



Pareto Corporation

**Second Quarter Report
For The Six Months Ended June 30, 2003**

To Our Shareholders:

The second quarter of 2003 was a one of continued growth and improvement for our Company as Pareto once again achieved record levels of revenue and EBITDA for the quarter. June 30th also marked the completion of a breakthrough first half of the year for Pareto.

Our Q2 revenues were \$4.5 million, up 74% from \$2.6 million in the second quarter of 2002. EBITDA increased to \$192,000, up from \$52,000 last year. For the six months ended June 30th, Pareto generated revenues of \$7.7 million, up 126% compared to \$3.4 million generated in 2002. One of our key goals for 2003 is to improve profitability which we have done in the first half of the year. Pareto improved EBITDA for the half year period by over \$700,000 versus last year with this improvement representing an attractive 16% of the revenue growth for the period – simply put we are getting better at making money.

Improving the financial position of our Company is another key goal for us and we have continued to due that. During Q2 we reduced our debt levels by over \$760,000 as a result of our improved profitability and operational cashflow.

Operationally, we continue to see strong future revenue growth coming from both existing and new clients, as we continue to develop stronger relationships and demonstrate our capabilities in both current and new service offerings. Perhaps one of our most significant operational accomplishments for 2003 happened on July 1st when Pareto relocated to new office space, thereby integrating all of our operations in one location. Having all of Pareto's employees in one place has already improved our effectiveness and will be a significant driver for our growth going forward.

I am excited at what we have accomplished so far in 2003 but there is much more to be done. All of us here at Pareto are committed continuing to improve our Company.

Thank you for your support.

A handwritten signature in blue ink, appearing to read 'K Shapansky', with a long horizontal flourish extending to the right.

Kerry Shapansky
President & Chief Executive Officer

Consolidated Summary Financial Information

For periods ended June 30
(Unaudited)

	Three Months		Six Months	
	2003	2002	2003	2002
Revenues	\$ 4,515,375	\$ 2,594,870	\$ 7,764,515	\$ 3,440,164
Gross Profit	1,337,460	549,223	2,398,585	626,337
EBITDA	191,876	52,063	359,186	(347,194)
Net income (loss) for the period	21,460	(32,755)	78,246	(444,528)
Basic and fully diluted earnings (loss) per common share	\$ 0.001	\$ (0.001)	\$ 0.002	\$ (0.020)
Basic weighted average number of common shares outstanding	32,109,229	23,332,414	32,082,655	22,821,998
Fully diluted weighted average number of common shares outstanding	33,014,814	23,358,414	32,996,531	22,358,414

Pareto Corporation

Management's Discussion and Analysis

The following discussion focuses on Pareto Corporation's (the "Company or "Pareto") operating results for the three months and six months ended June 30, 2003 and 2002, and the financial condition as at June 30, 2003. This analysis should be read in conjunction with the consolidated interim financial statements presented in this interim report and the annual audited financial statements for the year ended December 31, 2002.

Operating Results

Three Months Ended June 30, 2003 Compared to Three Months Ended June 30, 2002:

The Company's revenue was \$4,515,375 in the quarter, 74% higher than the \$2,594,870 reported in the second quarter of 2002. The significant growth in revenue is due to the organic business growth coupled with inclusion of the financial results of Naylor Event Management ("Event"), which the Company acquired effective May 31, 2002. Excluding the acquisition of Event, revenue increased by \$221,000 or 12% over last year.

During the second quarter of 2003, the Company's revenues derived from customers in a broad mix of industries with significant contributions from customers in the retail, food and beverage, pharmaceutical and technology sectors. All of the Company's operations are in Canada, however 4% (2002 – 7%) of the quarter's revenues were earned from customers based in the United States.

The Company achieved a gross profit percentage of 30% in the quarter compared to 21% gross profit in 2002. The overall gross profit percentage was achieved consistently over the Company's divisions and falls within the Company's expected range of 27% to 30%.

Operating expenses excluding depreciation totaled \$1,145,584 for the quarter compared to \$497,160 in 2002. This increase is equally related to business growth and the inclusion of the operating expenses of Event. Operating expenses in the quarter represented 25% of revenues.

