Management's Discussion and Analysis

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The following Management's Discussion and Analysis ("MD&A") for George Weston Limited and its subsidiaries (collectively, the "Company" or "Weston") should be read in conjunction with the consolidated financial statements and the accompanying notes on pages 63 to 111 of this Annual Report. The consolidated financial statements and the accompanying notes have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP") and are reported in Canadian dollars. These consolidated financial statements include the accounts of George Weston Limited and its subsidiaries and variable interest entities ("VIEs") that the Company is required to consolidate in accordance with Accounting Guideline 15, "Consolidation of Variable Interest Entities" ("AcG 15"). A Glossary of terms and ratios used throughout this Annual Report can be found beginning on page 114. The information in this MD&A is current as of March 12, 2008, unless otherwise noted.

1. FORWARD-LOOKING STATEMENTS

This Annual Report, including this MD&A, contains forward-looking statements about the Company's objectives, plans, goals, aspirations, strategies, financial condition, results of operations, cash flows, performance, prospects and opportunities. Words such as "anticipate", "expect", "believe", "could", "estimate", "goal", "intend", "plan", "seek", "strive", "will", "may" and "should" and similar expressions, as they relate to the Company and its management, are intended to identify forward-looking statements. These forward-looking statements are not historical facts but reflect the Company's current expectations concerning future results and events.

These forward-looking statements are subject to a number of risks and uncertainties that could cause actual results or events to differ materially from current expectations. These risks and uncertainties include, but are not limited to: changes in economic conditions; changes in consumer spending and preferences; heightened competition, whether from new competitors or current competitors; the availability and cost of raw materials and ingredients, fuels and utilities; changes in the Company's or its competitors' pricing strategies; failure of the Company's franchised stores to perform as expected; risks associated with the terms and conditions of financing programs offered to the Company's independent franchisees; failure to realize anticipated cost savings and operating efficiencies from the Company's major initiatives, including investments in the Company's information technology systems, supply chain investments and other cost reduction and simplification initiatives; the inability of the Company's information technology infrastructure to support the requirements of the Company's business; the inability of the Company to manage inventory to minimize the impact of obsolete or excess issues and to control shrink; failure to execute successfully and in a timely manner the Company's major initiatives, including the implementation of strategies and introduction of innovative products; unanticipated costs associated with the Company's strategic initiatives, including those related to compensation costs; the inability of the Company's supply chain to service the needs of the Company's stores; deterioration in the Company's relationship with its employees, particularly through periods of change in the Company's business; failure to achieve desired results in labour negotiations, including the terms of future collective bargaining agreements; changes to the regulatory environment in which the Company operates; the adoption of new accounting standards and changes in the Company's use of accounting estimates including in relation to inventory valuation; fluctuations in the Company's earnings due to changes in the value of stock-based compensation and equity forward contracts relating to the Company's and Loblaw's common shares; changes in the Company's tax liabilities resulting from changes in tax laws or future assessments; detrimental reliance on the performance of third-party service providers; public health events; the inability of the Company to obtain external financing; the inability of the Company to attract and retain key executives; and supply and quality control issues with vendors. These and other risks and uncertainties are discussed in the Company's materials filed with the Canadian securities regulatory authorities from time to time, including the Operating Risks and Risk Management and Financial Risks and Risk Management sections of this MD&A. Other risks and uncertainties not presently known to the Company or that the Company presently believes are not material could also cause actual results or events to differ materially from those expressed in its forward-looking statements.

In addition to these risks and uncertainties, the material assumptions used in making the forward-looking statements contained herein and in particular in the Report to Shareholders, on page 23 of Section 7.1, on page 26 of Section 7.2 and page 55 of Section 18 of this MD&A, include: there is no material change in economic conditions from those of 2007; patterns of consumer spending and preferences are reasonably consistent with historical trends; there is no significant change in competitive conditions, whether related to new competitors or current competitors; there is no unexpected change in the Company's or its competitors' current pricing strategies; the Company's franchised stores perform as expected; the Company successfully offers new and innovative products and executes its strategies as planned; anticipated cost savings and operating efficiencies are achieved, including those from the Company's cost reduction and simplification initiatives; there is no unexpected change in the Company's access to funding; and there are no significant regulatory, tax or accounting changes or other significant events occurring outside the ordinary course of business.

Readers are cautioned not to place undue reliance on these forward-looking statements, which reflect the Company's expectations only as of the date of this MD&A. The Company disclaims any intention or obligation to update or revise these forward-looking statements, whether as a result of new information, future events or otherwise, except as required by law.

2. OVERVIEW

Weston is a Canadian public company, founded in 1882, and is one of North America's largest food processing and distribution companies. Weston has two reportable operating segments: Weston Foods and Loblaw. The Weston Foods operating segment is primarily engaged in the baking and dairy industries within North America. The Loblaw operating segment, which is operated by Loblaw Companies Limited and its subsidiaries, is Canada's largest food distributor and a leading provider of general merchandise, drugstore, and financial products and services.

3. VISION

Weston's vision has been, and continues to be, centred on three main principles: growth, innovation and flexibility. Weston seeks long term, stable growth in its operating segments, while accepting prudent operating risks through continuous capital investment supported by a strong balance sheet, with the goal of providing sustainable returns to its shareholders through a combination of common share price appreciation and dividends.

The Company believes that to be successful over the long term, it must deliver on what its customers and consumers want, today and in the future. The Company encourages innovation in order to provide consumers with new products and convenient services at competitive prices that meet consumers' everyday household needs.

Looking ahead, the Company plans to achieve these goals by focusing on its long term operating and financial strategies as discussed below.

4. OPERATING AND FINANCIAL STRATEGIES

In order to be successful in achieving its vision, the Company employs various operating and financial strategies. Each of the Company's two reportable operating segments has its own risk profile and operating risk management strategies.

Weston Foods' long term operating strategies include:

- customer alignment;
- brand development including innovative new products to meet the nutritional and dietary concerns of consumers;
- plant and distribution optimization including capital investment to strategically position facilities across North America to support growth and enhance quality, productivity and efficiencies;
- ongoing cost reduction initiatives with the objective of ensuring a low cost operating structure and economies of scale;
- strategic acquisitions and relationships to broaden market penetration and expand geographic presence; and
- building leadership capability.

Loblaw's mission is to be Canada's best food, health and home retailer by exceeding customer expectations through innovative products at great prices. Under the principles of Simplify, Innovate, Grow, Loblaw employs various operating and financial strategies which guide Loblaw over the long term and represent a philosophy for the way in which it conducts its business. Loblaw has simplified its organization by more clearly defining accountabilities, eliminating duplication and establishing consistent, simple and efficient processes. A less complex organizational structure and a short list of key performance indicators are expected to lead to more focus in 2008 on customers and store operations, and for the first time ever, to enable Loblaw to fully leverage its national scale.

Innovation is one of the many strengths of Loblaw, most clearly exhibited by its control label offerings. Loblaw supports innovation based on the belief that providing consumers with new products and convenient services at competitive prices and stimulating shopping environments is critical to its success.

In 2006, Loblaw developed its Formula for Growth to define priorities for a three to five year turnaround plan. To provide an integrated offering of food, general merchandise and drugstore, Loblaw's Formula for Growth focuses on the following:

- best format: truly distinctive formats meeting customers' different needs;
- fresh first: best fresh food offering;
- control label advantage: leading in the development of unique, high quality control label products and services;
- 10% *Joe*: grow *Joe Fresh Style* brand by offering great style at an affordable price;
- health, home and wholesome: making healthy living affordable for all Canadians;
- priced right: providing best value for money, when compared to all relevant shopping choices;
- always available: best in-stock positions; and
- friendly colleagues motivated to serve: investing in colleagues to support customer satisfaction.

Loblaw's long term operating strategies are consistent with its Formula for Growth and continue to be as follows:

- use the cash flow generated in its business to invest in its future;
- own its real estate, where possible, to maximize flexibility for product and business opportunities in the future;
- use a multi-format approach to maximize market share over the longer term;
- focus on food but serve the consumer's everyday household needs;
- create customer loyalty and enhancing price competitiveness through a superior control label program;
- implement and execute plans and programs flawlessly; and
- constantly strive to improve its value proposition.

The Company's financial strategies include:

- maintain a strong balance sheet;
- minimize the risks and costs of its operating and financing activities; and
- maintain liquidity and access to capital markets.

The success of these and other plans and strategies discussed in this MD&A may be affected by risks and uncertainties, including those described in the Operating Risks and Risk Management and Financial Risks and Risk Management sections of this MD&A, beginning on pages 43 and 48, respectively.

The Company's Board of Directors (the "Board") and senior management meet annually to review the strategic imperatives. These strategic imperatives, which generally span a three to five year timeframe, target specific issues in response to the Company's performance and changes in consumer needs and the competitive landscape.

The Company believes that if it successfully implements and executes its various strategic imperatives in support of its long term operating and financial strategies, it will be well positioned to fulfill its vision of providing sustainable returns to its shareholders over the long term.

5. KEY PERFORMANCE INDICATORS

The Company continuously reviews and monitors its activities and key performance indicators, which it believes are important to measuring the success of the implementation of its operating and financial strategies. Some of the Company's key financial performance indicators are set out below:

Key Financial Performance Indicators	**2007**	2006
Sales growth	**2.0%**	3.1%
Sales growth excluding the impact of tobacco sales and VIEs(1)	**3.2%**	4.3%
Basic net earnings per common share from continuing operations growth (decline)	**811.6%**	(91.8)%
Adjusted basic net earnings per common share from continuing operations(1) (decline)	**(14.5)%**	(11.4)%
Free cash flow(1) ($ millions)	**$ 620**	$ 27
Net debt (excluding Exchangeable Debentures)(1) to equity ratio	**0.96:1**	0.96:1
Return on average common shareholders' equity	**12.7%**	1.3%

(1) See Non-GAAP Financial Measures beginning on page 55.

In addition, other operating performance indicators include but are not limited to: same-store sales growth, operating and administrative cost management, new product development, customer service ratings, product return rates, production waste, production efficiencies and market share.

6. OVERALL FINANCIAL PERFORMANCE

6.1 CONSOLIDATED RESULTS OF OPERATIONS

($ millions except where otherwise indicated)	2007	2006	2005[2]
Sales	$ 32,815	$ 32,167	$ 31,189
Sales excluding the impact of tobacco sales and VIEs[1]	$ 31,346	$ 30,361	$ 29,120
Operating income	$ 1,094	$ 537	$ 1,634
Adjusted operating income[1]	$ 1,408	$ 1,643	$ 1,891
Interest expense and other financing charges	$ 165	$ 253	$ 187
Net earnings from continuing operations	$ 563	$ 110	$ 716
Net earnings	$ 563	$ 121	$ 698
Basic net earnings per common share from continuing operations ($)	$ 3.92	$ 0.43	$ 5.25
Adjusted basic net earnings per common share from continuing operations ($)[1]	$ 4.26	$ 4.98	$ 5.62
Basic net earnings per common share ($)	$ 3.92	$ 0.52	$ 5.11

(1) See Non-GAAP Financial Measures beginning on page 55.

(2) During 2006, the Company implemented Emerging Issues Committee Abstract 156, "Accounting by a Vendor for Consideration Given to a Customer (Including a Reseller of the Vendor's Products)" ("EIC 156") on a retroactive basis. Accordingly certain sales incentives paid by Loblaw to independent franchisees, associates and independent accounts for prior years have been reclassified between sales and cost of sales, selling and administrative expenses.

Sales and Sales Growth Excluding the Impact of Tobacco Sales and VIEs[1]

($ millions except where otherwise indicated)	2007	2006	2005[2]
Total sales	$ 32,815	$ 32,167	$ 31,189
Less: Sales attributable to tobacco sales	1,013	1,423	1,654
Sales attributable to the consolidation of VIEs	456	383	415
Sales excluding the impact of tobacco sales and VIEs[1]	$ 31,346	$ 30,361	$ 29,120
Total sales growth	2.0%	3.1%	
Less: Impact on sales growth attributable to tobacco sales	(1.4)%	(1.0)%	
Impact on sales growth attributable to the consolidation of VIEs	0.2%	(0.2)%	
Sales growth excluding the impact of tobacco sales and VIEs[1]	3.2%	4.3%	

(1) See Non-GAAP Financial Measures beginning on page 55.

(2) During 2006, the Company implemented EIC 156 on a retroactive basis. Accordingly certain sales incentives paid by Loblaw to independent franchisees, associates and independent accounts for prior years have been reclassified between sales and cost of sales, selling and administrative expenses.

Adjusted Operating Income and EBITDA[1]

($ millions)	2007	2006	2005
Net earnings from continuing operations	$ 563	$ 110	$ 716
Add (deduct) impact of the following:			
Minority interest	130	(82)	288
Income taxes	236	256	443
Interest expense and other financing charges	165	253	187
Operating income	1,094	537	1,634
Add (deduct) impact of the following:			
Restructuring and other charges	227	90	118
Net effect of stock-based compensation and the associated equity derivatives	109	60	72
Commodity futures fair value adjustment	(19)		(3)
Inventory liquidation	15	68	
VIEs	(11)	(8)	
Curtailment of post-retirement plan	(7)		
Loblaw goodwill impairment charge		800	
Ontario collective labour agreement		84	
Departure entitlement charge		12	
Goods and Services Tax and provincial sales taxes			40
Direct costs associated with supply chain disruptions			30
Adjusted operating income[1]	1,408	1,643	1,891
Add (deduct) impact of the following:			
Depreciation and amortization	704	705	684
VIE depreciation and amortization	(33)	(24)	(26)
Adjusted EBITDA[1]	$ 2,079	$ 2,324	$ 2,549

(1) See Non-GAAP Financial Measures beginning on page 55.

Adjusted Basic Net Earnings per Common Share from Continuing Operations[(1)]

Per common share ($)	2007	2006	2005
Basic net earnings per common share from continuing operations	**$ 3.92**	$ 0.43	$ 5.25
Add (deduct) impact of the following:			
Restructuring and other charges	**0.72**	0.36	0.42
Net effect of stock-based compensation and the associated equity derivatives	**0.63**	0.38	0.46
Commodity futures fair value adjustment	**(0.10)**		(0.02)
Inventory liquidation	**0.04**	0.21	
VIEs	**0.04**		0.03
Curtailment of post-retirement plan	**(0.03)**		
Loblaw goodwill impairment charge		3.84	
Ontario collective labour agreement		0.26	
Departure entitlement charge		0.04	
Direct costs associated with supply chain disruptions			0.09
Goods and Services Tax and provincial sales taxes			0.14
Accounting for Loblaw forward sale agreement	**(0.81)**	(0.40)	(0.77)
Changes in statutory income tax rates	**(0.15)**	(0.14)	0.02
Adjusted basic net earnings per common share from continuing operations[(1)]	**$ 4.26**	$ 4.98	$ 5.62

(1) See Non-GAAP Financial Measures beginning on page 55.

Consolidated 2007 results reflect the impact of transformational changes being undertaken by both the Weston Foods and Loblaw operating segments in order to position the businesses for strong growth in the future.

In 2007, the Weston Foods operating segment achieved significantly improved financial results despite challenging market conditions. Inflationary commodity cost pressures continued and accelerated in 2007 and this, coupled with a continuation of changing consumer eating preferences and food shopping patterns, led to significant disparity in the financial performance of industry participants. Industry price increases mitigated the higher commodity costs; however, cost and productivity improvements and a mix shift to higher margin products resulted in above average earnings growth for the Weston Foods operating segment.

For the Loblaw operating segment, 2007 was a year of transformational change amid intense competition and pressured earnings. Loblaw's declining financial performance since the beginning of 2005 required action to prevent further erosion. Late in 2006, a significant number of changes in the senior leadership occurred and a strategic review was undertaken which resulted in the identification of a turnaround plan which was built on three core pillars: (i) simplify and sharpen Loblaw by making accountabilities clear and centralizing where it counts, while fixing the basics that matter to customers and matter financially, (ii) restore innovation to the heart of its culture in food and across all of its control labels, and (iii) grow through its Formula for Growth, as previously described in the Operating and Financial Strategies section of this MD&A, while spending capital wisely in an over-spaced market. Loblaw's three to five year turnaround commenced in 2007 and Loblaw has made good progress. The single most important accomplishment has been the organizational restructuring. This is a transformational change that will enable Loblaw, for the first time ever, to fully leverage its national scale. Supply Chain and Information Technology also produced roadmaps that Loblaw believes will make its infrastructure competitive.

Additional activities undertaken by Loblaw in 2006 included the negotiation of a new four-year collective agreement with members of certain Ontario locals of the United Food and Commercial Workers union ("UFCW"), the liquidation of certain general merchandise inventory and the closure of certain underperforming stores. During the third quarter of 2006, a major tobacco supplier commenced shipping directly to certain customers of Loblaw's Cash & Carry and wholesale club network, adversely impacting sales in 2006 and 2007. During 2006, Loblaw also continued to feel the effects from challenges encountered in 2005 during the execution of planned changes to its systems, supply chain and general merchandise areas, including certain supply chain systems conversions and the start-up of a new third-party owned and operated general merchandise warehouse and distribution centre for Eastern Canada which handles general merchandise and certain drugstore products. These challenges disrupted the flow of inventory to Loblaw's stores and resulted in additional operating costs.

The following discussion summarizes the factors and trends that have impacted the Company's financial performance over the past two fiscal years.

In 2007, consolidated sales increased 2.0% to $32.8 billion from $32.2 billion in 2006. Sales growth for 2007 included a negative impact of approximately 1.4% from declining tobacco sales and a positive impact of 0.2% from the consolidation of certain Loblaw independent franchisees as required by AcG 15. Sales excluding the impact of tobacco sales and VIEs[1] increased 3.2% over the prior year. In 2006, consolidated sales increased 3.1% from $31.2 billion in 2005. Sales growth for 2006 included a negative impact of approximately 1.0% from declining tobacco sales and 0.2% from the consolidation of certain Loblaw independent franchisees as required by AcG 15. In 2007, consolidated net earnings from continuing operations increased $453 million to $563 million from $110 million in 2006. In 2006, consolidated net earnings from continuing operations decreased $606 million, or 84.6%, from $716 million in 2005. Consolidated net earnings increased $442 million, or 365.3%, to $563 million in 2007 from $121 million in 2006. In 2006, consolidated net earnings decreased $577 million, or 82.7%, from $698 million in 2005.

