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PRESENTATION

Operator

Good morning. My name is Michelle, and I will be your conference operator today. At this time, I would like to welcome everyone to the Loblaw Companies Limited Fourth-Quarter 2014 Results conference call.

(Operator Instructions)

As a reminder, this call is being recorded. I will now turn the call over to Janet Craig. You may begin your conference.

Janet Craig - *Loblaw Companies Ltd - SVP of IR*

Thanks, Michele, and good morning. And welcome to the Loblaw Companies Limited fourth-quarter 2014 results webcast and conference call. I'm joined by Galen Weston, President and Executive Chairman; and Richard Dufresne, Chief Financial Officer.

Before we begin today's call, I want to remind you that the discussion will include forward-looking statements, such as the Company's beliefs and expectations regarding certain aspects of the financial performance in 2015 and future years. These statements are based on certain assumptions and reflect management's current expectations, and they are subject to a number of risks and uncertainties that could cause actual results or events to differ materially from our expectations. These risks and uncertainties are discussed in the Company's materials filed with the Canadian Regulators from time to time.

Any forward-looking statements speak only as of the date they are made. The Company disclaims any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, other than is required by law. Certain non-GAAP measures may be discussed or referred to today. Please refer to our annual report and other materials filed with the Canadian Securities Regulators for reconciliation of each of these measures to the most directly comparable GAAP financial measure.

And finally, we do plan on ending the call at about 11:50 AM today, due to other conference calls happening today that you may need to be on. I will now turn the call over to Richard.

Richard Dufresne - *Loblaw Companies Ltd - CFO*

Thank you, Janet, and good morning, everyone. This morning, we announced our financial results for the fourth quarter. We are pleased with the progress we are making as we continued to execute against our financial plan.

We maintained a stable trading environment in the quarter, which means our gross margin remained relatively stable. We delivered strong same-store sales performance in both our food and pharmacy businesses. Synergies continued to flow in, efficiencies are progressing, and we are well on our way to de-lever our balance sheet. As you know, the quarter had 13 weeks compared to 12 in 2013, and we have outlined the impact of the 13th week in our news release. We delivered solid same store sales growth in grocery this quarter, a bit shy of inflation, but our promo activity was particularly strong in Q4 of 2013 which affects year-over-year comparison.

Core grocery same-store sales growth was 3.3%, excluding gas and the effect of the loss of one tobacco supplier. Over the past several quarters, since we've been calling out gas separately in our comps, we have not generally seen a material difference between our headline same-store sales, and our same-store sales without gas. This quarter, with the dramatic decline in gas prices, the spread with material at 50 basis points.

At the same time, you might recall last quarter that we mentioned having very high same-store sales in our wholesale business. A large tobacco supplier changed its model to go DSD, cutting out the wholesaler. This had a very positive impact on comps into Q3, as customers who could no longer purchase the tobacco at a competitor were still able to purchase it at our wholesale clubs. In the fourth quarter, the supplier stopped delivering it to us as well, which had a negative impact of 40 basis points on same-store sales. We will feel this impact for the balance of the year.

Our internal inflation was slightly higher than food CPI of 3.5% driven by fresh. At Shoppers Drug Mart, our front of store same-store sales growth of 3.6% was driven by a very strong cough and cold season, and strong sales in cosmetics. In pharmacy, same-store sales grew 4.2%, driven by strong comp script growth of 6% offset by average trip deflation of 1.7%. With positive same-store sales growth in grocery, pharmacy, and front of store, the top line was strong with sales of CAD11.4 billion in the quarter up 49% over last year on a consolidated basis.

Turning to our retail segment. Revenue was CAD11.2 billion up over 50% year-over-year, with our core grocery business growing 9.3% to CAD8.1 billion. On a 12 week basis, grocery revenue grew 1.6%. Shoppers Drug Mart revenue grew over 11% to CAD3.1 billion in the quarter. Excluding the 13th week, sales growth was 3.4%. Adjusted gross margin of our retail business in Q4 stood at 26.8% up from 21.9% last year. Gross margin benefited from the addition of the Shoppers Drug Mart business, as well as synergies.

In our food retail business, we held adjusted gross margin flat at 21.9%. Our core gross margin in grocery retail was stable. Gross margin benefited from synergies. However, we booked higher than normal shrink as a result of the completion of our conversion of our Corporate stores to SAP, where stores that were converted early, experienced higher shrink than normal. In our drug retail business, gross margin grew 110 basis points to 40%. Cost of goods sold in the quarter benefited from synergies, as well as strong growth in front of store [margins].

