

***FIRST QUARTER REPORT***

***Three Months Ended  
January 31, 2008***



***ARBOR MEMORIAL SERVICES INC.***

## MANAGEMENT'S DISCUSSION AND ANALYSIS

Management's Discussion and Analysis for Arbor Memorial Services Inc. ("Arbor" or the "Company") has been prepared for the three months ended January 31, 2008 and includes material information available up to February 28, 2008. The financial data provided has been prepared in accordance with Canadian generally accepted accounting principles ("GAAP") and all figures provided are in Canadian dollars. Management's Discussion and Analysis herewith provided is the responsibility of the Company's management. The Board of Directors is responsible for reviewing and approving Management's Discussion and Analysis. Additional information relating to Arbor, including the Company's Annual Information Form, can be found on SEDAR at [www.sedar.com](http://www.sedar.com).

### Information Regarding Forward-Looking Statements

Certain statements contained in this Management's Discussion and Analysis including, but not limited to, information regarding the status and progress of the Company's operating and capital activities, the plans and objectives of the Company and assumptions regarding the Company's future performance are forward-looking statements. Forward-looking statements may include words such as "believes", "may", "should", "estimates", "continues", "indicates", "suggests", "anticipates", "intends", "plans", "expects" and similar expressions. These forward-looking statements are based on current expectations and various factors and assumptions. Accordingly, these forward-looking statements are subject to certain risks and uncertainties. The material factors and assumptions that were applied in making the forward-looking statements in this Management's Discussion and Analysis include, but are not limited to: reliance on third-party reports from government bodies and industry associations, the use of economic forecasts prepared by various financial institutions, historical experience, and financial reporting of competitors and suppliers. Risks and uncertainties that could cause or contribute to actual results differing from such statements include, but are not limited to, those discussed elsewhere in this Management's Discussion and Analysis, particularly under "Events and Uncertainties", and in the Company's 2007 Annual Information Form under "Description of the Business – Risk Factors" and 2007 Annual Report under "Risks, Events and Uncertainties". The Company cannot provide any assurance that forward-looking statements will materialize. The Company assumes no obligation to publicly release any revisions to these forward-looking statements to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events.

### Non-GAAP Financial Measures

In addition to the GAAP results provided in this Management's Discussion and Analysis, some of the discussion of operating performance is based on earnings before interest expense and income taxes ("EBIT"). EBIT excludes the impact of interest expense and income taxes as disclosed in the statements of earnings. EBIT is a non-GAAP financial measure that does not have any standardized meaning prescribed by GAAP and is therefore unlikely to be comparable to similar measures presented by other companies. This non-GAAP financial measure is provided as a supplement, and should not be considered an alternative to measurements required by GAAP. Management uses EBIT to assess its operating results, as it believes it is important to assess the cemetery, funeral, and corporate activities without these non-operating components. Management believes that this measure provides useful additional information to management and investors regarding the Company's performance as it provides a basis for analyzing the ongoing operating results, which may vary due to different market and economic factors than those that affect interest expense and income taxes.

### New Disclosure Requirements

In 2006, the Canadian Institute of Chartered Accountants ("CICA") issued the following new disclosure requirements: Financial Instruments – Disclosures ("Section 3862"); Financial Instruments – Presentation ("Section 3863") and Capital Disclosures ("Section 1535"). The standards require prospective application and are effective for the Company's first quarter of fiscal 2008.

Section 3862, together with Section 3863, replaces Section 3861 and requires that disclosures be provided in the financial statements that enable users to evaluate the significance of financial instruments for the Company's financial position and performance as well as the nature and extent of risks arising from financial instruments and how the Company manages those risks. As a result of implementing this standard, the Company has included additional disclosure in note 12, long term debt, and note 13, accounts receivable.

Section 3863, together with Section 3862, replaces Section 3861 and is intended to enhance understanding of the significance of financial instruments to the Company's financial position, performance and cash flows. This section establishes standards for the presentation of financial instruments and non-financial derivatives related to the

classification of financial instruments, from the perspective of the issuer, between liabilities and equity, the classification of related interest, dividends, losses and gains, and the circumstances in which financial assets and liabilities are offset. The presentation used by the Company in the 2007 annual consolidated financial statements met the requirements of the new accounting standard.

Section 1535 establishes standards for disclosing information about an entity's capital and how it is managed. The Section requires disclosure of information about the Company's objectives, policies and processes for managing capital and how it is meeting these objectives. As a result of implementing this standard, the Company has included additional disclosure in note 8 to the consolidated financial statements in this interim report.

### Future Accounting Policy Change

Revisions to CICA Handbook section 1000, Financial Statements and Concepts and section 3064, Goodwill and Intangible Assets, are applicable to fiscal years beginning on or after October 1, 2008. Adoption of these standards is effective for the Company for the first quarter of fiscal 2009. However, early adoption is currently being considered. The objectives of these revisions are to:

- remove material that may be interpreted as permitting the recognition of assets that would not otherwise meet the definition of an asset or the recognition criteria;
- include guidance to clarify the distinction between assets and expenses;
- include guidance on the definition of an intangible asset and the recognition of internally generated intangible assets; and
- withdraw section 3450, Research and Development Costs, as assets developed as a result of research and development activities would now be included within the scope of section 3064.

As a result of changes to these standards, deferred obtaining costs can no longer be classified as assets and these costs will be expensed as incurred. Based on preliminary estimates, the Company believes the impact on the income statement for 2007 is a reduction of net earnings of between \$2.0 million to \$2.8 million or \$0.19 to \$0.26 per share. The impact for 2008 is difficult to estimate at this time. The policy change will also require retroactive application for obtaining costs currently capitalized to the Company's balance sheet, resulting in an adjustment to opening retained earnings. The reduction to opening retained earnings is estimated to be between \$37 million to \$42 million.

### RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED JANUARY 31, 2008 COMPARED TO THE THREE MONTHS ENDED JANUARY 31, 2007

The data set forth herein should be read in conjunction with the Company's consolidated financial statements and accompanying notes included in the Company's 2007 Annual Report. Historical information provided is not necessarily indicative of the results to be expected in the future.

#### TOTAL COMPANY RESULTS

**Revenue** for the quarter ended January 31, 2008 was \$56.8 million compared to \$54.8 million for the quarter ended January 31, 2007. This represented an increase of \$2.0 million or 3.7%. Following is a breakdown of total revenue:

	2008		2007	
	\$Millions	% of Total	\$Millions	% of Total
Sales				
Cemetery	23.0	40.5	22.0	40.2
Funeral	29.8	52.5	29.0	52.9
	<u>52.8</u>	<u>93.0</u>	<u>51.0</u>	<u>93.1</u>
Investment and other income	4.0	7.0	3.8	6.9
	<u>56.8</u>	<u>100.0</u>	<u>54.8</u>	<u>100.0</u>

**Sales** increased by \$1.8 million or 3.6% in 2008 compared to 2007. Sales in the cemetery division increased by \$1.0 million or 4.7% and sales in the funeral division increased by \$0.8 million or 2.8%.

**Investment and other income** increased by \$0.2 million or 4.8% over 2007 as follows (in \$millions):

Cemetery care fund interest and dividends	0.1
Funeral and cemetery annuity and referral fees	0.1
Corporate interest and lease income	-
	<u>0.2</u>

**Operating expenses** increased by \$2.2 million or 5.3% over 2007. Cemetery division expenses increased by \$0.9 million or 4.2%, due mainly to increases in cost of sales, care and maintenance and reception centre expenses. Funeral division expenses increased by \$1.3 million or 6.5%, due mainly to increases in cost of sales, employee costs and facilities expenses.

**Corporate expenses** increased by \$0.3 million or 8.2% over 2007, due mainly to increases in stock based compensation and employee salaries. In the three months ended January 31, 2008, the expiration date of 15,500 options (three months ended January 31, 2007 – nil) was extended to January 10, 2008 since the original expiration date of December 17, 2007 occurred during a blackout period. These options were, therefore, effectively considered a new grant of stock options. The stock based compensation expense recognized in the three months ended January 31, 2008 as a result was \$0.1 million (three months ended January 31, 2007 – nil).