The 2007 basic net earnings per common share from continuing operations of $3.92 increased, in line with the increase in consolidated net earnings from continuing operations, when compared to $0.43 in 2006. The 2007 basic net earnings per common share of $3.92 also increased when compared to $0.52 in 2006. Both increases were primarily due to the inclusion in 2006 of a non-cash Loblaw goodwill impairment charge related to the goodwill established on the Loblaw acquisition of Provigo Inc. in 1998.

The Company's consolidated financial statements are expressed in Canadian dollars but a significant portion of its Weston Foods business occurs in United States dollars through its investment in self-sustaining foreign operations in the United States ("U.S. net investment"). Changes in the exchange rate for the United States dollar affect the Company's reported sales, net earnings and the value of the Company's assets and liabilities on its consolidated balance sheet, either positively or negatively, as a result of translating United States dollar denominated transactions and the U.S. net investment into Canadian dollars. In 2007 and 2006, due to the appreciation of the Canadian dollar relative to the United States dollar during the year on a weighted average basis, sales and net earnings growth were negatively impacted. Due to the strengthening of the Canadian dollar relative to the United States dollar from year end 2006, the value of the Company's net assets at year end 2007 was negatively impacted as a result of foreign currency translation. At year end 2006, due to the weakening of the Canadian dollar relative to the United States dollar from year end 2005, the value of the Company's net assets was positively impacted as a result of foreign currency translation.

Over the past two years, Weston Foods has operated in a challenging marketplace impacted by changing consumer eating preferences and food shopping patterns as well as accelerating inflationary cost pressures. Product rationalization and the planned exit of certain products have negatively impacted volume and sales. Additional factors over this two year period include:

- changing consumer eating preferences, including a focus on health and diet, challenged Weston Foods sales growth of certain traditional products including white bread, fresh-baked sweet goods and cookies. These challenges were largely offset by strong growth in the whole grain and higher-priced premium product categories and the development and introduction of new and expanded convenience and health related product offerings, including "on-the-go" individual portioned products, enhanced whole grain and whole wheat offerings, as well as Omega-3, no cholesterol, reduced fat, no trans fat and organic products;
- consumer shopping patterns continue to shift toward alternate format retail channels over traditional, conventional supermarket formats. Weston Foods has successfully penetrated these alternate channels while retaining its strong position in conventional supermarket formats; and
- inflationary cost pressures particularly for wheat, oils and energy have continued and accelerated over the period. Weston Foods achieved sales price increases across many of its product categories, which helped to offset the impact of this cost inflation.

Over the past two years, Weston Foods has increased investment behind its brands, continued to introduce new products geared towards changing consumer eating preferences, and invested capital to support growth, and enhance quality and productivity. These, coupled with a continued focus on customer service, cost improvement and a shift in product mix to higher margin offerings, have resulted in strong financial performance and improved competitive positioning. Management continues to monitor marketplace and competitive developments and believes that Weston Foods is well positioned to take advantage of any opportunities.

Loblaw has been undergoing a significant amount of change over the past two years including changes in senior leadership. Loblaw's three to five year turnaround plan based on Simplify, Innovate and Grow commenced in 2007 and Loblaw has made good progress. There were challenges, as would be expected, with an organizational change of such magnitude. Net earnings in 2007 were pressured by Loblaw's investment in lower retail prices and increased costs including significant expenses in restructuring and consulting.

(1) See Non-GAAP Financial Measures beginning on page 55.

2006 was also a difficult year for Loblaw as it continued to experience the effects in 2006 of certain of its 2005 initiatives which included restructuring of the supply chain operations, supply chain systems conversions, the reorganization of its merchandising, procurement and operations groups and the move of personnel to the head office in Brampton, Ontario. Additional activities undertaken by Loblaw in 2006 included the negotiation of a new four-year collective agreement with members of certain Ontario locals of the UFCW, the liquidation of certain general merchandise inventory and the closure of certain underperforming stores. During the third quarter of 2006, a major tobacco supplier commenced shipping directly to certain customers of Loblaw's Cash & Carry and wholesale club network, adversely impacting sales in 2006 and 2007.

The following analysis details factors that have impacted the Company's consolidated sales and net earnings over the past two years.

Sales

The Company's 2007 consolidated sales increased 2.0% to $32.8 billion from $32.2 billion in 2006. Sales growth for 2007 included a negative impact of approximately 1.4% from declining tobacco sales, and a positive impact of 0.2% from the consolidation of certain Loblaw independent franchisees as required by AcG 15. Sales excluding the impact of tobacco sales and VIEs[1] increased 3.2% over the prior year. The translation of United States dollar denominated sales in the Weston Foods operating segment reduced consolidated sales growth by approximately 0.5%.

Consolidated sales growth for 2007 was impacted by each reportable operating segment as follows:

- Negatively by 0.2% due to the sales decrease of 1.2% at Weston Foods, which included the negative impact of foreign currency translation of approximately 3.4%. Price increases across key product categories combined with changes in sales mix increased sales by 3.5% for 2007. Overall volume decreased 1.3% for 2007 and was negatively impacted by approximately 0.7% due to the combined effect of the exit from the United States frozen foodservice bagel business early in the third quarter of 2006 and the discontinuance of contract manufacturing of biscuits for certain customers during 2006. The remaining volume decline of 0.6% for the year was due to growth in certain higher margin categories being more than offset by declines in other categories.
- Positively by 2.3% due to the sales increase of 2.6% at Loblaw, which included a negative impact of approximately 1.7% from declining tobacco sales, and a positive impact of 0.3% from the consolidation of certain Loblaw independent franchisees as required by AcG 15. Same-store sales increased 2.4% and same-store sales excluding the impact of decreased tobacco sales grew by 3.4%. Loblaw experienced sales growth in all of its regions and concentrated on driving comparable sales growth in its existing asset base. Net retail square footage decreased 0.1 million square feet or 0.2% in 2007 from year end 2006. Corporate store sales per average square foot increased to $591 in 2007 from $585 in 2006.

The Company's 2006 consolidated sales increased 3.1% to $32.2 billion from $31.2 billion in 2005, including a negative impact of approximately 1.0% from declining tobacco sales and a negative impact of approximately 0.2% from the consolidation of certain Loblaw independent franchisees as required by AcG 15. The translation of United States dollar denominated sales in the Weston Foods operating segment reduced consolidated sales growth by approximately 0.7%.

Consolidated sales growth for 2006 was impacted by each reportable operating segment as follows:

- Negatively by 0.1% due to the sales decrease of 0.6% at Weston Foods, which included the negative impact of foreign currency translation of approximately 4.4%. Price increases across key product categories combined with changes in sales mix increased sales by 4.2% for 2006. Overall volume decreased 0.4% for 2006 and was negatively impacted by approximately 0.7% due to the combined effect of the exit from the United States frozen foodservice bagel business early in the third quarter of 2006 and the discontinuance of contract manufacturing of biscuits for certain customers during 2006.
- Positively by 3.2% due to the sales increase of 3.7% at Loblaw, which included a negative impact of approximately 1.2% from declining tobacco sales, and a negative impact of 0.1% from the consolidation of certain Loblaw independent franchisees as required by AcG 15. Same-store sales increased 0.8% and same-store sales excluding the impact of decreased tobacco sales grew by 2.0%. Sales increases were realized across all regions of the country and in all areas of food, general merchandise and drugstore. Net retail square footage increased 1.2 million square feet or 2.5% in 2006. Corporate store sales per average square foot increased to $585 in 2006 from $579 in 2005.

(1) See Non-GAAP Financial Measures beginning on page 55.

Operating Income

The Company's 2007 consolidated operating income increased by $557 million, or 103.7%, to $1,094 million. The consolidated operating margin in 2007 was 3.3% compared to 1.7% in 2006. 2007 consolidated operating income included the following:

- a charge of $227 million related to restructuring and other charges;
- a charge of $109 million for the net effect of stock-based compensation and the associated equity derivatives. The amount of net stock-based compensation cost recorded in operating income is mainly dependent upon the number of unexercised, vested stock options and restricted share units relative to the number of underlying common shares on the equity derivatives and the level of and fluctuations in the market prices of the underlying common shares;
- income of $19 million related to a commodity futures fair value adjustment at Weston Foods;
- a charge of $15 million related to the inventory liquidation at Loblaw;
- income of $11 million related to the consolidation of VIEs by Loblaw; and
- income of $7 million from the curtailment of a post-retirement plan at Weston Foods.

After adjusting for the impact of the items described above, consolidated adjusted operating income(1) for 2007 declined 14.3% to $1,408 million from $1,643 million in 2006.

The Company's 2007 consolidated adjusted operating income(1) was impacted by each of its reportable operating segments as follows:

- Positively by 3.5% due to an increase of 17.5% in adjusted operating income(1) at Weston Foods, including the negative impact of foreign currency translation as a result of the appreciation of the Canadian dollar relative to the United States dollar. Weston Foods adjusted operating income(1) was positively impacted by price increases, the shift in sales mix to higher margin products, and the benefits realized from the continued focus on cost reduction activities.
- Negatively by 17.8% due to a decrease of 22.2% in adjusted operating income(1) at Loblaw. In 2007, Loblaw invested in pricing in specific markets; however, cost reduction lagged the pricing investments which resulted in lower earnings.

The Company's 2007 consolidated adjusted operating margin(1) declined to 4.5% from 5.4% in 2006, and consolidated adjusted EBITDA margin(1) declined to 6.6% from 7.7% in 2006. Consolidated adjusted operating margin(1) declined in 2007 primarily due to the lower adjusted operating margin(1) at Loblaw, partially offset by the higher adjusted operating margin(1) at Weston Foods.

The Company's 2006 consolidated operating income decreased by $1,097 million, or 67.1%, to $537 million. The consolidated operating margin in 2006 was 1.7% compared to 5.2% in 2005. 2006 consolidated operating income included the following:

- a charge of $90 million related to restructuring and other charges;
- a charge of $60 million for the net effect of stock-based compensation and the associated equity derivatives;
- a charge of $68 million related to the inventory liquidation at Loblaw;
- income of $8 million related to the consolidation of VIEs by Loblaw;
- a charge of $800 million related to the non-cash Loblaw goodwill impairment charge;
- a charge of $84 million related to the Ontario collective labour agreement at Loblaw; and
- a charge of $12 million related to a departure entitlement charge at Loblaw.

After adjusting for the impact of the items described above, consolidated adjusted operating income(1) for 2006 was $1,643 million compared to $1,891 million in 2005, a decline of 13.1%.

The Company's 2006 consolidated adjusted operating income(1) was impacted by each of its reportable operating segments as follows:

- Positively by 1.4% due to an increase of 8.7% in adjusted operating income(1) at Weston Foods, including the negative impact of foreign currency translation as a result of the appreciation of the Canadian dollar relative to the United States dollar. In addition, Weston Foods adjusted operating income(1) was positively impacted by sales growth, including price increases in key product categories combined with changes in sales mix, and by the benefits realized from restructuring and other cost reduction activities.
- Negatively by 14.5% due to a decrease of 17.2% in adjusted operating income(1) at Loblaw. Adjusted operating income(1) in 2006 was adversely impacted by the effects of product supply issues, resulting from the implementation challenges arising from the 2005 conversions, and delays in program activities resulted in foregone sales and lost cost leverage on fixed components of operating and administrative expenses. In addition, the continued investment in lower food prices to drive sales growth had a negative impact on adjusted operating income(1). Higher information technology investments in addition to store and distribution centre operational costs, principally labour and higher third-party storage costs, were also incurred. Fixed assets impairment charges were recorded, due in part to a decision to suspend plans for a number of sites scheduled for future development as well as higher general merchandise mark downs taken to clear inventory through normal channels.

(1) See Non-GAAP Financial Measures beginning on page 55.

The Company's 2006 consolidated adjusted operating margin[1] declined to 5.4% from 6.5% in 2005, and consolidated adjusted EBITDA margin[1] declined to 7.7% from 8.8% in 2005. Consolidated adjusted operating margin[1] declined in 2006 primarily due to the lower adjusted operating margin[1] at Loblaw, partially offset by the higher adjusted operating margin[1] at Weston Foods.

The adjustments included to arrive at consolidated adjusted operating income[1] in 2005 were charges related to restructuring, the net effect of stock-based compensation and the associated equity derivatives, supply chain disruptions, the resolution of certain sales tax issues and income associated with the commodities futures fair value adjustment.

Interest Expense and Other Financing Charges

Interest expense and other financing charges consist primarily of interest on short and long term debt, interest and other financing charges on financial derivative instruments, net of interest earned on short term investments and interest capitalized to fixed assets.

In 2007, interest expense and other financing charges decreased $88 million, or 34.8%, to $165 million from $253 million in 2006.

The change is mainly due to:

- Interest expense on long term debt decreased $7 million, or 1.8%, to $386 million from $393 million in 2006 primarily as a result of lower average debt levels.
- Interest on financial derivative instruments, which includes the net effect of the Company's interest rate swaps, cross currency basis swaps and equity derivatives, resulted in a charge of $21 million (2006 – $15 million). The change in interest on financial derivative instruments was due mainly to an increase in United States short term interest rates and the cumulative loss transferred from other comprehensive loss and subsequent change in fair market value of the interest rate swaps previously designated as a cash flow hedge of the variable interest rate exposure on commercial paper.
- Non-cash income of $141 million (2006 – $73 million) was recorded in other financing charges representing the fair value adjustment of Weston's 2001 forward sale agreement for 9.6 million Loblaw common shares. See notes 6 and 24 to the consolidated financial statements for additional information.
- Net short term interest income increased to $53 million (2006 – $38 million) primarily due to higher interest income on United States dollar denominated cash, cash equivalents and short term investments and lower average short term debt levels partially offset by an increase in Canadian short term interest rates.
- Interest expense capitalized to fixed assets increased to $22 million (2006 – $21 million). Loblaw capitalizes interest incurred on debt related to real estate properties under development.

The 2007 weighted average fixed interest rate on long term debt (excluding capital lease obligations and the Exchangeable Debentures) was 6.6% (2006 – 6.6%) and the weighted average term to maturity was 16 years (2006 – 16 years).

In 2006, interest expense and other financing charges increased $66 million, or 35.3%, to $253 million from $187 million in 2005.

The change is mainly due to:

- Interest expense on long term debt decreased $11 million, or 2.7%, to $393 million from $404 million in 2005 primarily as a result of lower average debt levels.
- Interest on financial derivative instruments, which includes the net effect of the Company's interest rate swaps, cross currency basis swaps and equity derivatives, resulted in a charge of $15 million (2005 – income of $1 million). The change in interest on financial derivative instruments was due mainly to an increase in Canadian short term interest rates.
- Non-cash income of $73 million (2005 – $150 million) was recorded in other financing charges representing the fair value adjustment of Weston's 2001 forward sale agreement for 9.6 million Loblaw common shares. See notes 6 and 24 to the consolidated financial statements for additional information.
- Net short term interest income increased to $38 million (2005 – $25 million) primarily due to higher interest rates on United States dollar denominated cash, cash equivalents and short term investments partially offset by higher average short term debt and increased Canadian short term interest rates.
- Interest expense capitalized to fixed assets remained unchanged at $21 million as compared to 2005.

The 2006 weighted average fixed interest rate on long term debt (excluding capital lease obligations and the Exchangeable Debentures) was 6.6% (2005 – 6.6%) and the weighted average term to maturity was 16 years (2005 – 16 years).

(1) See Non-GAAP Financial Measures beginning on page 55.

Income Taxes

The Company's 2007 effective income tax rate decreased to 25.4% from 90.1% in 2006. In 2006, a non-deductible Loblaw goodwill impairment charge was recorded. The effective income tax rate in 2006 before the impact of the non-deductible goodwill impairment charge as presented in note 8 to the consolidated financial statements was 23.6%. The 2007 effective income tax rate was impacted by the following factors:

- the change in the proportion of taxable income earned across different tax jurisdictions and the income tax impact of the non-taxable amounts; and
- a $24 million net reduction to the future income tax expense recognized as a result of changes in the Canadian federal and certain provincial statutory income tax rates, the cumulative effect of which was included in the consolidated financial statements at the time of substantive enactment.

The Company's 2006 effective income tax rate increased to 90.1% from 30.6% in 2005. The increase was mainly the result of the non-deductible Loblaw goodwill impairment charge, which increased the 2006 effective income tax rate by 66.5%. The effective income tax rate before the impact of the non-deductible Loblaw goodwill impairment charge as presented in note 8 to the consolidated financial statements decreased to 23.6% in 2006 from 30.6% in 2005 as a result of the following factors:

- changes in the Canadian federal and certain provincial statutory income tax rates;
- a change in the proportion of taxable income earned across different tax jurisdictions; and
- a $24 million reduction to future income tax expense recognized as a result of changes in the Canadian federal and certain provincial statutory income tax rates, the cumulative effect of which was included in the consolidated financial statements at the time of substantive enactment.

Net Earnings from Continuing Operations

Net earnings from continuing operations for 2007 increased $453 million, or 411.8%, to $563 million from $110 million in 2006. Basic net earnings per common share from continuing operations for 2007 increased $3.49, or 811.6%, to $3.92 from $0.43 in 2006. The 2007 basic net earnings per common share from continuing operations of $3.92 included the impact of the following factors:

- a $0.72 per common share charge related to restructuring and other charges;
- a $0.63 per common share charge for the net effect of stock-based compensation and the associated equity derivatives;
- $0.10 per common share income related to the commodity futures fair value adjustment at Weston Foods;
- a $0.04 per common share charge related to the inventory liquidation at Loblaw;
- a $0.04 per common share charge related to the consolidation of VIEs by Loblaw;
- $0.03 per common share income related to the curtailment of a post-retirement plan at Weston Foods;
- $0.81 per common share non-cash income related to the accounting for Weston's 2001 forward sale agreement for 9.6 million Loblaw common shares; and
- $0.15 per common share income related to the adjustment to future income tax balances resulting from changes in Canadian federal and certain provincial statutory income tax rates.

