

# MANAGEMENT'S DISCUSSION AND ANALYSIS

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*Unless otherwise indicated, this Management's Discussion and Analysis ("MD&A") of our financial results for the interim period ended December 31, 2007 is as at February 5, 2008. In this MD&A, "we", "our", and "us" refer to Manitoba Telecom Services Inc. ("MTS"). This interim MD&A should be read in conjunction with our interim consolidated financial statements and the discussion and analysis that accompanies our audited consolidated financial statements for the year ended December 31, 2006. This interim MD&A for the three and twelve months ended December 31, 2007 updates the information contained in our interim MD&As for the first, second and third quarters of 2007, and our 2006 annual MD&A.*

*This interim MD&A includes forward-looking statements and information (collectively, the "statements") about our corporate direction, business opportunities, financial objectives and future financial results and performance that are subject to risks, uncertainties and assumptions. As a consequence, actual results in the future may differ materially from any conclusion, forecast or projection in such forward-looking information. Examples of statements that constitute forward-looking information may be identified by words such as "believe", "expect", "project", "anticipate", "could", "target", "forecast", "intend", "plan", "outlook", and other similar terms. Factors that could cause anticipated opportunities and actual results to differ materially from those expected, and the material factors or assumptions that were applied in drawing a*

*conclusion or making a forecast or projection set out in such forward-looking statements, include, but are not limited to, the items identified in this interim MD&A under the "Risks and Uncertainties" and "Material Assumptions" sections, our interim MD&As for the first, second and third quarters of 2007, and our 2006 annual MD&A. We disclaim any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. Additional information relating to our company, including our Annual Information Form, is available on SEDAR at [www.sedar.com](http://www.sedar.com). Unless otherwise stated, all amounts are expressed in Canadian dollars.*

## NON-GAAP MEASURES OF PERFORMANCE

In this MD&A, we provide information concerning continuing operations, EBITDA and free cash flow because we believe investors use them as measures of our financial performance. These measures do not have a standardized meaning as prescribed by Canadian generally accepted accounting principles ("GAAP"), and are not necessarily comparable to similarly titled measures used by other companies.

- **Continuing Operations** – We provide information that refers to our performance from continuing operations to assist investors in understanding the performance of our company.

Continuing operations in 2007 include synergies, and exclude restructuring costs; certain tax recoveries; the retroactive adjustment related to Telecom Decision CRTC 2007-10 ("Decision 2007-10") in which the Canadian Radio-television and Telecommunications Commission ("CRTC") determined that we had been billed twice over the past several years for basic service extension features charges; the impact of changes in income tax rates on our tax asset; solvency funding to our pension plans; and a reduction to our tax asset valuation allowance and other adjustment.

Continuing operations in 2006 include synergies and exclude our directories business, which has been classified as discontinued operations; integration costs; the impact of changes in income tax rates on our tax asset; solvency funding to our pension plans; the retroactive adjustment related to the Band F Decision<sup>1</sup>; the adjustment related to the Direct Connect/Access Tandem Decisions<sup>2</sup>; the taxes recoverable related to the sale of our investment in Bell West Inc. (the "Bell West gain"); the gain on the sale of our discontinued operations; and the tax asset valuation allowance adjustment.

- **EBITDA** – We define EBITDA as earnings before interest, taxes, amortization, other income (expense) and discontinued operations. EBITDA should not be construed as an alternative to operating income or to cash flows from operating activities (as determined in accordance with Canadian GAAP) as a measure of liquidity.
- **Free Cash Flow** – We define free cash flow as cash flow from operating activities, less capital expenditures, and excluding changes in working capital. Free cash flow is the amount of discretionary cash flow that we have for purchasing additional assets beyond our annual capital expenditure program, paying dividends, buying back shares or retiring debt.

Notes:

<sup>1</sup> Band F Decision means Telecom Decision CRTC 2006-20 in which the CRTC approved the application of MTS Allstream Inc. (“MTS Allstream”) to review and vary the CRTC’s decision in *MTS Allstream’s application to review and vary certain decisions relating to its Band F subsidy*, Telecom Decision CRTC 2005-52

<sup>2</sup> Direct Connect/Access Tandem Decisions means *Aliant Telecom, Bell Canada, MTS Allstream, SaskTel and TCI – Approval of rates on a final basis for Access Tandem service*, Telecom Decision CRTC 2006-22 and *Aliant Telecom, Bell Canada, MTS Allstream, SaskTel and TCI – Approval of rates on a final basis for Direct Connection service*, Telecom Decision CRTC 2006-23

## OVERVIEW

MTS commenced its operations in the province of Manitoba in 1908, first as a department of the provincial government, and then as a Crown corporation that was incorporated in 1933. In 1997, the company was reorganized and continued as a publicly traded company. MTS’s common shares are listed on The Toronto Stock Exchange under the trading symbol MBT.

MTS is a leading national communications provider in Canada. The company is organized into two reportable operating segments, the Enterprise Solutions division and the Consumer Markets division. The company, which operates under two principal brands, MTS and Allstream, builds upon its unique combination of market leadership in Manitoba and agile competitive presence in business markets across Canada to deliver innovative telecommunications solutions that bring value to customers. MTS employs approximately 6,000 people.

### **Enterprise Solutions division**

The Enterprise Solutions division, which operates under the Allstream brand nationally and under the MTS brand in Manitoba, is a leading competitor in the national business and wholesale markets. This division offers customers a portfolio of solutions tailored to the needs of medium and large businesses looking for success in a world of rapidly evolving technology – Internet protocol (“IP”)-based

communications, unified communications, voice and data connectivity services. The Enterprise Solutions division operates an extensive national broadband fibre optic network that spans more than 24,300 kilometres, and provides international connections through strategic alliances and interconnection agreements with other international service providers. The division’s advanced services, combined with the impressive reach of a state-of-the-art network and continued leadership in technological innovation, have allowed the company to forge strong relationships with top national business customers across the country.

### **Consumer Markets division**

The Consumer Markets division leads every telecommunications market segment in Manitoba, delivering a full suite of next generation wireless, high-speed Internet and data, digital television and wireline voice services under the MTS brand, as well as security and alarm monitoring services through AAA Alarm Systems Ltd., a subsidiary of MTS which also operates in other western provinces. This complete range of products is unmatched by any other provider in Manitoba, and the digital television service offered to customers in Winnipeg is recognized as one of the leading North American digital television services. With this innovative combination of products and services, the company connects people, homes and businesses everywhere. In addition, the Consumer Markets division is a leading player in the national small business telecommunications market outside Manitoba, providing customers in major Canadian centres with a range of innovative business Internet, data and voice services under the Allstream brand.

## RESULTS OF OPERATIONS

### *Earnings Per Share (“EPS”) (\$)*

<i>three months ended December 31</i>	<i>2007</i>	<i>2006</i>	<i>% change</i>
<b>EPS (Continuing Operations)</b>	<b>0.62</b>	<b>0.57</b>	<b>8.8</b>
Discontinued Operations	--	2.78	n.m.
Effective Tax Rate Adjustment	(0.77)	--	n.m.
Tax Asset Valuation Allowance Adjustment	0.40	0.17	n.m.
Restructuring Costs	(0.03)	(0.34)	n.m.
<b>Basic EPS</b>	<b>0.22</b>	<b>3.18</b>	<b>n.m.</b>

Note: EPS for the three months ended December 31 is based on weighted average shares outstanding of 64.6 million for 2007, and 68.0 million for 2006.

EPS from continuing operations increased by 8.8% or \$0.05 to \$0.62 in the fourth quarter of 2007 and by 15.6% or \$0.39 to \$2.89 for the full year, as compared to the same periods

last year. In addition, we exceeded our guidance range for 2007. Double-digit growth in our growth services, which include wireless, converged IP, unified communications, digital television and high-speed Internet services, contributed to this solid performance. We are confident in our business strategy as we continue to see success in tight competitive markets, managing the technology migration to IP-based services by customers in our industry. In addition to these factors, the execution of our cost reduction initiatives contributed to our solid performance.

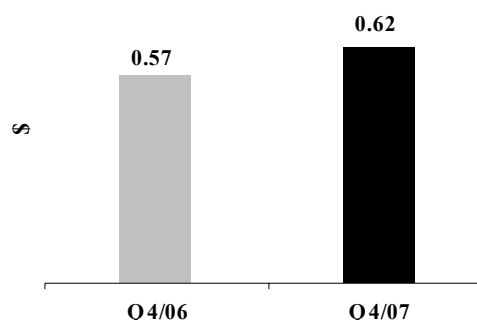
<i>twelve months ended December 31</i>	2007	2006	% change
<b>EPS (Continuing Operations)</b>	<b>2.89</b>	<b>2.50</b>	<b>15.6</b>
Reduction in Tax Asset Allowance	0.55	0.17	n.m.
Future Tax Rate Adjustment	(0.86)	(0.86)	0.0
Decision 2007-10	0.15	--	n.m.
Discontinued Operations	--	2.97	n.m.
Restructuring Costs	(0.12)	(0.53)	(77.3)
Retroactive Band F Decision	--	0.09	n.m.
Retroactive Direct Connect/Access Tandem Decisions	--	0.06	n.m.
<b>Basic EPS</b>	<b>2.61</b>	<b>4.40</b>	<b>(40.7)</b>

Note: EPS for the year ended December 31 is based on weighted average shares outstanding of 65.0 million for 2007, and 68.0 million for 2006.

In the fourth quarter of 2007, basic EPS decreased to \$0.22 from \$3.18 in the fourth quarter of the previous year. This decrease reflects a number of items that are not part of our continuing operations, including a non-cash future tax adjustment due to increases in statutory income tax rates. Also, the gain on the sale of discontinued operations is included in the fourth quarter of 2006 while restructuring costs and a positive adjustment from the tax asset allowance are included in the fourth quarters of 2006 and 2007.

Basic EPS for the year was \$2.61 in 2007 versus \$4.40 in 2006. As indicated in the table above, these increases reflect items that are not from continuing operations. For both 2006 and 2007, these include reductions in tax asset allowance, future tax rate non-cash adjustments due to decreases in statutory income tax rates, and restructuring costs. For 2006, items not from continuing operations include the gain on the sale of our discontinued operations, positive adjustments related to the retroactive Band F Decision and the retroactive Direct Connect/Access Tandem Decisions, and in 2007, the positive impact from Decision 2007-10 is included.

### EPS (Continuing Operations)



### EBITDA

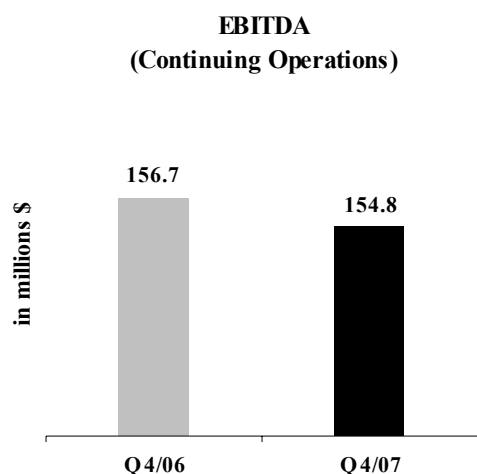
<i>(in millions \$)</i>	Q4/07	Q4/06	% change
<b>EBITDA (Continuing Operations)</b>	<b>154.8</b>	<b>156.7</b>	<b>(1.2)</b>
Restructuring Costs	(3.0)	(36.8)	(91.8)
EBITDA	151.8	119.9	26.6

<i>(in millions \$)</i>	YTD/07	YTD/06	% change
<b>EBITDA (Continuing Operations)</b>	<b>655.1</b>	<b>649.7</b>	<b>0.8</b>
Decision 2007-10	13.5	--	n.m.
Restructuring Costs	(11.9)	(56.8)	(79.0)
Retroactive Band F Decision	--	9.9	n.m.
Retroactive Direct Connect/Access Tandem Decisions	--	6.7	n.m.
EBITDA	656.7	609.5	7.7

EBITDA from continuing operations for the fourth quarter of 2007 slightly decreased to \$154.8 million as compared to the fourth quarter of 2006. Year to date EBITDA from continuing operations was up 0.8% to \$655.1 million in 2007 as compared to \$649.7 million in 2006. The strong performance of our growth services continued to drive this solid performance with significant revenue growth in wireless, unified communications, converged IP, digital television, and high-speed Internet services in combination with successful cost reduction initiatives.