Earnings before interest, taxes, loss on lease termination and amortization (EBITDA as defined by the Company as earnings before interest, taxes, depreciation, amortization and other charges) improved from \$52,063 in 2002 to \$191,877 for 2003 as higher revenues resulted in improved EBITDA. The Company expects EBITDA, as a percentage of revenues will improve as the revenue base grows relative to the Company's operating cost structure.

Amortization increased by \$14,407 for the quarter, as compared to 2002 and was primarily a result of amortization of intangible assets acquired in 2002 and the inclusion of the amortization of capital assets for Event.

During the second quarter of 2003, the Company recorded a \$100,000 loss on the termination of the lease for the Company's office space. Effective July 1, 2003, the Company has consolidated all of its office locations into a single new location.

Interest and finance charges decreased from \$33,804 in the second quarter of 2002 to \$20,237 in 2003. The reduction is primarily due to the inclusion, in 2002, of \$14,500 of imputed interest relating to the acquisition of Event.

During the quarter the Company recorded a net tax recovery of \$15,242. This included an expense of \$68,748 of current tax related to a shortfall in the realization of taxes recoverable and a recovery of \$83,990 of future income taxes resulting from a reduction in the valuation allowance relating to the Company's tax loss carryforwards.

The Company generated net income \$21,461 in the second quarter of 2003 compared to a net loss of \$32,755 for the second quarter of 2002. This improvement was as a result of the revenue growth in all divisions of Pareto as well as the inclusion of Event.

On a per share basis, the Company earned \$0.002 per share on both a basic and diluted basis compared to a loss of \$0.001 in the same period last year. The diluted weighted average number of shares outstanding increased from 23.4 million in 2002 to 33.0 million in 2003 primarily as a result of shares issued pursuant to the acquisition of Event and the private placement completed by the Company in August 2002.

As at June 30, 2003 the Company had \$561,066 of cash and equivalents compared to \$950,191 as at March 31, 2003, a decrease of \$329,125.

Cash flow derived from operations for the quarter was \$453,677 compared to 219,052 for the second quarter of 2002. This improvement was as a result of the Company's improved profitability and continued improvement in cashflow generated from changes in the Company's non-cash operating accounts. Changes in non-cash operating accounts resulted in a cash inflow of \$365,677 in the second quarter of 2003 versus an inflow of \$200,793 in 2002. The inflow was primarily a result of improved cashflow management, realization of taxes recoverable and an increase in deferred revenue relating to projects to be completed in the future within the Event division.

Investing activities included the purchase of \$21,598 of capital assets versus nil in 2002. In 2002 investing activities included an outflow of \$755,066 related to the business acquisition of Event.

The Company's financing activities in second quarter of 2003, resulted in the reduction of the Company's total debt by \$761,250 including retiring accrued acquisition notes payable by \$336,250, repayment of a shareholder loan of \$350,000 and reducing senior bank term debt by \$75,000. This compares to total inflows of \$148,464 in 2002.

Six Months Ended June 30, 2003 Compared to Six Months Ended June 30, 2002:

The Company's revenue for six months ended June 30, 2003 was \$7,764,515, 126% higher than the \$3,440,164 reported in the June 30, 2002. The significant growth in revenue is due to the organic business growth coupled with inclusion of the financial results of Event. Excluding Event, revenue increased by \$1.88 million representing a 69% increase over last year. For the six months 5% (2002 – 7%) of the Company's revenue were earned from customers based in the United States.

The Company achieved a gross profit percentage of 31% in the six months compared to 18% gross profit in 2002. The overall gross profit percentage was achieved consistently over the Company's divisions. Going forward company expects gross profit to represent 27% to 30% of revenues.

Operating expenses excluding depreciation totaled \$2,039,398 for the six months ended June 30, 2003 compared to \$973,531 in 2002. The quantum increase is equally related to business growth and the inclusion of the operating expenses of Event. Operating expenses in this period was 26% compared to 28% last year.