We achieved net efficiencies in our core grocery business this quarter, and remain focused on driving costs out of our business. As we discussed last quarter, we remain focused on improving core SG&A expense, and seeking to both better manage volatility in SG&A as well as providing visibility into the drivers. On a 12 week basis, our SG&A improved CAD28 million or 60 basis points relative to last year. Of the 60 basic point in SG&A benefit, approximately half came from efficiencies in labor and supply chain. The balance of the improvement could be characterized largely as non-recurring adjustments that had positive impacts. For example, we won a property tax appeal in the quarter that benefited SG&A.

We recorded CAD49 million in net synergies this quarter, for a total of CAD101 million since closing of the acquisition, which is one quarter ahead of our initial target. We expect to come close to CAD200 million in annual net synergies in 2015. The vast majority of synergies achieved to date have been in cost of goods sold. In 2015, we will benefit from the annualization of the COGs initiative, while GNFR starts to begin, as well as the beginning of the ramp-up of our food pilot offer in Shoppers Drug Mart. In 2015, as our focus turns to expense synergies and to a lesser extent revenue synergies. These synergies, by their very nature, take longer to achieve. We remain confident about achieving our three-year target of CAD300 million in net synergies.

At PC Financial, Q4 revenue increased by CAD27 million or 13.2%. Driven by higher interest and interchanging income, as a result of the growth in our credit card receivables portfolio. Operating income grew 14% to CAD49 million. Our adjusted interest expense for the quarter is CAD144 million, an increase of CAD52 million versus last year. Adjusted net earnings totaled CAD396 million in the quarter versus CAD160 million last year. An increase of CAD235 million. And finally, adjusted basic earnings-per-share stood at CAD0.96 versus CAD0.57 last year, an increase of 68%.

Moving to free cash flow. Free cash flow in the fourth quarter was CAD439 million, bringing us to over CAD975 million for the year. Since the closing of the acquisition of Shoppers Drug Mart last March, we have reduced our adjusted debt by almost CAD1.1 billion, of which CAD421 million was in the fourth quarter. Looking to Q1, we expect a slight increase in adjusted debt due to seasonal working capital requirements. That said, we remain on track to achieve our target of a CAD1.7 billion reduction by the end of March next year. Our capital expenditures this quarter were CAD400 million for a total of CAD1.1 billion in 2014. We ended the year below our budget. Also of note, we have modified our CapEx definition to now include intangibles, which was CAD42 million for the quarter and CAD90 million for the full 2014 year.

Turning to outlook. The environment in 2015 continues to be challenging, both in grocery, retail and in pharmacy. Square footage growth in grocery has moderated, but competition remains intense. In pharmacy, ongoing healthcare reform continues to be a factor, as governments continue to look for savings to manage healthcare costs and balance budgets. Our outlook for 2015, relative to 2014, is based on comparing a full-year financial for both Shoppers Drug Mart and Loblaw. As a baseline, revenue in 2014 on a combined basis was CAD45.1 billion and adjusted EBIT was CAD2.4 billion.

We expect to deliver positive same-store sales and stable gross margin, excluding synergies in our retail segment. We will continue to drive efficiencies across the core grocery business by achieving reductions in areas including supply chain, administrative functions, and IT, while still investing in key areas like e-commerce. We also expect to achieve cumulative annual net synergies as a result of the acquisition of Shoppers Drug Mart approaching CAD200 million.

Excluding synergies, we expect to grow adjusted operating income in our core grocery business, and experience a decline in adjusted operating income in our core pharmacy business. As a result of one-time expenses associated with the rollout and training associated it with our new pharmacy system, a new Patient Contact Centre initiative, and lost earnings from our divested stores. On a consolidated basis, we expect to grow adjusted net earnings, including synergies, with our adjusted net earnings-per-share growth for the year being moderated. Due to an increased weighted average share count. Our share count will be 412 million in 2015 versus approximately 380 million in 2014.

Looking at D&A. We expect approximately CAD1.1 billion in adjusted depreciation and amortization for the full-year 2015. We expect adjusted interest expense for the full year to be approximately CAD500 million, and CAD135 million in Q1 of this year. We expect our adjusted tax rate to remain between 26% and 27% for the full year. We expect to invest about CAD1.2 billion in capital expenditures in 2015.