After adjusting for the above noted items, Weston's 2007 adjusted basic net earnings per common share from continuing operations(1) was $4.26. This represents a 14.5% decrease compared to 2006 adjusted basic net earnings per common share from continuing operations(1) of $4.98, which was adjusted as outlined below.

Net earnings from continuing operations for 2006 decreased $606 million, or 84.6%, to $110 million from $716 million in 2005. Basic net earnings per common share from continuing operations for 2006 decreased $4.82, or 91.8%, to $0.43 from $5.25 in 2005. The 2006 basic net earnings per common share from continuing operations of $0.43 included the impact of the following factors:

- a $0.36 per common share charge related to restructuring and other charges;
- a $0.38 per common share charge for the net effect of stock-based compensation and the associated equity derivatives;
- a $0.21 per common share charge related to the inventory liquidation at Loblaw;
- a $3.84 per common share charge related to the non-cash Loblaw goodwill impairment;
- a $0.26 per common share charge related to the Ontario collective labour agreement at Loblaw;
- a $0.04 per common share charge related to a departure entitlement charge at Loblaw;
- $0.40 per common share non-cash income related to the accounting for Weston's 2001 forward sale agreement for 9.6 million Loblaw common shares; and
- $0.14 per common share income related to the adjustment to future income tax balances resulting from changes in the Canadian federal and certain provincial statutory income tax rates.

(1) See Non-GAAP Financial Measures beginning on page 55.

After adjusting for the above noted items, Weston's 2006 adjusted basic net earnings per common share from continuing operations[1] decreased 11.4% to $4.98 when compared to $5.62 in 2005. The adjustments to basic earnings per common share from continuing operations in 2005 were items related to restructuring, the commodities futures fair value adjustment, supply chain disruptions, the resolution of certain sales tax issues, the net effect of stock-based compensation and the associated equity derivatives, changes in statutory income tax rates, and VIE consolidation, as well as income related to the accounting for Weston's 2001 forward sale agreement for 9.6 million Loblaw shares.

Discontinued Operations

In 2007, the Company had no gain or loss from discontinued operations. The gain from discontinued operations in 2006 was $11 million. The 2006 gain from discontinued operations was primarily related to the final adjustments to the proceeds in 2006 associated with the previously completed 2005 sale of the remaining discontinued Fisheries operations.

For additional information, see note 10 to the consolidated financial statements.

Net Earnings

Net earnings of $563 million in 2007 increased from $121 million in 2006. Net earnings in 2006 decreased to $121 million from $698 million in 2005. Net earnings from continuing operations of $563 million increased from $110 million in 2006. Net earnings from continuing operations decreased to $110 million from $716 million in 2005. Changes in the Company's net earnings and net earnings from continuing operations over the past two years were impacted by the factors described above.

The new accounting standards implemented in 2007 and the resulting impact on the financial position and results of operations are outlined in the Accounting Standards Implemented in 2007 section of this MD&A. The accounting standards implemented in 2006 did not have a material impact on the financial position and results of operations of the Company.

Changes in minority interest did not have a significant impact on growth rates of the Company's net earnings over the past two years as Weston's ownership of Loblaw has not changed over this period.

6.2 CONSOLIDATED FINANCIAL CONDITION

($ millions except where otherwise indicated)	**2007**	2006	2005
Total assets	**$ 18,388**	$ 18,595	$ 18,593
Total long term debt (excluding amount due within one year)	**$ 5,494**	$ 5,918	$ 5,913
Dividends declared per share ($) – Common share	**$ 1.44**	$ 1.44	$ 1.44
– Preferred share:			
Series I	**$ 1.45**	$ 1.45	$ 1.45
Series II	**$ 1.29**	$ 1.29	$ 1.29
Series III	**$ 1.30**	$ 1.30	$ 0.92
Series IV	**$ 1.30**	$ 1.30	$ 0.54
Series V	**$ 1.19**	$ 0.83	

The Company's total assets in 2007 were less than in 2006 and 2005. The decrease in 2007 was primarily due to a significant strengthening of the Canadian dollar relative to the United States dollar, causing a decline in the translated balances of United States dollar denominated assets. The Company's total assets were higher in 2007 than in 2006 on a foreign currency adjusted basis. Accounts receivable also increased in 2007 and 2006. A substantial portion of credit card receivables of *President's Choice* Bank ("*PC* Bank"), a wholly owned subsidiary of Loblaw, is sold to independent trusts and the unsecuritized balance net of the allowance for credit losses increased by $301 million over 2005. After growing in 2006 as a result of capital expenditures in excess of depreciation, fixed assets declined in 2007 as a result of reduced capital expenditures and increased sales of fixed assets. Other assets increased in 2007 and 2006 due to an increase in the fair value of Weston's 2001 forward sale agreement for 9.6 million Loblaw shares, driven by the decline in the Loblaw share price. In addition, the strengthening of the Canadian dollar against the United States dollar increased Loblaw's unrealized cross currency basis swaps receivable in 2007. In 2006, goodwill decreased as a result of the non-cash Loblaw goodwill impairment charge.

(1) See Non-GAAP Financial Measures beginning on page 55.

Cash flows from operating activities have covered a large portion of the funding requirements for the Company over the past two years.

Over the past two years, the Company's funding requirements resulted primarily from:

- the capital investment program;
- dividends paid on common and preferred shares;
- credit card receivables, after securitization; and
- repayment of long term debt.

In 2007, as a result of the strengthening of the Canadian dollar relative to the United States dollar, the change in the cumulative foreign currency translation adjustment negatively impacted shareholders' equity by $508 million. In 2006, as a result of the slight decline of the Canadian dollar relative to the United States dollar, the change in the cumulative foreign currency translation adjustment positively impacted shareholders' equity by $15 million.

Financial Ratios

The Company's 2007 return on average total assets[(1)] of 6.7% was higher than the 2006 return of 3.2%. The Company's 2006 return on average total assets[(1)] of 3.2% was lower than the 2005 return of 10.0%. The return in 2006 was negatively impacted by the non-cash Loblaw goodwill impairment charge recorded in operating income as outlined above.

The Company's 2007 return on average common shareholders' equity of 12.7% was higher than the 2006 return of 1.3%. The increase in 2007 was largely the result of higher operating income mainly due to the 2006 non-cash Loblaw goodwill impairment charge and lower interest expense and other financing charges in 2007, including the $141 million non-cash income (2006 – $73 million) related to the fair value adjustment of Weston's 2001 forward sale agreement for 9.6 million Loblaw common shares. The five year average annual return on common shareholders' equity was 13.1%.

The Company's 2006 return on average common shareholders' equity of 1.3% decreased compared to the 2005 return of 16.7%, primarily due to the non-cash Loblaw goodwill impairment charge, incremental costs and charges recorded in operating income as outlined previously and higher interest expense and other financing charges due to the decline in non-cash income to $73 million in 2006 (2005 – $150 million) related to the fair value adjustment of Weston's 2001 forward sale agreement for 9.6 million Loblaw common shares.

The Company's 2007 net debt (excluding Exchangeable Debentures)[(1)] to equity ratio remained unchanged from 2006 at 0.96:1. The decrease in commercial paper and increase in cash and cash equivalents were offset by decreases in shareholders' equity resulting from the translation of the Company's U.S. net investment due to the appreciation of the Canadian dollar relative to the United States dollar in 2007, partially offset by higher retained earnings.

The Company's 2006 net debt (excluding Exchangeable Debentures)[(1)] to equity ratio was 0.96:1 compared to the 2005 ratio of 1.02:1. The change in this ratio from 2005 was the result of the following factors:

- the issuance of preferred shares by Weston; and
- an increase in United States dollar denominated cash, cash equivalents and short term investments;

partially offset by:

- lower net earnings primarily due to:
  - lower Loblaw earnings due to the non-cash Loblaw goodwill impairment charge and incremental costs and charges recorded in operating income as outlined previously; and
  - higher interest expense and other financing charges due to the decline in non-cash income to $73 million in 2006 (2005 – $150 million) related to the fair value adjustment of Weston's 2001 forward sale agreement for 9.6 million Loblaw common shares.

The 2007 interest coverage ratio increased to 5.9 times compared to 2.0 times in 2006 due to an increase in operating income and lower interest expense and other financing charges, including the non-cash income of $141 million (2006 – $73 million) recorded in 2007 related to the fair value adjustment of Weston's 2001 forward sale agreement for 9.6 million Loblaw common shares which positively impacted the interest coverage ratio by approximately 2.6 times.

(1) See Non-GAAP Financial Measures beginning on page 55.

The 2006 interest coverage ratio declined to 2.0 times compared to 7.9 times in 2005 due to the non-cash Loblaw goodwill impairment charge, incremental costs and charges as outlined above and higher interest expense and other financing charges, including the non-cash income of $73 million (2005 – $150 million) recorded in 2006 related to the fair value adjustment of Weston's 2001 forward sale agreement for 9.6 million Loblaw common shares. The Loblaw goodwill impairment charge, which is a significant non-cash item in operating income, combined with the non-cash income of $73 million related to the fair value adjustment of Weston's 2001 forward sale agreement for 9.6 million Loblaw common shares, adversely impacted the interest coverage ratio by approximately 1.9 times.

Dividends

The declaration and payment of dividends and the amount thereof are at the discretion of the Board, which takes into account the Company's financial results, capital requirements, available cash flow and other factors the Board considers relevant from time to time. Over the long term, the Company's objective is for its common dividend payment ratio to be in the range of 20% to 25% of the prior year's adjusted basic net earnings per common share from continuing operations[1]. Currently, there is no restriction that would prevent the Company from paying common dividends at historical levels. During 2007, the Board declared quarterly dividends as follows:

($)	2007 Quarterly Dividends Declared per Share
Common shares	$ 0.36
Preferred shares – Series I	$ 0.36
– Series II	$ 0.32
– Series III	$ 0.32
– Series IV	$ 0.32
– Series V	$ 0.30

The 2007 annualized dividend per common share of $1.44 was equal to 28.9% of the 2006 adjusted basic net earnings per common share from continuing operations[1]. Subsequent to year end, the Board declared a quarterly dividend of $0.36 per common share, payable April 1, 2008.

Outstanding Share Capital

The Company's outstanding share capital is comprised of common shares and preferred shares. The following table details the authorized and outstanding common shares and preferred shares.

Share Capital	Authorized	Outstanding
Common shares	Unlimited	129,074,526
Preferred shares – Series I	Unlimited	9,400,000
– Series II	Unlimited	10,600,000
– Series III	Unlimited	8,000,000
– Series IV	Unlimited	8,000,000
– Series V	Unlimited	8,000,000

For preferred shares Series I, Series II, Series III, Series IV and Series V holders, Weston may, at its option redeem for cash, in whole or in part, these outstanding preferred shares on or after the redemption dates specified by the terms of each series of preferred shares. Weston may at any time after issuance give the holders of these preferred shares the right, at the option of the holder, to convert their preferred shares into preferred shares of a further series designated by Weston on a share-for-share basis on a date specified by Weston. In addition, Series II preferred shares are convertible on or after July 1, 2009, at the option of the holder, into a number of Weston common shares determined by dividing $25.00 by the greater of $2.00 and 95% of the then current market price of Weston common shares. Further information on the Company's outstanding share capital is provided in note 21 to the consolidated financial statements.

At year end, a total of 2,299,914 stock options and share appreciation rights were outstanding and represented 1.8% of Weston's issued and outstanding common shares, which was within Weston's guideline of 5%. Further information on Weston's stock-based compensation is provided in note 23 to the consolidated financial statements.

(1) See Non-GAAP Financial Measures beginning on page 55.

7. RESULTS OF REPORTABLE OPERATING SEGMENTS

The following discussion provides details of the 2007 results of operations of each of the Company's reportable operating segments.

7.1 WESTON FOODS OPERATING RESULTS

($ millions except where otherwise indicated)	2007	2006	Change
Sales	**$ 4,296**	$ 4,350	(1.2)%
Operating income	**$ 366**	$ 256	43.0%
Operating margin	**8.5%**	5.9%	
Adjusted operating income(1)	**$ 382**	$ 325	17.5%
Adjusted operating margin(1)	**8.9%**	7.5%	
Adjusted EBITDA(1)	**$ 498**	$ 440	13.2%
Adjusted EBITDA margin(1)	**11.6%**	10.1%	
Return on average total assets(1)	**9.9%**	6.6%	

(1) See Non-GAAP Financial Measures beginning on page 55.

Adjusted Operating Income and EBITDA(1)

($ millions)	2007	2006
Operating income	**$ 366**	$ 256
Add impact of the following:		
Restructuring and other charges	**5**	46
Net effect of stock-based compensation and the associated equity derivatives	**37**	23
Commodity futures fair value adjustment	**(19)**	
Curtailment of post-retirement plan	**(7)**	
Adjusted operating income(1)	**382**	325
Add impact of the following:		
Depreciation and amortization	**116**	115
Adjusted EBITDA(1)	**$ 498**	$ 440

(1) See Non-GAAP Financial Measures beginning on page 55.

Approximately 86% of Weston Foods 2007 sales were generated by the North American baking divisions, with the remaining sales in the Canadian dairy division.

Sales and operating income in 2007 were impacted by the following trends:

- The shift in consumer eating preferences toward healthier and more nutritious offerings, as well as toward products that are more convenient, portion controlled and that can be consumed away from home, continued in 2007. Weston Foods has responded to these trends with innovative and expanded products across its product portfolio resulting in new sales growth as well as improved operating margins. These trends are expected to continue into 2008 and Weston Foods is well positioned to participate in this growth with its strong portfolio of on-trend offerings under its *Thomas*', *Arnold*, *Wonder*, *Country Harvest* and *Neilson* brands, as well as continued support of the licensed brand, *Weight Watchers®*.
- The continuing shift in consumer food shopping patterns toward alternate format retail channels rather than traditional, conventional supermarket formats resulted in sales growth with alternate format retailers, specifically mass merchandisers. Weston Foods continues to focus on ensuring its products are well aligned to serve all its customers' needs.
- Price increases in key product categories combined with a shift in sales mix to higher margin products had a positive impact on both sales and operating income. Continued efforts to focus on identifying and supporting key core brands and higher margin offerings contributed to the positive change in mix.

- Inflationary cost pressures related to certain ingredients continued and accelerated in 2007.
- The continued focus on productivity and cost reduction contributed to the growth in operating income.
- The negative impact of translating United States dollar denominated sales and operating income resulted in negative sales growth and constrained operating income growth.

A detailed discussion on how these trends and other factors impacted sales and operating income in 2007 is set out below.

Sales

Weston Foods sales for 2007 of $4.3 billion decreased 1.2% compared to 2006. Foreign currency translation negatively impacted reported sales growth by approximately 3.4%. Price increases across key product categories combined with changes in sales mix increased sales by 3.5% for 2007. Overall volume decreased 1.3% for 2007 and was negatively impacted by approximately 0.7% due to the combined effect of the exit from the United States frozen foodservice bagel business early in the third quarter of 2006 and the discontinuance of contract manufacturing of biscuits for certain customers during 2006. The remaining volume decline of 0.6% for the year was due to growth in certain higher margin categories being more than offset by declines in other categories.

The following sales analysis excludes the impact of foreign currency translation.

Fresh bakery sales, principally bread, rolls, English muffins and bagels, increased approximately 4.5% in 2007 compared to 2006 and represented approximately 51% of total Weston Foods sales in both 2007 and 2006. Sales growth was driven by price increases in key product categories combined with changes in sales mix. Branded volume increases in the *Arnold* and *Thomas*' brands in the United States and the *D'Italiano* brand in Canada were more than offset by volume declines in other categories particularly in food service and private label products. Sales growth in whole grain and whole wheat products exceeded the sales growth of white flour based products. The introduction of new and expanded product offerings contributed positively to branded sales growth in 2007, including:

- *Thomas'* Mini Squares Bagelbread, which combines traditional bagel flavour with the softness of bread in a portion-controlled serving size;
- *Thomas'* 100 Calorie English Muffin; and
- the *Wonder+* line expansion into new categories, all of which offer the same *Wonder* taste with the goodness of whole wheat.

Fresh-baked sweet goods sales, primarily sold under the *Entenmann's* brand, decreased approximately 0.8% in 2007 compared to 2006 and represented approximately 13% of total Weston Foods sales, down from approximately 14% in 2006. The sales decline for this category in 2007 was due to lower volumes driven by softness in full size categories that was partially offset by growth in the hand-held category and the introduction of new and expanded products, such as the *Entenmann's* 100 Calorie *Little Bites*.

Frozen bakery sales, principally bread, rolls, bagels, English muffins and sweet goods, increased approximately 3.8% in 2007 compared to 2006 and represented approximately 15% of total Weston Foods sales, up from approximately 14% in 2006. Sales growth for this category in 2007 was due to price increases combined with changes in sales mix. Volumes for the year were flat, as volume gains were offset by the decline in volumes caused by the exit from the United States frozen foodservice bagel business early in the third quarter of 2006.

Dairy and bottled beverage sales increased approximately 3.6% in 2007 compared to 2006 and represented approximately 14% of total Weston Foods sales, up from approximately 13% in 2006. Sales growth for this category in 2007 was driven mainly by pricing, volume gains and the improvement in sales mix as growth continued to be experienced in a number of key categories, particularly value-added and flavoured milk products. Strong growth in aseptically bottled products was achieved in 2007 with the expansion of products offered under *The Ultimate* line by *Neilson*.

Biscuit sales, principally wafers, ice-cream cones, cookies and crackers, decreased approximately 11.0% in 2007 compared to 2006 and represented approximately 7% of total Weston Foods sales, down from approximately 8% in 2006. The sales decline for this category in 2007 was due to lower sales volume in certain categories and the discontinuance of contract manufacturing of biscuits for certain customers during 2006. This discontinuance was a result of the previously approved plan to restructure the Weston Foods United States biscuit operations.

Operating Income

Weston Foods operating income increased $110 million, or 43.0%, to $366 million from $256 million in 2006 and was impacted by lower restructuring and other charges, higher net stock-based compensation and non-cash income items.