In the fourth quarter of 2007, consolidated EBITDA increased by 26.6% to \$151.8 million as compared to \$119.9 million in the same period last year. This increase is primarily a result of lower restructuring costs in 2007.

Year to date consolidated EBITDA increased by 7.7% to \$656.7 million in 2007 versus \$609.5 million in the same period in 2006. This increase is a result of improvements from continuing operations, lower restructuring costs, and the net impact of positive regulatory adjustments associated with Decision 2007-10 received in 2007 versus positive regulatory adjustments relating to the Band F Decision and the Direct Connect/Access Tandem Decisions received in 2006.



## REVENUES

### Operating Revenues

<i>(in millions \$)</i>	Q4/07	Q4/06	% change
<b>Revenue (Continuing Operations)</b>	<b>489.2</b>	<b>479.1</b>	<b>2.1</b>
<b>Revenue</b>	<b>489.2</b>	<b>479.1</b>	<b>2.1</b>

<i>(in millions \$)</i>	YTD/07	YTD/06	% change
<b>Revenue (Continuing Operations)</b>	<b>1,906.6</b>	<b>1,916.5</b>	<b>(0.5)</b>
Retroactive Band F Decision	--	9.9	n.m.
Decision 2007-10	(0.8)	--	n.m.
<b>Revenue</b>	<b>1,905.8</b>	<b>1,926.4</b>	<b>(1.1)</b>

Consolidated revenues from continuing operations were \$489.2 million in the fourth quarter of 2007 and \$1,906.6 million year to date, representing an increase of 2.1% and decrease of 0.5%, respectively.

Revenues from our growth services continued with strong performance in the three-month and twelve-month periods ending December 31, 2007, and these revenues partially offset the decline in revenues from our legacy services. The impact of reduced network traffic from Rogers Communications Inc. ("Rogers") and AT&T Corp. ("AT&T") as they transition their business to their own networks is continuing with a decline of \$11.1 million in the fourth quarter or \$49.4 million for the year to date. If these revenues were excluded, our revenues would have grown by 4.8% in the fourth quarter, or by 2.3% for the year. As the proportion of our revenue that is derived from growth services increases, we expect that the impact of continuing migration from legacy-related services to next generation communications services to lessen, and lead to overall revenue growth in 2008.

We are pleased with the continuing solid performance of our Consumer Markets division and the steady improvements of our Enterprise Solutions division. In the fourth quarter of 2007, we experienced overall growth in our revenues from continuing operations without excluding the impact of the network migrations of Rogers and AT&T described above. The strengthening performance of our Enterprise Solutions division demonstrates the growing demand for this division's service offerings from Canadian business customers.

### Segmented Revenues (Continuing Operations)

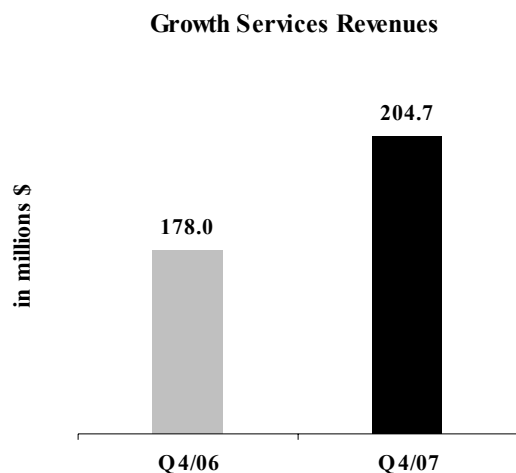
<i>(in millions \$)</i>	Q4/07	Q4/06	% change
Growth services	204.7	178.0	15.0
Legacy services	284.5	301.1	(5.5)
<b>Total</b>	<b>489.2</b>	<b>479.1</b>	<b>2.1</b>

<i>(in millions \$)</i>	YTD/07	YTD/06	% change
Growth services	759.5	674.3	12.6
Legacy services	1,147.1	1,242.2	(7.7)
<b>Total</b>	<b>1,906.6</b>	<b>1,916.5</b>	<b>(0.5)</b>

### Growth Services Revenues

Revenues from our growth services were up by 15.0% or \$26.7 million in the fourth quarter of 2007, and by 12.6% or \$85.2 million for the year, as compared to the same periods in 2006. Strong growth in wireless, converged IP, unified communications, digital television, and high-speed Internet services were the primary drivers of the double-digit growth in our growth services revenues in these periods.



### Legacy Services Revenues

As expected, our revenues from legacy services were down for the three and twelve months ended December 31, 2007, primarily resulting from the migration of communications traffic by Rogers and AT&T to their own networks. In 2007, legacy services revenues decreased by 5.5% or \$16.6 million to \$284.5 million in the fourth quarter, and by 7.7% or \$95.1 million to \$1,147.1 million for the year as compared to the same periods of the previous year. In addition, re-pricing and customer churn influenced year-over-year revenues. We are managing these impacts through targeted marketing strategies and successful service bundles. These strategies are already well in place, and are contributing to new and growing revenue streams by profitably accelerating our customer transition to growth services products.

### Operating Revenues (Continuing Operations)

(in millions \$)	Q4/07	Q4/06	% change
Wireless	68.7	61.1	12.4
Data	176.7	167.8	5.3
Local	133.4	134.2	(0.6)
Long Distance	90.2	97.3	(7.3)
Other	20.2	18.7	8.0
<b>Total</b>	<b>489.2</b>	<b>479.1</b>	<b>2.1</b>

(in millions \$)	YTD/07	YTD/06	% change
Wireless	269.1	234.1	15.0
Data	667.7	664.3	0.5
Local	533.3	546.2	(2.4)
Long Distance	358.3	401.6	(10.8)
Other	78.2	70.3	11.2
<b>Total</b>	<b>1,906.6</b>	<b>1,916.5</b>	<b>(0.5)</b>

Our operating revenues include those earned from the provision of wireless, data, local voice, long distance voice, and other services which include our digital television service.

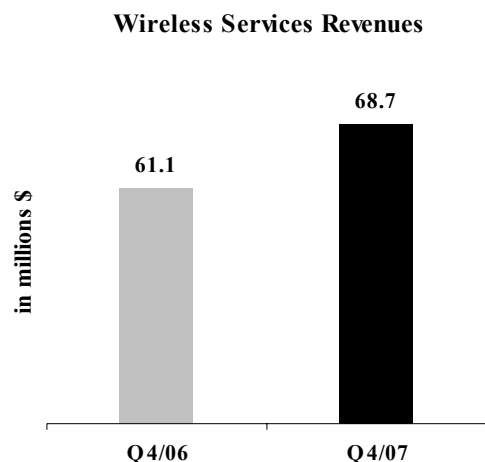
### Wireless Services

(in millions \$)	2007	2006	% change
Q4	68.7	61.1	12.4
YTD	269.1	234.1	15.0

Our wireless portfolio consists of cellular, wireless data, paging and group communications services that we offer in the Manitoba market.

Revenues from wireless services increased by 12.4% or \$7.6 million to \$68.7 million in the fourth quarter of 2007, and increased by 15.0% or \$35.0 million to \$269.1 million for the year, as compared to the same periods in 2006. Contributing to these significant increases are a larger year-over-year wireless subscriber base and increased average revenue per user ("ARPU"). As at December 31, 2007, our cellular customer base had grown by 11.0% to 394,463, while ARPU had increased by 4.2% to \$59.01, as compared to the same period last year. The strength of our wireless marketing programs are continuing to drive our subscriber additions and providing further momentum to our growth in new subscribers.

The increasing popularity of next generation wireless data services complemented by higher revenues from system access fees and roaming services continued to drive our ARPU throughout 2007. In 2007, our revenues from wireless data services grew by 89.5% year-over-year as our customers increasingly utilized such features as text messaging and Web browsing services.



### Data Services

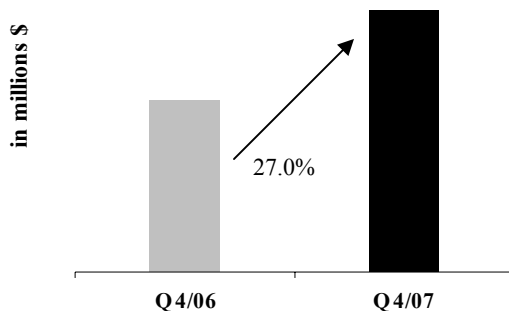
(in millions \$)	2007	2006	% change
Q4	176.7	167.8	5.3
YTD	667.7	664.3	0.5

Our data line of business includes revenues earned from providing data, Internet and professional services. Data services connect data, video and voice networks to establish private connections across office locations and to integrate traffic over highly secure networks. We provide a wide range of Internet connectivity services to meet the needs of residential customers in Manitoba and business customers across the country. We also offer numerous hosting and security services to business customers across Canada.

During the three months and year ended December 31, 2007, data services revenues increased by 5.3% or \$8.9 million to \$176.7 million and by 0.5% or \$3.4 million to \$667.7 million, respectively, as compared to the same periods last year. Contributing to these year-over-year increases is strong performance by our data growth services, which was offset partly by customers transitioning from legacy services to growth services, and by reduced traffic on our network from Rogers and AT&T. If the revenues of these two customers are excluded from our performance, our total revenues for the year would have shown an increase of 2.3%, which reflects growing attractiveness of our next generation products and services. We are achieving our desired results as customers are continuing to migrate to IP solutions that utilize our state-of-the-art IP multiprotocol label switching (“MPLS”) network and customer service capabilities.

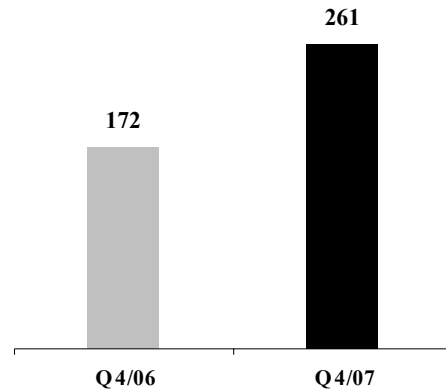
We experienced a strong year-over-year revenue increase of 27.0% in the fourth quarter and 17.2% for the year from our next generation data services, which include converged IP and unified communications services. Driving our strong overall growth in this segment were new additional customers and volume increases from business IP domestic MPLS, enterprise IP telephony (“IPT”), switched Ethernet, network resident IPT, and consumer high-speed Internet services.

#### Next Generation Data Services Revenues



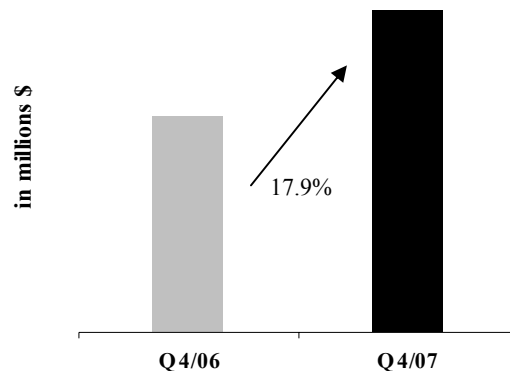
The capabilities of the suite of products offered by our Enterprise Solutions division continued to be demonstrated by strong growth in our IP-virtual private network (“IP-VPN”) customer base. As at December 31, 2007, we were supporting 261 customers, which is 51.7% more than last year.