A couple of other considerations which are included in our assumptions for our outlook. We expect a reduction in adjusted operating income of approximately CAD13 million in 2015 from the divestitures required as part of the consent agreement with the Competition Bureau to complete the acquisition of Shoppers Drug Mart. We had benefits to non-core operating expense in 2014 of approximately CAD28 million. And finally, before turning the call over to Galen, I wanted to mention how we intend to reflect Shoppers Drug Mart in our financials this year. We will present our retail segment on a combined basis, which includes Loblaw and Shoppers together. But will still comment on key metrics per business, such as same-store sales, sales, and gross margin.

Thank you. I will now turn over the call to Galen.

Galen Weston - *Loblaw Companies Ltd - President & Executive Chairman*

Thank you, Richard, and good morning, everyone. As you just heard, Loblaw continues to execute against its financial plan. We are maintaining a stable trading platform, synergies that are in line with expectations, efficiencies are on track, and our deleveraging target is unchanged. I'm pleased with our performance.

In addition to delivering our financial plan, Loblaw has shaped its strategy around the idea of helping Canadians live life well. As part of that strategy, we continue our relentless focus on delivering the best in food experience. This includes an unyielding commitment to value in our discount division, the continued expansion of market-leading service and assortment in our market division, and accelerating momentum in multi-cultural brands like T&T and Fortinos. Our control brand portfolio has also seen a step change in growth, as we have expanded Presidents Choice into more fresh food categories. And rolled out over 800 products across the Shoppers Drug Mart network.

As Canada's leading drugstore chain, our strategy also calls on us to deliver the best health and beauty proposition available to Canadians. This includes strong convenience-driven growth in our front of store, and continued innovation in our beauty departments. In pharmacy, expanding our scope of practice to improve patient outcomes, while at the same time reducing provincial health-care costs, is another manifestation of this purpose. This is a long-term journey, and in 2014, we made significant progress. An example that we are particularly proud of is our newly opened Patient Contact Centre. Each year in North America, over 125,000 patients lose their lives as a result of taking prescription medication improperly, or in some cases not taking it at all. This lack of adherence is estimated to cost the Canadian healthcare system close to CAD8 billion annually. The Patient Contact Centre is specifically designed to help overcome this significant issue.

The first of its kind in Canada, our facility has a team of more than 50 pharmacists and 75 pharmacy assistants who conduct follow-up calls across the country. Their focus is on patients who may not be taking their medications as intended. Including those newly diagnosed and starting prescriptions, those on multiple medications and complex regimes, and those who have missed a refill. By contacting patients centrally, we're able to free up the time of our local retail pharmacists. Time which they can then spend with patients providing an expanding range of valuable and cost-effective services, such as flu shots and minor ailment prescribing in those provinces where it is permitted.

Delivering on our purpose of helping Canadians live life well represents a powerful sustainable competitive advantage for Loblaw. And hereto, I am pleased with our performance. The grocery and pharmacy industries remain intensely competitive. But looking forward in 2015, as our outlook discusses, we expect adjusted net earnings growth. The momentum in the grocery business continues, and we remain focused on a stable trading platform while growing earnings excluding synergies.

Although operating income excluding synergies in Shoppers Drug Mart is expected to decline in 2015. Due to the investments we are making in key projects as well as the ongoing pressure of healthcare reform, the underlying business at Shoppers Drug Mart remains strong. We are making strategic investments to increase the efficiency and effectiveness of our pharmacies and patient care. Front of store, including beauty, is robust, and I'm enthusiastic about what we've seen to date in the enhanced convenience food pilots. We'll be expanding this pilot through a new test market in the Spring.

In addition to the food proposition at Shoppers Drug Mart, I see other important opportunities for our business, including e-commerce. The next stage of our PC Plus program and the digitization of custom optimum offers. Longer-term opportunities will arise from the insights that we gain from SAP, as well as the cost savings that it will surface. Our franchise stores are the next crucial step in its implementation, having successfully completed all of our Corporate stores and distribution centers in 2014.

In closing, our strategic framework is clear, our entire organization is focused on delivering against it, best in food experience, best in health and beauty, operational excellence and growth. This strategy is supported by our commitment to stable and consistent trading, realizing synergies and efficiencies in our business, and deleveraging of the balance sheet. Once we are at the appropriate leverage targets, we will start to look more actively at other ways to return capital to shareholders through dividend increases and share repurchases. Looking forward, I'm confident that as we build our portfolio of independent complementary businesses, along with a balanced capital return strategy, we will accrue long-term value for shareholders.

Thank you. I'll now pass the call back to Janet to take some questions.

Janet Craig - *Loblaw Companies Ltd - SVP of IR*

Thanks, Galen. Michelle, we're ready to take questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Perry Caicco, CIBC World Markets.