**Earnings before interest expense and income taxes (“EBIT”)** were \$9.0 million, which represented a decrease of \$0.5 million or 5.1% from 2007. The decrease was driven by the funeral division, which declined by \$0.5 million or 4.9% from 2007 due to an increase in expenses, which exceeded the increase in revenue. In addition, Corporate earnings were lower by \$0.3 million due to an increase in expenses of the same amount. Partially offsetting the decrease in the funeral and the corporate divisions was an increase in the earnings of the cemetery division of \$0.3 million or 9.4%, which mainly occurred as a result of increased sales.

**Interest expense** included interest on floating-rate bank term debt, a capital lease and the cost of the Company's interest rate swap contracts. Interest expense decreased by \$0.2 million or 16% to \$1.0 million in 2008 due to a lower weighted-average balance of long-term debt outstanding of \$17.1 million or 18.5% and a decrease of \$0.1 million in swap costs. The decrease occurred despite a higher average floating rate of interest of 5.5% compared to 5.1% in the first quarter of 2007. The overall weighted-average rate of interest on long-term debt for the period was 5.5% compared to 5.4% in 2007. The weighted-average long-term debt balance decreased due to repayments on the bank term loans in the third and fourth quarters of 2007. The proportion of fixed-rate debt to total debt at January 31, 2008 was 52% compared to 47% at October 31, 2007 and 48% at January 31, 2007.

**Income taxes** for the first quarter of 2008 resulted in an effective tax rate of 32.0% compared to 34.5% in the first quarter of 2007. The decrease in the effective rate of 2.5 percentage points was mainly due to a lower combined basic federal and provincial tax rate of 1.8 percentage points and a reduction of 0.8 of a percentage point due to future tax changes, compared to the increase of 0.6 of a percentage point due to future tax changes in 2007. These reductions were partially offset by the unfavourable impact of capital losses of 0.7 of a percentage point. The lower combined basic rate was due to a decrease in the federal rate and the elimination of the federal surtax effective January 1, 2008. The decrease in the rate as a result of future tax changes also primarily resulted from federal tax rate reductions.

**Net earnings and earnings per share** were \$5.4 million and \$0.51 per share in the first quarter of 2008 and the first quarter of 2007. While net earnings were consistent with 2007, net earnings in 2007 increased by \$1.0 million or 22.1% over the first quarter of 2006.

## **CEMETERY DIVISION**

**Cemetery sales** in the first quarter of 2008 increased by \$1.0 million or 4.7% over 2007 to \$23.0 million. Sales in the year, including finance charges and net of cancellation allowances, consisted of:

- \$8.5 million (2007 - \$7.8 million) of at-need sales of interment rights and deliveries of at-need merchandise and services
- \$7.8 million (2007 - \$7.9 million) of pre-need sales of interment rights; and
- \$6.7 million (2007 - \$6.3 million) of pre-need sales of merchandise and services, recognized when merchandise was delivered or services were performed, including income earned on related pre-need trust funds.

The following is a breakdown of the \$1.0 million increase in cemetery sales (in \$millions):

<u>At-Need</u>	
Interment rights	(0.1)
Merchandise	0.7
Services	<u>0.1</u>
	<u>0.7</u>
<u>Pre-Need</u>	
Interment rights	(0.1)
Merchandise	0.3
Services	<u>0.1</u>
	<u>0.3</u>
	<u>1.0</u>

The \$0.7 million or 21.2% increase in the delivery of at-need merchandise resulted from \$0.3 million higher sales of bronze memorials, \$0.3 million higher sales of upright monuments and \$0.1 higher sales of urns. The increase in sales of at-need bronze memorials was due to 6.3% higher contracts written in 2007 compared to 2006, which resulted in higher deliveries in the quarter, a 14.4% increase in contracts written in 2008 compared to the first quarter of 2007 and timing of delivery. The increase in at-need upright monument sales was due to an increase of 17.8% in contracts written in 2007 compared to 2006, which resulted in higher deliveries in the quarter, an increase of 28.7% in 2008 compared to the first quarter of 2007 and timing of delivery.

The increase in the delivery of pre-need merchandise of \$0.3 million or 7.2% occurred as follows (in \$millions):

Bronze memorials	0.2
Upright monuments	0.2
Bases	(0.2)
Vaults and liners	<u>0.1</u>
	<u>0.3</u>

Deliveries of upright monuments and bronze memorials (“markers”) can vary significantly from period to period since delivery is dependent on many factors, including, but not limited to:

- the timing of full payment by the customer;
- the amount of time it takes for customers to approve the manufacture and delivery of their marker;
- the amount of time it takes for orders to be submitted to the manufacturers;
- the amount of time it takes to manufacture the markers; and
- projects undertaken to contact customers and get markers manufactured and stored or installed.

In the first quarter of 2008, the number of interments performed by the Company decreased by 3.1% to 4,093 and the number of cremations increased by 2.5% to 3,873 compared to the first quarter of 2007. For comparative purposes, interments increased by 4.1% and cremations increased by 1.1% in fiscal 2007 as compared to fiscal 2006.

**Cemetery investment income** for the quarter increased by \$0.1 million or 5.7% over 2007 to \$2.5 million due mainly to an increase in care fund income of \$0.1 million or 6.0%. The increase in care fund income was due to a higher average balance in the funds of \$11.4 million or 7.2%. The annualized rate of return on the funds was 5.0% in both periods. Interest and dividend income on the care funds is recognized as earned in order to defray cemetery care and maintenance costs.

Interest and dividend income earned on pre-need cemetery merchandise and services trust funds increased by 1.2% to \$1.5 million in the first quarter of 2008. The higher average balance in the funds of \$10.3 million or 5.5% was partially offset by the effect of a decrease in the average rate of return from 3.3% to 3.2%. Interest and dividend income earned on the pre-need trust funds is deferred and recognized as sales revenue when the underlying merchandise is delivered or the service is performed.

**Cemetery expenses** for the first quarter of 2008 increased by \$0.9 million or 4.2% over 2007 as follows (in \$millions):

Cost of sales	0.3
Care and maintenance	0.2
Other	<u>0.4</u>
	<u>0.9</u>

The \$0.3 million or 2.9% increase in the cost of sales expense was due to the improvement in sales. The cost of sales percentage for 2008 was 46.2%, which was 0.8 of a percentage point lower than the cost of sales percentage for 2007, due mainly to mix of sales by product and branch. One significant change in mix was that crypt sales, which carry a higher cost of sales percentage, were lower than the first quarter of 2007 by \$0.3 million. In addition, a group sale in Quebec contributed a higher gross margin in the quarter due to a lower commission rate as well as a lower care funding rate.

Care and maintenance expenses increased by \$0.2 million or 4.2% due to higher employee costs and maintenance and supplies expenses. All other expense categories increased by \$0.1 million or less.

**EBIT** in the cemetery division increased by \$0.3 million or 9.4%, due mainly to increased sales.

### **FUNERAL DIVISION**

As at January 31, 2008, the Company wholly owned 91 funeral branch operations, four of which were classified as discontinued operations. Subsequent to January 31, 2008, the Company sold the assets of one funeral branch operation and agreed to sell the assets of two additional funeral branch operations, pursuant to a letter of intent.

**Funeral sales** in the first quarter of 2008 increased by \$0.8 million or 2.8% over the first quarter of 2007 to \$29.8 million. The increase in sales was due to an increase in the number of services of 0.6% and an improvement in the average sale per funeral service of 2.1%. The increase in the average sale per funeral service was the result of the Company's continued efforts to provide customers with value-added merchandise and services such as receptions, catering, custom printing and ancillary merchandise, as well as price increases.

Sales in the period consisted of:

- \$19.8 million (2007 - \$19.7 million) of at-need sales of funeral merchandise and services;
- \$9.9 million (2007 - \$9.2 million) from the fulfilment of funeral merchandise and services sales that were arranged on a pre-need basis; and
- \$0.1 million (2007 - \$0.1 million) of flower shop sales.