In 2007, Weston Foods recognized the following in operating income:

- a charge of $37 million (2006 – $23 million) for the net effect of stock-based compensation and the associated equity derivatives;
- income of $19 million (2006 – nil) related to the commodity futures fair value adjustment;
- a charge of $5 million (2006 – $46 million) related to restructuring and other charges; and
- income of $7 million (2006 – nil) related to the curtailment of a post-retirement plan.

Weston Foods is exposed to price fluctuations primarily as a result of anticipated purchases of certain raw materials, fuels and utilities. In accordance with the Company's risk management strategy, Weston Foods enters into commodity futures to reduce the impact of price fluctuations in a specified percentage of forecasted raw material purchases over a specified period of time. These commodity futures are not acquired for trading or speculative purposes. These futures are not designated as cash flow hedges of anticipated future raw material purchases, therefore hedge accounting does not apply. Accordingly, the changes in fair value of these futures are recorded in operating income. During 2007, Weston Foods recorded in operating income a non-cash gain of $19 million (2006 – nil) related to the fair value adjustment of exchange traded futures that were not designated within a hedging relationship. Regardless of designation for accounting, these futures had the economic impact of largely mitigating the associated risks arising from price fluctuations in the underlying commodities.

During 2007, the amendment of a post-retirement benefit plan resulted in a significant reduction in the number of future years of service, thereby triggering a curtailment. Accordingly, a $7 million pro rata portion of the unamortized past service gain from a previous plan amendment was recognized as a curtailment gain in 2007. A detailed discussion of the impact of restructuring and other charges is set forth in the Restructuring and Other Charges section below.

After adjusting for the above-noted items, adjusted operating income[(1)] for 2007 was $382 million, an increase of 17.5% from $325 million in 2006. Adjusted operating margin[(1)] and adjusted EBITDA margin[(1)] for 2007 were 8.9% and 11.6%, respectively (2006 – 7.5% and 10.1%). In addition, foreign currency translation negatively impacted 2007 adjusted operating income[(1)] growth by approximately 4.3 percentage points.

Weston Foods 2007 adjusted operating income[(1)] was positively impacted by sales growth, primarily due to price increases combined with changes in sales mix, and the benefits realized from the continued focus on cost reduction initiatives, including restructuring activities and reduced product returns. Pricing and other actions mitigated the impact of inflationary cost pressures related to certain ingredients, primarily flour, oils and sugar. For the year, lower plant and distribution costs were partially offset by an increased investment in marketing initiatives. Gross margin and adjusted operating margin[(1)] both improved as a result of the factors described above.

During 2007, a reduction in insurance reserves, relating primarily to workers' compensation benefits in the United States, resulted in a benefit of $8 million and was recorded in operating income. This benefit was largely a result of favourable experience in workers' compensation claims and an increased focus on workplace safety programs.

Profitability in the United States fresh-baked sweet goods category declined in 2007 and remained a challenge as a result of changing consumer eating and shopping preferences and a high fixed cost manufacturing and distribution structure. Weston Foods is addressing these challenges with the previously announced downsizing of its fresh-baked goods facility in Bay Shore, New York, which is expected to be complete by the third quarter of 2008.

Weston Foods continues to evaluate strategic and cost reduction initiatives related to its manufacturing assets, distribution networks and administrative infrastructure with the objective of ensuring a low cost operating structure. Certain of these initiatives are in progress, are nearing completion or have been completed. Individual actions will be initiated as plans are finalized and approved. A further discussion of these activities is included in the Restructuring and Other Charges section below.

(1) See Non-GAAP Financial Measures beginning on page 55.

Management's Discussion and Analysis

Restructuring and Other Charges

The following table summarizes the restructuring and other charges by plan for 2007 and 2006:

($ millions)	Employee Termination Benefits and Site Closing and Other Exit Costs	Fixed Asset Impairment and Accelerated Depreciation	(Gain) Loss on Sale of Fixed Assets	Total
Costs recognized in 2007:				
Manufacturing asset restructuring:				
Biscuit operations	**$ 2**		**$ (6)**	**$ (4)**
Ice-cream cone operations			**(9)**	**(9)**
Fresh bakery operations	**1**	**$ 6**		**7**
Frozen bagel operations			**1**	**1**
	3	**6**	**(14)**	**(5)**
Distribution network restructuring	**7**			**7**
Administrative restructuring and consolidation of offices	**3**			**3**
Total costs recognized in 2007	**$ 13**	**$ 6**	**$ (14)**	**$ 5**
Costs recognized in 2006:				
Manufacturing asset restructuring:				
Biscuit operations	$ 10	$ 6		$ 16
Sweet goods operations	5	4		9
Frozen bagel operations	2	5		7
Ice-cream cone operations	2	3		5
Fresh bakery operations	1	1		2
	20	19		39
Distribution network restructuring	6			6
Completion of other prior year plans			$ 1	1
Total costs recognized in 2006	$ 26	$ 19	$ 1	$ 46

Manufacturing Asset Restructuring

During 2007, Weston Foods approved the following manufacturing asset restructuring activities:

- Weston Foods approved and completed a plan to transfer two manufacturing lines for certain private label English muffins in the United States to third-party producers or other Weston Foods manufacturing lines already in place. As a result of this decision, Weston Foods recognized $2 million of accelerated depreciation during 2007.
- Weston Foods approved and completed a plan to exit certain bread and roll manufacturing lines in the Southeastern United States. All production associated with these lines will be transferred to third-party producers or other Weston Foods manufacturing facilities. As a result of this decision, Weston Foods recognized $4 million of accelerated depreciation and $1 million of employee termination benefits and other exit related costs during 2007.

During 2006, Weston Foods approved a plan to close a frozen bagel plant in Nebraska, which was completed in that year. As a result of this restructuring, Weston Foods recognized total accelerated depreciation of $5 million and $2 million of employee termination benefits and other exit related costs during 2006. During 2007, Weston Foods completed the sale of this facility for proceeds of $1 million and recognized a loss on sale of fixed assets of $1 million.

During 2006, Weston Foods approved a plan to close an ice-cream cone baking facility in Los Angeles, California and transfer the production to other existing Weston Foods facilities. This restructuring was completed in the first quarter of 2007. As a result of this restructuring, Weston Foods recognized total accelerated depreciation of $3 million and $2 million of employee termination benefits and other exit related costs during 2006. During 2007, Weston Foods completed the sale of this facility for proceeds of $11 million and recognized a gain on sale of fixed assets of $9 million.

During 2005, Weston Foods approved a plan to restructure its United States biscuit operations. This plan included the closure of two biscuit facilities located in Elizabeth, New Jersey and Richmond, Virginia by the end of 2006, with the majority of the production relocated to a new facility in Virginia and an existing Weston Foods facility already operating in South Dakota. The sales of these two facilities were completed in 2005. All manufacturing activities ceased in the Elizabeth, New Jersey and Richmond, Virginia facilities by the end of 2006. During 2007, Weston Foods vacated the Elizabeth, New Jersey facility in accordance with the terms and conditions of the sale lease-back arrangement and accordingly, recognized the previously deferred gain on the sale of fixed assets of $6 million. In addition, during 2007, Weston Foods recognized nil (2006 – $6 million) of accelerated depreciation and $2 million (2006 – $10 million) of employee termination benefits and other exit related costs. By the end of 2007, total charges of $21 million of accelerated depreciation and $40 million of employee termination benefits and other exit related costs had been recognized on a cumulative basis related to this restructuring plan, which is now complete.

Additional activities during 2006 included:

- During 2006, Weston Foods approved a restructuring plan to downsize its fresh-baked sweet goods facility in Bay Shore, New York. The plan involves the transfer of full-size dessert cake and cookie production to other existing Weston Foods facilities. Once the downsizing is complete, the Bay Shore location will be a more focused facility producing primarily danish and pie products. This restructuring is expected to be completed by the third quarter of 2008. As a result of this restructuring, Weston Foods recognized a total fixed asset impairment charge of $4 million and a total charge of $5 million for employee termination benefits and other exit related costs during 2006.
- During 2006, Weston Foods approved and completed a plan to close a fresh bakery manufacturing facility in Quebec. During 2006, Weston Foods recognized $1 million of accelerated depreciation and $1 million of employee termination benefits and other exit related costs.

Distribution Network Restructuring

During 2007, Weston Foods approved the following distribution network restructuring activities:

- Weston Foods approved plans to restructure its Ontario frozen bakery distribution operations, to further restructure its Quebec fresh bakery distribution operations and to restructure the dairy distribution network. These plans involve the closure and/or consolidation of certain warehouses, outsourcing certain warehousing and distribution functions to third-party warehousing service providers and certain route restructurings. As a result of these restructuring plans, Weston Foods recognized $3 million of employee termination benefits and other exit related costs during 2007 and expects to record an additional $1 million related to other exit costs in 2008 when these plans are expected to be substantially completed.
- Weston Foods also approved a restructuring plan to exit and transfer certain distribution and transportation activities in the mid-Western United States to third-party logistic providers which is expected to be completed by the end of the second quarter of 2008. As a result of this plan, Weston Foods recognized $2 million of employee termination benefits during 2007.

During 2006, Weston Foods approved a plan to restructure a portion of its distribution network in Quebec. During 2007, Weston Foods recognized $2 million (2006 – $6 million) of employee termination benefits and other exit related costs pursuant to this plan which is expected to be substantially completed in 2008.

Administrative Restructuring and Consolidation of Offices

During 2007, Weston Foods approved plans to consolidate, relocate and restructure certain sales and administrative functions in the United States. These plans will be completed by the second quarter of 2008. As a result of this decision, Weston Foods recognized $3 million of employee termination benefits and other exit related costs during 2007 and no additional restructuring and other charges are anticipated.

Completion of Other Prior Year Plans

During 2006, Weston Foods recognized a loss on the sale of fixed assets of $1 million related to a restructuring plan approved prior to 2006.

Further information on Weston Foods restructuring and other charges is provided in note 4 to the consolidated financial statements.

In 2008, Weston Foods anticipates challenging market conditions as unprecedented increases for ingredient and other input costs are expected. Weston Foods plans to offset these higher input costs by ongoing cost reduction initiatives and pricing as necessary.

This outlook should be read in conjunction with the Forward-Looking Statements section of the MD&A on page 5.

7.2 LOBLAW OPERATING RESULTS

($ millions except where otherwise indicated)	2007	2006	Change
Sales	$ 29,384	$ 28,640	2.6%
Sales excluding the impact of tobacco sales and VIEs[1]	$ 27,915	$ 26,834	4.0%
Operating income	$ 728	$ 281	159.1%
Operating margin	2.5%	1.0%	
Adjusted operating income[1]	$ 1,026	$ 1,318	(22.2)%
Adjusted operating margin[1]	3.7%	4.9%	
Adjusted EBITDA[1]	$ 1,581	$ 1,884	(16.1)%
Adjusted EBITDA margin[1]	5.7%	7.0%	
Return on average total assets[1]	5.7%	2.2%	

(1) See Non-GAAP Financial Measures beginning on page 55.

Sales and Sales Growth Excluding the Impact of Tobacco Sales and VIEs[1]

($ millions except where otherwise indicated)	2007	2006
Total sales	$ 29,384	$ 28,640
Less: Sales attributable to tobacco sales	1,013	1,423
Sales attributable to the consolidation of VIEs[1]	456	383
Sales excluding the impact of tobacco sales and VIEs[1]	$ 27,915	$ 26,834
Total sales growth	2.6%	3.7%
Less: Impact on sales growth attributable to tobacco sales	(1.7)%	(1.2)%
Impact on sales growth attributable to the consolidation of VIEs	0.3%	(0.1)%
Sales growth excluding the impact of tobacco sales and VIEs[1]	4.0%	5.0%
Same-store sales growth	2.4%	0.8%
Same-store sales growth excluding the impact of decreased tobacco sales[1]	3.4%	2.0%

(1) See Non-GAAP Financial Measures beginning on page 55.

Adjusted Operating Income and EBITDA[1]

($ millions)	2007	2006
Operating income	$ 728	$ 281
Add (deduct) impact of the following:		
Restructuring and other charges	222	44
Net effect of stock-based compensation and the associated equity forwards	72	37
Inventory liquidation	15	68
VIEs	(11)	(8)
Goodwill impairment charge		800
Ontario collective labour agreement		84
Departure entitlement charge		12
Adjusted operating income[1]	1,026	1,318
Add (deduct) impact of the following:		
Depreciation and amortization	588	590
VIE depreciation and amortization	(33)	(24)
Adjusted EBITDA[1]	$ 1,581	$ 1,884

(1) See Non-GAAP Financial Measures beginning on page 55.

Sales

Full year sales for 2007 increased $744 million, or 2.6%, to $29.4 billion compared to $28.6 billion in 2006. Total sales excluding the impact of tobacco sales and VIEs[1] increased by $1.1 billion or 4.0% over 2006. The following factors further explain the major components in the change in sales over the prior year:

- same-store sales growth excluding the impact of decreased tobacco sales[1] increased 3.4% (2006 – 2.0%). In the third quarter of 2006, a major tobacco supplier commenced shipping directly to certain customers of Loblaw's Cash & Carry and wholesale club network, adversely impacting sales. This loss of sales affects comparisons to 2006 for the first three quarters of 2007;
- same-store sales growth by format in 2007 for Superstore, Hard Discount and Great Food were 3.8%, 4.6% and 0.4%, respectively, compared to 2006. The pricing investments in 2007 were targeted primarily within the Superstore and Hard Discount formats;
- national food price inflation as measured by "The Consumer Price Index for Food Purchased from Stores" ("CPI") in 2007 was 2.7% (2006 – 2.3%). Loblaw's analysis indicates that its internal retail food price inflation for 2007 was approximately 1.3% compared to 2006;
- positive volume growth based on retail units sold in 2007 of 1.9% (2006 – 1.6%); and
- 34 (2006 – 37) new corporate and franchised stores were opened and 79 (2006 – 33) stores were closed, including 46 stores that were closed as part of a previously announced store operations restructuring plan, and stores which underwent conversions and major expansions. Net retail square footage decreased 0.1 million square feet (2006 – increased 1.2 million square feet), or (0.2)%, in 2007 from year end 2006.

Sales of control label products for 2007 amounted to $6.6 billion compared to $6.2 billion in 2006. Control label penetration, which is measured as control label retail sales as a percentage of total retail sales, was 24.0% for 2007, compared to 22.9% for 2006. Loblaw introduced over 600 new control label products in 2007, plus 800 new home products. Loblaw's control label program, which includes *President's Choice*, *PC*, *President's Choice Organics*, *Blue Menu*, *Mini Chefs*, *no name*, *Joe Fresh Style*, *Club Pack*, *President's Choice GREEN*, *EXACT*, *Teddy's Choice* and *Life@Home*, provides additional sales growth potential.

Loblaw will be focusing on the following initiatives, coupled with continued focus on value-for-money, promotions and advertising where appropriate:

- focus on on-shelf availability of product through an enhancement of customer focus and supply chain, and stronger store processes;
- restoring innovation as a competitive advantage both for control label products as well as distinctive environments in each retail format;
- refining three distinctive retail formats: Superstore, Great Food and Hard Discount;
- increasing the number of stores carrying the *Joe Fresh Style* brand apparel offering;
- emphasizing a fresh first focus by raising presentation and quality standards; and
- investing in employees and providing training to encourage meeting customer needs.

Operating Income

Operating income of $728 million for 2007 increased by $447 million or 159.1% compared to $281 million in 2006 resulting in an increase in operating margin to 2.5% in 2007 from 1.0% in 2006.

Operating income in both 2007 and 2006 was affected by a number of specific items as outlined below:

- a charge of $197 million (2006 – nil) related to Project Simplify involving restructuring and streamlining of merchandising and store operations. Costs were comprised of $139 million for employee termination benefits including severance, additional pension costs resulting from the termination of employees and retention costs; and $58 million of other costs, primarily consulting. Total restructuring costs under this plan, comprised primarily of severance costs, are now anticipated to be approximately $200 million with the remaining costs to be expensed in 2008;
- a charge of $9 million (2006 – $8 million) in connection with the previously announced plan to restructure Loblaw's supply chain network;
- a charge of $16 million (2006 – $35 million) in connection with the previously announced closure of certain stores in the Quebec and Atlantic markets and in the wholesale network that were part of store operations restructuring activities;

(1) See Non-GAAP Financial Measures beginning on page 55.

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- a charge of $72 million (2006 – $37 million) for the net effect of stock-based compensation and the associated equity forwards. The majority of the expense in 2007 included a non-cash loss on equity forwards of $67 million (2006 – $32 million) resulting from a decline in Loblaw's share price during the year;
- a charge of $15 million (2006 – $68 million) for the liquidation of general merchandise inventory;
- income of $11 million (2006 – $8 million) resulting from the consolidation of VIEs;
- nil (2006 – charge of $1 million) related to the head office move and reorganization of the operation support functions;
- nil (2006 – charge of $800 million) for a non-cash goodwill impairment charge related to the goodwill established on the acquisition of Provigo Inc. in 1998;
- nil (2006 – charge of $84 million) related to the ratification of a new four-year collective agreement with members of certain Ontario locals of the UFCW; and
- nil (2006 – charge of $12 million) related to a departure entitlement charge.

In 2007, restructuring and other charges of $222 million (2006 – $44 million) were recorded within operating income. A summary of restructuring and other charges is included in the table for the years indicated below:

($ millions)	**Costs Recognized 2007**	Costs Recognized 2006	Costs Recognized 2005	Total Expected Costs	Total Expected Costs Remaining
Project Simplify	**$ 197**			$ 200	$ 3
Store operations	**16**	$ 35		51	
Supply chain network	**9**	8	$ 62	90	11
Office move and reorganization of the operation support functions		1	24	25	
Total restructuring and other charges	**$ 222**	$ 44	$ 86	$ 366	$ 14

Details regarding the nature of the above charges are described in note 4 to the consolidated financial statements.

After adjusting for the above-noted items, adjusted operating income(1) for 2007 decreased by $292 million, or 22.2%, to $1,026 million compared to $1,318 million in 2006. Adjusted operating margin(1) decreased to 3.7% in 2007 compared to 4.9% in 2006 as growth in operating expenses exceeded growth in sales. Adjusted EBITDA margin(1) decreased to 5.7% from 7.0% in 2006.