#### IP-VPN Customers

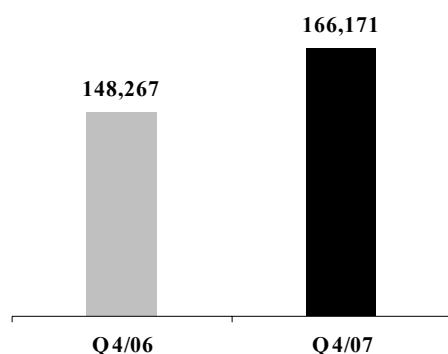


Our consumer Internet services revenue continued to grow, climbing 17.9% and 14.1% in the three and twelve months ended December 31, 2007. Contributing to these increases is continued growth in our consumer high-speed Internet customer base, which reached 166,171 customers as at December 31, 2007. In addition, price increases that were announced in the third quarter came into effect in the fourth quarter, and will provide additional growth to our revenues going forward.

#### Consumer Internet Services Revenues



### Consumer High-Speed Internet Services Customers



### Local Services

(in millions \$)	2007	2006	% change
Q4	133.4	134.2	(0.6)
YTD	533.3	546.2	(2.4)

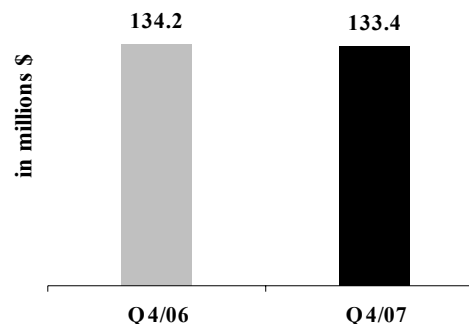
Local services revenues include basic voice connections for residential customers, including enhanced calling features (such as Call Answer, Call Display, Call Waiting, and 3-Way Calling), payphone revenue, wholesale revenues from services provided to third parties, as well as a full range of local services to business customers. These services allow customers to complete calls in their local calling areas and to access long distance, cellular networks and the Internet.

During the three and twelve months ended December 31, 2007, our revenues from local services declined by 0.6% or \$0.8 million to \$133.4 million, and by 2.4% or \$12.9 million to \$533.3 million, respectively, as compared to the previous year.

Competitive pressures continued to be felt in the Winnipeg, Manitoba market, and their impact is the primary cause of decreased revenues from local services. However, we believe that we have positioned ourselves for long-term success by bundling our residential service offerings such as wireless, Internet, digital television and alarm services. With these programs in place, we continued to deliver best in class performance against the cable company competitors. Consequently, the pace of our residential line losses has decelerated. In the fourth quarter of 2007, our residential line loss was less than 3,000 after adjusting for seasonal temporary disconnections of lines mainly from cottages and summer homes. Residential lines that are typically added each year in the second quarter and then are removed during the third or fourth quarters, account for our seasonal temporary disconnections of lines. The adjusted level of line loss in the fourth quarter not only is consistent with the levels of line loss we experienced in each of the prior three quarters of 2007 and the fourth quarter of 2006, but also demonstrates the success of our service bundle plans. Our customer connections, which include network access

services, high-speed Internet, wireless and digital television subscribers, increased by 3.6% as compared to 2006.

### Local Voice Services Revenues



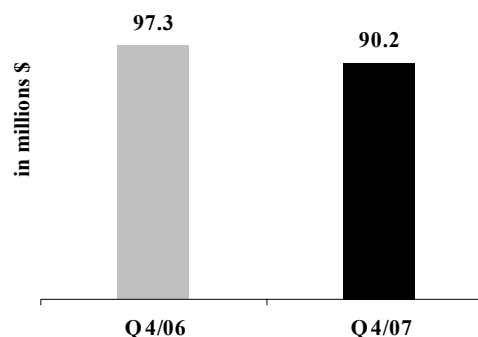
### Long Distance Services

(in millions \$)	2007	2006	% change
Q4	90.2	97.3	(7.3)
YTD	358.3	401.6	(10.8)

Long distance services enable residential customers in Manitoba and business customers across Canada to communicate with destinations outside the local exchange. Our long distance voice service portfolio includes basic, domestic, cross-border and international outbound long distance, basic and enhanced toll-free services, calling cards and audio conferencing, as well as a variety of enhanced long distance services and features.

Revenues from long distance services were \$90.2 million in the fourth quarter and \$358.3 million for the year, reflecting year-over-year decreases of 7.3% and 10.8% respectively. The effects of customer losses and competitive pricing on our Consumer Markets division were offset partially by increased calling card usage throughout the year. Lower cross-border, international and domestic rates, and lower domestic volumes and other revenues impacted the market segments serviced by our Enterprise Solutions division.

### Long Distance Services Revenues



## Other Revenues

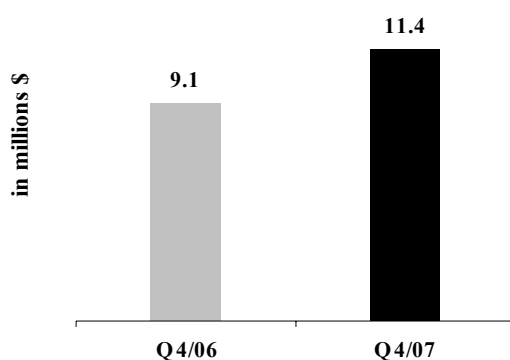
(in millions \$)	2007	2006	% change
Q4	20.2	18.7	8.0
YTD	78.2	70.3	11.2

Other revenues consist of revenues earned from our digital television and home security services, and miscellaneous items. Our digital television service is offered across our broadband network platform and is targeted at residential customers in Winnipeg. Miscellaneous revenues primarily consist of the sale and maintenance of terminal equipment.

Strong increases of 8.0% to \$20.2 million and 11.2% to \$78.2 million were experienced by other revenues in the three-month and twelve-month periods ending December 31, 2007, as compared to the same periods of 2006. Digital television services revenues continued to drive these increases to other revenues in the fourth quarter and throughout the year.

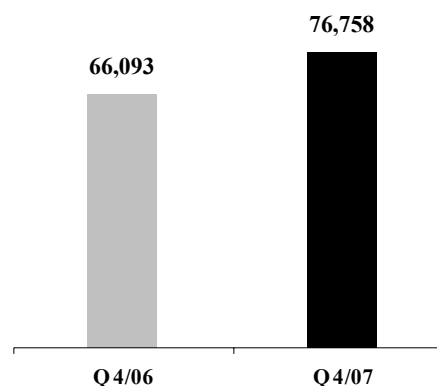
For the three and twelve months ended December 31, 2007, digital television services revenues increased by 25.3% to \$11.4 million and by 31.7% to \$42.4 million, respectively. These strong year-over-year increases in revenues were driven by increased revenues from our core television and video-on-demand services, which were complemented by pay-per-view and high-definition services revenues. We implemented increased pricing for our basic packages and specialty channels in the first quarter of 2007, which contributed to the increases in revenue from our core television services and an increase in average revenue per subscriber of 2.8% year-over-year to \$47.36.

## Digital Television Services Revenues



As at December 31, 2007, our subscriber base increased by 16.1% to reach 76,758, representing a 2% increase of market share. Our current share of the market is at 32%.

## Digital Television Services Customers



## OPERATING EXPENSES

### Operations Expense

(in millions \$)	2007	2006	% change
Q4	334.4	322.4	3.7
YTD	1,237.2	1,260.1	(1.8)

Operations expense in the three and twelve months ended December 31, 2007 increased by 3.7% or \$12.0 million, and decreased by 1.8% or \$22.9 million respectively, as compared to the same periods last year. The year to date decrease was impacted by a one-time net positive adjustment of \$14.3 million related to Decision 2007-10 which reflects the retroactive impact of a competitor service for which we had been double-billed by incumbent carriers, which was offset by the positive impact of the retroactive Direct Connect/Access Tandem Decisions in the amount of \$6.7 million in the second quarter of 2006.

We continue to focus on our cost reduction initiatives which contribute to these year-over-year decreases. Our 2007 efficiency program achieved \$41.6 million in annualized savings as at December 31, 2007, which is in line with our 2007 objective for expense savings of \$40 million to \$50 million with this program. Partly offsetting these savings were higher expenses from our growth operations.

### ***Restructuring and Integration Expenses***

<i>(in millions \$)</i>	2007	2006	% change
Q4	<b>3.0</b>	36.8	(91.8)
YTD	11.9	56.8	(79.0)

Restructuring expenses were \$3.0 million in the fourth quarter of this year as compared to \$36.8 million of integration expenses in the fourth quarter of 2006. For the year, restructuring and integration expenses were \$11.9 million, while in 2006, expenses were \$56.8 million.

We expected to achieve annualized expense savings of \$40 million to \$50 million in relation to our 2007 efficiency program. As at December 31, 2007, we have achieved \$41.6 million in annualized expense savings.

The costs of our 2007 efficiency program were expected to be \$30 million to \$40 million. As at December 31, 2007, total costs of \$45.2 million were incurred under this program, of which \$11.9 million was expensed in 2007 and \$8.5 million was expensed in 2006 relating to a workforce reduction element, and \$24.8 million was capitalized in 2007. We applied payments against the liability relating to the workforce reduction element of the program in the amount of \$3.7 million. This is outlined in Note 3 to our interim consolidated financial statements.

### ***Amortization Expense***

<i>(in millions \$)</i>	2007	2006	% change
Q4	<b>79.7</b>	85.7	(7.0)
YTD	318.7	330.6	(3.6)

Amortization expense in the fourth quarter of 2007 decreased to \$79.7 million as compared to \$85.7 million in the fourth quarter of 2006. For all of 2007, amortization expense decreased to \$318.7 million from \$330.6 million in 2006. These year-over-year decreases are due primarily to lower composite amortization rates and a reduction in the carrying value of intangible assets recorded as part of a future tax asset valuation adjustment in the fourth quarter of 2006.

### ***Other Income (expense)***

<i>(in millions \$)</i>	2007	2006	% change
Q4	<b>(0.5)</b>	2.1	n.m.
YTD	6.7	5.5	21.8

In the fourth quarter of 2007, other expense was \$0.5 million as compared to other income of \$2.1 million in the fourth quarter of 2006, and for the year, other income was \$6.7 million in 2007 versus \$5.5 million in 2006.

In the fourth quarter of 2007, other expense was higher by \$2.6 million due to the impact of interest expense related to a provincial sales tax audit, lower interest income and loss

on the sale of accounts receivable. For the year, other income was higher primarily due to increased interest income from short-term investments and gains from disposal of assets which were primarily offset by increased banking transactions.

### ***Debt Charges***

<i>(in millions \$)</i>	2007	2006	% change
Q4	<b>12.3</b>	14.3	(14.0)
YTD	51.7	60.6	(14.7)

In the fourth quarter, debt charges decreased to \$12.3 million from \$14.3 million, and for the year, decreased to \$51.7 million from \$60.6 million. These decreases resulted primarily from lower year-over-year long-term debt levels that were refinanced with short-term debt at a lower interest rate and temporary cash on hand.

Our debt to total capitalization ratio as at December 31, 2007 was 34.8%, and continues to provide us with financial strength and flexibility going forward.

### ***Income Tax Expense***

<i>(in millions \$)</i>	2007	2006	% change
Q4	<b>45.0</b>	(4.8)	n.m.
YTD	123.3	126.7	(2.7)

We are able to reduce our taxable income to zero without utilizing our substantial and growing capital cost allowance ("CCA") pools as a result of our acquisition of Allstream Inc. in 2004 along with its income tax loss carryforwards. Through the utilization of these loss carryforwards, followed by the utilization of our deferred CCA deduction, we project that we will not pay cash taxes before 2014.

When comparing our income tax expense in 2007 to 2006, an increase to \$45.0 million from (\$4.8) million occurred in the fourth quarter, while a decrease to \$123.3 million from \$126.7 million was experienced for the year. The increase in the fourth quarter in income tax expense is due to higher income before tax and the effect of federal rate reductions enacted in 2007, which were partially offset by reductions in the valuation allowance. Income tax expense for the year was lower primarily due to the \$38.5 million reduction we made in 2007 to our tax asset valuation allowance to reflect a higher forecasted taxable income, offset by adjustments related to changes in federal and provincial statutory tax rates of \$55.6 million in 2007 versus \$58.6 million in 2006.