Pre-need funeral contracts written in the first quarter of 2008 increased by \$0.2 million or 2.1%. Pre-need funeral contracts written under the trust program represented 43.3% (2007 - 39.9%) of total contracts written, while contracts written under the group annuity program represented 56.7% (2007 - 60.1%).

**Investment and other income** in the funeral division increased by 4.1% to \$1.1 million in 2008 due to higher annuity fees. The higher annuity fees primarily resulted from a higher payout rate, which is based on the age of the customer and the payment terms.

Interest and dividend income earned on the pre-need funeral funds in the quarter decreased by 1.2% to \$1.9 million compared to the first quarter of 2007. The annualized rate of return on the funds was 3.3% for both periods and the average balance in the funds decreased by \$0.9 million or 0.4%. Interest and dividend income on the pre-need funeral funds is deferred and recognized as sales revenue when the underlying merchandise is delivered or the service is performed.

**Funeral expenses** in the first quarter of 2008 increased by \$1.3 million or 6.5% over 2007. A breakdown of the \$1.3 million increase in expenses by type of expenditure follows (in \$millions):

Cost of sales	0.3
Services	0.7
Facilities	0.2
Other	<u>0.1</u>
	<u>1.3</u>

The cost of sales increase was mainly due to the improvement in sales and mix of sales related to custom printing and services sales. The cost of sales percentage for the period was higher than 2007 by 0.5 of a percentage point at 16.6% due to mix of sales.

The increase in services expenses of \$0.7 million or 7.5% was mainly due to higher employee salaries and bonuses. Salaries were \$0.4 million higher in 2008 due to annual increases, incremental employees and market adjustments, while the \$0.1 million increase in bonuses was due to an under-accrual of bonuses in 2007.

The \$0.2 million or 9.7% increase in facilities expenses was mainly due to higher maintenance expenses, of which \$0.1 million was weather related.

**EBIT** in the funeral division decreased by \$0.5 million or 4.9% to \$9.2 million, due mainly to an increase in expenses, which exceeded the increase in revenue.

### **CORPORATE DIVISION**

**Corporate revenue**, consisting of rental income from leasing a portion of the Company's head office building and interest on the Company's bank accounts and a mortgage receivable, increased by 1.6% to \$0.4 million in the first quarter of 2008 due to bank interest income.

**Corporate expenses** increased by \$0.3 million or 8.2% in the first quarter of 2008 to \$3.8 million. The main contributors to the increase were a stock based compensation expense of \$0.1 million, higher salaries, wages and benefits of \$0.1 million or 5.9% as result of annual increases and incremental employees and a \$0.1 million increase in other various expenses. Excluding the impact of the stock based compensation expense, corporate expenses grew by 5.3%.

As a percentage of total Company revenue, corporate expenses increased to 6.7% in 2008 from 6.4% in 2007. This was attributable to an increase in revenue of 3.7% while corporate costs grew 8.2%. Excluding the impact of the stock based compensation expense, corporate expenses were 6.5% of revenue. For comparative purposes, corporate expenses as a percentage of revenue were 6.2% in fiscal 2007, 6.4% in fiscal 2006 and 6.7% in fiscal 2005.

### **CONSOLIDATED BALANCE SHEETS**

**Key financial indicators** for the balance sheets as at January 31, 2008, and October 31, 2007, were as follows:

	<b>January 31 2008</b>	<b>October 31 2007</b>
Current ratio	<b>3.53:1</b>	2.53:1
Working capital (in \$millions)	<b>70.86</b>	61.61
Debt to equity ratio	<b>0.35:1</b>	0.35:1
Long-term debt to EBITDA <sup>(1)</sup>	<b>1.63:1</b>	1.62:1
Interest coverage ratio <sup>(1)</sup>	<b>5.98:1</b>	5.88:1

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<sup>(1)</sup> Bank covenant: long-term debt to EBITDA must be less than or equal to 3.50 and interest coverage ratio must equal or exceed 3.25.

The current ratio and working capital increased by 1.00 and \$9.3 million respectively from October 31, 2007 to January 31, 2008. The improvements were due mainly to an increase in cash of \$4.7 million and a decrease in accounts payable and accrued liabilities of \$10.9 million, partially offset by a reduction in the mortgage receivable of \$6.8 million.

**Cash** increased by \$4.7 million mainly due to the collection of \$6.8 million on the repayment of the mortgage receivable, which was partially offset by payment of fiscal year end accruals such as bonuses, vacation pay, dividends and income taxes.

**Pre-need receivables and funds**, including the current portion thereof, decreased by \$1.7 million or 0.3% to \$496.9 million at January 31, 2008 compared to October 31, 2007. The \$1.7 million decrease was mainly due to a \$2.6 million withdrawal for deliveries in prior years, a \$0.7 million decrease in instalment accounts receivable due to a 1% decrease in the Goods and Services Tax rate as of January 1, 2008, and \$0.4 million in realized capital

losses due primarily to currency exchange. Excluding these items, and a \$0.8 million fair value gain, pre-need receivables and funds increased by \$1.2 million or 0.2%. This compared to a \$2.2 million or 0.5% increase in 2007 excluding a fair value gain of \$0.7 million. The smaller increase in 2008 was mainly due to higher withdrawals from the funds for current period deliveries of \$0.9 million.

**Cemetery care funds and non-controlling interests in cemetery care funds** increased by \$1.6 million or 0.9% in the first quarter of 2008, despite a reduction of \$0.1 million due to a fair value loss and \$0.8 million in realized capital losses due primarily to currency exchange. Excluding the fair value adjustment and realized capital losses, cemetery care funds increased by \$2.5 million or 1.5% due to deposits made to the funds as a result of at-need and pre-need cemetery interment right sales. This compared to an increase of \$3.3 million or 2.1% in the first quarter of 2007.

**Fixed assets** decreased by \$0.9 million or 0.5% in the first quarter of 2008 to \$186.6 million due to depreciation of \$2.6 million (2007 - \$2.5 million), offset by additions of \$1.7 million (2007 - \$1.6 million). Of the \$1.7 million in additions, \$1.0 million was spent on maintenance capital and \$0.7 million was spent on new initiatives. The only significant project in the period was the development of a reception centre in Windsor, Ontario, on which the Company spent \$0.3 million.

**Mortgage receivable** decreased by \$6.8 million due to the principal balance being repaid in the quarter in accordance with the terms of the agreement.

**Deferred obtaining costs and stored merchandise** increased by \$0.7 million or 1.0% in 2008 due to more pre-need contracts being written than being delivered in the quarter.

**Accounts payable and accrued liabilities** decreased by \$10.9 million or 32.9% as follows (in \$millions):

Trade accounts payables	3.6
Accrued liabilities	5.7
Other accounts payable	<u>1.6</u>
	<u>10.9</u>

The decrease in trade accounts payable was mainly related to lower payables for construction and development and trust funds and a lower volume of expense activity for the first quarter of 2008 compared to the fourth quarter of 2007. The decrease in accrued liabilities was largely related to a reduction in accrued bonuses, vacation pay and payroll. Other accounts payable decreased by \$1.6 million mainly due to a reduction in dividends and commissions payable of \$0.7 million and \$0.6 million respectively.

**Income taxes payable** decreased by \$1.1 million or 100%. The income taxes payable at October 31, 2007 of \$1.1 million represented the difference between accrued taxes for 2007 and tax instalments paid in the year, which were based on the lower earnings in 2006. As at January 31, 2008, income taxes were in a receivable position of \$0.1 million since the 2008 instalments, which were based on strong 2007 results, exceeded the income tax provision for the first quarter of 2008.

**Deferred revenue** at January 31, 2008 plus the non-controlling interests in pre-need funds, plus the accumulated benefit of the pre-need funeral group annuity funds excluded from the balance sheet was \$714.2 million compared to \$706.7 at October 31, 2007, an increase of \$7.5 million or 1.1%. Of the \$7.5 million increase, \$0.8 million was a fair value gain on the pre-need trust funds. The remaining increase was \$6.7 million or 0.9% (first quarter of 2007 - \$8.9 million or 1.3%) and represented deferral of revenue in the period in excess of amounts recognized upon delivery of merchandise and services.