Perry Caicco - *CIBC World Markets - Analyst*

Just a few questions on the outlook, if I could. The goal of positive same-store sales, is there an inflation assumption in there, or is that exclusive of inflation?

Galen Weston - *Loblaw Companies Ltd - President & Executive Chairman*

We generally don't budget inflation. So the way to think about is we're looking for comp store sales growth that would be slightly -- would be in line or slightly ahead of inflation. But it's not something we're obsessed over at this point, Perry. We think we're reasonably happy with where the sales are running relative to inflation at the moment.

Perry Caicco - *CIBC World Markets - Analyst*

And does a stable gross margin mean similar to 2014, or just that they don't fluctuate?

Galen Weston - *Loblaw Companies Ltd - President & Executive Chairman*

That means similar to 2014.

Perry Caicco - *CIBC World Markets - Analyst*

And the investments that you're making in key areas like e-commerce, do you see those as offsetting the reductions in supply chain, admin and IT?

Galen Weston - *Loblaw Companies Ltd - President & Executive Chairman*

I don't see that -- no I don't see them offsetting completely, but they are making a difference in the speed at which you see the SG&A numbers coming down.

Perry Caicco - *CIBC World Markets - Analyst*

Okay. And my last question, I just wondered if you could split the CapEx out the billing too among infrastructure in stores.

Richard Dufresne - *Loblaw Companies Ltd - CFO*

The majority is going into retail, where the portion on infrastructure is reducing every year and it's continuing to reduce next year.

Perry Caicco - *CIBC World Markets - Analyst*

Any specific numbers Richard?

Richard Dufresne - *Loblaw Companies Ltd - CFO*

No.

Perry Caicco - *CIBC World Markets - Analyst*

Okay, thank you.

Operator

Irene Nattel, RBC Capital Markets.

Irene Nattel - *RBC Capital Markets - Analyst*

Just focusing on the SG&A piece. In your remarks, Richard, you indicated probably about somewhere in the range of 30 bps of efficiencies resurface. And I was wondering if you could just talk about which areas in particular, and whether you see this level being sustained and or increased in 2015?

Richard Dufresne - *Loblaw Companies Ltd - CFO*

Our focus always -- remains on showcasing that we're reducing our costs. And the areas that you should start you should continue to see benefits are in supply chain, in IT and admin. And we're going to continue to make progress this year.

So our focus is trying to eliminate the noise to show you the benefits that we're making. Fortunately this quarter, we had noise that went the right way. But we will try to continue to show you the benefits as they progress.

Irene Nattel - *RBC Capital Markets - Analyst*

That's very helpful. And just on the shrink site. Again, you noted that some of the stores that had complete SAP earlier are actually seeing higher shrink. Does this mean that that's something you expect to see in 2015, or can you take the learnings from the first batch of stores and adapt it so that we don't see that falling through?

Richard Dufresne - *Loblaw Companies Ltd - CFO*

Yes. We won't see it going forward, hopefully. Essentially what that means is that we had some costing issues when we started to convert the first few stores.

And therefore, when shrink was calculated, it gave out some higher numbers. So, what we did at year end, is we trued up the shrink for these stores, and that's what we booked in our gross margin. But if you look at our count results since year end, these stores are performing back to normal.

Irene Nattel - *RBC Capital Markets - Analyst*

That's very helpful. Thank you.

Operator

Peter Sklar, BMO Capital Markets.

Peter Sklar - *BMO Capital Markets - Analyst*

For both Shoppers and Loblaw, I believe you gave an adjusted EBITDA number for the quarter. If we wanted to know how that number looked without the extra week, if we just did a prorated, would that be a good way to get at that number?

Richard Dufresne - *Loblaw Companies Ltd - CFO*

The only thing I'd tell you, Peter, there's obviously more EBITDA attributed to Loblaw than Shoppers. On the CAD71 million that you can get by looking at page 1 of our press release.

Peter Sklar - *BMO Capital Markets - Analyst*

Okay. In Shoppers, I believe in the fourth quarter, you divested 11 stores that you were required to -- . Can you quantify how much impact that had on the EBITDA of Shoppers? Was it at the beginning of the quarter, the end of the quarter.

Richard Dufresne - *Loblaw Companies Ltd - CFO*

In Q4, there was some impact. But the way to look at it is going forward, the impact of all of these stores is CAD13 million, and that's the number you should care about.

Peter Sklar - *BMO Capital Markets - Analyst*

Right. Can you be a little more definitive on the fourth quarter? Was it a small number?

