recognize the additional responsibilities and duties that directors and officers have to BCRC. The implementation of the Standards of Ethical Conduct includes the appointment by the Board of Directors of an Ethics Advisor to provide advice to directors and officers on the application and interpretation of the standards.

In accordance with present guidelines for corporate governance, all members of the Board are independent and unrelated, having no other affiliation with BCRC. The roles of the Chair and the CEO are separate, with no overlap of responsibilities.

BCRC will continue to review its governance practices to ensure that they are consistent with the Code and that they contribute to the sound direction and management of BCRC. The Board of Directors carries out its duties with the primary objective of enhancing shareholder value. The Board has the authority and duty to supervise management of the Company's business affairs. Management reviews and revises the objectives for the Company with the Board, which considers and approves them and monitors progress towards their achievement.

The business plan and forecast are reviewed and approved by the Board prior to the start of each fiscal year. The approval of the business plan and budget establishes the authority of senior management to take the actions indicated in the business plan and their responsibility for implementation. Other material matters not reflected in the budget, including raising capital, acquisitions and divestitures require approval of the Board. Through reports distributed to the Board, and at quarterly directors' meetings, management reviews with the Board the progress of business units in meeting the business plan and budgets.

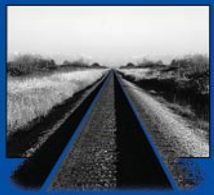
The Board regards the selection and compensation of senior management as an important element of meeting the Company's objectives. It has delegated this function to an independent Human Resources, Governance and Nominating Committee consisting of three directors. The committee, with the assistance of independent consultants, considers compensation for senior management, which is designed to reward effort, reflect the Company's performance in relation to current objectives and to be consistent with market rates of compensation.

STATEMENT OF CORPORATE GOVERNANCE

The Board recognizes the importance of maintaining effective internal, financial and other controls, sound management information systems and timely, consistent financial reporting. The Board has delegated the overseeing of management's performance of these functions to a three-member Audit, Finance and Risk Management Committee whose members have been selected for their ability and experience with these functions. The committee meets at least twice annually with the Company's auditors to review annual planning for the audit of the Company's accounts, to monitor the progress of the audit and to review the auditor's report and recommendations. The committee has direct access to the Company's internal audit staff. The committee also approves all other financial information prepared by management for public release.

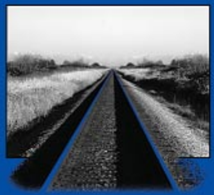
The Board recognizes the imperative of safe and environmentally responsible operations. To oversee management's responsibilities in these matters, the Board established a two-member Environment and Safety Committee whose members are experienced in the operation of heavy industry. Subsequent to the year-end, this committee was expanded to three directors. The committee meets as required, but at least twice annually, to review the safety performance of the Company's operations and to assess the progress of the programs to manage the impact of the Company's operations on its surrounding environment.

Management has primary responsibility for establishing objectives for the Company. The objectives are designed to exploit opportunities available to the Company and to diminish the risks to which its business is subject so as to enhance returns to the shareholder. Management regularly reviews the objectives to ensure that they are in keeping with the state of the Company's development and the markets in which it operates. In pursuit of these objectives, management prepares an annual business plan and a three-year strategic plan, including financial forecasts.



CONSOLIDATED FIVE-YEAR REVIEW

	FISCAL YEAR 2002	2001	2000	1999	1998
Income Statement Items (thousands)					
Continuing Operations					
Revenues	$ 313,255	$ 301,764	$ 333,501	$ 341,071	$ 338,326
Expenses	241,940	266,583	293,047	271,256	284,487
Operating income	71,315	35,181	40,454	69,815	53,839
Financing costs and income taxes	15,277	29,746	28,747	22,621	21,767
Income from continuing operations before special charges	56,038	5,435	11,707	47,194	32,072
Special charges	–	(79,777)	(8,000)	(605,792)	–
Results of discontinued operations	(140,236)	(32,565)	(10,428)	(23,461)	(7,939)
Net income (loss)	$ (84,198)	$ (106,907)	$ (6,721)	$ (582,059)	$ 24,133
Rate of Return (income from continuing operations before special charges)					
On shareholder's equity	14.8%	1.1%	2.2%	5.7%	2.8%
Other Financial Highlights					
Capital additions of continuing operations (millions)	$ 43	$ 50	$ 89	$ 95	$ 119
Total assets (millions)	$ 1,207	$ 1,330	$ 1,372	$ 1,387	$ 1,944
Operating ratio of continuing operations	78%	92%	88%	80%	84%
Debt to equity ratio	1.76	1.54	1.18	1.21	0.54
Employees (number)	1,618	2,016	1,999	2,088	2,249
Traffic and Operating Statistics					
BC Rail Business Unit					
Revenue ton-miles (millions)	4,695	4,865	5,058	5,106	4,947
Gross ton-miles (millions)	8,205	8,696	8,914	9,090	8,986
Net : gross ton-miles	36:64	36:64	36:64	36:64	36:64
Revenue tons (thousands)	14,283	13,988	15,273	16,177	16,230
Carloadings	164,848	168,120	184,125	193,627	193,882
Revenue tons per carload	87	83	83	84	84
Revenue ton-miles per BC Rail employee (thousands)	3,059	2,900	2,882	2,685	2,446
Number of locomotives at year end	121	125	129	127	122
Number of freight cars at year end	9,002	9,186	9,563	9,538	9,846



CONSOLIDATED FIVE-YEAR REVIEW

	FISCAL YEAR				
	2002	2001	2000	1999	1998
BCR Marine Business Unit					
Vancouver Wharves Limited Partnership					
Tonnage shipped (thousands)	**3,681**	4,046	4,292	3,463	3,772
Tons handled per employee	**22,175**	22,603	20,321	15,552	17,097
Canadian Stevedoring Company Limited (Note 1)					
Tonnage handled (thousands)	**7,550**	9,633	10,041	8,816	1,525
Tons handled per employee	**13,726**	17,030	15,763	14,645	2,495
BCR Properties Business Unit					
Leased square feet (thousands)	**536**	536	309	1,663	1,340
Revenue per employee (thousands)	**$ 877**	$ 914	$ 1,192	$ 1,489	$ 1,346

Note 1: Canadian Stevedoring Company Limited was purchased October 31, 1998.

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