**Non-controlling interests in pre-need funds** increased by \$2.4 million or 0.6% to \$416.9 million. Of the \$2.4 million increase, \$0.7 million was due to a fair value adjustment. The remaining increase of \$1.7 million or 0.4% was due to higher deferred merchandise and services contracts written compared to the amount of merchandise and services delivered to customers in the period.

**Other liabilities** increased by \$0.8 million or 6.8%. The \$0.8 million increase was due to a \$1.0 million fair value loss on the interest rate swap agreements, offset by lower GST and HST payable.

## CONSOLIDATED STATEMENTS OF CASH FLOWS

**Net cash used by operating activities of continuing operations** increased by \$1.0 million or 66.8% from the first quarter of 2007 due mainly to an increase in the net change in other operating balance sheet items (“net change”) of \$1.2 million.

The most significant items in the net change of \$1.2 million included:

- a net increase in cash used for accounts payable and accrued liabilities of \$4.8 million;
- a net decrease in cash used for income taxes payable of \$1.5 million;
- a net decrease in cash used for accounts receivable of \$2.5 million; and
- a net increase in cash used for other items of \$0.4 million.

The increase in cash used for accounts payable and accrued liabilities of \$4.8 million was mainly due to higher cash used for the payment of construction and development liabilities, higher trust fund payments, and higher payments for accrued bonuses, commissions and payroll expenses.

**Net cash provided by investing activities of continuing operations** was \$4.1 million, compared to cash used in 2007 of \$8.1 million, an increase in cash of \$12.2 million. The increase was mainly due to:

- \$6.8 million in proceeds received on repayment of the mortgage receivable in the first quarter of 2008;
- a \$4.0 million net change in pre-need funds, which was primarily due to \$2.6 million withdrawn from the funds for prior year deliveries;
- a \$1.7 million net change in cemetery care funds, which was primarily due to \$0.8 million in realized capital losses in the fund and lower deposits to the funds due to lower burial space sales in the quarter.

## LIQUIDITY

Based on historical cash inflows and outflows, management believes that cash on hand and future cash flow from operating activities are sufficient to sustain ongoing operations as well as the routine maintenance and orderly replacement of the Company’s fixed assets. The Company has no plans to borrow additional debt on its bank term loans in fiscal 2008 based on its current cash position, expected cash from operations and projected capital and burial space inventory expenditures.

## CAPITAL EXPENDITURES AND CEMETERY BURIAL SPACE INVENTORY

The following are projects on which the Company had expended significant funds prior to January 31, 2008 but that had not yet generated operating revenue.

**Glendale Memorial Gardens Mausoleum:** As at January 31, 2008, the Company had spent \$2.5 million on this project. The Company estimates that an additional \$17.3 million will be spent to complete this project and anticipates completing the project in fiscal 2009.

**Glen Oaks Memorial Gardens Mausoleum:** As at January 31, 2008, the Company had spent \$0.8 million on this project. The Company estimates that an additional \$2.1 million will be spent to complete the project and anticipates completing the project in fiscal 2008.

**Brampton Memorial Gardens Chapel and Reception Centre:** As at January 31, 2008, the Company had spent \$0.6 million on this project. The Company estimates that an additional \$6.2 million will be spent to complete the project and anticipates completing the project early in fiscal 2009.

The Company had committed to the following expenditures for capital and cemetery burial space inventory at January 31, 2008 (in \$millions):

Cemetery burial space inventory	6.7
Cemetery maintenance capital expenditures	0.5
New reception centres	0.4
Funeral maintenance capital expenditures	0.1
	<u>7.7</u>

The Company anticipates funding these expenditures from existing cash and cash from operations generated in 2008.

Following is the Company's planned capital and cemetery burial space inventory spending for the remainder of fiscal 2008 (in \$millions):

Maintenance capital expenditures	12.1
New initiatives	14.4
Cemetery burial space inventory	17.4
	<u>43.9</u>

Estimates of future capital and cemetery burial space spending may change positively or negatively depending on factors including, but not limited to, the availability of labour and materials, delays in the construction planning and approval process and future changes in the nature or details of the projects.

## **UNAUDITED QUARTERLY RESULTS**

	<b>Four Fiscal Quarters Ended January 31, 2008</b>			
	<b>Apr-30 (Q2)</b>	<b>Jul-31 (Q3)</b>	<b>Oct-31 (Q4)</b>	<b>Jan-31 (Q1)</b>
<b>Revenue (\$millions)</b>	<b>59.3</b>	<b>57.1</b>	<b>58.1</b>	<b>56.8</b>
<b>Net earnings from continuing operations (\$millions)</b>	<b>6.9</b>	<b>4.1</b>	<b>4.2</b>	<b>5.4</b>
<b>Net earnings (\$millions)</b>	<b>7.0</b>	<b>4.2</b>	<b>2.7</b>	<b>5.4</b>
<b>Basic and diluted earnings per share from continuing operations (\$) <sup>(1)</sup></b>	<b>0.65</b>	<b>0.39</b>	<b>0.39</b>	<b>0.51</b>
<b>Basic and diluted earnings per share (\$) <sup>(1)</sup></b>	<b>0.66</b>	<b>0.40</b>	<b>0.25</b>	<b>0.51</b>

	<b>Four Fiscal Quarters Ended January 31, 2007</b>			
	<b>Apr-30 (Q2)</b>	<b>Jul-31 (Q3)</b>	<b>Oct-31 (Q4)</b>	<b>Jan-31 (Q1)</b>
Revenue (\$millions)	55.1	52.9	55.2	54.8
Net earnings from continuing operations (\$millions)	6.2	4.2	4.6	5.4
Net earnings (\$millions)	6.4	4.2	4.2	5.4
Basic and diluted earnings per share from continuing operations (\$) <sup>(1)</sup>	0.59	0.39	0.43	0.51
Basic and diluted earnings per share (\$) <sup>(1)</sup>	0.61	0.39	0.39	0.51

Prepared in accordance with GAAP. All amounts are in Canadian dollars.

<sup>(1)</sup> All earnings per share figures presented are applicable to both Class A and Class B shares.

### **Revenue**

Seasonality was a factor contributing to an increase in revenue in the second quarter compared to the first quarter and a decrease in revenue in the third quarter compared to the second quarter both in 2007 and 2006. Seasonality also contributed to fourth quarter revenues, which were higher in both years compared to most other quarters.

Revenue in the second quarter of 2007 was affected by a 12.4% increase in funeral division sales compared to the second quarter of 2006, which was driven by an improvement in the number of services provided of 9.7%.

Revenue in the second quarter of 2006 was affected by an increase in the delivery of at-need cemetery merchandise and services of \$1.2 million, of which \$0.5 million was related to an administrative project.

### **Net Earnings From Continuing Operations and Earnings Per Share From Continuing Operations**

Net earnings from continuing operations and earnings per share from continuing operations in the fourth quarter of 2007 were low as a result of after-tax impairment provisions of \$0.7 million.

Net earnings from continuing operations and earnings per share from continuing operations in the third quarter of 2007 were low as a result of \$2.0 million in after-tax termination expenses that occurred in the cemetery, funeral and corporate divisions.

Net earnings from continuing operations and earnings per share from continuing operations in the second quarter of 2007 were positively affected by an improvement in sales in the funeral division.

Net earnings from continuing operations and earnings per share from continuing operations in the fourth quarter of 2006 were negatively affected by an increase in provisions for cancellation of pre-need merchandise and services of \$0.9 million after income taxes.

Net earnings from continuing operations and earnings per share from continuing operations in the second quarter of 2006 were higher due to an improvement in sales in both the cemetery and funeral divisions and positive adjustments to cost of sales in the cemetery division.

### ***Net Earnings and Earnings Per Share***

Net earnings and earnings per share did not vary significantly from net earnings from continuing operations and earnings per share from continuing operations in most of the reporting periods with the exception of the fourth quarters of 2007 and 2006, which were lower as a result of impairment provisions for discontinued operations of \$1.5 million and \$0.5 million respectively.