Richard Dufresne - *Loblaw Companies Ltd - CFO*

Yes.

Peter Sklar - *BMO Capital Markets - Analyst*

And lastly, Richard, one of the reasons you attributed to the Loblaw's SG&A decline, there's something called changes in fair value of companies franchise investments. Can you explain what that is, and is that an adjustment or not an adjustment?

Richard Dufresne - *Loblaw Companies Ltd - CFO*

This is an adjustment, and this is just -- we changed the way we account for these franchise stores going forward to eliminate impairments. And so therefore, this is not any change in the business itself, but it's improving the way we account for the business going forward. So, the one-time number you saw is a one-time event, and that's it.

Peter Sklar - *BMO Capital Markets - Analyst*

Okay. Thank you.

Operator

Jim Durran, Barclays.

Jim Durran - *Barclays Capital - Analyst*

I just wanted to talk about the comp store sales outlook for grocery. Obviously, a lot of moving parts right now. What's your comfort level with pass-through and FX inflation? We've gone through this, obviously, in 2014, but we're at it again in 2015.

Galen Weston - *Loblaw Companies Ltd - President & Executive Chairman*

Yes. So as you know, that inflation is generally a positive for the industry. That's been something I think that's contributed to a reasonable amount of robust sales growth for all of us over the course of 2014. And with the decline in the Canadian dollar, we expect that to continue into 2015. Again, I think that's a positive that's helpful.

However, the changes have been pretty significant, with the decline in the price of oil, the decline in the price of the value of the Canadian dollar, just in the last six months. And so we're watching this very, very carefully to see the extent to which the consumer begins to resist this pass through. And at this stage, we don't see anything that's causing us concern. However, it is something we're thinking carefully about.

Jim Durran - *Barclays Capital - Analyst*

Is there any insight on center of the store? There's not been a lot of inflation in that area for a quite a while. Are we starting to see the CPG players announce price increases and try to implement them?

Galen Weston - *Loblaw Companies Ltd - President & Executive Chairman*

Yes, so that is where we would expect to see a little bit more inflation in the Business than we had in 2014. Although, that's the place where you have the most aggressive competition at the alternative retailers, and also the rest of the traditional grocers really fighting hard for share in that space. So it's not going to -- we're not going to be able to pass it through in 100 cents on the dollar, that's for sure. But there might be a little bit more than last year.

Jim Durran - *Barclays Capital - Analyst*

Okay. And then gas prices and tobacco drains. So on the gas price side, it was very difficult to model accurately how the retail price is going to impact your comp store sales. Can you give us anything to hold on to in terms of trying to be able to model that on a more accurate basis?

Richard Dufresne - *Loblaw Companies Ltd - CFO*

I'd like to be able to model it myself. So, Jim, what we'll do is we'll tell you each quarter on gas.

And tobacco, it's only to be for one year, it's like it happened eight years ago, if you remember. So, it's going to take a year to lapse, so we'll comment on it for the next 12 months and after that you won't hear about it.

Jim Durran - *Barclays Capital - Analyst*

It's difficult, but on the tobacco drainage, would you expect the same 40 basis point impact on the next three quarters?

Richard Dufresne - *Loblaw Companies Ltd - CFO*

I don't know, to be very honest with you. We'll see.

Jim Durran - *Barclays Capital - Analyst*

I appreciate that. And last question, just on your CapEx spend with the square footage. Can you give us some idea on what kind of square footage growth you expect for grocery and for Shoppers?

Richard Dufresne - *Loblaw Companies Ltd - CFO*

Shoppers, it's mid-2%, and for us it's below 1%.

Jim Durran - *Barclays Capital - Analyst*

Great. Thank you very much.

Operator

Vishal Shreedhar, National Bank.

Vishal Shreedhar - *National Bank Financial - Analyst*

Just on the outlook statement for Shoppers on the operating income, is the decline in operating income that you anticipate in 2015 relative to 2014 pre-synergy. Is that entirely due to investments in store closures? Is drug reform still a significant impact?

Richard Dufresne - *Loblaw Companies Ltd - CFO*

There is drug reform -- there was drug reform in 2014. There is drug reform in 2015. What I was referring to is our three specific items that are not typically normal in the business, and those were the items I was talking about.

Vishal Shreedhar - *National Bank Financial - Analyst*

So order of magnitude, could you give us a sense of the impact of drug reform on your numbers in 2015?

Galen Weston - *Loblaw Companies Ltd - President & Executive Chairman*

It's not something we typically disclose. But suffice to say, it's a big number. Although, we consider it part of the normal course of business. And it's our expectation -- we'll make every effort to close the gap. Notwithstanding extreme or unanticipated incremental impacts coming from different governments.