## CONSOLIDATED QUARTERLY DATA

Unaudited quarterly financial data for our eight most recently completed quarters is presented below:

<i>(in millions \$, except earnings per share)</i>	<b>Q4 2007</b>	<b>Q3 2007</b>	<b>Q2 2007</b>	<b>Q1 2007</b>
Operating Revenues	489.2	475.9	474.1	466.6
Operating Income	72.1	82.5	92.2	91.2
Net Income before discontinued operations	14.3	45.5	57.0	52.9
Net Income	14.3	45.5	57.0	52.9
Earnings Per Share before discontinued operations	0.22	0.70	0.88	0.80
Diluted Earnings Per Share before discontinued operations	0.22	0.70	0.88	0.80
Earnings Per Share	0.22	0.70	0.88	0.80
Diluted Earnings Per Share	0.22	0.70	0.88	0.80
<i>(in millions \$, except earnings per share)</i>	<b>Q4 2006</b>	<b>Q3 2006</b>	<b>Q2 2006</b>	<b>Q1 2006</b>
Operating Revenues	479.1	477.9	489.0	480.4
Operating Income	34.2	69.8	95.1	79.8
Net Income (Loss) before discontinued operations	26.8	35.8	(6.2)	40.7
Net Income (Loss)	216.1	40.5	(1.2)	44.0
Earnings (Loss) Per Share before discontinued operations	0.39	0.53	(0.09)	0.60
Diluted Earnings (Loss) Per Share before discontinued operations	0.39	0.52	(0.09)	0.60
Earnings (Loss) Per Share	3.18	0.60	(0.02)	0.65
Diluted Earnings (Loss) Per Share	3.17	0.59	(0.02)	0.65

Our consolidated financial results for the eight most recently completed quarters reflect the ongoing performance of our business in the marketplace, as well as the following:

- The recognition of restructuring expenses for our 2007 efficiency program in each of the four quarters of 2007 in the amounts of \$3.9 million, \$2.7 million, \$2.3 million and \$3.0 million, listed chronologically, and the related workforce reduction initiative that we undertook in the fourth quarter of 2006 in the amount of \$8.5 million.
- The recording of amounts respecting a number of regulatory decisions: a \$5.0 million positive impact in the second quarter of 2007 and a \$9.9 million positive impact in the first quarter of 2007, which are related to Decision 2007-10; and a \$9.9 million retroactive positive impact from the Band F Decision and a \$6.7 million retroactive positive impact from the Direct Connect/Access Tandem Decisions, which both occurred in the second quarter of 2006.
- Adjustments in the amounts of \$12.8 million and \$25.7 million for reductions to our tax asset valuation allowance in the second and fourth quarters of 2007, respectively, and \$11.8 million for reductions to our tax asset valuation allowance in the fourth quarter of 2006.
- Effective October 2, 2006, we sold our directories business and recorded a net gain on the sale of discontinued operations of \$189.3 million in the fourth quarter of 2006.
- The recording of charges of \$6.0 million and \$58.6 million in the second quarters of 2007 and 2006, respectively, and \$49.6 million in the fourth quarter of 2007 to reflect decreases in the value of our income tax asset as a result of reductions in future income tax rates.
- The recognition of restructuring costs for our Transition Phase II cost reduction program in the first, second, third and fourth quarters of 2006 in the amounts of \$3.1 million, \$7.1 million, \$9.8 million and \$28.3 million, respectively. Included in the amount recognized in the fourth quarter of 2006 are costs associated with a workforce reduction initiative that was announced on October 2, 2006, which resulted in restructuring charges of \$19.0 million.

## LIQUIDITY AND CAPITAL RESOURCES

### Cash Flows from Operating Activities

<i>(in millions \$)</i>	2007	2006	\$ change
Q4	<b>172.8</b>	39.5	133.3
YTD	588.7	422.5	166.2

*Cash flows from operating activities refer to cash we generate from our normal business activities.*

Cash flows from operating activities for the three and twelve months ended December 31, 2007 increased by \$133.3 million to \$172.8 million, and by \$166.2 million to \$588.7 million, respectively, as compared to the same periods in 2006. The increase in the fourth quarter is due primarily to changes in working capital as a result of the utilization of our accounts receivable securitization program, higher consolidated EBITDA and lower pension solvency funding. The increase for the year is due primarily to lower pension solvency funding, changes in working capital as a result of the utilization of accounts receivable securitization program and higher consolidated EBITDA, which were offset partially by increased deferred wireless costs.

### Cash Flows used in Investing Activities

<i>(in millions \$)</i>	2007	2006	\$ change
Q4	<b>135.6</b>	38.7	96.9
YTD	323.0	221.5	101.5

*Investing activities represent cash used for acquiring, and cash received from disposing of, long-term assets and other long-term investments.*

In the fourth quarter of 2007, cash flows used in investing activities increased by \$96.9 million to \$135.6 million, and for the year, they increased by \$101.5 million to \$323.0 million, as compared to the same periods in 2006. Primarily driving this year-over-year increase is the sale of commercial real estate in Winnipeg, Manitoba, for which the proceeds were received in the fourth quarter of 2006, increased capital expenditures, which include \$24.8 million of capital that was spent as part of our restructuring and integration programs, and our acquisition of MCS-Multinet Communications Services Inc. in the fourth quarter.

### Free Cash Flow

<i>(in millions \$)</i>	Q4/07	Q4/06	% change
<b>Free Cash Flow (Continuing Operations)</b>	<b>10.1</b>	<b>37.6</b>	<b>(73.1)</b>
Pension Solvency Funding	(0.9)	(18.1)	95.0
Restructuring Expense	(3.0)	(36.8)	91.8
Restructuring Capital Expenditures	(12.0)	(8.0)	(50.0)
Tax Recovery	0.8	--	n.m.
Taxes on Bell West gain	--	4.1	n.m.
Consolidated Free Cash Flow	(5.0)	(21.2)	76.4

*Free cash flow refers to cash flow from operating activities, less capital expenditures, and excluding changes in working capital.*

Free cash flow from continuing operations decreased by 73.1% to \$10.1 million in the fourth quarter of 2007 as compared to the fourth quarter of 2006. This decrease is due primarily to higher capital expenditures in 2007 than in 2006, which was offset partly by decreased debt charges.

Consolidated free cash flow increased to (\$5.0) million in the fourth quarter of 2007 and includes items not from continuing operations as detailed in the table above and in Note 6 to our interim consolidated financial statements. Primarily reflected in this increase are lower pension solvency funding and lower restructuring expenses, which were partly offset by higher capital expenditures in the fourth quarter and lower tax recoveries.

<i>(in millions \$)</i>	<i>YTD/07</i>	<i>YTD/06</i>	<i>% change</i>
<b>Free Cash Flow (Continuing Operations)</b>	<b>258.5</b>	<b>287.1</b>	<b>(10.0)</b>
Decision 2007-10	14.9	--	n.m.
Pension Solvency Funding	(3.2)	(87.5)	96.3
Restructuring Expense	(11.9)	(56.8)	79.0
Restructuring Capital Expenditures	(24.8)	(9.9)	n.m.
Retroactive Direct Connect/Access Tandem Decisions	--	6.7	n.m.
Retroactive Band F Decision	--	9.9	n.m.
Taxes on Bell West gain	--	20.5	n.m.
Tax Recoveries	14.2	--	n.m.
Consolidated Free Cash Flow	247.7	170.0	45.7

*Free cash flow refers to cash flow from operating activities, less capital expenditures, and excluding changes in working capital.*

Free cash flow from continuing operations decreased by 10.0% to \$258.5 million in 2007 as compared to 2006. This decrease is the result of higher capital expenditures in 2007 than in 2006, and higher deferred wireless costs, which were offset partly by higher EBITDA from continuing operations and lower debt charges.

Consolidated free cash flow was \$247.7 million in 2007, as compared to \$170.0 million in the same period of 2006, and includes items not from continuing operations as detailed in the table above and in Note 6 to our interim consolidated financial statements. Primarily impacting the increase is decreased pension solvency funding and lower restructuring expenses, which were offset partly by lower restructuring charges.

### **Cash Flows used in Financing Activities**

<i>(in millions \$)</i>	<i>2007</i>	<i>2006</i>	<i>\$ change</i>
Q4	<b>41.8</b>	152.1	(110.3)
YTD	382.5	378.6	3.9

*Financing activities refer to actions we undertake to fund our operations through equity capital and borrowings.*

The decrease in the fourth quarter of 2007 for cash flows used in financing activities is due to our purchase for cancellation of 1,363,600 common shares for \$61.9 million under our normal course issuer bid, and the repayment of notes payable in the amount of \$47.0 million in 2006.

In 2007, we paid cash dividends of \$170.6 million, and repaid long-term debt in the amount of \$106.5 million. In

2006, we paid cash dividends of \$176.6 million, and repaid notes payable and long-term debt in the amount of \$108.0 million and \$48.1 million, respectively.

In December 2006, we announced a plan to purchase for cancellation approximately \$320 million worth of common shares through an Issuer Bid (the "Issuer Bid") using the proceeds from non-core assets to fund these buybacks. This Issuer Bid expired in December 2007. Prior to its expiry, we purchased \$172.9 million worth of shares for cancellation, representing more than half the amount permitted under the Issuer Bid.

We believe that it was prudent to have refrained from purchasing additional common shares for cancellation under the Issuer Bid until we have completed the evaluation of various opportunities, including a potential national wireless initiative, presented by the rapidly changing Canadian telecommunications landscape. Purchases of common shares under any new Issuer Bid will be made by us when we and our Board view such purchases to be the most appropriate use of our funds.

### **Credit Facilities**

<i>(in millions \$)</i>	<i>capacity*</i>	<i>utilized at December 31/07</i>
Medium Term Note Program	350.0	n/a
Commercial Paper	150.0	--
Accounts Receivable Securitization	150.0	43.0
Revolving Credit Facility	200.0	74.4
Total	850.0	117.4

\* As at January 18, 2008.

We have arrangements in place that allow us to access the debt and commercial paper markets for funding when required. Borrowings under these facilities typically are used to fund new initiatives, refinance maturing debt, and manage cash flow fluctuations.

We established our \$350 million medium term note ("MTN") program on January 18, 2008. In addition to our MTN program, we have credit facilities available in the amount of \$500.0 million, which consist of a fully back-stopped commercial paper program of \$150.0 million, an accounts receivable securitization program of \$150.0 million, and a \$200.0 million revolving credit facility. As at December 31, 2007, our commercial paper program was unutilized, while we utilized \$43.0 million of our accounts receivable securitization program, and \$74.4 million of our revolving credit facility, which represent undrawn letters of credit. Of this amount, \$52.5 million represents letters of credit issued under the new *Solvency Funding Relief Regulations* enacted under the *Pension Benefits Standards Act, 1985* (Canada), which permit the extension of pension solvency payments from a five-year amortization period to a 10-year amortization period for our defined benefit pension plans.

## Capital Structure

(in millions \$)	December 31/07	December 31/06
Bank Indebtedness	10.1	--
Long-term Debt	739.5	845.9
Shareholders' Equity	1,404.0	1,505.9
Total Capitalization	2,153.6	2,351.8
Debt to Capitalization	34.8%	36.0%

Our capital structure illustrates the amount of our assets that are financed by debt versus equity. Our debt to total capitalization ratio of 34.8% as at December 31, 2007 continues to represent excellent financial strength and flexibility.