### **OUTSTANDING SHARES**

The Company has an unlimited number of Preferred Shares, Class A Voting Shares and Class B Non-Voting Shares authorized for issue. The Class A and Class B shares have identical rights and privileges, except that the Class A shares are voting. In certain circumstances, if an offer is made by the Company or a third party to purchase Class A shares from each holder in Ontario, each Class B share is convertible into one Class A share. At January 31, 2008, the Company had issued 2,525,497 Class A shares and 8,188,246 Class B shares for \$1.7 million and \$73.7 million respectively.

### **EVENTS AND UNCERTAINTIES**

#### ***Seasonality***

While the death care industry is fairly stable and predictable, the Company's at-need business and pre-need deliveries of some merchandise and services can be affected by seasonal fluctuations in the death rate. Death rates are generally higher in the winter months. The Company's pre-need cemetery sales of interment rights can also have seasonal fluctuations, whereby sales are generally lower in the winter and summer months.

### **DISCLOSURE CONTROLS AND PROCEDURES AND INTERNAL CONTROL OVER FINANCIAL REPORTING**

With respect to internal control over financial reporting, during the Company's most recent interim period, there were no changes in the Company's internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

***February 28, 2008***

**Arbor Memorial Services Inc.**  
**UNAUDITED CONSOLIDATED STATEMENTS OF EARNINGS**

<b>Three Months Ended January 31 (\$000)</b>	<b>2008</b>	<b>2007 <sup>(1)</sup></b>
<b>Revenue</b>		
Sales	52,829	50,988
Investment and other income (note 6)	4,040	3,854
	<b>56,869</b>	<b>54,842</b>
<b>Expenses</b>		
Operating	44,068	41,849
Corporate	3,814	3,524
	<b>47,882</b>	<b>45,373</b>
<b>Earnings before interest expense and income taxes</b>	<b>8,987</b>	<b>9,469</b>
Interest expense	1,039	1,237
<b>Earnings before income taxes</b>	<b>7,948</b>	<b>8,232</b>
Income taxes (note 9)	2,542	2,841
Net earnings from continuing operations	5,406	5,391
Net earnings from discontinued operations (note 10)	22	20
<b>Net earnings</b>	<b>5,428</b>	<b>5,411</b>

**Basic and diluted earnings per share (in \$)**

Basic and diluted earnings per share from continuing operations	0.51	0.51
Basic and diluted income per share from discontinued operations	-	-
<b>Basic and diluted earnings per share (in \$)</b>	<b>0.51</b>	<b>0.51</b>

<sup>(1)</sup> Certain figures provided for 2007 have been reclassified to conform with the current year's presentation - see note 10. In addition, lease income in the corporate division was reclassified from sales to investment and other income.

**UNAUDITED CONSOLIDATED STATEMENTS OF RETAINED EARNINGS**

<b>Three Months Ended January 31 (\$000)</b>	<b>2008</b>	<b>2007</b>
Retained earnings, beginning of period	137,488	118,886
Net earnings for the period	5,428	5,411
<b>Retained earnings, end of period</b>	<b>142,916</b>	<b>124,297</b>

See accompanying notes to the unaudited consolidated financial statements.

*Arbor Memorial Services Inc.*

**UNAUDITED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**

<b>Three Months Ended January 31 (\$000)</b>	<b>2008</b>	<b>2007</b>
<b>Net earnings</b>	<b>5,428</b>	<b>5,411</b>
<b>Other comprehensive income:</b>		
<b>Net change in gains (losses) on effective portion of derivatives designated as cash flow hedges net of income taxes of \$364 (2007- \$93) (note 5)</b>	<b>(643)</b>	<b>166</b>
<b>Net change in unrealized gains associated with available for sale securities of the pre-need trust funds (note 3)</b>		
Change in unrealized gains associated with available for sale securities of the pre-need trust funds, net of income taxes of \$286 (2007 - \$246)	<b>529</b>	<b>454</b>
Net change in unrealized gains associated with available for sale securities of the pre-need trust funds attributable to non-controlling interests and deferred revenue, net of income taxes of \$286 (2007 - \$246)	<b>(529)</b>	<b>(454)</b>
	<b>-</b>	<b>-</b>
<b>Net change in unrealized losses associated with available for sale securities of the cemetery care funds (note 4)</b>		
Change in unrealized losses associated with available for sale securities of the cemetery care funds, net of income taxes of \$26 (2007- \$168)	<b>(49)</b>	<b>(309)</b>
Net change in unrealized losses associated with available for sale securities of the cemetery care funds attributable to non-controlling interests, net of income taxes of \$26 (2007 - \$168)	<b>49</b>	<b>309</b>
	<b>-</b>	<b>-</b>
<b>Other comprehensive (loss) income</b>	<b>(643)</b>	<b>166</b>
<b>Comprehensive income</b>	<b>4,785</b>	<b>5,577</b>

**UNAUDITED CONSOLIDATED STATEMENTS OF ACCUMULATED OTHER COMPREHENSIVE LOSS**

<b>Three Months Ended January 31 (\$000)</b>	<b>2008</b>	<b>2007</b>
Accumulated other comprehensive income (loss), beginning of period	<b>88</b>	<b>(555)</b>
Other comprehensive (loss) income for the period	<b>(643)</b>	<b>166</b>
<b>Accumulated other comprehensive loss, end of period</b>	<b>(555)</b>	<b>(389)</b>

*See accompanying notes to the unaudited consolidated financial statements.*

**Arbor Memorial Services Inc.**  
**UNAUDITED CONSOLIDATED BALANCE SHEETS**

<b>In \$000</b>	<b>As at</b>	
	<b>January 31</b>	<b>October 31</b>
	<b>2008</b>	<b>2007</b>
<b>Assets</b>		
Current assets		
Cash	29,176	24,483
Accounts receivable (note 13)	19,176	18,715
Merchandise inventories	9,608	9,670
Prepaid expenses	825	1,395
Income taxes receivable	60	-
Mortgage receivable, current portion	-	6,750
Pre-need receivables, current portion (note 3)	39,146	40,088
Future income taxes, current portion	216	251
Assets related to discontinued operations, current portion (note 10)	698	631
	<b>98,905</b>	<b>101,983</b>
Pre-need receivables and funds (note 3)	457,764	458,473
Cemetery care funds (note 4)	171,918	170,315
Crypts and niches	22,226	22,162
Cemetery land	35,001	34,974
Fixed assets	186,628	187,537
Goodwill	51,168	51,168
Deferred obtaining costs and stored merchandise	74,385	73,666
Intangible and other assets	2,100	2,178
Future income taxes	3,720	4,230
Assets related to discontinued operations (note 10)	7,506	7,537
	<b>1,111,321</b>	<b>1,114,223</b>
<b>Liabilities</b>		
Current liabilities		
Accounts payable and accrued liabilities	22,259	33,187
Income taxes payable	-	1,088
Long-term debt, current portion (note 12)	5,184	4,087
Future income taxes, current portion	1,700	2,016
	<b>29,143</b>	<b>40,378</b>
Long-term debt (note 12)	70,042	71,142
Other liabilities	13,026	12,200
Deferred revenue	183,108	183,368
Non-controlling interests in pre-need funds	416,910	414,550
Future income taxes	5,628	6,163
Liabilities related to discontinued operations (note 10)	3,797	3,811
	<b>721,654</b>	<b>731,612</b>
Non-controlling interests in cemetery care funds	171,918	170,315
<b>Shareholders' equity</b>		
Share capital (note 7)	75,388	74,720
Retained earnings	142,916	137,488
Accumulated other comprehensive (loss) income	(555)	88
	<b>142,361</b>	<b>137,576</b>
	<b>217,749</b>	<b>212,296</b>
	<b>1,111,321</b>	<b>1,114,223</b>

See accompanying notes to the unaudited consolidated financial statements.