Richard Dufresne - *Loblaw Companies Ltd - CFO*

And, Vishal, the impact of the three items that I specifically mentioned is around CAD30 million.

Vishal Shreedhar - *National Bank Financial - Analyst*

Got it. So with respect to the adherence the adherence in the adherence in the technology investments that I see, so that's about [CAD20 million] or [CAD17 million] ish. Are those investments going to fade in 2016, and then we should expect benefits there after, is that the way to think about it?

Richard Dufresne - *Loblaw Companies Ltd - CFO*

Exactly. For the pharmacy system, it's training and rollout. That's around CAD10 million. And the patient contact sector is essentially labor, there's north of 100 people that are now working at that center, of which, half are pharmacists, so that's another CAD10 million. And the divestitures, it's around CAD11 million.

Vishal Shreedhar - *National Bank Financial - Analyst*

Got it.

Galen Weston - *Loblaw Companies Ltd - President & Executive Chairman*

And, Vishal, I would just add to that when you think about the transition that's taking place in the Shoppers business, and to a lesser extent the Loblaw business when it comes to pharmacy, as the regulations compress margin in basic prescription drugs, what we've been trying to articulate to you and we talked at length with the provincial governments about this is, the opportunity for expanded scope of practice, a good example of which would be pharmacy is delivering flu shots across Canada over the course of the last two years, this is an opportunity for the government to download basic healthcare services to pharmacies at a much improved cost to them.

So remember, the government would be typically paying CAD30 for a GP to administer a flu shot; they'd be paying Shoppers Drug Mart CAD9 to administer a flu shot, and with the increased access that the pharmacies have versus the GPs, you actually get to drive up the rate of inoculation, which also saves the government money. So these are the kinds of programs that the healthcare teams inside Shoppers and Loblaw are working hard to develop. The Patient Contact Centre is another example of that.

And the potential savings that we think these kinds of investments represent to the government, are meaningful. And as we sit in the room with them and negotiate the pace of this relentless healthcare reform, we're trying to explain. And I think we have people listening to us, that we need to ramp up, one, at the same -- in line with the pace at which we ramped down the other so that we're not creating undue disruption in the marketplace.

And I think that is a dialogue that has become very much more constructive over the last two years with the provincial governments. But they still have fiscal pressures, and I'd say the discussions continue to be intense.

Vishal Shreedhar - *National Bank Financial - Analyst*

Okay. And just last question on the back of what you said. Could you give us order of magnitude, any sort of indication of how large the professional services revenue is for Shoppers? Is it still very small in relation to the RX revenue?

Galen Weston - *Loblaw Companies Ltd - President & Executive Chairman*

Yes, it's pretty small and growing fast.

Vishal Shreedhar - *National Bank Financial - Analyst*

Got it. Thanks.

Operator

Michael Van Aelst, TD Securities.

Michael Van Aelst - *TD Securities - Analyst*

I just wanted to clarify a few things on those CAD30 million of impact you mentioned, Richard, from those three items. Are those, as you look at to 2016, and I know that's a little bit further. But I'd assume these are all projects with the exception of the divestiture's obviously, the other two projects are items that you expect to get a return from down the road?

Richard Dufresne - *Loblaw Companies Ltd - CFO*

Yes.

Michael Van Aelst - *TD Securities - Analyst*

And then in Ontario, I believe you have a labor contract that's up for or it's starting a negotiation. Can you give us a bit of a timeframe on what we should expect from those negotiations, or at least the timeline of those negotiations?

Galen Weston - *Loblaw Companies Ltd - President & Executive Chairman*

Yes. Absolutely, so those conversations have begun in earnest. If you'll recall, these are three big banners specifically in Ontario. The Real Canadian Superstore, Loblaw's and [Zara's], and it's an important contract both for us and for the UFCW.

And that will likely come to a head in the early part of the Summer. And at this stage, our conversations are constructive. I think we've both clearly outlined our perspectives and our expectations of how to come to terms with the deal.

But these are always again difficult things, and we'll keep you updated as things move forward. I think our expectations, as always, is to construct a fair and appropriate deal and keep the idea of a work stoppage as far from the table as possible.

Michael Van Aelst - *TD Securities - Analyst*

Thank you.

Operator

David Hartley, Credit Suisse.

David Hartley - *Credit Suisse - Analyst*

Just a question on the SAP implementation. I understand you're focusing on the franchise side now. What's the timeframe for that to be completed? Could you remind us? And for non-franchise and non-Corporate stores, what's the timeframe for that?