EBITDA improved from a loss of \$347,194 in 2002 to earnings of \$359,187 for 2003 as higher revenues resulted in positive EBITDA. This improvement in EBITDA of \$706,381 represents 16% of the increase in revenue from 2002 to 2003.

Amortization increased by \$67,101 for the first six months of 2003, as compared to 2002. This increase was primarily a result of amortization of intangible assets acquired in 2002 and the inclusion of the amortization of capital assets of Event.

Interest and finance charges increased from \$45,735 in the first six months of 2002 to \$70,981 in 2003. The increase is due primarily to amortization of deferred finance cost related to long term debt issued in 2002.

The Company recorded net income \$78,245 for the six month period ended June 30, 2003 compared to a net loss of \$444,528 for the same period in 2002, an improvement of \$522,773. This improvement was as a result of the profitability growth in all divisions of Pareto as well as the inclusion of Event.

On a per share basis, the Company earned \$0.002 per share on both a basic and diluted basis compared to a loss of \$0.001 in the same period last year. The diluted weighted average number of shares outstanding increased from 22.9 million in 2002 to 33.0 million in 2003 primarily as a result of shares issued pursuant to the acquisition of Event and the private placement completed by the Company in August 2002.

As at June 30, 2003 the Company had \$561,066 of cash and equivalents compared to \$685,489 as at December 31, 2003, a decrease of \$64,423.

Cash flow derived from operations for the six months was \$847,269 compared to a cash outflow of \$384,625 for the same period of 2002. This improvement was as a result of the Company's improved profitability an improvement in the cashflow generated from changes in non-cash operating accounts which resulted in a cash inflow of \$611,167 in 2003 versus an outflow of \$16,649 in 2002.

In 2003, the Company has purchased \$45,442 of capital assets 2003 compared to capital asset purchases of \$31,975 in 2002.

The Company's financing activities for the six month period of 2003, included retiring total debt by \$866,250 compared to the issuance of \$338,802 of debt in the same period in 2002. The total debt reduction included the reduction of acquisition notes payable by \$366,250, repayment of a shareholder loan of \$350,000 and reducing senior term debt by \$150,000.

The Company did not pay any dividends in the six month period ended June 30, 2003 and does not currently anticipate paying any dividends in the foreseeable future.

This report to shareholders contains forward-looking statements related to expected future events and financial operating results of the Company that involves risks and uncertainties. Actual results may differ materially from management expectations as projected in such forward-looking statements for a variety of reasons, including market and general economic conditions and the risks and uncertainties detailed from time to time in the Company's SEDAR filings.

Pareto Corporation Consolidated Balance Sheets

	June 30, 2003 (unaudited)	December 31, 2002 (audited)
ASSETS		
Current		
Cash and equivalents	\$ 621,066	\$ 685,489
Accounts receivable	2,177,171	2,458,341
Income and other taxes recoverable	19,595	748,336
Work in progress	771,081	149,321
Inventory and other current assets	112,660	62,553
	<u>3,701,573</u>	4,104,040
Deferred finance costs	42,792	71,459
Capital assets	470,492	533,240
Goodwill	5,709,775	5,730,775
	<u>9,924,632</u>	<u>10,439,514</u>
	\$ 9,924,632	\$ 10,439,514
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current		
Accounts payable and accrued liabilities	\$ 2,026,253	\$ 3,145,043
Deferred revenue	2,477,472	997,580
Current portion of long-term debt	300,000	300,000
Current portion of acquisition notes payable	426,250	426,250
	<u>5,229,975</u>	4,868,873
Future income tax liability	184,640	272,620
Acquisition notes payable	160,000	526,250
Long-term debt	550,000	1,050,000
	<u>6,124,615</u>	6,717,743
Shareholders' equity		
Share capital (Note 3)	4,067,939	4,044,539
Special warrants	116,600	140,000
Deficit	(384,522)	(462,768)
	<u>3,800,017</u>	3,721,771
	<u>9,924,632</u>	<u>10,439,514</u>
	\$ 9,924,632	\$ 10,439,514

The accompanying summary of significant accounting policies is an integral part of these financial statements.