## Credit Ratings

S&P – Senior debentures	BBB+
S&P – Commercial paper	A-2
DBRS – Senior debentures	BBB
DBRS – Commercial paper	R-2 (high)

Two leading rating agencies, Standard & Poor's ("S&P") and DBRS Limited ("DBRS"), analyze us and assign ratings based on their assessments. We have consistently been assigned solid investment grade credit ratings. DBRS confirmed our credit ratings on December 20, 2007 at "BBB" on our senior debentures and "R-2 (high)" on our commercial paper, and maintained its stable outlook. On December 17, 2007, S&P confirmed our credit ratings on our long-term corporate credit and senior unsecured debt of "BBB+", and our commercial paper of "A-2". The outlook remained unchanged at negative.

## Outstanding Share Data as at January 29, 2008

### Authorized:

- Unlimited number of Preference Shares of two classes issuable in one or more series
- Unlimited number of Common Shares of a single class

### Issued:

Shares	Number	Book Value (in millions \$)
Common	64,631,667	1,265.5

### Stock options:

Options	Number	Weighted Average Exercise Price Per Share
Outstanding	1,876,090	\$42.12
Exercisable	762,170	\$39.86

## Contractual Obligations, Financial Instruments, Off-Balance Sheet Arrangements, and Other Financial Arrangements

Our contractual obligations, financial instruments, off-balance sheet arrangements, and other financial arrangements remain substantially unchanged from those that were disclosed in our interim MD&As for the first, second and third quarters of 2007, and our 2006 annual MD&A. For additional details, please consult our interim MD&As for the first, second and third quarters of 2007, and our 2006 annual MD&A, which are available on our Web site at [www.mtsallstream.com](http://www.mtsallstream.com).

## CRITICAL ACCOUNTING ESTIMATES AND ASSUMPTIONS

Our critical accounting estimates and assumptions remain substantially unchanged from those that were disclosed in our interim MD&As for the first, second and third quarters of 2007, and our 2006 annual MD&A. For additional details, please consult our interim MD&As for the first, second, and third quarters of 2007, and our 2006 annual MD&A, which are available on our Web site at [www.mtsallstream.com](http://www.mtsallstream.com).

## CHANGES IN ACCOUNTING POLICIES, INCLUDING INITIAL ADOPTION

Our accounting policies, including initial adoption, remain substantially unchanged from those that were disclosed in our interim MD&As for the first, second and third quarters of 2007, and our 2006 annual MD&A. For additional details, please consult our interim MD&As for the first, second and third quarters of 2007, and our 2006 annual MD&A, which are available on our Web site at [www.mtsallstream.com](http://www.mtsallstream.com).

## RISKS AND UNCERTAINTIES

Our risks and uncertainties remain substantially unchanged from those that were disclosed in our interim MD&As for the first, second and third quarters of 2007, and our 2006 annual MD&A, except as noted below. For additional details, please consult our interim MD&As for the first, second and third quarters of 2007, and our 2006 annual MD&A, which are available on our Web site at [www.mtsallstream.com](http://www.mtsallstream.com).

### *Changes in Government Policy and CRTC Regulation*

The CRTC governs the telecommunications and broadcast industries in which we operate. We operate as both an incumbent local exchange carrier ("ILEC") in Manitoba and as a competitive local exchange carrier nationally. In addition, pursuant to Broadcasting Decision CRTC 2002-235, the CRTC granted us a Class 1 regional

broadcasting distribution licence to operate as a broadcasting distribution undertaking serving Winnipeg and the surrounding areas. Current regulatory proceedings and policy issues, which present significant risk and uncertainty on our business, are described below.

#### *Telecommunications Policy Review*

On March 22, 2006, the final telecommunications policy review report (“TPR Report”) of the Telecommunications Policy Review Panel was submitted to the federal Minister of Industry and released to the public. The TPR Report is substantial, including over 120 recommendations for modernization of the telecommunications policy framework in Canada. The Government of Canada began the process of responding to, and implementing portions of, the TPR Report by issuing a Policy Direction (the “Policy Direction”) to the CRTC on December 18, 2006. The Policy Direction calls on the CRTC to rely upon market forces to the greatest extent possible. As we and other competitive providers had requested, the Policy Direction requires the CRTC, as part of its current review of essential access by competitors to network infrastructure controlled by the ILECs, to take account of the principles of technological and competitive neutrality, the potential for incumbents to exercise retail market power absent competitor wholesale access, and the impediments faced by competitors in seeking to develop competing network facilities. We were participants in the proceeding that recently has concluded to review the definition of essential facilities.

The federal government also has made reference to the TPR Report in its announcement of a revised framework for local forbearance and in its consultation on the auction of spectrum licenses in the 2 GHz range, including advanced wireless services (“AWS”), both of which are referred to below. To date, the federal government has not disclosed its intentions with respect to further implementation of the recommendations in the TPR Report.

#### *Essential Facilities*

On November 9, 2006, the CRTC issued *Review of regulatory framework for wholesale services and definition of essential service*, Telecom Public Notice CRTC 2006-14. This is the first time since 1997 that a review of the definition of essential facilities has been undertaken. We have been active participants throughout this CRTC proceeding, including the hearing conducted by the CRTC in Gatineau, Quebec in October and November 2007. At the hearing and throughout the proceeding, we have argued that a robust essential facilities regime that provides competitors with cost-based access to next generation network facilities controlled by the former monopoly incumbents will spur innovation, investment and competitive benefit for the customer. We have emphasized to the CRTC that such a framework is also required to support the streamlined approach to retail deregulation adopted by the government. This proceeding concluded with final comments and reply submitted to the CRTC in early December 2007. A decision is expected in the first quarter of 2008.

#### *Deferral Account*

On February 16, 2006, the CRTC issued Decision 2006-9. In this decision, the CRTC determined that the funds accumulated in our deferral account should be used for certain reductions in rates for basic local residential services and for certain optional features; for the expansion of broadband services; and for initiatives to improve accessibility to telecommunications services for persons with disabilities. After using approximately \$5 million to fund the required rate reductions which came into effect on June 1, 2006, the estimate of the balance to be cleared from our deferral account for the remaining initiatives is approximately \$23.7 million. The final calculation of the balance to be cleared is dependent upon certain other CRTC proceedings.

Groups representing consumers and Bell Canada were each granted leave to appeal Decision 2006-9 by the Federal Court of Appeal (“FCA”). This appeal was argued in January 2008, and a decision is expected later in the year. As well, another company, Barrett Xplore Inc., had appealed this decision to the federal government and had made an application to the CRTC to review and vary its decision. However, both this appeal and the review and vary application were dismissed.

We have submitted proposals for broadband expansion and other initiatives for the CRTC’s consideration which meet the goals and objectives of Decision 2006-9, and which are consistent with our business goals. On November 30, 2006, the CRTC issued *Review of proposals to dispose of the funds accumulated in the deferral accounts*, Telecom Public Notice CRTC 2006-15. This public notice initiated a CRTC proceeding to review the proposals submitted by the ILECs. While the proceeding was underway, the CRTC issued Decision 2007-50 on July 6, 2007, which approved several of the proposals that we submitted for broadband expansion. On January 17, 2008, the CRTC issued Decision 2008-1 in which it approved the proposals we had submitted for roll out of broadband to 16 of 26 communities and approved our proposals for enhancement of accessibility measures. The CRTC directed that the remaining balance of the deferral account be rebated to our urban residential customers. On January 24, 2008, the FCA granted a stay with respect to Decision 2006-9 pending its consideration of the appeals. We await the decision of the FCA and are considering our rights of appeal of Decision 2008-1 in as much as the issues raised in the appeals are directly relevant to the determinations made by the CRTC in that decision.

#### *Local Forbearance*

On April 4, 2007, the federal government issued an Order in Council (“OIC”) which varies the forbearance framework previously established by the CRTC in *Forbearance from the regulation of retail local exchange services*, Telecom Decision CRTC 2006-15 (the “Forbearance Decision”).

The OIC purports to accelerate the deregulation of retail local telephone services offered by ILECs within their operating territories by substituting the market share test established by the CRTC with a test based on the presence of competitive infrastructure; narrowing the relevant geographic market for any forbearance determination; maintaining the requirement for satisfaction of competitor quality of service indicators with some modification; and ending restrictions on winback and marketing promotional activity by ILECs in their operating territories. In response to the OIC, we were among the first incumbents to be granted local forbearance in the Winnipeg residential market pursuant to Telecom Decision 2007-63 dated August 3, 2007. On November 7, 2007, we were also granted local forbearance in the Portage la Prairie residential market pursuant to Telecom Decision 2007-104. In December 2007, we also applied for residential forbearance in Southport, Manitoba. In a number of major urban markets across the country, the incumbents have been granted forbearance pursuant to the OIC.

#### *Basic Service Extension Feature (“BSEF”) Charges*

On February 15, 2007, the CRTC issued Telecom Decision CRTC 2007-10 in which it determined that the ILECs had been incorrectly applying BSEF charges to certain competitor digital network access services requested by competitors. The CRTC ordered that the ILECs cease applying these charges prospectively, and that they refund overbilled amounts. This decision will lower the network access costs of our Enterprise Solutions division going forward. We also have reciprocally refunded relevant BSEF charges that were charged by our Consumer Markets division to competitors.

#### *AWS Spectrum Consultation*

In February 2007, the federal government initiated a consultation on a framework to auction spectrum in the 2 GHz range, including AWS. We submitted comments in that consultation on May 25, 2007, and on June 27, 2007 we submitted reply comments. Our submissions identified the need for the federal government to adopt rules for the AWS spectrum auction that will allow the competitive entry of new national and regional wireless providers in Canada. In particular, we asked the federal government to designate two blocks of spectrum for new entrant bidding only, and to mandate commercially reasonable roaming and tower sharing on a non-discriminatory basis. In November 2007, the federal government issued its *Policy Framework for the Auction for Spectrum Licenses for Advanced Wireless Services and other Spectrum in the 2 GHz Range* (the “Policy Framework”) which was followed by the release of the *Licensing Framework for the Auction for Spectrum Licenses for Advanced Wireless Services and other Spectrum in the 2 GHz Range* (the “Licensing Framework”) in late December 2007. In both the Policy Framework and the Licensing Framework, the federal government clearly expressed the importance it places on encouraging new wireless entry and specifically decided to set aside 40 MHz of spectrum for new entrant bidding only, and to

mandate both in-region and out-of-region roaming as well as tower sharing, all on commercially reasonable terms. We are reviewing our options in light of the auction framework prior to the application deadline of March 10, 2008.

#### *Competition Policy Review*

On October 30, 2007, the Competition Policy Review Panel (the “Panel”) appointed by the federal government to review competition and investment policy in Canada, released a consultation paper entitled *Sharpening Canada’s Competitive Edge*. This consultation paper asks for submissions dealing with a range of issues concerning competition and investment policy, including the continued utility of foreign investment restrictions in the telecommunications industry and the state of competition policy in Canada. On January 11, 2008, we filed our submission and argued in favour of removal of the sector-specific foreign investment restrictions applicable to the telecommunications industry as well as for an updating of competition policy to deal with an increasingly deregulated telecommunications industry. In response to our submission, the Panel requested that we appear before them to comment further which we did on January 24, 2008. The Panel is expected to issue its report by the end of June 2008.