*Arbor Memorial Services Inc.*

**UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS**

<b>Three Months Ended January 31 (\$000)</b>	<b>2008</b>	<b>2007 <sup>(1)</sup></b>
<b>Cash provided by (used for)</b>		
<b>Operating activities</b>		
Net earnings from continuing operations	5,406	5,391
Add (deduct) items not affecting cash:		
Depreciation and amortization	2,654	2,494
Gain on disposal of assets	(9)	-
Future income taxes (note 9)	58	142
Stock based compensation	104	-
Net change in other operating balance sheet items (note 11)	(10,776)	(9,564)
<b>Net cash used by continuing operations</b>	<b>(2,563)</b>	<b>(1,537)</b>
<b>Net cash used by discontinued operations</b>	<b>(28)</b>	<b>(49)</b>
<b>Investing activities</b>		
Additions to fixed assets	(1,737)	(1,610)
Additions to cemetery land held for future development	(97)	(37)
Proceeds on disposal of assets	16	-
Proceeds from mortgage receivable payment	6,750	-
Change in pre-need funds	856	(3,105)
Change in cemetery care funds	(1,678)	(3,344)
<b>Net cash provided by (used for) continuing operations</b>	<b>4,110</b>	<b>(8,096)</b>
<b>Net cash provided by discontinued operations</b>	<b>32</b>	<b>15</b>
<b>Financing activities</b>		
Repayment of long-term debt	(3)	(174)
Dividends paid	(744)	(742)
Proceeds on exercise of stock options	564	-
Change in non-controlling interests in pre-need funds	1,679	2,999
Change in non-controlling interests in cemetery care funds	1,678	3,344
<b>Net cash provided by continuing operations</b>	<b>3,174</b>	<b>5,427</b>
<b>Net cash used for discontinued operations</b>	<b>(32)</b>	<b>(18)</b>
<b>Increase (decrease) in cash</b>	<b>4,693</b>	<b>(4,258)</b>
Cash, beginning of period	24,483	11,857
<b>Cash, end of period</b>	<b>29,176</b>	<b>7,599</b>
<b>Supplementary information</b>		
Income taxes paid	3,643	5,426
Interest paid	1,043	1,228

<sup>(1)</sup> Certain figures provided for 2007 have been reclassified to conform with the current year's presentation - see note 10.

*See accompanying notes to the unaudited consolidated financial statements.*

**Arbor Memorial Services Inc.**

**UNAUDITED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**Three Months Ended January 31, 2008 and 2007**

**1. BASIS OF PRESENTATION**

The accompanying unaudited interim consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles and are consistent with the accounting policies used to prepare the 2007 annual consolidated financial statements, except as otherwise noted herein. While management considers the interim disclosures presented to be adequate, these consolidated financial statements do not include all of the disclosures required for annual financial statements and should be read in conjunction with the Company's 2007 annual consolidated financial statements.

While the death care industry is fairly stable and predictable, the Company's at-need business and pre-need deliveries of some merchandise and services can be affected by seasonal fluctuations in the death rate. Death rates are generally higher in the winter months. The Company's pre-need cemetery sales of interment rights can also have seasonal fluctuations, whereby sales are generally lower in the winter and summer months.

**2. NEW DISCLOSURE REQUIREMENTS**

In 2006, the Canadian Institute of Chartered Accountants ("CICA") issued the following new disclosure requirements: Financial Instruments – Disclosures ("Section 3862"); Financial Instruments – Presentation ("Section 3863") and Capital Disclosures ("Section 1535"). The standards require prospective application and are effective for the Company's first quarter of fiscal 2008.

Section 3862, together with Section 3863, replaces Section 3861 and requires that disclosures be provided in the financial statements that enable users to evaluate the significance of financial instruments for the Company's financial position and performance as well as the nature and extent of risks arising from financial instruments and how the Company manages those risks. As a result of implementing this standard, the Company has included additional disclosure in note 12, long term debt, and note 13, accounts receivable.

Section 3863, together with Section 3862, replaces Section 3861 and is intended to enhance understanding of the significance of financial instruments to the Company's financial position, performance and cash flows. This section establishes standards for the presentation of financial instruments and non-financial derivatives related to the classification of financial instruments, from the perspective of the issuer, between liabilities and equity, the classification of related interest, dividends, losses and gains, and the circumstances in which financial assets and liabilities are offset. The presentation used by the Company in the 2007 annual consolidated financial statements met the requirements of the new accounting standard.

Section 1535 establishes standards for disclosing information about an entity's capital and how it is managed. The Section requires disclosure of information about the Company's objectives, policies and processes for managing capital and how it is meeting these objectives. As a result of implementing this standard, the Company has included additional disclosure in note 8 to these unaudited consolidated financial statements.

**3. PRE-NEED RECEIVABLES AND FUNDS**

	<u>January 31</u> <u>2008</u>	<u>October 31</u> <u>2007</u>
	(\$000)	
Cemetery trust funds	<b>201,323</b>	200,726
Funeral trust funds	<b>202,109</b>	202,277
	<b>403,432</b>	403,003
Instalment accounts receivable	<b>68,741</b>	70,351

Pre-need group annuity funds	<u>24,737</u>	25,207
	<b>496,910</b>	498,561
Less: current portion of instalment accounts receivable	<u>39,146</u>	40,088
	<b>457,764</b>	458,473

The consolidated balance sheets do not include pre-need funeral and cemetery contracts that will be funded by third-party insurers under group annuity programs, upon delivery of pre-need merchandise and services, where the Company is not the policyholder. At January 31, 2008, the accumulated benefit of all such contracts sold by the Company's sales counsellors was \$114.2 million (October 31, 2007 - \$108.8 million). In addition, the accumulated benefit of all such contracts sold by the Company's third-party insurer's licensed agents was \$3.5 million (October 31, 2007 - \$3.4 million).

The trust funds consisted of investments with fixed and floating interest rates, equity securities and bond and equity funds as follows:

	<u>Fair Value</u>		<u>Cost</u>	
	<u>January 31</u> <u>2008</u>	<u>October 31</u> <u>2007</u>	<u>January 31</u> <u>2008</u>	<u>October 31</u> <u>2007</u>
	(\$000)		(\$000)	
Cash	3,420	9,184	3,420	9,184
Term deposits	217,475	214,105	216,135	214,569
Bonds	130,210	125,466	129,486	126,326
Equities	22,934	25,345	17,664	17,341
Equity fund	29,393	28,903	28,251	27,922
	<u>403,432</u>	<u>403,003</u>	<u>394,956</u>	<u>395,342</u>

#### 4. CEMETERY CARE FUNDS

Cemetery care funds consisted of investments with fixed and floating interest rates and equity securities as follows:

	<u>Fair Value</u>		<u>Cost</u>	
	<u>January 31</u> <u>2008</u>	<u>October 31</u> <u>2007</u>	<u>January 31</u> <u>2008</u>	<u>October 31</u> <u>2007</u>
	(\$000)		(\$000)	
Cash and term deposits	10,614	8,430	10,614	8,430
Bonds	144,416	143,021	144,530	145,032
Equities	16,888	18,864	15,126	15,129
	<u>171,918</u>	<u>170,315</u>	<u>170,270</u>	<u>168,591</u>

#### 5. DERIVATIVE FINANCIAL INSTRUMENTS

As of January 31, 2008, the Company's use of interest rate swap agreements was limited to seven (October 31, 2007– six) interest rate swaps with a Canadian chartered bank, whereby the Company fixed a portion of its term loan financing at interest rates ranging from 4.28% to 6.2% plus a bank margin. At the end of the period, these swaps had a total notional amount of \$37.5 million (October 31, 2007 – \$33.3 million). Two of the swaps amortize quarterly on a straight-line basis. The swaps expire in 2008, 2009, 2012 and 2014. Total swaps and other fixed rate debt represented 52% (October 31, 2007 – 47%) of the total amount of long-term debt outstanding. Swap costs for the first quarter of 2008 were nil (first quarter of 2007 – \$0.1 million).