Galen Weston - *Loblaw Companies Ltd - President & Executive Chairman*

So the non-franchise Corporate stores are done. The franchise stores in the Loblaw business will be complete by the end of the year. We've started that implementation in earnest.

And so it's a lot of work to do. The franchise implementation is a little bit different to the Corporate, because of the franchise contracts and the unique way that we do business with those independent operators. At this stage, we feel it's on track and we're optimistic about finishing it on time.

David Hartley - *Credit Suisse - Analyst*

On the wholesale side of the business, where you deal with affiliate banners or other independents that aren't franchises, is there any implementation involved there? Could you give us some color on that?

Galen Weston - *Loblaw Companies Ltd - President & Executive Chairman*

Yes. So our wholesale business, that does go on to an SAP. The impact on the independent affiliates is inconsequential.

David Hartley - *Credit Suisse - Analyst*

Okay. Sounds good. And just with the President's Choice and no-name brands, you've had an opportunity now to put them into the Shoppers Drug Mart store. How far along are you in that process of doing that? I understand you've got some pilots going on, more towards the fresh side and a fuller offering, but how beneficial has it been for Loblaw's overall so far and what do you see going forward?

Galen Weston - *Loblaw Companies Ltd - President & Executive Chairman*

So as I mentioned in my remarks, we have 800 no-name and President's Choice SKUs largely deployed across the small grocery departments and the existing Shoppers Drug Mart network. So it's a big deployment, President's Choice Decadent cookies, baby food, and so on and so forth. And the response from the associate owners and the response from the customers have been very positive.

Given that these are still two businesses with disparate distribution infrastructures and different buying teams on the day-to-day side of things, there is some friction, some complexity I would say. I'm not happy with the consistency of the service level, the in-stock positions on the new control brands, and that's where will we would be prioritizing our efforts over the next four or five months. And it'd be at that point where we can better measure the true extent of the positive impact. But suffice to say, the indications are looking very good.

David Hartley - *Credit Suisse - Analyst*

Okay. And final question, just on the RX business. I noticed of course that Shoppers is putting up some decent numbers, both in RX and the front. But your own in grocery store business has been relatively flat. Can you talk a little bit about the differences and why that is?

Galen Weston - *Loblaw Companies Ltd - President & Executive Chairman*

Yes. There's a couple of differences. The biggest one probably being that Shoppers took a longer time to wave their co-pay in Ontario. And as they waved that co-pay, they saw a real spike in volume, because the value proposition Shoppers was offering in the market was fundamentally better. They're seeing a carry-on of that through 2014, although not quite the same; it's starting to slow.

And also one of the other big drivers, particularly in Q4, was the implementation of the and ramping up of the flu shot program. Where Shoppers by virtue of its convenience network disproportionately outperformed the Loblaw pharmacy network. And remember, each of one of those flu shots represents a prescription, so that contributed nicely to the volume in Q4.

And then just the third thing which we've now lapped in the Loblaw businesses, we've been doing some successive and quite meaningful pharmacy acquisitions. And as we lap that on an annualized basis, you'll start to see a bit more of a normalized growth rate. And it's beginning to turn more positive.

David Hartley - *Credit Suisse - Analyst*

Thank you.

Operator

Chris Li, Bank of America.

Chris Li - *BofA Merrill Lynch - Analyst*

First question is, for the corporate stores that have been moved over to SAP for close to a year now, have the benefits from things like inventory control and sales productivity, have they been starting to be reflected in the numbers? Or would it take a few quarters before we begin to see the benefits?

Galen Weston - *Loblaw Companies Ltd - President & Executive Chairman*

Yes. So it's going to take a few quarters. Think about SAP in two stages; there's implementation and then there's optimization. And we're now, for those early stores, we're well into the stage of implementation. But you can't really start to optimize the system until it's had a full company-wide deployment.

So, the teams are working with the information that's coming out of the system. And I think as Richard mentioned in the meeting in our call last quarter, they're being inundated with high-quality information that they have never seen before. That's showing a tremendous amount of promise.

But actually implementing the changes that come from that information take a bit more time. And then for it to show up in the actual performance of the stores itself, it's taking some more time.

But probably the principal benefit that we see now is that we've moved through the friction that comes with implementation. The stores are performing now at the level that they were before we rolled it out, and we have better visibility. And so we're starting to put more focus on inventory, more focus on labor productivity, and all the things that you would expect are going to show some benefits.