## **2008 OUTLOOK**

### ***Forward-looking statements disclaimer***

*This outlook includes forward-looking statements and information (collectively, the “statements”) about our corporate direction, business opportunities, financial objectives, and future financial results and performance that are subject to risks, uncertainties and assumptions. As a consequence, actual results in the future may differ materially from any conclusion, forecast or projection in such forward-looking information. Forward-looking statements reflect our expectations as at February 5, 2008. Examples of statements that constitute forward-looking information may be identified by words such as “believe”, “expect”, “project”, “anticipate”, “could”, “target”, “forecast”, “intend”, “plan”, “outlook”, “pending”, and other similar terms. Factors that could cause actual results to differ materially from those expected, and the material factors or assumptions that were applied in drawing a conclusion or making a forecast or projection set out in such forward-looking statements, include, but are not limited to, the items identified in this interim MD&A, our interim MD&As for the first, second and third quarters of 2007, and our 2006 annual MD&A. We disclaim any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. Additional information relating to our company, including our Annual Information Form, is available on SEDAR at [www.sedar.com](http://www.sedar.com). This outlook and the financial information contained herein have been reviewed by our Audit Committee.*

Factors that could cause anticipated opportunities and actual results to differ materially include, but are not limited to, the intensity of competitive activity from both traditional and new competitors (competitive conditions); the ability to retain major customers (customer relationships); decisions by the federal regulator that affect our ability to compete effectively or to enter into new business opportunities (developments in federal regulation); general economic and market conditions and the level of consumer confidence and spending, and the demand for, and prices of, our products and services (market conditions and economic fluctuations); the ability to manage labour relations effectively (collective agreements); the ability to anticipate, and respond to, changes in technology (technology); and other risk factors listed from time to time in our comprehensive public disclosure documents, including our 2006 Annual Report and in other filings with the Canadian securities regulatory authorities.

For further information, refer to the "Risks and Uncertainties" sections in this interim MD&A, our interim MD&As for the first, second and third quarters of 2007, and our 2006 annual MD&A.

Our financial outlook from continuing operations, as detailed below, remains unchanged since originally announced on December 7, 2007.

### **2008 Financial Outlook - Continuing Operations**

Revenues	\$1.920 billion to \$1.980 billion
EBITDA	\$660 million to \$680 million
EPS	\$2.95 to \$3.15
Free Cash Flow	\$250 million to \$280 million
Capital Expenditures	14% to 15% of revenues

Looking beyond 2007, we expect consolidated revenue and EBITDA growth in the range of 1% to 3% for 2008 and into the near future.

#### ***A Sharpened Strategic Focus***

We have a unique position in the Canadian communications services industry. We are the leading full-service communications provider in Manitoba, and have a leading presence in national enterprise markets.

We are building on our unique combination of market leadership in Manitoba and agile competitive presence in business markets across Canada to deliver innovative telecommunications solutions that bring value to customers. Following a thorough strategic business review in 2006, we have been pursuing opportunities to increase our focus on serving the national mid-market and small business segments. Our mid-market strategy is centred on the

availability of our market-leading IP network in major urban centres. Together, our new initiatives are forecasted to achieve \$200 million of incremental revenues by 2010.

In our Consumer Markets division, where local competition has intensified, our emphasis will be on growth products and bundles in areas such as high-speed Internet, wireless and digital television services. Our goal is to maintain our position as the one-stop provider of clear choice to Manitoba households and consumers by delivering double-digit growth in our Internet, digital television and wireless services in 2008 in a more competitive and deregulated market. In August, we were forborne in the local market in Winnipeg, which has enhanced our ability to compete against new market entrants.

In our Enterprise Solutions division, we will build on our established leadership in advanced IP, MPLS solutions and unified communications services. As part of this new strategy, we will strive to reduce our direct costs through the migration of customers to our network, and we will continue to improve our productivity and cost structure. From a growth perspective, revenues from our IP connectivity and unified communications product lines are forecasted to grow at double-digit rates.

#### ***Material Assumptions***

We have made a number of assumptions in preparing our outlook and making certain other forward-looking statements, including, but not limited to, the following assumptions:

##### ***Economic Assumptions***

The general economic activity in the national and regional markets in which we operate influences our performance. Consistent with the Manitoba Finance Survey of forecasts, which includes the Conference Board of Canada, we assumed a growth rate of approximately 3% for gross domestic product for the Manitoba and national markets.

##### ***Market Assumptions***

As competition in the overall marketplace escalates, the broad market segment trends that have taken shape in recent years also will persist in 2008. Growth in service areas such as wireless, Internet, digital television, converged IP and unified communications for business customers is expected to continue at similar levels in 2008. The competitive pressure experienced in traditional legacy services, which include data connectivity, and local and long distance services, will continue in similar trends as it did in 2007. Likewise, we anticipate that customer demand will continue to migrate to next generation services. To face continued strong competition in business markets, we are refining our market focus, creating innovative IP solutions, reducing our cost structure, and investing selectively in high-margin opportunities. Although competition from an incumbent cable operator is expected to continue in the Manitoba residential market, we are confident that we have

prepared our operations and strategies prudently to counter these threats. Through our broadband network initiative and our residential service offerings, which include local and long distance, wireless, Internet, digital television and alarm services, we believe that we are well-positioned to compete successfully.

#### *Financial and Operational Assumptions*

We have made the following financial and operating assumptions with respect to the forward-looking information in this outlook:

- double-digit growth for growth services, to represent approximately 45% of total revenue in 2008 as compared to 40% in 2007; and
- overall revenue growth of 1% to 3%.

We have future tax assets resulting from net operating loss carryforwards, which, to the extent utilized, will reduce future taxable income. As such, we do not expect to pay any cash taxes on earnings from operations in 2008.

#### *Cost Reduction Assumptions*

Key to our operating and financial progress will be our restructuring activities. We expect to achieve further cost reductions in 2008 of between \$20 million and \$30 million. To capture these additional savings, we expect to incur further restructuring costs of approximately \$10 million in 2008. These costs are not included in our 2008 outlook from continuing operations.

#### *Liquidity and Capital Resources Assumptions*

Our operations historically have delivered strong cash flows, and we expect this positive trend to continue in 2008. We will continue to invest in our core operations with a focus on our growth products and services to ensure success in the markets in which we operate. Significant investments have been made in modernizing our network infrastructure both in Manitoba and nationally. In 2005, we saw the completion of a five-year, \$300 million broadband expansion program in Manitoba, which positions our network capabilities second to none in Canada. These investments, in addition to the investment choices we are making nationally, are placing us in a favourable position in terms of capital requirements going forward. In 2008, our capital program is expected to comprise 14% to 15% of our revenues.

Our cash requirements for 2008 include two non-recurring obligations. These consist of approximately \$10 million for restructuring programs in 2008. Based on January 1, 2007 valuations, our pension solvency funding expectation for 2008 is approximately \$25 million. From a 2008 cash flow perspective, we anticipate funding all of our requirements, including quarterly dividend payments, capital expenditures, restructuring costs and all pension contributions, from operations with no incremental borrowings.

#### ***AWS Spectrum Auction***

In late November, Industry Canada announced the much anticipated AWS spectrum auction rules, and set the auction date for May 2008.

Based on a preliminary review, we believe that the rules will permit a new entrant to be competitive with significantly less committed capital than assumed in the past. Rules regarding mandated roaming, tower and rooftop sharing and license acquisitions, in addition to improvements in the technology and pricing for wireless network equipment, make it a considerably different environment for new entrants from that of the late 1990s.

We believe that the opportunity for a wireless expansion is significant and has the potential, under the right circumstances, to create meaningful long-term value for our shareholders. We will not make any decisions about whether or how to proceed until we have completed our analysis and discussions with potential partners regarding the range of strategies available for entry, and strategies that will respect the interests of all shareholders.

Opportunities to partner with financial and/or strategic players, as well as collaboration with other new entrants, also open up a range of potential strategies for bringing forward a compelling customer value proposition which makes sound business and financial sense.

## **FIRST QUARTER DIVIDEND**

The Board of Directors of MTS today declared a quarterly cash dividend of \$0.65 per share. The first quarter dividend is payable on April 15, 2008 to shareholders of record at the close of business on March 17, 2008.

The first quarter dividend is designated as an “eligible” dividend under the *Income Tax Act* (Canada) and any corresponding provincial legislation. Under this legislation, individuals resident in Canada may be entitled to enhanced dividend tax credits which reduce income tax otherwise payable.

Notes:

1. Supplementary financial information is available in the Investors section of the MTS Web site at [www.mtsallstream.com](http://www.mtsallstream.com).
2. MTS's fourth quarter 2007 conference call with the investment community is scheduled for 4:00 p.m. Eastern time on February 5, 2008. The dial-in number is 1-800-733-7560. A live audio Webcast of the investor conference call can be accessed by visiting the Investors section of the MTS Web site ([www.mtsallstream.com](http://www.mtsallstream.com)). A replay of the conference call will be available until midnight February 15, 2008 and can be accessed by dialing 1-877-289-8525 or 1-416-640-1917 (access code 21257662#). The audio Webcast will be archived on MTS's Web site.

*This interim MD&A contains forward-looking statements and there are risks that actual results may differ materially from those contemplated by these forward-looking statements. Forward-looking statements reflect our expectations as at February 5, 2008. Additional information on these risks can be found in our filings with the Canadian securities regulatory authorities. We disclaim any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. This interim MD&A, and the financial information contained herein have been reviewed by our Audit Committee and approved by our Board of Directors.*

*In addition, investors should read the forward-looking statements disclaimer in the "2008 Outlook" section for the various factors, including economic, competitive, regulatory and company-specific, that could cause actual future financial and operating results to differ materially from the forward-looking information in this interim MD&A.*

#### ***About Manitoba Telecom Services Inc.***

*Manitoba Telecom Services Inc. is one of Canada's leading national communication solutions providers, delivering innovative products and services through its Enterprise Solutions and Consumer Markets divisions. The Enterprise Solutions division, which operates under the Allstream brand nationally and under the MTS brand in Manitoba, is a leading competitor in the national business and wholesale markets. This division offers customers a portfolio of solutions tailored to the needs of medium and large businesses looking for success in a world of rapidly evolving technology – Internet protocol-based communications, unified communications, voice and data connectivity services. The Consumer Markets division leads every telecommunications market segment in Manitoba, delivering a full suite of next generation wireless, high-speed Internet and data, digital television and wireline voice services under the MTS brand, as well as small business services across Canada under the Allstream brand, and security and alarm monitoring services through a subsidiary AAA Alarm Systems Ltd., which also operates in other western provinces. The company's extensive national broadband fibre optic network spans more than 24,300 kilometres, and provides international connections through strategic alliances and interconnection agreements with other international service providers. Manitoba Telecom Services Inc.'s common shares are listed on The Toronto Stock Exchange (trading symbol: MBT). For more information, please visit: [www.mtsallstream.com](http://www.mtsallstream.com).*

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**MANITOBA TELECOM SERVICES INC.**  
**CONSOLIDATED STATEMENTS OF NET INCOME AND**  
**COMPREHENSIVE INCOME**

(unaudited)

For the periods ended December 31 (in millions, except earnings per share)	Three months ended		Twelve months ended	
	2007	2006	2007	2006
Operating revenues	\$ 489.2	\$ 479.1	\$ 1,905.8	\$ 1,926.4
Operating expenses				
Operations	334.4	322.4	1,237.2	1,260.1
Restructuring and integration (Note 3)	3.0	36.8	11.9	56.8
Amortization	79.7	85.7	318.7	330.6
	417.1	444.9	1,567.8	1,647.5
Operating income	72.1	34.2	338.0	278.9
Other income	(0.5)	2.1	6.7	5.5
Debt charges	(12.3)	(14.3)	(51.7)	(60.6)
Income before income taxes and discontinued operations	59.3	22.0	293.0	223.8
Income tax expense (recovery) (Note 5)				
Current	(0.8)	0.8	(14.0)	(17.4)
Future	45.8	(5.6)	137.3	144.1
	45.0	(4.8)	123.3	126.7
Income before discontinued operations	14.3	26.8	169.7	97.1
Income from discontinued operations, net of tax	-	189.3	-	202.3
Net income and comprehensive income for the period	\$ 14.3	\$ 216.1	\$ 169.7	\$ 299.4
Basic earnings per share (Note 7)				
Income before discontinued operations	\$ 0.22	\$ 0.39	\$ 2.61	\$ 1.43
Net income	\$ 0.22	\$ 3.18	\$ 2.61	\$ 4.40
Diluted earnings per share (Note 7)				
Income before discontinued operations	\$ 0.22	\$ 0.39	\$ 2.60	\$ 1.42
Net income	\$ 0.22	\$ 3.17	\$ 2.60	\$ 4.39