Pareto Corporation

Consolidated Statement of Operations and Deficit

For the periods ended June 30
(Unaudited)

	Three Months		Six Months	
	2003	2002	2003	2002
Revenues	\$ 4,515,375	\$ 2,594,870	\$ 7,764,515	\$ 3,440,164
Direct Costs	3,177,915	2,045,647	5,365,930	2,813,827
Gross Profit	1,337,460	549,223	2,398,585	626,337
Expenses				
Facilities	83,256	95,169	177,376	193,482
Selling and administration	1,062,328	401,991	1,862,023	780,049
	1,145,584	497,160	2,039,399	973,531
	191,876	52,063	359,186	(347,194)
Amortization of capital assets	54,921	51,014	108,191	62,099
Amortization of intangible assets	10,500	-	21,000	-
Loss on lease termination	100,000	-	100,000	-
Interest and finance charges	20,237	33,804	70,981	45,735
	185,658	84,818	300,172	107,834
Income (loss) before income taxes	6,218	(32,755)	59,014	(455,028)
Income taxes				
Current	68,748	-	68,748	-
Future (recovery)	(83,990)	-	(87,980)	(10,500)
	(15,242)	-	(19,232)	(10,500)
Net income (loss) for the period	21,460	(32,755)	78,246	(444,528)
Deficit, beginning of period	(405,982)	(3,054,202)	(462,768)	(2,642,429)
Deficit, end of period	\$ (384,522)	\$ (3,086,957)	\$ (384,522)	\$ (3,086,957)
Basic and fully diluted earnings (loss) per common share	\$ 0.001	\$ (0.001)	\$ 0.002	\$ (0.020)
Basic weighted average number of shares outstanding	32,109,229	23,332,414	32,082,655	22,821,998
Diluted weighted average number of shares outstanding	33,014,814	23,358,414	32,996,531	22,870,748

The accompanying summary of significant accounting policies is an integral part of these financial statements.

Pareto Corporation

Consolidated Statements of Cash Flow

For the periods ended June 30
(Unaudited)

	Three Months		Six Months	
	2003	2002	2003	2002
Cash provided by (used in)				
Operating activities				
Net income (loss) for the period	\$ 21,459	\$ (32,755)	\$ 78,245	\$ (444,528)
Items not involving cash				
Amortization of capital assets	54,921	51,014	108,191	62,099
Amortization of intangible assets	10,500	-	21,000	-
Amortization of deferred financing costs	1,166	-	28,666	-
Non-cash interest expense	-	14,500	-	14,500
	88,046	32,759	236,102	(367,929)
Changes in non-cash operating accounts	365,677	186,293	611,167	(16,696)
	453,723	219,052	847,269	(384,625)
Investment activities				
Capital asset additions	(21,598)	-	(45,442)	(31,975)
Acquisitions, net of cash acquired	-	755,066	-	755,066
	(21,598)	755,066	(45,442)	723,091
Financing Activities				
Bank indebtedness	-	(107,622)	-	(13,700)
Issuance of long-term debt	-	258,851	-	358,851
Repayment of long-term debt	(425,000)	(3,715)	(500,000)	(7,299)
Payment of acquisition notes payable	(336,250)	-	(366,250)	-
Share issuance costs	-	950	-	950
	(761,250)	148,464	(866,250)	338,802
Increase (decrease) in cash for the period	(329,125)	1,122,582	(64,423)	677,268
Cash and equivalents, beginning of period	950,191	718,126	685,489	1,163,440
Cash and equivalents, end of period	\$ 621,066	\$ 1,840,708	\$ 621,066	\$ 1,840,708

The accompanying summary of significant accounting policies is an integral part of these financial statements.

Pareto Corporation

Notes to Consolidated Financial Statements

June 30, 2003
(unaudited)

1. Significant Accounting Policies

The financial statements of the Company have been prepared by management in accordance with generally accepted accounting principles in Canada for interim financial statements. The financial statements have, in management's opinion, been properly prepared using judgment within reasonable limits of materiality. These interim financial statements do not include all the note disclosures required for annual financial statements and, therefore, should be read in conjunction with the Company's audited annual financial statements for the year ended December 31, 2002. The significant accounting policies follow that of the most recently reported annual financial statements.