In addition, the 2007 adjusted operating income(1) was influenced by the following items:

- incremental consulting costs compared to the prior year, other than those in connection with Project Simplify, amounted to $75 million including expenses related to new supply chain and information technology improvement initiatives of $16 million;
- pharmacy-related operating income was reduced by $25 million due to legislative changes introduced in 2006 by the Ontario government;
- adjustments in estimates related to post-employment and long term disability benefits and deferred product development and information technology costs reduced operating income by $24 million;
- costs associated with the change in Loblaw's executive bonus plan were $11 million;
- a gain of $11 million from the sale of an office building in Calgary, Alberta;
- an incremental non-cash fixed asset impairment charge of $6 million related to asset carrying values in excess of fair values at specific store locations. The 2007 charge was $33 million compared to $27 million in 2006; and
- a decline in the gross margin, primarily due to targeted price reductions to provide value to customers and changes in sales mix partially offset by improvements in shrink.

Loblaw's sales volumes have been positively responding to its investments in lower prices to give value to its customers. Loblaw expects this to continue in 2008. Investments in price will also continue. However, Loblaw expects that cost reductions in 2008 will help to support its profitability. Sales, margins and profitability in the first half of 2008 in relation to 2007 may be affected by more difficult comparables.

(1) See Non-GAAP Financial Measures beginning on page 55.

8. LIQUIDITY AND CAPITAL RESOURCES

8.1 MAJOR CASH FLOW COMPONENTS

($ millions)	2007	2006	Change
Cash flows from operating activities of continuing operations	**$ 1,673**	$ 1,452	$ 221
Cash flows used in investing activities of continuing operations	**$ (832)**	$ (1,715)	$ 883
Cash flows used in financing activities of continuing operations	**$ (511)**	$ (70)	$ (441)

Cash Flows from Operating Activities of Continuing Operations

Cash flows from operating activities of continuing operations increased in 2007 to $1.7 billion from $1.5 billion in 2006. The change in cash flows from operating activities of continuing operations for the year was mainly due to the change in non-cash working capital due to the timing of income tax refunds relating to prior years, an increase in accounts payable and accrued liabilities and a reduction in pension funding.

Cash Flows used in Investing Activities of Continuing Operations

Cash flows used in investing activities of continuing operations in 2007 were $0.8 billion compared to $1.7 billion in 2006. The change was primarily due to a decline of $0.4 billion in capital expenditures, an increase in the proceeds from fixed asset sales, and the shorter term to maturity profile of the Company's short term investments portfolio, which resulted in less of a shift to short term investments from cash and cash equivalents, partially offset by an increase in credit card receivables, after securitization.

Capital investment amounted to $0.7 billion (2006 – $1.1 billion). Weston Foods capital investment in 2007 was $109 million (2006 – $184 million). The capital was directed toward the completion of one new plant in the United States, the Bay Shore restructuring, facility improvements and upgrades of production lines and distribution assets. Weston Foods capital investment benefited all of its operations to varying degrees and strengthened its processing and distribution capabilities.

Loblaw's capital investment amounted to $0.6 billion (2006 – $0.9 billion) for the year as Loblaw restrained capital spending in an over-spaced market. Approximately 31% (2006 – 38%) of the capital investment was for new store development, expansions and land, approximately 43% (2006 – 51%) for store conversions and remodels, and approximately 26% (2006 – 11%) for infrastructure investment. The continued capital investment activity benefited all regions to varying degrees and strengthened the existing store base. Some of the new, larger stores replaced older, smaller, less efficient stores that did not offer the broad range of products and services demanded by today's consumer.

Loblaw is investing in higher return expansions and renovations to its existing store base, with a focus on improving same-store sales. Loblaw expects to invest in 2008 an estimated $700 to $800 million in net capital expenditures. Approximately two-thirds of these funds are expected to be used in remodeling, expanding and maintaining existing stores and a small increase in square footage, with the remainder split two-thirds in upgrading information systems and one-third on supply chain infrastructure.

Loblaw's 2007 corporate and franchised store capital investment program, which includes the impact of store openings and closures, resulted in a decrease in net retail square footage of 0.2% compared to 2006. During 2007, 34 (2006 – 37) new corporate and franchised stores were opened and 73 (2006 – 147) underwent renovation or minor expansion. The 34 new stores, net of 79 (2006 – 33) store closures, including 46 stores that were closed as part of the store operations restructuring plan, and stores which underwent conversions and major expansion, decreased net retail square footage 0.1 million square feet (2006 – increased 1.2 million square feet). The 2007 average corporate store size increased 5.9% to 60,800 square feet (2006 – 57,400) and the average franchised store size increased 2.2% to 28,000 square feet (2006 – 27,400).

At year end 2007, Loblaw had committed approximately $113 million (2006 – $153 million) with respect to capital investment projects such as the construction, expansion and renovation of buildings and the purchase of real property.

During 2007, the Company also generated $244 million (2006 – $116 million) from fixed asset sales.

Cash Flows used in Financing Activities of Continuing Operations
Cash flows used in financing activities of continuing operations were $511 million in 2007 compared to $70 million in 2006.

During 2007, Weston and Loblaw completed the following financing activities:
- consolidated commercial paper outstanding was reduced by $229 million; and
- Weston issued $42 million of Series B Debentures.

During 2006, Weston and Loblaw completed the following financing activities:
- consolidated commercial paper outstanding increased by $340 million;
- Weston repaid $200 million of 5.25% Medium Term Notes ("MTN");
- Weston issued 8.0 million preferred shares, Series V for total proceeds of $194 million;
- Loblaw repaid $125 million of 8.70% Series 1996 Provigo Inc. Debenture; and
- Weston issued $40 million of Series B Debentures.

See notes 18 and 21 to the consolidated financial statements for the terms and details of the debt and share capital transactions.

In 2007, Weston renewed its Normal Course Issuer Bid ("NCIB") to purchase on the Toronto Stock Exchange or enter into equity derivatives to purchase up to 5% of its common shares outstanding. Weston did not purchase any shares under its NCIB during 2007 or 2006. The Company intends to file a NCIB in 2008 to purchase on the Toronto Stock Exchange or enter into equity derivatives to purchase up to 5% of each class of its common and preferred shares outstanding.

At the end of 2007, Weston had no preferred share or MTN prospectuses outstanding.

8.2 SOURCES OF LIQUIDITY
The Company obtains short term financing through a combination of cash generated from operating activities, cash, cash equivalents, short term investments, bank indebtedness and has limited access to commercial paper programs. Loblaw relies on cash, cash equivalents and short term investments of $977 million, a $500 million committed credit facility provided by several banks, as well as $845 million in uncommitted operating lines of credit, for its short term funding requirements. Weston relies on cash, cash equivalents and short term investments of $979 million, a $300 million committed credit facility provided by several banks, as well as $265 million in uncommitted operating lines of credit, for its short term funding requirements.

In the first quarter of 2007, Loblaw entered into the 364-day revolving committed credit facility of $500 million, provided by several banks for general corporate purposes, which matures in March 2008. At the end of the year, no amounts were drawn on the committed or uncommitted facilities. Weston's $300 million 364-day revolving committed credit facility provided by several banks will expire in May 2008. At the end of the year, $30 million was drawn on the committed facility and nil on its uncommitted facilities. Neither committed credit facility has financial covenants and borrowings are based on short term floating interest rates.

Subsequent to year end, Loblaw entered into discussions, which have not yet been finalized, with a syndicate of banks to replace its $500 million committed credit facility with a new, longer term committed credit facility of a higher amount. It is anticipated that any new credit facility will contain financial covenants and will be the primary source of Loblaw's short term funding requirements. Concurrent with these discussions, Loblaw obtained a 60-day extension of the existing facility, extending the maturity date to May 2008. The new facility is expected to close prior to the expiry of the existing facility.

Subsequent to year end, Weston also entered into discussions, which have not yet been finalized, with a syndicate of banks to replace its $300 million committed credit facility with a new, longer term committed credit facility. It is anticipated that any new credit facility will contain financial covenants and will be the primary source of Weston's short term funding requirements.

Securitization of credit card receivables provides *PC* Bank with an additional source of funds for the operation of its business. Under *PC* Bank's securitization program, a portion of the total interest in the credit card receivables is sold to independent trusts. *PC* Bank securitized an aggregate $225 million of credit card receivables during 2007 (2006 – $240 million). In the absence of securitization, Loblaw would be required to raise alternative financing by issuing additional debt or equity instruments. Further information about *PC* Bank's credit card receivables and securitization is provided in notes 1 and 12 to the consolidated financial statements and in the Off-Balance Sheet Arrangements section of this MD&A.

In 2006, *PC* Bank restructured its credit card securitization program and Eagle Credit Trust ("Eagle"), a previously established independent trust, issued $500 million of five year senior notes and subordinated notes due in 2011 at a weighted average rate of 4.5%. The restructuring of the portfolio yielded a nominal net loss.

In the normal course of business, the Company enters into certain arrangements, such as providing comfort letters to third-party lenders in connection with financing activities of certain franchisees, with no recourse liability to the Company. In addition, the Company establishes standby letters of credit used in connection with certain obligations related to the financing program for Loblaw's independent franchisees, securitization of *PC* Bank's credit card receivables, real estate transactions and benefit programs. At year end, the aggregate gross potential liability related to the Company's standby letters of credit was approximately $531 million (2006 – $552 million), a portion of which is recorded on the consolidated balance sheet, against which the Company had $628 million (2006 – $615 million) in credit facilities available to draw on.

Between the second quarter of 2007 and February 7, 2008, Loblaw's MTN, other notes and debentures ratings were downgraded twice and the commercial paper ratings once by each of Dominion Bond Rating Service ("DBRS") and Standard & Poor's ("S&P"). The following table sets out the current credit ratings of Loblaw.

	Dominion Bond Rating Service		Standard & Poor's	
Credit Ratings (Canadian Standards)	Credit Rating	Trend	Credit Rating	Outlook
Commercial paper	R-2 (high)	Stable	A-2	Negative
Medium term notes	BBB (high)	Negative	BBB	Negative
Other notes and debentures	BBB (high)	Negative	BBB	Negative

The rating organizations listed above base their credit ratings on quantitative and qualitative considerations. These credit ratings are forward-looking and intended to give an indication of the risk that Loblaw will not fulfill its obligations in a timely manner.

As a result of the DBRS downgrade of the short term credit rating, Loblaw has limited access to commercial paper. Loblaw expects it will be able to secure short term funding from other sources, primarily a new longer term committed credit facility of a higher amount.

Certain independent franchisees of Loblaw obtain financing through a structure involving independent trusts, which were created to provide loans to the independent franchisees to facilitate their purchase of inventory and fixed assets, consisting mainly of fixtures and equipment. The gross principal amount of loans issued to Loblaw's independent franchisees outstanding as of year end 2007 was $418 million (2006 – $419 million), including $153 million (2006 – $124 million) of loans payable by VIEs consolidated by Loblaw in 2007. Based on a formula, Loblaw has agreed to provide credit enhancement in the form of a standby letter of credit for the benefit of the independent funding trust equal to approximately 10% of the principal amount of the loans outstanding at any point in time, $44 million (2006 – $44 million) as of year end 2007. This credit enhancement allows the independent funding trust to provide favourable financing terms to Loblaw's independent franchisees. As well, each independent franchisee provides security to the independent funding trust for its obligations by way of a general security agreement. In the event that an independent franchisee defaults on its loan and Loblaw has not, within a specified time period, assumed the loan, or the default is not otherwise remedied, the independent funding trust shall assign the loan to Loblaw and draw upon this standby letter of credit. Loblaw has agreed to reimburse the issuing bank for any amount drawn on the standby letter of credit.

Automatic termination of the agreement can only occur if specific, predetermined events occur and are not remedied within the time periods required, including downgrades of Loblaw below a long term credit rating of "A (low)" or a short term credit rating of "R-1 (low)" as issued by DBRS. On February 7, 2008, DBRS downgraded Loblaw's long term credit rating to "BBB (high)" from "A (low)" and also lowered Loblaw's short term credit rating to "R-2 (high)" from "R-1 (low)". Subsequent to the DBRS downgrades, Loblaw was notified that an Event of Termination of the independent funding trust agreement for the Loblaw's franchisees had occurred as a result of the credit rating downgrades. The $44 million (2006 – $44 million) standby letter of credit provided to the independent funding trust by Loblaw has not been drawn upon.

To address this issue, Loblaw is currently in the process of securing alternative financing with a syndicate of banks, in the form of a 364-day committed credit facility for the benefit of its franchisees. This new financing is expected to be completed during the second quarter of 2008. Upon closing, this new alternative financing that might be arranged could result in higher financing costs to the franchisees, which in turn could adversely affect operating results. Although Loblaw anticipates that appropriate financing for the franchisees will continue to be secured in the future, any failure to do so could adversely affect Loblaw's franchise programs and may impact its operating results. In addition, any new financing structure which might be implemented would need to be reviewed to determine if there are any implications with respect to the consolidation of VIEs.

Between the second quarter of 2007 and February 12, 2008, Weston's MTN, Exchangeable Debentures, other notes and debentures and preferred share ratings were downgraded twice and the commercial paper ratings once by DBRS. Weston's MTN, other notes and debentures, preferred share and commercial paper ratings were downgraded once by S&P. The following table sets out the current credit ratings of Weston.

	Dominion Bond Rating Service		Standard & Poor's	
Credit Ratings (Canadian Standards)	Credit Rating	Trend	Credit Rating	Outlook
Commercial paper	R-2 (high)	Stable	A-2	Credit Watch with Negative Implications
Medium term notes	BBB	Stable	BBB	Credit Watch with Negative Implications
Exchangeable Debentures	BBB (low)	Stable		
Preferred shares	Pfd-3	Stable	P-3 (high)	Credit Watch with Negative Implications
Other notes and debentures	BBB	Stable	BBB	Credit Watch with Negative Implications

The rating organizations listed above base their credit ratings on quantitative and qualitative considerations. These credit ratings are forward-looking and intended to give an indication of the risk that Weston will not fulfill its obligations in a timely manner.

As a result of the DBRS downgrade of Weston's commercial paper credit rating, Weston has limited access to commercial paper. However, Weston expects to be able to secure short term funding through other sources including a new committed facility with a syndicate of banks, cash flow from operations, cash, cash equivalents and short term investments.

The Company has obtained its long term financing primarily through MTN and preferred share programs. The Company may also refinance maturing long term debt and preferred share programs with MTN if market conditions are appropriate following the refiling of a Base Shelf Prospectus or it may consider other alternatives. Weston does not have any MTN maturing in 2008.

Loblaw has obtained its long term financing primarily through a MTN program. Loblaw may also refinance maturing long term debt, including $390 million of 6.00% MTN maturing in 2008, with MTN if market conditions are appropriate following the refiling of a Base Shelf Prospectus or it may consider other alternatives.

The Company's ability to obtain funding from external sources may be restricted by further downgrades in the Company's credit ratings, should the Company's financial performance and condition deteriorate. In addition, credit and capital markets are subject to inherent global risks that may negatively affect the Company's access and ability to fund its short term and long term debt requirements. The Company mitigates these risks by actively maintaining appropriate levels of cash and cash equivalents, actively monitoring market conditions and diversifying its sources of funding and maturity profile.

8.3 CONTRACTUAL OBLIGATIONS

The following illustrates certain of the Company's significant contractual obligations and discusses other obligations as at December 31, 2007:

Summary of Contractual Obligations

	Payments due by year						
($ millions)	2008	2009	2010	2011	2012	Thereafter	Total
Long term debt(1)	$ 432	$ 399	$ 326	$ 676	$ 24	$ 3,912	$ 5,769
Operating leases(2)	222	194	168	144	121	718	1,567
Contracts for purchase of real property and capital investment projects(3)	110	4					114
Purchase obligations(4)	792	589	574	568	376	4	2,903
Total contractual obligations	$ 1,556	$ 1,186	$ 1,068	$ 1,388	$ 521	$ 4,634	$ 10,353

(1) Long term debt includes capital lease obligations and excludes Exchangeable Debentures.

(2) Represents the minimum or base rents payable. Amounts are not offset by any expected sub-lease income.

(3) These obligations include agreements for the purchase of real property and capital commitments for construction, expansion and renovation of buildings. These agreements may contain conditions that may or may not be satisfied. If the conditions are not satisfied, it is possible the Company will no longer have the obligation to proceed with the transaction.

(4) These include contractual obligations of a material amount to purchase goods or services where the contract prescribes fixed or minimum volumes to be purchased or payments to be made within a fixed period of time for a set or variable price. These are only estimates of anticipated financial commitments under these arrangements and the amount of actual payments will vary. The purchase obligations do not include purchase orders issued or agreements made in the ordinary course of business which are solely for goods which are meant for resale, nor do they include any contracts which may be terminated on relatively short notice or with insignificant cost or liability to the Company. Also excluded are purchase obligations related to commodities or commodity-like goods for which a market for resale exists.

At year end, the Company had other long term liabilities which included accrued benefit plan liability, future income tax liability, stock-based compensation liability, unrealized equity derivatives liability and accrued insurance liabilities. These long term liabilities have not been included in the table above for the following reasons:

- future payments of accrued benefit plan liability, principally post-retirement benefits, depend on when and if retirees submit claims;
- future payments of income taxes depend on the levels of taxable earnings and income tax rates;
- future payments of restricted share units depend on the market prices of Weston's and Loblaw's common shares;
- future payments related to equity derivatives depend on the market price of the Company's common shares; and
- future payments of insurance claims can extend over several years and depend on the timing of anticipated settlements and results of litigation.

8.4 OFF-BALANCE SHEET ARRANGEMENTS

In the normal course of business, the Company enters into the following off-balance sheet arrangements:

- standby letters of credit used in connection with certain obligations mainly related to real estate transactions and benefit programs, the aggregate gross potential liability of which was approximately $221 million (2006 – $221 million) at year end;
- the securitization of a portion of *PC* Bank's credit card receivables through independent trusts; and
- guarantees.

Guarantees

The Company has entered into various guarantee agreements, including standby letters of credit in relation to the securitization of *PC* Bank's credit card receivables, third-party financing made available to the Company's independent franchisees and obligations to indemnify third parties in connection with leases, business dispositions and other transactions in the normal course of the Company's business. For a detailed description of the Company's guarantees, see note 25 to the consolidated financial statements.