The fair value of the interest rate swaps is estimated as the discounted unrealized gain or loss calculated based on the market price at January 31, 2008, which generally reflects the estimated amount that the Company would receive or pay to terminate the contracts at the balance sheet date. The fair value of the swaps is provided to the Company by the chartered bank that is the counter-party to the transactions. The estimated fair value of the interest rate swaps was a loss of \$0.9 million (October 31, 2007 – gain of \$0.1

million). Losses due to non-performance by the counter-party are not anticipated due to their high credit standing.

All of the Company's interest rate swaps are designated as cash flow hedges. At January 31, 2008, the critical terms of the swaps did not match the terms of the underlying floating rate debt. Therefore, the hypothetical derivative method was used to perform a quantitative, retrospective and prospective assessment of the effectiveness of the swaps. This methodology involved regression analysis of historical interest rates for the floating rate portion of the swaps and historical interest rates for the underlying debt. The result of the analysis was that the fair value of the cash flows from the interest rates of the swaps was highly effective at offsetting the variability in cash flows from the interest rates of the underlying debt. Therefore, hedge accounting was used to record the swaps and related activity for the period.

## 6. INVESTMENT AND OTHER INCOME

	<i>Three Months Ended January 31</i>									
	<i>Pre-Need Cemetery Funds</i>		<i>Pre-Need Funeral Funds</i>		<i>Cemetery Care Funds</i>		<i>Other</i>		<i>Consolidated</i>	
	<i>2008</i>	<i>2007</i>	<i>2008</i>	<i>2007</i>	<i>2008</i>	<i>2007</i>	<i>2008</i>	<i>2007</i>	<i>2008</i>	<i>2007</i>
	<i>(\$000)</i>									
Realized earnings of funds:										
Interest and dividends <sup>(1)</sup>	<b>1,549</b>	1,530	<b>1,871</b>	1,894	<b>2,114</b>	1,994	-	-	<b>5,534</b>	5,418
Realized gains	-	1	-	3	-	6	-	-	-	10
Realized losses	<b>(52)</b>	(9)	<b>(297)</b>	(10)	<b>(825)</b>	(2)	-	-	<b>(1,174)</b>	(21)
Trust expenses	<b>(41)</b>	(39)	<b>(35)</b>	(35)	<b>(72)</b>	(70)	-	-	<b>(148)</b>	(144)
	<b>1,456</b>	1,483	<b>1,539</b>	1,852	<b>1,217</b>	1,928	-	-	<b>4,212</b>	5,263
Deferred revenue	<b>(12)</b>	(12)	-	-	-	-	-	-	<b>(12)</b>	(12)
Trust expenses classified as operating expenses	<b>41</b>	39	<b>35</b>	35	<b>72</b>	70	-	-	<b>148</b>	144
Non-controlling interests in funds	<b>(1,485)</b>	(1,510)	<b>(1,574)</b>	(1,887)	<b>805</b>	(23)	-	-	<b>(2,254)</b>	(3,420)
	-	-	-	-	<b>2,094</b>	1,975	-	-	<b>2,094</b>	1,975
Fee income	<b>425</b>	409	<b>1,130</b>	1,085	-	-	-	-	<b>1,555</b>	1,494
Other	-	-	-	-	-	-	<b>391</b>	385	<b>391</b>	385
	<b>425</b>	409	<b>1,130</b>	1,085	<b>2,094</b>	1,975	<b>391</b>	385	<b>4,040</b>	3,854

<sup>(1)</sup> Includes interest income of \$4.8 million (2007 - \$5.1 million)

## 7. SHARE CAPITAL

### **Authorized:**

Unlimited number of Preferred Shares  
 Unlimited number of Class A Voting Shares  
 Unlimited number of Class B Non-Voting Shares

### **Issued and outstanding:**

	<i>Number of Shares</i>		<i>Amount</i>	
	<i>January 31 2008</i>	<i>October 31 2007</i>	<i>January 31 2008</i>	<i>October 31 2007</i>
	<i>(\$000)</i>			
Class A Voting shares	<b>2,525,497</b>	2,525,497	<b>1,734</b>	1,734
Class B Non-Voting shares	<b>8,188,246</b>	8,164,246	<b>73,654</b>	72,986
	<b>10,713,743</b>	10,689,743	<b>75,388</b>	74,720

The Class A and Class B shares have identical rights and privileges, except that the Class A shares are voting. In certain circumstances, if an offer is made by the Company or a third party to purchase Class A shares from each holder in Ontario, each Class B share is convertible into one Class A share. The weighted-average shares outstanding at January 31, 2008 were 10,699,613 (January 31, 2007 – 10,595,243).

At January 31, 2008, there were nil options outstanding. During the three months ended January 31, 2008, 4,500 options, having an exercise price of \$23.50, expired and 24,000 options, having an exercise price of \$23.50, were exercised resulting in 24,000 Class B Non-Voting Shares being issued for cash proceeds of \$0.6 million, which was credited to share capital (three months ended January 31, 2007 – 45,000 options expired). Included in the share capital balance is contributed surplus of less than \$0.1 million related to expired options.

In the three months ended January 31, 2008, the expiration date of 15,500 fully vested options (three months ended January 31, 2007 – nil) was extended to January 10, 2008 since the original expiration date of December 17, 2007 occurred during a blackout period. These options were, therefore, effectively considered a new grant of stock options. The fair value of the options thereby granted was estimated at the effective date of the grant using the Black-Scholes valuation model with the following assumptions:

(i) risk free rate of interest	4.3%
(ii) expected option life	0.03 years
(iii) expected volatility	12.9%
(iv) expected dividend yield	nil%

The weighted-average fair value thereby calculated was \$7.53 per option and the stock based compensation expense recognized in the three months ended January 31, 2008 was \$0.1 million (three months ended January 31, 2007 – nil).

## 8. CAPITAL MANAGEMENT

The Company's objectives, when managing equity capital, are to invest in business opportunities that generate a return to shareholders that exceeds the Company's weighted-average cost of capital ("WACC") and to generate annual growth in earnings per share with a limited risk profile. Business investment opportunities are evaluated utilizing discounted cash flow models to ensure the rate of return, on a risk-adjusted basis, exceeds the WACC.

The WACC is calculated by determining the estimated cost of equity and debt, weighted by the proportions that the Company intends to employ. The Company calculates the cost of equity using the Capital Asset Pricing Model ("CAPM"). Under CAPM, the cost of equity is the sum of the risk-free rate (considered to be a 10-year Government of Canada bond) plus an equity risk premium multiplied by Beta. Beta is a measure of stock price volatility relative to the overall benchmark index. Arbor's Beta ranges from an estimate based on the average of the Beta factors for public companies in the same industry and 1.0 because there isn't sufficient trading volume in Arbor's stock to permit a meaningful estimate of Beta. The cost of debt is based on a ten-year swap rate plus a stamping fee, on an after-tax basis.

The Company's Board of Directors determines the level of dividend payments. To date, the strategy has been to maintain a nominal dividend policy on the premise that as long as the Company has investment opportunities whose returns exceed its WACC, it will use retained earnings and bank debt to finance these projects. If the Company has retained earnings remaining after financing all acceptable investment opportunities, those earnings would be distributed in the form of cash dividends.

The decision to repay outstanding debt is based on assessing current levels of cash in relation to expected cash that will be generated from operations and anticipated cash required for planned capital and burial space development projects in the remainder of the fiscal year. The Company has unused debt capacity in its bank loan that can be utilized when other investment opportunities arise.

When making decisions to borrow additional debt, the Company ensures that certain covenants still comply with the requirements within the bank loan agreements. In particular, the Company monitors the long-term debt to earnings before interest, taxes, depreciation and amortization ("EBITDA") ratio as well as the interest coverage ratio. The long-term debt to EBITDA ratio is calculated as the total long-term debt divided by earnings before interest expense and income taxes before deducting other income (expenses), interest, taxes, depreciation and amortization expenses. This ratio must be less than or equal to 3.50:1. The long-term debt to EBITDA ratio at January 31, 2008 was 1.63:1 (October 31, 2007 – 1.62:1). The interest coverage ratio must

equal or exceed 3.25:1. The interest coverage ratio at January 31, 2008 was 5.98:1 (October 31, 2007 – 5.88:1).