Chris Li - *BofA Merrill Lynch - Analyst*

Okay, that's helpful. My next question is just in terms of the improvement in the profitability of the general merchandise business. Are most of those benefits now behind us, or are there more potential for improvements in that segment?

Galen Weston - *Loblaw Companies Ltd - President & Executive Chairman*

The general merchandise business is now stable in terms of the amount of change that's been going on with the departments and inventory. So we're reasonably comfortable with the way it's performing. Now having said that, we are in the process of expanding substantially the Joe Fresh proposition inside 50 stores across Canada over the course of this year.

And we see that resulting in an improvement in sales productivity, because apparel is one of the highest sales productivity categories on that right-hand side. And also we expect to see an improvement in those 50 stores in actually the margin. Because from a margin mix perspective, apparel is also stronger than some of the other categories.

So that implementation is going to begin at the end of the first quarter. It's probably not going to show up in a meaningful way in the P&L of the stores until 2016.

Chris Li - *BofA Merrill Lynch - Analyst*

Okay. And my last question is if you can maybe share with us what your feel on the Target stores are when you look at potentially looking at acquiring some of the leases? How many do you think are addressable both for you, and how many would you consider acquiring the leases if they become available?

Galen Weston - *Loblaw Companies Ltd - President & Executive Chairman*

So the Target impact, I think as we talked about last time, probably the one we're focused on most is what the impact on the overall sales of the network. As these stores go through liquidation, we think that's going to be a negative for us. And as they close in the back half of the year, we think that's going to be a positive for us. It will probably disproportionately benefit some of the GM categories and beauty specifically, much more so than food.

In terms of our potential interest in the Target network, this network of stores has been out and on the market for many, many years in one way, shape or form, and we haven't invested particularly in any meaningful number of stores.

That's because their network is not particularly complementary to the Loblaw network. The nature of food restrictions that exist on certain sites, as well as also constraints. So we have a team looking at the assets, we have identified a number of stores that we think would be complementary, but don't think of it as anything significant or material.

Chris Li - *BofA Merrill Lynch - Analyst*

Okay. Thank you.

Operator

(Operator Instructions) Keith Howlett, Desjardins Securities.

Keith Howlett - *Desjardins Securities - Analyst*

I had a question on the SAP implementation. I think the expectation was to save 60 basis points by -- during 2016. And I was wondering how that looks at this point? And also I was wondering in terms of the benefits of SAP, when or whether you'd be willing to quantify what they're likely to be in terms of the positive benefit?

Galen Weston - *Loblaw Companies Ltd - President & Executive Chairman*

Yes. I know you ask this question every quarter. So the 60 basis points will include the SAP implementation. Basically the decline in spend, is what we've articulated. We're all on track there. It's also a function of improvements in supply chain efficiency, and were very much on track there.

And then another piece of it is the admin headcount reduction, which the bulk of it in the P&L from an admin perspective at Loblaw is now done. All in anticipation of when we have full deployment of SAP and we start to optimize it, then there's going to be another wave of benefits.

We haven't quantified those. They're incremental to the 60 basis points. We have a very specific business case by line item associated with this SAP implementation. But at this stage, we're still not prepared to share it.

Keith Howlett - *Desjardins Securities - Analyst*

And just one question on the synergies, which seem to be running a little bit of head of target. Is that because one of the categories is generating -- one of the early categories is generating more synergies, or are you getting to further categories of synergies faster than you thought?

Richard Dufresne - *Loblaw Companies Ltd - CFO*

It's essentially -- we're essentially done, the COGS piece. There's a few remnants to reign in, but and those were discrete in numbers that we had to go after. So that's essentially behind us now.

And now were going more into the GNFR stuff, where we're going to be looking at stuff in terms of number of opportunities, the size is -- the number is significant. And the amount of effort also is going to be significant. So but we have a plan to go and get those, but it will take a little bit more time.

So that's why we're confident that we're going to approach CAD200 million this year, but it's not at the same pace that we did for the first nine months.

Keith Howlett - *Desjardins Securities - Analyst*

Thank you.

Janet Craig - *Loblaw Companies Ltd - SVP of IR*

Michelle, are there any more callers?

Operator

There are no further questions at this time. I will turn the call back to Janet Craig.

Janet Craig - *Loblaw Companies Ltd - SVP of IR*

Thanks, Michelle. And thanks everyone for joining us today. If you have any questions, you can obviously contact us in IR and have a good day. Thank you.

Operator

Ladies and gentlemen, this does conclude the conference call for today You may now disconnect your line, and have a great day.