2. Accounting Estimates

The preparation of interim financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements. Actual results could differ from those estimated.

3. Share Capital

(a) Authorized

Unlimited common shares
Unlimited special shares assumable in series

(b) Issued common shares

	Number of Shares	Amount
Balance, December 31, 2002	32,056,081	\$ 4,044,539
Issued upon conversion of Special Warrants	116,667	23,400
Balance, June 30, 2003	<u>32,172,748</u>	<u>\$ 4,067,939</u>

(c) Stock options

The Company has a stock option plan (the "Plan") for employees, consultants, directors and officers of the company. Pursuant to the plan, a total of 4,000,000 of the company's common shares have been reserved for issue. One-third of granted options vest on each of the anniversary dates of the grant.

Pareto Corporation

Notes to Consolidated Financial Statements

June 30, 2003
(unaudited)

3. Share Capital (continued):

Stock option transactions under the Plan during the period are as follows:

	Number of Options	Weighted Average Exercise Price
Options outstanding, December 31, 2002	2,990,286	\$ 0.28
Granted in 2003	400,000	0.25
Cancelled in 2003	(142,000)	0.22
Options outstanding, June 30, 2003	<u>3,248,286</u>	<u>\$ 0.28</u>
Options exercisable, June 30, 2003	<u>718,762</u>	<u>\$ 0.35</u>
Options exercisable, December 31, 2002	<u>320,571</u>	<u>\$ 0.35</u>

As at June 30, 2003, the Company had the following options outstanding pursuant to the Plan:

Number of Options	Exercise Price Per share	Expiry Date
558,000	\$0.35	March 31, 2006
381,715	\$0.35	November 30, 2006
658,571	\$0.35	February 15, 2007
680,000	\$0.20	August 1, 2007
570,000	\$0.20	November 4, 2007
400,000	\$0.25	June 23, 2008

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Notes to Consolidated Financial Statements

June 30, 2003
(unaudited)

3. Share Capital (continued)

The Company does not record compensation expense when stock options are granted to employees. Had compensation expense been determined based on the fair value at the grant dates, the net income and earnings per share amounts have been changed to the pro forma amounts indicated below:

	Three months ended June 30		Six months ended June 30	
	2002	2003	2002	2003
Net Income				
- as reported	\$ 21,461	\$ (32,755)	\$ 78,247	\$ (444,528)
- pro forma	4,737	(42,935)	42,750	(459,799)
Earnings per share – basic and diluted				
- as reported	\$ 0.001	\$ (0.001)	\$ 0.002	\$ (0.020)
- pro forma	-	(0.001)	0.001	(0.020)

The fair value of share options was estimated using the Black – Scholes option-pricing model with the following assumptions:

Dividend yield	0%
Expected Volatility	40%
Risk-free interest rate	3.5% to 4.75%
Expected option life	2 to 4 years

(d) Special warrants:

Pursuant to the acquisition of Solutions, the Company issued 700,000 special warrants. The special warrants are convertible upon exercise to common shares of the Company for no further consideration in six tranches, exercisable every six months beginning May 19, 2003. The fair value of the special warrants at the date of issuance was \$140,000. As at June 30, 2003, 583,333 Special Warrants remain outstanding.

(e) Escrow common shares:

- i. Pursuant to an Escrow Agreement with the former shareholders of Campbell, the 628,724 common shares issued on the acquisition will be released during 2003 provided specific revenue targets are met.
- ii. Pursuant to an Escrow Agreement with the CDNX, the founders of Alouettes and certain shareholders of Caxton were required to place a total of 8,705,000 shares in escrow. 10% of the 8,705,000 shares were released from escrow in February 2002 and 15% of the 8,705,000 shares will be released every six months thereafter. As at June 30, 2003, 5,223,000 of these shares remain in escrow.