Securitization of Credit Card Receivables

Loblaw, through *PC* Bank, securitizes credit card receivables through an independent trust administered by a major Canadian chartered bank and through Eagle, also an independent trust. In these securitizations, *PC* Bank sells a portion of its credit card receivables to the trusts in exchange for cash. The trusts fund these purchases by issuing debt securities in the form of asset-backed commercial paper ("ABCP") and asset-backed term notes respectively, to third-party investors. The securitizations are accounted for as asset sales only when *PC* Bank transfers control of the transferred assets and receives consideration other than beneficial interests in the transferred assets. All transactions between the trusts and *PC* Bank have been, and are expected to continue to be, accounted for as sales as contemplated by Canadian GAAP, specifically Accounting Guideline ("AcG") 12, "Transfers of Receivables". As *PC* Bank does not control or exercise any measure of influence over the trusts, the financial results of the trusts have not been included in the Company's consolidated financial statements.

When *PC* Bank sells credit card receivables to the trusts, it no longer has access to the receivables but continues to maintain credit card customer account relationships, and certain servicing and administrative responsibilities. *PC* Bank does not receive a servicing fee from the trusts for its servicing responsibilities and accordingly, a servicing obligation is recorded. When a sale occurs, *PC* Bank retains rights to future cash flows after obligations to the investors in the trusts have been met, which is considered to be a retained interest. The ABCP issuing trust's recourse to *PC* Bank's assets is limited to *PC* Bank's retained interests and is further supported through a standby letter of credit provided by a major Canadian chartered bank for 9% (2006 – 9%) on a portion of the securitized amount. This standby letter of credit could be drawn upon in the event of a major decline in the income flow from, or in the value of, the securitized credit card receivables. Loblaw has agreed to reimburse the issuing bank for any amount drawn on the standby letter of credit. The subordinated notes issued by Eagle provide credit support to those notes which are more senior. Effective January 1, 2007, the retained interests are recorded at fair value.

As at year end 2007, the total amount of securitized credit card receivables outstanding which *PC* Bank continues to service was $1.5 billion (2006 – $1.3 billion) and the associated retained interests amounted to $8 million (2006 – $5 million). The standby letter of credit supporting a portion of these securitized receivables amounted to approximately $89 million (2006 – $68 million). During 2007, *PC* Bank received income of $141 million (2006 – $114 million) in securitization revenue from the independent trusts relating to the securitized credit card receivables. In the absence of securitization, Loblaw would be required to raise alternative financing by issuing debt or equity instruments. Further disclosure regarding this arrangement is provided in notes 12 and 25 to the consolidated financial statements.

Independent Funding Trust

Certain independent franchisees of Loblaw obtain financing through a structure involving independent trusts, which were created to provide loans to the independent franchisees to facilitate their purchase of inventory and fixed assets, consisting mainly of fixtures and equipment. These trusts are administered by a major Canadian chartered bank. The independent funding trust within the structure finances its activities through the issuance of short term ABCP to third-party investors. The independent funding trust has a global style liquidity agreement from a major Canadian chartered bank in the event that it is unable to issue short term ABCP. The gross principal amount of loans issued to Loblaw's independent franchisees outstanding as of year end 2007 was $418 million (2006 – $419 million) including $153 million (2006 – $124 million) of loans payable by VIEs consolidated by the Company in 2007. Based on a formula, Loblaw has agreed to provide credit enhancement in the form of a standby letter of credit for the benefit of the independent funding trust equal to approximately 10% of the principal amount of the loans outstanding at any point in time, $44 million (2006 – $44 million) as of year end 2007. This credit enhancement allows the independent funding trust to provide favourable financing terms to Loblaw's independent franchisees. As well, each independent franchisee provides security to the independent funding trust for its obligations by way of a general security agreement. In the event that an independent franchisee defaults on its loan and Loblaw has not, within a specified time period, assumed the loan, or the default is not otherwise remedied, the independent funding trust shall assign the loan to Loblaw and draw upon this standby letter of credit. Loblaw has agreed to reimburse the issuing bank for any amount drawn on the standby letter of credit. As a result of implementing Section 3855, "Financial Instruments – Recognition and Measurement" ("Section 3855") (see note 2 to the consolidated financial statements), a liability of $7 million related to the fair value of this standby letter of credit was recognized.

Neither the independent funding trust nor Loblaw can voluntarily terminate the agreement prior to December 2009, and following that date only upon six months' prior notice. Automatic termination of the agreement can only occur if specific, predetermined events occur and are not remedied within the time periods required including downgrades of Loblaw below a long term credit rating of "A (low)" or a short term credit rating of "R-1 (low)" as issued by DBRS. On February 7, 2008, DBRS downgraded Loblaw's long term credit rating to "BBB (high)" from "A (low)" and also lowered Loblaw's short term credit rating to "R-2 (high)" from "R-1 (low)".

Subsequent to the DBRS downgrades, Loblaw was notified that an Event of Termination of the independent funding trust agreement for the Loblaw's franchisees had occurred as a result of the credit rating downgrades. The $44 million standby letter of credit provided to the independent funding trust by Loblaw has not been drawn upon.

If such an event were to occur, long term debt in the amount of $126 million would need to be reclassified to short term liabilities. This amount relates to certain franchisees that are VIEs that Loblaw currently consolidates. Loblaw is currently in the process of securing alternative financing with a syndicate of banks, in the form of a 364-day committed credit facility for the benefit of its franchisees to address this issue. Any new alternative financing structure which may be implemented would need to be reviewed to determine if there are any implications with respect to the consolidation of VIEs.

8.5 DERIVATIVE INSTRUMENTS

Commencing January 1, 2007, the Company adopted accounting standards which impacted the recognition, measurement, disclosure and presentation of its derivative instruments. With the adoption of these standards, all financial derivative instruments are accounted for on the Company's balance sheet at fair value. In addition, non-financial derivative instruments are recorded at fair value on the consolidated balance sheet unless they are exempt from this treatment based upon expected purchase, sale or usage requirements. Prior to January 1, 2007, interest rate swaps which were designated within a hedging relationship were not recorded on the balance sheet. In addition, embedded derivative and certain non-financial derivative instruments were also not recorded. For a detailed description of the Company's derivative instruments and the related accounting policies, see notes 1, 2 and 24 to the consolidated financial statements.

9. QUARTERLY RESULTS OF OPERATIONS

The 52-week reporting cycle followed by the Company is divided into four quarters of 12 weeks each except for the third quarter, which is 16 weeks in duration. The following is a summary of selected consolidated financial information derived from the Company's unaudited interim consolidated financial statements for each of the eight most recently completed quarters. This information was prepared in accordance with Canadian GAAP and is reported in Canadian dollars.

9.1 QUARTERLY FINANCIAL INFORMATION (UNAUDITED)

($ millions except where otherwise indicated)		First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total (audited)
Sales	**2007**	**$ 7,221**	**$ 7,739**	**$ 10,163**	**$ 7,692**	**$ 32,815**
	2006	$ 6,997	$ 7,507	$ 10,085	$ 7,578	$ 32,167
Net earnings (loss) from continuing operations	**2007**	**$ 104**	**$ 129**	**$ 179**	**$ 151**	**$ 563**
	2006	$ 128	$ 184	$ 226	$ (428)	$ 110
Net earnings (loss)	**2007**	**$ 104**	**$ 129**	**$ 179**	**$ 151**	**$ 563**
	2006	$ 128	$ 184	$ 226	$ (417)	$ 121
Net earnings (loss) per common share from continuing operations ($)						
Basic	**2007**	**$ 0.70**	**$ 0.90**	**$ 1.25**	**$ 1.07**	**$ 3.92**
	2006	$ 0.91	$ 1.32	$ 1.62	$ (3.42)	$ 0.43
Diluted	**2007**	**$ 0.70**	**$ 0.90**	**$ 1.25**	**$ 1.07**	**$ 3.92**
	2006	$ 0.91	$ 1.32	$ 1.62	$ (3.42)	$ 0.43
Net earnings (loss) per common share ($)						
Basic	**2007**	**$ 0.70**	**$ 0.90**	**$ 1.25**	**$ 1.07**	**$ 3.92**
	2006	$ 0.91	$ 1.32	$ 1.62	$ (3.33)	$ 0.52
Diluted	**2007**	**$ 0.70**	**$ 0.90**	**$ 1.25**	**$ 1.07**	**$ 3.92**
	2006	$ 0.91	$ 1.32	$ 1.62	$ (3.33)	$ 0.52

Results by Quarter

Consolidated sales and sales growth in 2007 were impacted by various factors including the impact of Weston Foods foreign currency translation. For Loblaw, sales and same-store sales growth were positive in all four quarters of 2007 compared to 2006. Sales growth during the first three quarters of 2007 continued to be negatively impacted by the loss in tobacco sales as discussed previously. Tobacco sales are not a large earnings contributor. Quarterly same-store sales growth for each of the four quarters of 2007 when compared to 2006 was 2.4%, 2.7%, 1.6% and 2.6%, respectively. Quarterly same-store sales growth excluding the impact of decreased tobacco sales[1] for each of the four quarters of 2007 when compared to 2006 was 4.0%, 4.2%, 2.8% and 2.7%, respectively.

Food price inflation fell as the year progressed resulting, in part, from Loblaw's investment in lower retail pricing during 2007 as well as pricing activity within the industry. National food price inflation as measured by CPI was 3.8% in the first quarter of 2007 but decreased to 0.8% in the fourth quarter of 2007. During each consecutive quarter of 2007, Loblaw's internal retail food price inflation decreased, ranging from 3.0% inflation in the first quarter of 2007 to 1.6% deflation in the fourth quarter.

Weston Foods 2007 quarterly sales were positively impacted by price increases across key product categories combined with changes in sales mix. Volumes were negatively impacted by the combined effect of the exit from the United States frozen foodservice bagel business early in the third quarter of 2006 and the discontinuance of contract manufacturing of biscuits for certain customers during 2006. Foreign currency translation negatively impacted reported sales growth, particularly in the third and fourth quarters of 2007.

Fluctuations in quarterly net earnings reflect the impact of a number of specific items in operating income at both Weston Foods and Loblaw as outlined previously, including a charge of $800 million related to the non-cash Loblaw goodwill impairment charge in the fourth quarter of 2006. At Loblaw, solid sales were achieved in all four quarters of 2007 but earnings were pressured from investments in pricing, particularly in the third and fourth quarters as cost reductions lagged the pricing investments. At Weston Foods, pricing, a shift in sales mix to higher margin products and cost reduction and productivity initiatives more than offset the impact of inflationary cost pressures.

Interest expense and other financing charges fluctuate mainly as a result of the accounting for Weston's 2001 forward sale agreement for 9.6 million Loblaw common shares which results in non-cash income or non-cash charges due to the change in the market price of Loblaw common shares.

The change in the effective income tax rates for 2007 over 2006 was primarily due to the non-cash goodwill impairment charge recorded in 2006 which is not deductible for income tax, the change in the proportion of taxable income earned across different tax jurisdictions, and a reduction to future income tax expense resulting from changes in the Canadian federal and certain provincial statutory income tax rates.

During 2007, the Company did not purchase common shares for cancellation pursuant to its NCIB (2006 – nil).

(1) See Non-GAAP Financial Measures beginning on page 55.

9.2 FOURTH QUARTER RESULTS (UNAUDITED)

The following is a summary of selected unaudited consolidated financial information for the fourth quarter of 2007. This information was prepared in accordance with Canadian GAAP and is reported in Canadian dollars. The analysis of the data contained in the table focuses on the results of operations and changes in the financial condition and cash flows in the fourth quarter.

Selected Consolidated Information

(unaudited) ($ millions except where otherwise indicated)	**2007**	2006
Sales	**$ 7,692**	$ 7,578
Sales excluding the impact of tobacco sales and VIEs(1)	**$ 7,365**	$ 7,244
Adjusted EBITDA(1)	**$ 458**	$ 513
Operating income (loss)	**$ 181**	$ (630)
Adjusted operating income(1)	**$ 302**	$ 359
Interest (income) expense and other financing charges	**$ (38)**	$ 90
Income taxes	**$ 46**	$ (3)
Net earnings (loss) from continuing operations	**$ 151**	$ (428)
Net earnings (loss)	**$ 151**	$ (417)
Net earnings (loss) per common share from continuing operations ($)		
Basic and diluted	**$ 1.07**	$ (3.42)
Adjusted basic(1)	**$ 0.89**	$ 1.14
Cash flows from (used in) continuing operations:		
Operating activities	**$ 602**	$ 889
Investing activities	**$ (236)**	$ (383)
Financing activities	**$ (197)**	$ (391)

(1) See Non-GAAP Financial Measures beginning on page 55.

Sales and Sales Growth Excluding the Impact of Tobacco Sales and VIEs(1)

(unaudited) ($ millions except where otherwise indicated)	**2007**	2006
Total sales	**$ 7,692**	$ 7,578
Less: Sales attributable to tobacco sales	**219**	242
Sales attributable to the consolidation of VIEs	**108**	92
Sales excluding the impact of tobacco sales and VIEs(1)	**$ 7,365**	$ 7,244
Total sales growth	**1.5%**	3.2%
Less: Impact on sales growth attributable to tobacco sales	**(0.4)%**	(1.8)%
Impact on sales growth attributable to the consolidation of VIEs	**0.2%**	(0.1)%
Sales growth excluding the impact of tobacco sales and VIEs(1)	**1.7%**	5.1%

(1) See Non-GAAP Financial Measures beginning on page 55.

Sales

Sales for the fourth quarter of 2007 of $7.7 billion increased 1.5% compared to 2006, including a decline of approximately 0.4% due to the continued decrease in tobacco sales at Loblaw and an increase of 0.2% in sales related to the consolidation of certain Loblaw franchisees. The translation of United States dollar denominated sales in the Weston Foods operating segment reduced consolidated sales growth by 1.2% for the fourth quarter.

Consolidated sales growth for the fourth quarter of 2007 was impacted by each reportable operating segment as follows:

- Negatively by 0.7% due to the sales decrease of 5.5% at Weston Foods, which included the negative impact of foreign currency translation of approximately 9.4%. Price increases across key product categories combined with changes in sales mix offset slight volume declines in the quarter.
- Positively by 2.4% due to the sales increase of 2.7% at Loblaw which was achieved by positive growth in both item and customer count despite internal food price deflation.

Operating Income

The Company's consolidated operating income in the fourth quarter increased $811 million from a loss of $630 million in 2006 to income of $181 million in 2007. 2007 consolidated operating income for the fourth quarter included the following:

- a charge of $39 million (2006 – $51 million) related to restructuring and other charges;
- a charge of $77 million (2006 – income of $11 million) for the net effect of stock-based compensation and the associated equity derivatives;
- a charge of $6 million (2006 – income of $3 million) related to a commodity futures fair value adjustment at Weston Foods;
- a charge of $3 million (2006 – $68 million) related to the inventory liquidation at Loblaw;
- income of $4 million (2006 – nil) resulting from the consolidation of VIEs;
- nil (2006 – charge of $800 million) related to the non-cash Loblaw goodwill impairment charge; and
- nil (2006 – charge of $84 million) related to the Ontario collective labour agreement at Loblaw.

After adjusting for the impact of the items described above, consolidated adjusted operating income(1) for the fourth quarter of 2007 declined 15.9% to $302 million from $359 million in 2006.

The Company's 2007 consolidated adjusted operating income(1) was impacted by each of its reportable operating segments as follows:

- Positively by 2.2% due to an increase of 10.7% in adjusted operating income(1) at Weston Foods. The improvement in adjusted operating income(1) resulted from positive pricing actions and favourable mix and productivity improvements.
- Negatively by 18.1% due to a decrease of 22.9% in adjusted operating income(1) at Loblaw due to pricing investments which were lagged by cost reductions.

The Company's 2007 consolidated adjusted operating margin(1) for the fourth quarter declined to 4.1% from 5.0% in 2006, and consolidated adjusted EBITDA margin(1) declined to 6.2% from 7.1% in 2006. Consolidated adjusted operating margin(1) declined in 2007 primarily due to the lower adjusted operating margin(1) at Loblaw, partially offset by the higher adjusted operating margin(1) at Weston Foods.

Interest (Income) Expense and Other Financing Charges

Interest expense and other financing charges for the fourth quarter of 2007 decreased $128 million from 2006, resulting in interest income and other financing charges of $38 million. The decrease was primarily as a result of the non-cash income of $110 million (2006 – non-cash charge of $17 million), reflecting the accounting for Weston's 2001 forward sale agreement of 9.6 million Loblaw common shares.

Income Taxes

The effective income tax rate for the fourth quarter of 2007 was 21.0% compared to 0.4% in 2006. This significant change in the effective income tax rate was due to the non-cash Loblaw goodwill impairment charge recorded in the fourth quarter of 2006 which is non-deductible for income tax purposes. In addition, the effective income tax rate was impacted due to the change in the proportion of taxable income earned across the different tax jurisdictions in which the Company operated. A reduction to future income tax expense was recognized in the fourth quarter of 2007 as a result of changes in the Canadian federal and certain provincial statutory income tax rates.

(1) See Non-GAAP Financial Measures beginning on page 55.

Net Earnings (Loss) from Continuing Operations

For the fourth quarter, basic net earnings per common share from continuing operations was $1.07 compared to a basic net loss per common share from continuing operations of $3.42 in 2006. Basic net earnings per common share for the fourth quarter was also $1.07, compared to a net loss per common share of $3.33 in 2006.

Basic net earnings (loss) per common share from continuing operations include the following:

- a $0.13 per common share charge (2006 – $0.20 per common share charge) related to restructuring and other charges;
- a $0.41 per common share charge (2006 – $0.03 per common share income) for the net effect of stock-based compensation and the associated equity derivatives;
- a $0.02 per common share non-cash charge (2006 – $0.01 per common share income) related to the commodity futures fair value adjustment at Weston Foods;
- a $0.05 per common share charge (2006 – nil) related to the consolidation of VIEs by Loblaw;
- $0.64 per common share non-cash income (2006 – $0.09 per common share charge) related to the accounting for Weston's 2001 forward sale agreement for 9.6 million Loblaw common shares;
- $0.15 per common share non-cash income (2006 – nil) related to the adjustment to future income tax balances resulting from changes in federal statutory income tax rates;
- nil (2006 – $0.21 per common share charge) related to the inventory liquidation at Loblaw;
- nil (2006 – $3.84 per common share charge) related to the non-cash Loblaw goodwill impairment charge; and
- nil (2006 – $0.26 per common share charge) related to the Ontario collective labour agreement at Loblaw.