**MANITOBA TELECOM SERVICES INC.**  
**CONSOLIDATED STATEMENT OF RETAINED EARNINGS**  
(unaudited)

For the periods ended December 31 (in millions)	Three months ended		Twelve months ended	
	2007	2006	2007	2006
Retained earnings, beginning of period	\$ 148.5	\$ 47.3	\$ 183.9	\$ 96.6
Net income and comprehensive income for the period	14.3	216.1	169.7	299.4
Dividends declared	(42.0)	(44.3)	(168.3)	(176.9)
Purchase of outstanding shares (Note 7)	-	(35.2)	(64.5)	(35.2)
Retained earnings, end of period	\$ 120.8	\$ 183.9	\$ 120.8	\$ 183.9

**MANITOBA TELECOM SERVICES INC.**  
**CONSOLIDATED BALANCE SHEET**  
(unaudited)

(in millions)	December 31, 2007	December 31, 2006
<b>Assets</b>		
Current assets		
Cash and cash equivalents	\$ -	\$ 106.7
Accounts receivable (Note 4)	171.0	215.8
Future income taxes (Note 5)	109.1	111.4
Other current assets (Note 6)	48.6	31.2
	328.7	465.1
Property, plant and equipment	3,750.5	3,600.7
Accumulated amortization	2,264.4	2,148.0
	1,486.1	1,452.7
Other assets	334.8	297.7
Future income taxes (Note 5)	517.9	654.0
Goodwill and other intangible assets	58.5	51.8
	\$ 2,726.0	\$ 2,921.3
<b>Liabilities and shareholders' equity</b>		
Current liabilities		
Bank indebtedness	\$ 10.1	\$ -
Accounts payable and accrued liabilities	390.9	387.0
Advance billings and payments	49.2	38.8
Current portion of long-term debt	89.7	106.5
Current portion of capital lease obligations	6.1	4.5
	546.0	536.8
Long-term debt	649.8	739.4
Long-term portion of capital lease obligations	16.4	18.3
Deferred employee benefits	45.0	46.4
Other long-term liabilities	62.1	71.3
Future income taxes (Note 5)	2.7	3.2
	1,322.0	1,415.4
Shareholders' equity		
Share capital (Note 7)		
64,631,667 Common Shares (2006 - 66,817,707)	1,265.5	1,305.1
Contributed surplus	17.7	16.9
Retained earnings	120.8	183.9
	1,404.0	1,505.9
	\$ 2,726.0	\$ 2,921.3

**MANITOBA TELECOM SERVICES INC.**  
**CONSOLIDATED STATEMENT OF CASH FLOWS**  
(unaudited)

For the periods ended December 31 (in millions)	<b>Three months ended</b>		<b>Twelve months ended</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
<b>Cash flows from operating activities</b>				
Income before discontinued operations	\$ 14.3	\$ 26.8	\$ 169.7	\$ 97.1
Add items not affecting cash				
Amortization	79.7	85.7	318.7	330.6
Future income taxes (Note 5)	45.8	(5.6)	137.3	144.1
Deferred wireless costs	(14.7)	(11.5)	(41.0)	(31.4)
Pension funding and net pension credit	(7.1)	(23.9)	(23.3)	(99.7)
Other, net	1.6	4.9	(1.7)	0.9
Changes in non-cash working capital	53.2	(36.9)	29.0	(19.1)
Cash flows from operating activities	172.8	39.5	588.7	422.5
<b>Cash flows from investing activities</b>				
Capital expenditures, net	(124.6)	(97.6)	(312.0)	(271.6)
Acquisition (Note 8)	(8.1)	-	(8.1)	(4.3)
Proceeds from sale of buildings	-	54.2	-	54.2
Other, net	(2.9)	4.7	(2.9)	0.2
Cash flows used in investing activities	(135.6)	(38.7)	(323.0)	(221.5)
<b>Cash flows from financing activities</b>				
Dividends paid	(42.0)	(44.3)	(170.6)	(176.6)
Repayment of long term debt	-	-	(106.5)	(48.1)
Repayment of notes payable, net	-	(47.0)	-	(108.0)
Issuance of share capital (Note 7)	-	0.7	5.9	15.1
Purchase of outstanding shares (Note 7)	-	(61.9)	(111.0)	(61.9)
Other, net	0.2	0.4	(0.3)	0.9
Cash flows used in financing activities	(41.8)	(152.1)	(382.5)	(378.6)
Cash flows before discontinued operations	(4.6)	(151.3)	(116.8)	(177.6)
Cash flows from discontinued operations	-	275.9	-	294.2
Change in cash and cash equivalents	(4.6)	124.6	(116.8)	116.6
Cash and cash equivalents (bank indebtedness), beginning of period	(5.5)	(17.9)	106.7	(9.9)
(Bank indebtedness) cash and cash equivalents, end of period	\$ (10.1)	\$ 106.7	\$ (10.1)	\$ 106.7

**MANITOBA TELECOM SERVICES INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**FOR THE YEARS ENDED DECEMBER 31, 2007 AND 2006**  
(unaudited)  
(All financial amounts are in \$ millions, except where noted.)

**1. Summary of significant accounting policies**

The consolidated financial statements of Manitoba Telecom Services Inc. (the “Company”) have been prepared in accordance with Canadian generally accepted accounting principles (“GAAP”). These interim consolidated financial statements have been prepared using the same accounting policies and methods of their application as the Company’s audited consolidated financial statements for the year ended December 31, 2006, except as described in Note 2. These consolidated financial statements should be read in conjunction with the Company’s audited consolidated financial statements for the year ended December 31, 2006.

**2. Changes in accounting policies**

Effective January 1, 2007, the Company adopted the following new accounting standards relating to financial instruments, as issued by the Canadian Institute of Chartered Accountants (“CICA”): Section 3855 Financial Instruments – Recognition and Measurement; Section 3861, Financial Instruments – Disclosure and Presentation; Section 1530, Comprehensive Income; and Section 3865, Hedges. These changes in accounting policy were applied in accordance with the transitional provisions contained in each of these sections.

**Financial Instruments**

CICA Handbook section 3855, Financial Instruments – Recognition and Measurement, and CICA Handbook section 3861, Financial Instruments – Disclosure and Presentation, provide guidance for the recognition, measurement, presentation and disclosure of financial assets, financial liabilities and non-financial derivatives. These standards require financial assets, liabilities and derivatives to initially be recognized at fair value. After initial recognition, financial instruments are measured at fair value, amortized cost or cost, depending on the classification of the financial instrument. These standards also require the Company to recognize and measure derivative instruments embedded in host contracts that were issued on or after January 1, 2003.

The following is a summary of the Company’s financial instruments, their classification and measurement basis, and the financial statement impact of adopting the new standards:

- Cash and cash equivalents are classified as held-for-trading and are measured at fair value with changes in fair value recognized in net income. This classification had no impact on the Company’s financial statements at the time of adoption.
- Accounts receivable are classified as loans and receivables and are measured at amortized cost. This classification had no impact on the Company’s financial statements at the time of adoption.
- Accounts payable, long-term debt and other long-term liabilities are classified as other liabilities and are measured at amortized cost. This classification had no impact on the Company’s financial statements at the time of adoption.

The carrying values of cash and cash equivalents equal fair value. The carrying values of accounts receivable, accounts payable and other long-term liabilities approximate their fair values. The fair value of short-term financial instruments approximates their carrying amounts due to their short-term nature. The fair value of long-term debt, including the current portion, is \$740.3 million as at December 31, 2007. The fair value of long-term debt, which has fixed interest rates, is estimated by discounting the expected future cash flows using the relevant risk free interest rate adjusted for an appropriate risk premium for the Company’s credit profile.

The Company has elected to account for deferred costs associated with the issuance of long-term debt as a reduction in the carrying value of long-term debt. Upon initial application of this change in amortization method, the impact on the Company’s financial statements was insignificant. These costs, which are amortized over the life of long-term debt using the effective interest rate method, are included in debt charges. As at December 31, 2007, total deferred costs presented as a reduction of long-term debt are \$2.1 million (December 31, 2006 – \$2.2 million).

**MANITOBA TELECOM SERVICES INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**FOR THE YEARS ENDED DECEMBER 31, 2007 AND 2006**

(unaudited)

(All financial amounts are in \$ millions, except where noted.)

**2. Changes in accounting policies (continued)**

**Comprehensive Income**

CICA Handbook section 1530, Comprehensive Income, establishes standards for the reporting and display of comprehensive income. The Company has adopted this section and has determined that it does not have any items that require separate recognition in Other Comprehensive Income.

**Foreign exchange hedging**

The Company purchases foreign currency forward contracts in U.S. dollars to manage foreign currency exchange exposure, which arises in the normal course of business operations. Under CICA Handbook section 3865, Hedges, the application of hedge accounting is optional. The Company has elected not to designate any of its foreign currency forward contracts as accounting hedges. Foreign exchange gains and losses on these foreign currency forward contracts are recorded in the consolidated balance sheet as an asset or liability, with changes in fair value recognized in the consolidated statement of income.

**Inventories**

During 2007, the Company adopted the recommendations of CICA Handbook section 3031, Inventories. As a result of the adoption of this new section, the impact on the Company's financial statements has been a separate classification of inventory on the balance sheet. The Company values its inventory at the lower of cost and net realizable value.

**3. Restructuring and integration**

During the years ended December 31, 2007 and 2006, the Company recorded restructuring and integration expenses as follows:

	Consumer Markets		Enterprise Solutions		Other		Total	
	2007	2006	2007	2006	2007	2006	2007	2006
<b>Restructuring</b>								
Workforce reduction	-	-	-	8.5	-	-	-	8.5
Other	2.4	-	9.5	-	-	-	11.9	-
	2.4	-	9.5	8.5	-	-	11.9	8.5
<b>Integration</b>								
Phase two								
Workforce reduction	-	18.6	-	(3.6)	-	0.4	-	15.4
Other	-	16.5	-	16.4	-	-	-	32.9
	-	35.1	-	12.8	-	0.4	-	48.3
	2.4	35.1	9.5	21.3	-	0.4	11.9	56.8

**Restructuring**

In the fourth quarter of 2006, the Company commenced a restructuring program in order to improve efficiencies and reduce operating costs. This program included severance and other employee-related expenses, as well as costs to automate and consolidate certain systems and processes. Total costs of \$45.2 million were incurred under this program, of which \$11.9 million was expensed in 2007, \$8.5 million was expensed in 2006 relating to a workforce reduction element, and \$24.8 million was capitalized in 2007. While the Company has substantially completed all initiatives under this restructuring program, some employee departures will continue into 2008. The outstanding liability as at December 31, 2006 relating to the workforce reduction element of the program was \$8.5 million. During 2007, payments of \$3.7 million were applied against this liability, leaving an outstanding liability of \$4.8 million as at December 31, 2007.

**MANITOBA TELECOM SERVICES INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**FOR THE YEARS ENDED DECEMBER 31, 2007 AND 2006**  
(unaudited)  
(All financial amounts are in \$ millions, except where noted.)

**3. Restructuring and integration (continued)**

**Integration**

In the fourth quarter of 2005, the Company launched the second phase of its integration and restructuring program to integrate its operating divisions and corporate functions. This followed the first phase of integration and restructuring, which was completed in 2005. This cost reduction program included both workforce reduction initiatives and activities to improve network access costs and further integrate compatible functions and processes. While the Company completed substantially all initiatives under this second phase of integration and restructuring in 2006, some employee departures were scheduled to occur after 2006. The outstanding liability as at December 31, 2006 relating to the workforce reduction element of the program was \$23.3 million. During 2007, payments of \$20.2 million were applied against this liability, leaving an outstanding liability of \$3.1 million as at December 31, 2007.