The Company also monitors capital levels on the basis of a debt to equity ratio. This ratio is calculated as total long-term debt (as shown in the balance sheet) divided by equity. Equity includes all components of shareholders' equity. During the first quarter of 2008, the Company's strategy, which was unchanged from 2007, was to maintain the debt to equity ratio at no higher than 1:1. The debt to equity ratio is measured and reported to the Board of Directors monthly. The Board of Directors approves changes to the share capital issued, as required. The debt to equity ratio at January 31, 2008 was 0.35:1 (October 31, 2007 – 0.35:1).

## 9. INCOME TAXES

### *Income tax expense:*

Income tax expense for the three months ended January 31 consisted of the following:

	<b>January 31 2008</b>	January 31 2007
	(\$000)	
Current tax expense	2,484	2,699
Future income tax benefit relating to the origination and reversal of temporary differences	124	142
Future income tax benefit resulting from change in tax rates	<b>(66)</b>	-
Income tax expense	<b>2,542</b>	2,841

### *Effective income tax rate:*

The reconciliation of the Company's effective income tax rate is as follows:

	<b>January 31 2008</b>	January 31 2007
	%	%
Combined basic federal and provincial income tax rate	32.4	34.2
Change in the basic tax rate resulting from:		
Dividends/RDTOH	<b>(0.8)</b>	(0.8)
Impact of future tax changes	<b>(0.8)</b>	0.6
Impact of capital losses	<b>0.7</b>	-
Meals and entertainment	<b>0.4</b>	0.4
Other items	<b>0.1</b>	0.1
Effective income tax rate	<b>32.0</b>	34.5

At January 31, 2008, the Company had \$4.4 million in unrecognized capital losses (October 31, 2007 – \$4.4 million), the benefit of which is unlikely to be realized.

## 10. DISCONTINUED OPERATIONS

In the fourth quarter of 2006, the assets of two funeral branch operations met the criteria for being classified as discontinued operations. The sale of one of these operations was completed in the fourth quarter of 2007 for net cash proceeds of \$0.9 million. The gain on the sale was \$0.1 million. In the fourth quarter of 2007, the assets of three additional funeral branch operations met the criteria for being classified as discontinued operations. For all four branch operations classified as discontinued at January 31, 2008, the Company is committed to a plan to sell the operations at a price that is likely to be realized within one year. The decision to sell these branches was based on continued under performance, despite measures undertaken to improve the performance, and increased competition in the marketplace.

Revenue associated with discontinued operations in the first quarter of 2008 was \$0.5 million (first quarter of 2007 – \$0.6 million) and pre-tax profit was less than \$0.1 million for both periods. The prior year comparative amounts in the statements of earnings, balance sheets and the statements of cash flows have been reclassified for the funeral branches identified as discontinued operations in the fourth quarter of 2007.

## 11. NET CHANGE IN OTHER OPERATING BALANCE SHEET ITEMS

	<u>January 31</u> <u>2008</u>	<u>January 31</u> <u>2007</u>
		(\$000)
Accounts receivable	(461)	(3,006)
Instalment accounts receivable	1,610	921
Deferred obtaining costs and stored merchandise	(719)	(887)
Accounts payable and accrued liabilities	(10,184)	(5,421)
Developed land, crypt and niche cost of sales	1,958	2,145
Additions to developed land, crypts and niches	(1,952)	(1,039)
Income taxes receivable/ payable	(1,148)	(2,623)
Deferred revenue	(394)	257
Other liabilities	(181)	359
Other changes	695	(270)
	<u>(10,776)</u>	<u>(9,564)</u>

## 12. LONG-TERM DEBT

Increases in interest rates would increase the interest cost of the Company's variable rate long-term debt and have an adverse effect on the Company's net income and earnings per share. Based on long-term debt at January 31, 2008, a 1% increase or decrease in the market interest rate could impact the Company's annual interest expense by approximately \$0.4 million (January 31, 2007 – \$0.5 million).

## 13. ACCOUNTS RECEIVABLE

The Company records a provision for uncollectible at-need accounts receivable. The balance at January 31, 2008 was \$1.4 million (October 31, 2007 – \$1.3 million). The amount written off against the provision in the three months ended January 31, 2008 was \$0.1 million (three months ended January 31, 2007 – \$0.2 million).

## 14. CONTRACTUAL COMMITMENTS

At January 31, 2008, the Company was contractually committed to capital and cemetery burial space inventory expenditures of \$7.7 million (October 31, 2007 – \$9.0 million).

## 15. SUBSEQUENT EVENTS

### ***Repayment of floating-rate bank term debt:***

Subsequent to January 31, 2008, the Company made a \$10.2 million repayment on its floating-rate bank term debt with surplus cash.

### ***Dispositions:***

Subsequent to January 31, 2008, the Company sold the assets of one funeral branch operation that was reported as a discontinued operation at January 31, 2008, for cash proceeds of \$0.7 million. The after-tax gain on the sale of these assets is estimated to be \$0.1 million. In addition, the Company agreed to sell the assets of two additional funeral branch operations, also reported as discontinued operations, for cash proceeds of \$1.8 million and \$0.3 million in vendor financing pursuant to a letter of intent. The after-tax loss on the sale of these assets is estimated to be \$0.1 million. The sale is expected to close in the second quarter of 2008.

## 16. SEGMENT DISCLOSURE

### Industry segments (\$000)

	<i>Cemetery</i>		<i>Funeral</i>		<i>Corporate</i> <sup>(2)</sup>		<i>Consolidated</i>	
	<i>2008</i>	<i>2007</i>	<i>2008</i>	<i>2007</i>	<i>2008</i>	<i>2007</i>	<i>2008</i>	<i>2007</i>
Sales <sup>(1)</sup>	<b>22,991</b>	21,953	<b>29,838</b>	29,035	-	-	<b>52,829</b>	50,988
Investment and other income <sup>(1)</sup>	<b>2,519</b>	2,384	<b>1,130</b>	1,085	<b>391</b>	385	<b>4,040</b>	3,854
Revenue	<b>25,510</b>	24,337	<b>30,968</b>	30,120	<b>391</b>	385	<b>56,869</b>	54,842
Depreciation and amortization <sup>(1)</sup>	<b>942</b>	841	<b>1,325</b>	1,294	<b>387</b>	359	<b>2,654</b>	2,494
Earnings (loss) before interest expense and income taxes <sup>(1)</sup>	<b>3,174</b>	2,900	<b>9,236</b>	9,708	<b>(3,423)</b>	(3,139)	<b>8,987</b>	9,469
Interest expense	-	-	-	-	<b>1,039</b>	1,237	<b>1,039</b>	1,237
Earnings (loss) before income taxes <sup>(1)</sup>	<b>3,174</b>	2,900	<b>9,236</b>	9,708	<b>(4,462)</b>	(4,376)	<b>7,948</b>	8,232
Identifiable assets <sup>(3)</sup>	<b>612,165</b>	609,638	<b>467,999</b>	469,870	<b>31,157</b>	34,715	<b>1,111,321</b>	1,114,223
Capital expenditures	<b>1,351</b>	1,061	<b>163</b>	481	<b>223</b>	68	<b>1,737</b>	1,610
Developed land, crypt and niche additions	<b>1,952</b>	1,039	-	-	-	-	<b>1,952</b>	1,039
Cemetery land held for future development additions	<b>97</b>	37	-	-	-	-	<b>97</b>	37
Pre-need contracts written	<b>16,399</b>	16,472	<b>12,268</b>	12,020	-	-	<b>28,667</b>	28,492

<sup>(1)</sup> Figures provided for 2007 have been reclassified to conform with the current year's presentation - see note 10. In addition, lease income in the corporate division was reclassified from sales to investment and other income.

<sup>(2)</sup> The corporate balances are provided principally to reconcile the reportable segments to consolidated results.

<sup>(3)</sup> Identifiable assets shown for 2007 are as at October 31.