After adjusting for the above noted items, Weston's adjusted basic net earnings per common share from continuing operations[1] was $0.89 for the fourth quarter compared to $1.14 for the fourth quarter of 2006, a decline of 21.9%.

Discontinued Operations

In the fourth quarter, the Company had no gain or loss from discontinued operations. The gain from discontinued operations in the fourth quarter of 2006 was $11 million. The 2006 gain from discontinued operations was primarily related to final adjustments to the proceeds in 2006 associated with the previously completed 2005 sale of the remaining discontinued Fisheries operations.

Net Earnings (Loss)

Net earnings for the fourth quarter of 2007 was $151 million compared to a net loss of $417 million in 2006. Basic net earnings per common share for the fourth quarter of 2007 was $1.07 compared to a basic net loss per common share of $3.33 in 2006 as a result of the factors discussed above.

Reportable Operating Segments

The Company's consolidated sales and operating income were impacted by each of its reportable operating segments as follows:

WESTON FOODS

(unaudited)
($ millions except where otherwise indicated)

	2007	2006
Sales	**$ 932**	$ 986
Adjusted EBITDA[1]	**$ 111**	$ 101
Operating income	**$ 49**	$ 67
Adjusted operating income[1]	**$ 83**	$ 75

(1) See Non-GAAP Financial Measures beginning on page 55.

During the year, Weston Foods sales were positively impacted by pricing actions taken and the continued shift to premium products. The negative impact of translating United States dollar denominated sales was the primary factor in the decline in sales growth in the fourth quarter.

(1) See Non-GAAP Financial Measures beginning on page 55.

Weston Foods sales for the fourth quarter of 2007 of $932 million decreased 5.5% compared to the same period in 2006 mainly as a result of the negative impact of foreign currency translation on reported sales growth of approximately 9.4%. Price increases across key product categories combined with changes in sales mix increased sales by 4.3% for the fourth quarter of 2007. Overall volume decreased 0.4% for the fourth quarter of 2007 as growth in certain higher margin categories was more than offset by declines in other categories.

In the fourth quarter, the following sales analysis excludes the impact of foreign currency translation:

- fresh bakery sales increased approximately 5.9%, driven by price increases in key product categories combined with changes in sales mix. For the fourth quarter, branded volume increases in the *Arnold* and *Thomas'* brands in the United States and *D'Italiano* brand in Canada were more than offset by volume declines in other categories, particularly in food service and in private label products. Continued growth in whole grain products and the introduction of new and expanded products, such as *Thomas'* 100 Calorie English Muffin, *Thomas'* Mini Squares Bagelbread and product innovation in the *Wonder+* line, contributed positively to branded sales growth in the fourth quarter;
- fresh-baked sweet goods sales, primarily sold under the *Entenmann's* brand, were flat due to lower volumes. The volume decline was driven by softness in full size categories that was partially offset by the introduction of new and expanded products, such as the *Entenmann's* 100 Calorie *Little Bites*;
- frozen bakery sales increased approximately 4.3% driven by higher volumes, price increase and changes in sales mix;
- dairy and bottled beverage sales increased approximately 4.2% driven mainly by pricing, volume gains and improvements in sales mix as growth continued to be experienced in a number of key categories, particularly value-added and bottled products; and
- biscuit sales were flat compared to last year due to lower sales volumes in certain categories.

Weston Foods operating income of $49 million for the fourth quarter of 2007 decreased by $18 million, or 26.9%, compared to operating income of $67 million in 2006. Operating margin was 5.3% compared to 6.8% in the fourth quarter of 2006.

In the fourth quarter of 2007, Weston Foods recognized the following in operating income:

- a charge of $25 million (2006 – income of $5 million) for the net effect of stock-based compensation and the associated equity derivatives;
- a charge of $6 million (2006 – income of $3 million) related to the commodity futures fair value adjustment; and
- a charge of $3 million (2006 – $16 million) related to restructuring and other charges.

After adjusting for the above-noted items, adjusted operating income[(1)] in the fourth quarter of 2007 increased by $8 million, or 10.7%, to $83 million compared to $75 million in the fourth quarter of 2006. Adjusted operating margin[(1)] increased to 8.9% in the fourth quarter of 2007 compared to 7.6% in 2006. Foreign currency translation negatively impacted 2007 adjusted operating income[(1)] growth by approximately 12.0 percentage points. Adjusted EBITDA margin[(1)] increased to 11.9% from 10.2% in 2006.

The improvement in adjusted operating margin[(1)] was the result of positive pricing actions net of inflation, favourable mix and productivity improvements. Inflationary cost pressures related to certain ingredients, primarily flour, oils and sugar, continued to escalate in the fourth quarter relative to the first three quarters of 2007. Pricing and other actions, including cost reduction initiatives such as reduced product returns, mitigated the impact of inflationary cost pressures and resulted in improved gross margins.

During the fourth quarter of 2007, a reduction in insurance reserves, relating primarily to workers' compensation benefits in the United States, resulted in a benefit of $8 million and was recorded in operating income. This benefit was largely a result of favourable experience in workers' compensation claims and an increased focus on workplace safety programs.

(1) See Non-GAAP Financial Measures beginning on page 55.

LOBLAW
(unaudited)
($ millions except where otherwise indicated)

	2007	2006
Sales	$ 6,967	$ 6,784
Sales excluding the impact of tobacco sales and VIEs[1]	$ 6,640	$ 6,450
Adjusted EBITDA[1]	$ 347	$ 412
Operating income (loss)	$ 132	$ (697)
Adjusted operating income[1]	$ 219	$ 284

(1) See Non-GAAP Financial Measures beginning on page 55.

Sales and Sales Growth Excluding the Impact of Tobacco Sales and VIEs[1]
(unaudited)
($ millions except where otherwise indicated)

	2007	2006
Total sales	$ 6,967	$ 6,784
Less: Sales attributable to tobacco sales	219	242
Sales attributable to the consolidation of VIEs	108	92
Sales excluding the impact of tobacco sales and VIEs[1]	$ 6,640	$ 6,450
Total sales growth	2.7%	3.5%
Less: Impact on sales growth attributable to tobacco sales	(0.4)%	(2.0)%
Impact on sales growth attributable to the consolidation of VIEs	0.2%	(0.2)%
Sales growth excluding the impact of tobacco sales and VIEs[1]	2.9%	5.7%
Same-store sales growth	2.6%	1.3%
Same-store sales growth excluding the impact of decreased tobacco sales[1]	2.7%	3.3%

(1) See Non-GAAP Financial Measures beginning on page 55.

Total sales for the fourth quarter of 2007 increased $183 million, or 2.7%, to $7.0 billion compared to $6.8 billion in the fourth quarter of 2006. Same-store sales increased by 2.6%. Total sales excluding the impact of tobacco sales and VIEs[1] increased by 2.9%.

Total sales increases in the fourth quarter of 2007 were achieved by positive growth in both item and customer counts despite internal food price deflation. Total sales increases were realized in Ontario, Quebec and Western Canada. Total sales increased in food and drugstore while general merchandise sales were lower because of the intentional restriction of inventory as Loblaw continued to work on optimizing inventory controls, product mix and markdown strategies.

The *Real Canadian Superstore* banner in Ontario continued to achieve solid sales growth in the fourth quarter of 2007. Loblaw also experienced positive volume growth, based on retail units sold, of 3.6% in the fourth quarter of 2007 compared to the fourth quarter of 2006. The volume growth in the fourth quarter of 2006 was 2.4% compared to the fourth quarter of 2005.

Loblaw's analysis indicates that it had internal retail food price deflation of approximately 1.6% compared to the fourth quarter of 2006. National food price inflation as measured by CPI was 0.8% for the fourth quarter of 2007 compared to approximately 1.5% in the same period of 2006. This measure of inflation does not necessarily reflect the effect of inflation on the specific mix of goods offered in Loblaw stores.

During the fourth quarter of 2007, 8 new corporate and franchised stores were opened and 8 were closed, resulting in a net increase of 0.1 million square feet, or 0.1%, compared to the third quarter of 2007.

(1) See Non-GAAP Financial Measures beginning on page 55.

Operating income of $132 million for the fourth quarter of 2007 increased by $829 million, compared to an operating loss of $697 million in 2006. Operating margin was 1.9% compared to (10.3)% in the fourth quarter of 2006. The 2006 operating loss was affected by an $800 million non-cash goodwill impairment charge related to the goodwill associated with the acquisition of Provigo Inc. in 1998.

In the fourth quarter of 2007, Loblaw recognized the following in operating income:

- a charge of $29 million (2006 – nil) related to Project Simplify involving restructuring and streamlining of merchandising and store operations. Costs were comprised of $19 million for employee termination benefits including severance, additional pension costs resulting from the termination of employees and retention costs; and $10 million of other costs, primarily consulting;
- a charge of $7 million (2006 – nil) in connection with the restructuring of Loblaw's supply chain network;
- nil (2006 – $35 million) in connection with the closure of certain stores in the Quebec and Atlantic markets and in the wholesale network that was part of the store operations restructuring activities;
- a charge of $52 million (2006 – income of $6 million) for the net effect of stock-based compensation and the associated equity forwards. The majority of the expense in the fourth quarter of 2007 included a non-cash loss on equity forwards of $55 million (2006 – income of $10 million) resulting from a decline in Loblaw's share price during the fourth quarter of 2007. At the end of the fourth quarter of 2007, Loblaw had cumulative equity forwards to buy 4.8 million (2006 – 4.8 million) of its common shares;
- a charge of $3 million (2006 – $68 million) from the liquidation of excess general merchandise inventory. The liquidation was completed as expected in the fourth quarter of 2007;
- income of $4 million (2006 – nil) resulting from the consolidation of VIEs;
- nil (2006 – charge of $800 million) for a non-cash goodwill impairment charge related to the goodwill established on the acquisition of Provigo Inc. in 1998; and
- nil (2006 – charge of $84 million) related to the ratification of a new four-year collective agreement with members of certain Ontario locals of the UFCW.

After adjusting for the above-noted items, adjusted operating income(1) in the fourth quarter of 2007 decreased by $65 million, or 22.9%, to $219 million compared to $284 million in the fourth quarter of 2006. Adjusted operating margin(1) decreased to 3.3% in the fourth quarter of 2007 compared to 4.4% in 2006 as growth in operating expenses exceeded growth in sales. Adjusted EBITDA margin(1) decreased to 5.2% from 6.4% in 2006.

In addition, adjusted operating income(1) in the fourth quarter of 2007 was influenced by the following items:

- gross margin declined approximately $60 million from 2006, which represents 0.9% of sales, primarily due to targeted price reductions, to provide value to customers and drive same-store sales and sales volumes, and changes in sales mix, partially offset by improvements in shrink;
- incremental consulting costs compared to the prior year, other than those in connection with Project Simplify, amounted to $12 million including expenses related to new supply chain and information technology improvement initiatives of $6 million;
- a gain of $11 million from the sale of an office building in Calgary, Alberta; and
- incremental non-cash fixed asset impairment charge of $9 million related to asset carrying values in excess of fair values at specific store locations. The charge in the fourth quarter of 2007 was $33 million compared to $24 million in the fourth quarter of 2006.

Gross margin percentage continued to decline in the fourth quarter of 2007 as a result of Loblaw's continued investment in lower prices, as part of its Credit for Value initiative, to drive same-store sales growth in a targeted manner across the country. Sales increases in the quarter were insufficient to offset margin declines. Loblaw continued to experience higher store labour costs due to marketplace pressures and achieved reduced inventory shrink expenses in the fourth quarter of 2007 compared to the same quarter in 2006.

(1) See Non-GAAP Financial Measures beginning on page 55.

Liquidity and Capital Resources

Cash flows from operating activities of continuing operations

Fourth quarter cash flows from operating activities of continuing operations were $602 million in 2007 compared to $889 million in the comparable period of 2006. The decrease was mainly due to the change in non-cash working capital, primarily as a result of changes in inventory, accounts payable and accrued liabilities.

Cash flows used in investing activities of continuing operations

Fourth quarter 2007 cash flows used in investing activities of continuing operations were $236 million in 2007 compared to $383 million in 2006, primarily driven by an increase in proceeds from fixed asset sales of $156 million. Capital investment for the fourth quarter amounted to $206 million (2006 – $307 million).

During the fourth quarter, Loblaw sold property and a partially constructed building for a purchase price of approximately $110 million. Loblaw leased back the property from the buyer for a term of 20 years, with options to renew, and in turn subleased the property to a third-party logistics provider. Loblaw also entered into a warehousing and distribution agreement with the third-party logistics provider, which will use this property to provide services to Loblaw.

Cash flows used in financing activities of continuing operations

Fourth quarter 2007 cash flows used in financing activities of continuing operations were $197 million in 2007 compared to $391 million in 2006. In 2006, Weston repaid $200 million of 5.25% MTN as they matured.

10. INTERNAL CONTROL OVER FINANCIAL REPORTING

Management is responsible for establishing and maintaining adequate internal control over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Canadian GAAP.

Management of Loblaw has concluded that, as of year end 2007, a previously reported weakness no longer exists in the design of the Company's internal control over financial reporting in the area of inventory controls. This design weakness was first identified in the first quarter of 2007 and was caused primarily by the lack of sufficient compensating controls in the absence of a perpetual inventory system.

Loblaw management continues to monitor and improve controls related to inventory and has designed and implemented the following compensating controls:

- New policies and procedures were developed and implemented throughout the third and fourth quarters of 2007 relating to:
  - Authorization procedures for the recommendation and processing of inventory markdowns;
  - Excess inventory review procedures; and
  - Regular assessments of the appropriateness of assumptions used in identifying excess inventory.
- Loblaw management has enhanced the quarterly retail count process by designing and implementing a statistically sound count method that is able to be extrapolated across Loblaw inventory.
- The assumptions used to determine the discount rate to calculate the cost value of inventory are now evaluated on a more standardized and regular basis.
- The assumptions and guidance used to identify excess inventory and apply related markdowns are now evaluated on a more standardized and regular basis.

Other than the remediation steps discussed above, there was no change in the Company's internal controls over financial reporting that occurred during the quarter ended December 31, 2007 that materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

11. MANAGEMENT'S CERTIFICATION OF DISCLOSURE CONTROLS AND PROCEDURES

Management is responsible for designing disclosure controls and procedures to provide reasonable assurance that all material information relating to the Company and its subsidiaries is gathered and reported to senior management on a timely basis so that appropriate decisions can be made regarding public disclosure. As required by Multilateral Instrument 52-109 (Certification of Disclosure in Issuers' Annual and Interim Filings) of the Canadian Securities Administrators, the Chairman & President and the Chief Financial Officer have evaluated the effectiveness of such disclosure controls and procedures and have concluded that the Company's disclosure controls and procedures were effective as at December 31, 2007.

12. OPERATING RISKS AND RISK MANAGEMENT

Each year, the Company performs an Enterprise Risk Assessment ("ERA"), which identifies the key risks facing the Company and evaluates the risk management effectiveness for each of these risks. The assessment is primarily carried out through interviews with senior management, who assess the potential impact of risks and the likelihood that a negative impact will occur. The results of the ERA are used to prioritize risk management activities, allocate resources effectively and develop a risk-based internal audit plan. The risks identified through its ERA process are presented and discussed with the Audit Committee.

A description of the risks and risk management strategies identified by the ERA is included in the risks discussed below, any of which has the potential to negatively affect financial performance. The Company has operating and risk management strategies including insurance programs, which help to mitigate the potential financial impact of these operating risks. While the Company employs strategies to minimize these risks, these strategies do not guarantee that events or circumstances will not occur which could negatively affect the Company's financial condition and performance.

Industry and Competitive Environment

The North American food processing and retail industries are evolving and operate in increasingly competitive markets. Consumers' needs drive changes in the industries, and are impacted by changing demographic and economic trends such as changes in disposable income, ethnic diversity, health and environmental awareness and time availability. Customer satisfaction is central to the Company's business. Over the past several years, consumers have demanded more choice, value and convenience. If the Company is ineffective in responding to these trends or ineffective in executing its strategies, its financial performance could be negatively impacted.

The Company reviews and monitors operating plans and results, including market share in its reportable operating segments. When necessary, the segments will modify their operating strategies, including relocating production facilities or stores, closing underperforming stores, reviewing pricing and adjusting product offerings, brand positioning and/or marketing programs to take into account competitive activity. A significant competitive advantage the Company has developed is its brands. Both segments focus on brand development and building upon their core brand equity. Weston Foods' premium and mainstream brands provide Weston Foods with strong core brands and product lines that enhance consumer loyalty, trusted as they are for quality, great taste and freshness. Loblaw's control label program represents a competitive advantage because it enhances customer loyalty by offering superior value and provides some protection against national brand pricing strategies.

As a result of the continuing and accelerating cost pressures being experienced by the food processing industry and the difficult sales environment being experienced by many food retailers, Weston Foods anticipates that industry restructurings are likely. Although the outcome and the impact, if any, on the Company's consolidated financial results from this anticipated restructuring are uncertain, Weston Foods will closely monitor developments in the food processing industry and food retail market and, if required, adjust its strategies and programs as necessary.

Loblaw's competitors include traditional supermarket operators, as well as mass merchandisers, warehouse clubs, drugstores, limited assortment stores, discount stores, convenience stores and specialty stores. Many of these competitors now offer a selection of food, drugstore and general merchandise. Others remain focused on supermarket-type merchandise. Loblaw is also subject to competitive pressures from new entrants into the marketplace and from the expansion of existing competitors, particularly those expanding into the grocery market. These competitors may have extensive resources which will allow them to compete effectively with Loblaw in the long term. Increased competition could adversely affect Loblaw's ability to achieve its objectives. Loblaw's inability to compete effectively with its current or any future competitors could result in, among other things, lessening of market share and lower pricing in response to its competitors' pricing activities. Accordingly, Loblaw's competitive position and financial performance could be negatively impacted.