**4. Accounts receivable securitization**

Under the terms of the Company's accounts receivable securitization program, the Company has the ability to sell, on a revolving basis, an undivided ownership interest in its accounts receivable to a securitization trust, up to a maximum of \$150.0 million. During the term of the agreement, the Company is subject to certain risks of default which, should they occur, could cause the agreement to be terminated early. The undivided ownership interest is sold on a fully-serviced basis and the Company receives no fee for ongoing servicing responsibilities. As a result of selling the interest in certain of the trade receivables on a fully serviced basis, a service liability of \$0.2 million (2006 – nil) has been recognized by the Company as at December 31, 2007.

The Company is required to maintain reserve accounts, classified as retained interests, in the form of additional accounts receivable over and above the cash proceeds received, to absorb credit losses on the receivables sold. For financial statement purposes, the reserve accounts have been included in accounts receivable. The trust has no recourse to the undivided ownership interest in the retained receivables, other than through the reserve accounts. The fair value of the reserve accounts approximates carrying value as a result of the short collection cycle and negligible credit losses. As at December 31, 2007, the Company had received \$43.0 million (2006 – nil) on the sale of its accounts receivable to the trust, which is comprised of the outstanding undivided ownership interest held by the trust of \$55.2 million (2006 – nil) and the reserve accounts of \$12.2 million (2006 – nil).

During 2007, the Company recognized a pre-tax loss of \$0.4 million (2006 – \$0.2 million) on the sale of accounts receivable, which is recorded in other income.

The following table is a summary of cash flows received and paid to the trust during the year:

	<b>2007</b>	<b>2006</b>
Proceeds from new securitizations	-	150.0
Proceeds from collections reinvested in revolving period securitizations	845.0	803.0

The key assumptions used to determine the loss on sale of receivables and the fair values attributed to the retained interest for the year are as follows:

	<b>2007</b>	<b>2006</b>
Annual discount rate	5.27%	4.50%
Weighted average life of receivables sold (days)	37	39
Credit loss ratio	0.60%	0.61%
Servicing fee liability	1.0%	1.0%

**MANITOBA TELECOM SERVICES INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**FOR THE YEARS ENDED DECEMBER 31, 2007 AND 2006**

(unaudited)

(All financial amounts are in \$ millions, except where noted.)

**5. Income taxes**

A reconciliation of the statutory income tax rate to the effective income tax rate is as follows:

	<b>2007</b>	<b>2006</b>
Combined basic federal and provincial statutory income tax rate	35.7%	35.9%
Change in substantively enacted tax rates	18.9	26.2
Reduction of valuation allowance	(13.1)	(5.3)
Other items	0.6	(0.2)
Effective tax rate	42.1%	56.6%

The balances of future income taxes as at December 31, 2007 and December 31, 2006 represent the future benefit of unused tax losses, and temporary differences between the tax and accounting bases of assets and liabilities. The major items giving rise to future income tax assets and liabilities are presented below:

	<b>2007</b>	<b>2006</b>
Non-capital loss carryforwards	360.6	584.2
Property, plant and equipment	374.6	330.4
Other	(46.5)	(44.7)
Total future income tax asset	688.7	869.9
Valuation allowance	(64.4)	(107.7)
Net future income tax asset	624.3	762.2

Future tax assets as at December 31, 2007 and 2006 were reduced by valuation allowances of \$64.4 million and \$107.7 million, respectively. During 2007, the Company lowered the valuation allowance by \$38.5 million (2006 – \$41.0 million) to reflect a change in management's estimate of the expected utilization of acquired income tax losses. The change in the valuation allowance was allocated as a reduction of income tax expense for 2007 and for 2006 was allocated first to reduce the net carrying value of acquired intangible assets to nil, with the remainder allocated as a reduction of income tax expense. In addition, the allowance was reduced by \$4.8 million (2006 – \$9.7 million) to reflect a change in substantively enacted tax rates.

Future income taxes are comprised of:

	<b>2007</b>	<b>2006</b>
Current future income tax asset	109.1	111.4
Long-term future income tax asset	517.9	654.0
Long-term future income tax liability	(2.7)	(3.2)
Net future income tax asset	624.3	762.2

During the twelve months ended December 31, 2007, the Company recovered \$3.0 million in cash income taxes (2006 recovered \$20.3 million).

As at December 31, 2007, the Company had non-capital loss carryforwards available to reduce future years' taxable income, which expire as follows:

2009	1,076.5
2014 and beyond	34.0
	1,110.5

**MANITOBA TELECOM SERVICES INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**FOR THE YEARS ENDED DECEMBER 31, 2007 AND 2006**

(unaudited)

(All financial amounts are in \$ millions, except where noted.)

**6. Other current assets**

	<b>2007</b>	<b>2006</b>
Prepaid expenses	33.9	24.3
Inventories	14.7	6.9
	<b>48.6</b>	<b>31.2</b>

The Company's inventory balance consists of wireless handsets, parts and accessories and communications equipment held for resale. The Company performs periodic reviews of inventory for obsolescence and, during 2007, expensed \$0.3 million in obsolete inventory (2006 – \$0.2 million). During 2007, the Company expensed \$42.0 million of inventory relating to cost of goods sold (2006 – \$32.0 million).

**7. Share capital**

During 2007, 191,460 stock options were exercised (2006 – 442,050 stock options) for cash consideration of \$5.9 million (2006 – \$15.1 million), of which \$6.9 million was credited to share capital (2006 – \$16.8 million) and \$1.0 million was charged to contributed surplus (2006 – \$1.7 million).

During 2007, the Company purchased 2,377,500 Common Shares for cancellation (2006 – 1,363,600 Common Shares) for cash consideration of \$111.0 million pursuant to its normal course issuer bid (2006 – \$61.9 million). The excess of the purchase price over the stated capital in the amount of \$64.5 million was charged to retained earnings (2006 – \$35.2 million).

**Earnings per share reconciliation**

The following table provides a reconciliation of the information used to calculate basic and diluted earnings per share:

	<b>2007</b>	<b>2006</b>
<b>Net income – basic and diluted</b>		
Income before discontinued operations	169.7	97.1
Income from discontinued operations, net of tax	-	202.3
Net income	169.7	299.4
<b>Weighted average shares outstanding (in millions)</b>		
Weighted average number of shares outstanding – basic	65.0	68.0
Dilutive effect of outstanding stock options	0.2	0.2
Weighted average number of shares outstanding - diluted	65.2	68.2
<b>Basic earnings per share (\$)</b>		
Income before discontinued operations	2.61	1.43
Discontinued operations	-	2.97
Net income	2.61	4.40
<b>Diluted earnings per share (\$)</b>		
Income before discontinued operations	2.60	1.42
Discontinued operations	-	2.97
Net income	2.60	4.39

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**8. Acquisition**

Effective October 31, 2007, the Company acquired all of the outstanding shares of MCS-Multinet Communications Services Inc., a provider of telephony systems and customer network solutions based in Montreal, for a preliminary purchase price of \$8.1 million. The purchase price is subject to adjustments which are expected to be resolved within 90 days from the date of acquisition. This acquisition was accounted for using the purchase method, and the purchase price was allocated to assets of \$9.6 million, liabilities of \$6.0 million, and goodwill of \$4.5 million. The acquired assets included intangible assets of \$5.4 million. The intangible assets represent customer contracts and relationships of \$4.7 million and a non-competition agreement of \$0.7 million. The intangible assets are being amortized over estimated periods of benefit of two to five years. The goodwill amount has been allocated to the Enterprise Solutions division operating segment. The operating results of this business are included in the Company's consolidated operating results from the effective date of acquisition.

**9. Stock-based compensation**

The following tables provide further information on outstanding stock options:

	2007		2006	
	Number of shares	Weighted average exercise price per share	Number of shares	Weighted average exercise price per share
Outstanding, beginning of year	1,721,150	40.01	2,301,960	39.32
Granted	413,000	47.18	362,000	39.57
Exercised	(191,460)	30.14	(442,050)	33.73
Terminated	(66,600)	44.90	(500,760)	42.08
Outstanding, end of year	1,876,090	42.12	1,721,150	40.01
Exercisable, end of year	725,070	39.39	638,890	36.68

Year granted	Options outstanding	Options exercisable	Weighted average exercise price per share	Range of exercise price per share	Expiry date
2007	413,000	-	47.18	44.00 – 49.37	2017
2006	313,500	59,100	39.69	38.78 – 47.76	2016
2005	660,500	267,200	43.09	40.44 – 49.03	2015
2004	157,280	93,520	45.61	45.61	2014
2003	103,360	76,280	34.84	34.75 – 35.81	2013
2002	124,100	124,100	34.29	31.82 – 34.71	2012
2001	56,500	57,020	37.07	36.42 – 38.81	2011
2000	40,000	40,000	31.89	23.81 – 35.60	2010
1999	7,850	7,850	16.99	16.99	2009

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**10. Financial instruments**

**Foreign currency forward contracts**

The Company enters into foreign currency forward contracts to manage foreign currency exposure, which arises in the normal course of business operations. As at December 31, 2007, the Company has outstanding foreign currency forward contracts to purchase \$59.7 million U.S. As part of the Company's accounting policy to adjust outstanding foreign currency forward contracts from book value to fair value, the Company has recorded a \$1.2 million loss at December 31, 2007. These contracts mature periodically beginning in January 2008 and ending in December 2008.

**11. Segmented information**

As at December 31, 2007, the Company had two reportable operating segments: the Consumer Markets division and the Enterprise Solutions division. The Consumer Markets division provides a full range of wireless, high-speed Internet and data, digital television, and wireline voice services to residential and small business customers in Manitoba. The Consumer Markets division also provides alarm monitoring services to residential and small business customers in the western provinces, and Internet, data, and voice services to small business customers in Canada. The Enterprise Solutions division provides Internet protocol-based communications, unified communications, voice, and data connectivity services to medium and large business customers in Canada. In 2006, the Company announced that it was adopting this organizational structure, and effective January 1, 2007, the reporting structure of these divisions was changed for both revenues and expenses to match this organizational structure. Accordingly, segmented information for 2007 and 2006 is provided under this new basis of segmentation.

The Company evaluates performance based on EBITDA (earnings before interest, taxes, amortization, other income, and discontinued operations). EBITDA, as reported below, includes intersegment revenues and expenses. The Company accounts for intersegment revenues and expenses at either prices that approximate current market prices or cost, depending on the type of service.

The following tables provide further segmented information:

	Years ended December 31							
	Consumer Markets		Enterprise Solutions		Other		Total	
	2007	2006	2007	2006	2007	2006	2007	2006
Operating revenue								
External	802.3	794.4	1,103.5	1,132.0	-	-	1,905.8	1,926.4
Internal	0.4	-	0.1	-	32.1	34.1	32.6	34.1
EBITDA	402.0	352.3	261.5	258.8	(6.8)	(1.6)	656.7	609.5
Amortization	234.1	239.8	84.1	90.4	0.5	0.4	318.7	330.6
Goodwill	11.8	11.8	28.7	24.2	-	-	40.5	36.0
Assets	1,966.5	2,239.8	1,468.3	1,433.5	46.5	158.1	3,481.3	3,831.4
Capital expenditures, net	167.5	165.7	144.4	105.7	0.1	0.2	312.0	271.6

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**11. Segmented information (continued)**

Reconciliations of net income and assets are as follows:

	<b>Years ended December 31</b>	
	<b>2007</b>	<b>2006</b>
<b>Consolidated net income</b>		
Total EBITDA	656.7	609.5
Amortization	(318.7)	(330.6)
Other income	6.7	5.5
Debt charges	(51.7)	(60.6)
Income tax expense	(123.3)	(126.7)
Income before discontinued operations	169.7	97.1
Income from discontinued operations, net of tax	-	202.3
	169.7	299.4
<b>Assets</b>		
Assets for operating segments	3,481.3	3,831.4
Eliminations	(1,382.3)	(1,675.5)
Future income taxes	627.0	765.4
Consolidated total assets	2,726.0	2,921.3

**12. Comparative figures**

The prior period figures have been reclassified when necessary to conform to the current year's presentation.