Loblaw monitors its market share and the markets in which it operates, and will adjust its operating strategies, which include, but are not limited to, closing underperforming stores, relocating stores or reformatting them under a different banner, reviewing pricing and adjusting product offerings and marketing programs.

Change Management and Execution

2007 was a year of significant change for the Company. Project Simplify resulted in changes to Loblaw's structures and business processes. Other significant initiatives in support of Loblaw's multi-year turnaround plan are underway or planned. While these changes are expected to bring benefits to Loblaw in the form of a more agile and consumer-focused business, success is dependent on management effectively realizing the intended benefits.

Ineffective change management may result in disruptions to the operations of the business or affect the ability of the Company to implement and achieve its strategic objectives, due to a lack of clear accountabilities or lack of requisite knowledge which may cause employees to act in a manner which is inconsistent with Company objectives. Any of these events could negatively impact the Company's performance. The Company may not always achieve the expected cost savings and other benefits of its initiatives.

Information Technology

To support the current and future requirements of the business in an efficient, cost-effective and well-controlled manner, the Company is reliant on information technology ("IT") systems. These have been assessed by management as needing significant upgrading in certain areas in order to act as an enabler for the businesses. These systems may not provide the appropriate degree of efficiency to support the required changes to business processes of the Company. These systems are essential in providing management with the appropriate information for decision making, including its key performance indicators. Change management risk and other associated risks will arise from the various projects which will be undertaken to upgrade existing systems and introduce new systems to enhance effective management of the business going forward. Failure by the Company to appropriately invest in information technology or failure to implement information technology infrastructure in a timely or effective manner may negatively impact the Company's financial performance. During 2007, Loblaw developed an IT strategic plan to guide the new systems environment it requires. This plan will begin to be implemented in 2008.

Any failures in the Company's information security systems or non-compliance with information security standards, including those in relation to personal information belonging to the Company's customers, could result in harm to the reputation or competitive position of the Company and could negatively affect financial performance.

Supply Chain

The need to invest in and improve the Company's supply chain may adversely affect the Company's capacity to effectively and efficiently access current and potential customers. A significant restructuring of Loblaw's supply chain is planned for the next several years. Although this initiative is expected to result in improved service levels for Loblaw's stores, the scale of the change and the implementation of new processes could cause disruption in the flow of goods to stores, which would negatively affect sales. Loblaw's plans to grow its apparel business depend on improvements to the current supply chain processes related to that merchandise. Before and as these changes are implemented, it is possible that the flow of these goods could also be negatively affected, which could negatively affect sales.

Food Safety and Public Health

The Company is subject to risks associated with product defects, food safety and product handling. Such liabilities may arise in relation to the manufacturing, preparation, storage, distribution and display of products and, with respect to the Company's control label and contract manufactured products, in relation to the production, packaging and design of products. Any event related to these matters has the potential to adversely affect the Company's reputation and its financial performance.

A majority of the Company's sales are generated from food products and the Company could be vulnerable in the event of a significant outbreak of food-borne illness or increased public health concerns in connection with certain food products. Such an event could negatively affect the Company's financial performance. Procedures are in place to manage such events, should they occur. These procedures identify risks, provide clear communication to employees and consumers and are aimed at ensuring that potentially harmful products are expeditiously removed from inventory. The Company has food safety procedures and programs, which address safe food handling and preparation standards. The Company endeavours to employ best practices for the storage and distribution of food products and also actively supports consumer awareness of safe food handling and consumption. The ability of these procedures to address such events is dependent on their successful execution. The existence of these procedures does not mean that the Company will in all circumstances be able to mitigate these risks.

The Company strives to ensure its brands and Loblaw's control label products meet all applicable regulatory requirements including having nutritional labelling so that today's health conscious consumer can make informed choices.

Labour
A significant portion of the Company's workforce is unionized. Renegotiating collective agreements may result in work stoppages or slowdowns, which could negatively affect the Company's financial performance, depending on their nature and duration. The Company is willing to accept the short term costs of labour disruption in order to negotiate competitive labour costs and operating conditions for the longer term. Significant labour negotiations took place across the Company in 2007 as 104 collective agreements expired and 101 collective agreements were successfully negotiated which represented a combination of agreements expiring in 2007, those carried over from prior years and those negotiated early. In 2008, 101 collective agreements affecting approximately 17,000 employees will expire, with the single largest agreement covering approximately 3,100 employees. The Company will also continue to negotiate the 75 collective agreements carried over from 2005 to 2007. The Company has good relations with its employees and unions and, although it is possible, does not anticipate any unusual difficulties in renegotiating these agreements.

Several of the Company's competitors operate in a non-union environment. These competitors may benefit from lower labour costs and more favourable operating efficiencies, making it more difficult for the Company to compete.

Franchisees
A substantial portion of Loblaw's revenues and earnings come from amounts paid by franchisees. Franchisees are independent businesses and, as a result, their operations may be negatively affected by factors beyond the Company's control, which in turn may damage the Company's reputation and potentially affect revenues and earnings. Revenues and earnings would also be negatively affected and the Company's reputation could be harmed if a significant number of franchisees were to: experience operational failures, including health and safety exposures; experience financial difficulty; be unwilling or unable to pay Loblaw for products, rent or other fees; or fail to enter into renewals of franchise agreements. The Company's franchise system is also subject to franchise laws and regulations enacted by a number of provinces. Any new legislation or failure to comply with existing legislation may negatively affect operations, and could add administrative costs and burdens associated with these regulations, all of which could affect the Company's relationship with its franchisees.

Commodity Prices
Weston Foods costs are directly impacted by fluctuations in the price of commodities such as wheat, flour, sugar, vegetable oil, cocoa, natural gas and fuel. Increases in the price of these commodities could adversely affect the Company's financial performance. In order to minimize the economic effect of these price fluctuations, Weston Foods hedges a portion of its anticipated raw material purchases. As at year end 2007, Weston Foods had entered into commodity future contracts that mitigate the economic impact of price fluctuations on some commodities for approximately 6 months, on average, into 2008.

However, in 2007 and 2006, the prices of many of these commodities increased at unprecedented rates. There can be no assurance that the Company's hedging arrangements will continue to minimize the short term economic impact on the Company's financial results, particularly if commodity prices continue to be volatile.

Employee Future Benefit Contributions
The Company's funded defined benefit pension plans are currently adequately funded and returns on defined benefit pension plan assets are in line with expectations; however, there is no assurance that this will continue. An extended period of depressed capital markets and low interest rates could require the Company to make contributions to its funded defined benefit pension plans in excess of those currently contemplated, which in turn could have a negative effect on the Company's financial performance.

During 2007, the Company contributed $88 million (2006 – $125 million) to its funded defined benefit pension plans. During 2008, the Company expects to contribute approximately $86 million to these plans. This estimate may vary subject to the completion of actuarial valuations, market performance and regulatory requirements. The Company also expects to make contributions in 2008 to defined contribution pension plans and multi-employer pension plans, as well as benefit payments to the beneficiaries of the unfunded defined benefit pension and other benefit plans.

Multi-Employer Pension Plans
In addition to the Company-sponsored pension plans, the Company participates in various multi-employer pension plans, providing pension benefits in which approximately 41% (2006 – 41%) of employees of the Company and of its independent franchisees participate. The administration of these plans and the investment of their assets are legally controlled by boards of independent trustees generally consisting of an equal number of union and employer representatives. In some circumstances, the Company may have a representative on the board of trustees of these multi-employer pension plans. The Company's responsibility to make contributions to these plans is limited by the amounts established pursuant to its collective agreements; however, poor performance of these plans could have an adverse impact on the Company's employees and former employees who are members of these plans. Pension cost for these plans is recognized as contributions are due.

During the first quarter of 2007, Weston and Loblaw were two of 17 defendants served with an action brought in the Superior Court of Ontario by certain beneficiaries of a multi-employer pension plan in which employees of Loblaw and those of its independent franchisees participate. In their claim against the employers and the trustees of the multi-employer pension plan, the plaintiffs claim that assets of the multi-employer pension plan have been mismanaged and are seeking, among other demands, damages of $1 billion. The action is framed as a representative action on behalf of all beneficiaries of the multi-employer pension plan. The Company has received notice from counsel for the plaintiffs indicating that he has received instructions from his client to discontinue the action against the employers including the Company. The action against the trustees is ongoing and one of the trustees, an officer of Loblaw, may be entitled to indemnification from Loblaw.

Third-Party Providers

Certain aspects of the Company's business are significantly affected by third-party providers. Although appropriate contractual arrangements are put in place with these third parties, the Company has no direct influence over how such third parties are managed. It is possible that negative events affecting these third parties could in turn negatively impact the Company's operations and its financial performance.

A large portion of Loblaw's case-ready meat products are produced by a third party which operates facilities dedicated to Loblaw.

In addition, certain of Weston Foods products and Loblaw's control label products are manufactured under contract by third-party vendors. To preserve the brands' equity, these vendors are held to high standards of quality but there is no assurance that these standards will be achieved. The Company also uses third-party logistic services including those in connection with a dedicated warehouse and distribution centre in Pickering, Ontario, a planned warehouse and distribution centre in Ajax, Ontario, and third-party common carriers. Any disruption in these services could interrupt the flow of goods and therefore could negatively impact sales.

President's Choice Financial banking services are provided by a major Canadian chartered bank. *PC* Bank uses third-party service providers to process credit card transactions, operate call centres and monitor a portion of credit and fraud for the *President's Choice Financial* MasterCard®. To minimize operating risk, *PC* Bank and Loblaw actively manage and monitor their relationship with all third-party providers. *PC* Bank has developed a vendor management policy, approved by its Board of Directors, and has established a vendor management team that provides its Board with regular reports on vendor management and risk assessment.

PC Financial home and auto insurance products are provided by companies within the Aviva Canada group, the Canadian subsidiary of a major international property and casualty insurance provider.

Excess Inventory

It is possible that certain of Loblaw's general merchandising programs will result in excess inventory that cannot be sold profitably through Loblaw's stores. Excess inventory may result in mark downs, shrink or the need to liquidate the inventory, all of which may negatively impact the Company's financial performance. In addition, Loblaw's current inventory management infrastructure, including its information technology systems, is not efficient in its tracking of inventory through all stages of the supply chain. Loblaw has implemented procedures and information technology workarounds which provide management with the ability to adequately detect and quantify excess and obsolete inventory.

Real Estate

Real estate development plans may be contingent on successful negotiation of labour agreements with respect to same-site expansion or redevelopment. As Loblaw continues to offer general merchandise, on-time execution of the real estate program becomes increasingly important due to significantly longer lead times required for ordering this merchandise. Delays in execution could lead to inventory management issues. Loblaw maintains a significant portfolio of owned retail real estate and, whenever practical, pursues a strategy of purchasing sites for future store locations. This enhances Loblaw's operating flexibility by enabling it to introduce new departments and services that could be precluded under third-party operating leases. At year end 2007, Loblaw owned 73% (2006 – 72%) of its corporate store square footage and owned 46% (2006 – 45%) of its franchise square footage.

Seasonality

The Company's operations as they relate to food, specifically inventory levels, sales volumes and sales mix, are impacted to some degree by certain holiday periods throughout the year. Both of the Company's reportable operating segments continuously monitor the impact holidays may have on their operations and adjust inventory levels and production and delivery schedules as required.

Employee Development and Retention

The degree to which the Company is not effective in developing its employees and establishing appropriate succession planning processes and retention strategies could lead to a lack of requisite knowledge, skills and experience which could, in turn, affect the Company's ability to execute its strategies, efficiently run its operations and meet its goals for financial performance. The Company continues to focus on the development of employees at all levels and across all regions. Effective employee development and succession planning are essential to sustaining the growth and success of the Company. However, these areas are not yet fully developed and the Company is implementing such processes.

The tight labour market in Western Canada has created unique challenges to effectively operate manufacturing facilities, stores and distribution centres thereby affecting the Company's ability to meet its business objectives. The Company has implemented programs to attract the appropriate calibre of employees in a very competitive environment, but there is no certainty that these programs will continue to be effective.

Utility and Fuel Prices

The Company is a significant consumer of electricity, other utilities and fuel. The Company has entered into contracts to fix the price of a portion of its future variable costs associated with electricity and natural gas, and financial contracts to fix a portion of variable costs associated with heating oil requirements for 2008. Despite these arrangements, unanticipated cost increases in these items could negatively affect the Company's financial performance.

Environmental, Health and Safety

Adverse environmental and health and safety events could negatively affect the Company's reputation and financial performance. The Company has environmental, health and workplace safety programs in place and has established policies and procedures aimed at ensuring compliance with applicable legislative requirements. To this end, the Company employs environmental risk assessments and audits using internal and external resources together with employee awareness programs throughout its operating locations.

The Company endeavours to be socially and environmentally responsible, and recognizes that the competitive pressures for economic growth and cost efficiency must be integrated with sound environmental stewardship and ecological considerations. Environmental protection requirements do not and are not expected to have a material effect on the Company's financial performance.

The Environmental, Health and Safety Committee of the Board receives regular reporting from management, addressing current and potential future issues, identifying new regulatory concerns and related communication efforts. The Company's dedicated Environmental Affairs staff work closely with the operations to help ensure that corporate requirements are met.

Ethical Business Conduct

The Company has adopted a Code of Business Conduct which employees and directors of the Company are required to acknowledge and agree to on a regular basis. The Company has in place an Ethics and Business Conduct Committee, comprised of senior management, which monitors compliance with the Code of Business Conduct and determines how the Company can best ensure it is conducting its business in an ethical manner. The Company encourages reporting of unethical conduct and has established a toll-free anonymous response line, which can be used by employees to report suspected accounting, internal control or auditing irregularities and unethical behaviour impacting the Company. Loblaw has also adopted a Vendor Code of Conduct, which outlines its ethical expectations to its vendor community in a number of areas, including social responsibility. Any failure of the Company or its vendors to adhere to these policies, the law or ethical business practices could significantly affect the Company's reputation and brands and could, therefore, negatively impact the Company's financial performance.

Legal, Taxation and Accounting

Changes to any of the laws, rules, regulations or policies related to the Company's business, including the production, processing, preparation, distribution, packaging and labelling of its products, could have an adverse impact on its financial and operational performance. In the course of complying with such changes, the Company may incur significant costs. Failure by the Company to fully comply with applicable laws, rules, regulations and policies may subject it to civil or regulatory actions or proceedings, including fines, assessments, injunctions, recalls or seizures, which may have an adverse effect on the Company's financial results.

The Company is subject to various laws regarding the protection of personal information and has adopted a Privacy Code setting out guidelines for the handling of personal information. Any failure of the Company to comply with these laws may result in damage to its reputation and negatively affect financial performance.

There can be no assurance that the tax laws and regulations in the jurisdictions affecting the Company will not be changed in a manner which could adversely affect the Company. New accounting pronouncements introduced by appropriate authoritative bodies may also impact the Company's financial results.

Insurance

The Company attempts to limit its exposure to certain risks through a combination of appropriate levels of self-insurance and the purchase of various insurance coverages, including an integrated insurance program. The Company's insurance program is based on various lines and limits of coverage. Insurance is arranged on a multi-year basis with reliable, financially stable insurance companies as rated by A.M. Best Company, Inc. The Company combines comprehensive risk management programs and the active management of claims handling and litigation processes by using internal professionals and external technical expertise. These programs do not guarantee that any given risk will be mitigated in all circumstances.

Holding Company Structure

Weston is a holding company. As such, it does not carry on all of its business directly but does so through its subsidiaries. It has no major source of income or assets of its own, other than the interests it has in its subsidiaries, which are all separate legal entities.

Weston is therefore financially dependent on dividends and other distributions it receives from its subsidiaries.

13. FINANCIAL RISKS AND RISK MANAGEMENT

In the normal course of business, the Company is exposed to financial risks that have the potential to negatively affect its financial performance, including financial risks related to changes in interest rates, foreign currency exchange rates, the market prices of Weston and Loblaw common shares and liquidity. The Company is also exposed to credit and counterparty risks on certain of its financial instruments. These risks and the actions taken to minimize them are discussed below. While the Company employs strategies to minimize these risks, these strategies do not guarantee that events or circumstances will not occur that negatively affect the Company's financial condition and performance.

Liquidity

The Company's ability to obtain funding from external sources may be restricted by further downgrades in the Company's credit ratings, should the Company's financial performance and condition deteriorate. In addition, credit and capital markets are subject to inherent global risks that may negatively affect the Company's access and ability to fund its short term and long term debt requirements.

The Company mitigates these risks by actively maintaining appropriate levels of cash and cash equivalents, actively monitoring market conditions and diversifying its sources of funding and maturity profile.

Derivative Instruments

The Company uses over-the-counter derivative instruments, specifically cross currency basis swaps, interest rate swaps, equity forwards and swaps, and commodity futures and options, to manage its risks and costs associated with its net assets, financing activities, stock-based compensation plans and future purchases of raw materials. The fair value of derivative instruments is subject to changing market conditions which could negatively impact earnings. The Company maintains treasury centres that operate under policies and guidelines approved by the Board, covering funding, investing, equity, foreign currency exchange and interest rate management. The Company's policies and guidelines prohibit the use of any derivative instrument for trading or speculative purposes. See notes 1 and 24 to the consolidated financial statements for additional information about the Company's derivative instruments.

Foreign Currency Exchange Rate

Loblaw enters into cross currency basis swaps to manage its current and anticipated exposure to fluctuations in foreign currency exchange rates. Loblaw's cross currency basis swaps are transactions in which floating interest payments and principal amounts in United States dollars are exchanged against the receipt of floating interest payments and principal amounts in Canadian dollars. These cross currency basis swaps limit Loblaw's exposure to foreign currency exchange rate fluctuations on a portion of its United States dollar denominated assets, principally cash, cash equivalents and short term investments.

The Company's consolidated financial statements are expressed in Canadian dollars but a significant portion of its Weston Foods business occurs in United States dollars through its U.S. net investment. The U.S. net investment is translated into Canadian dollars at the foreign currency exchange rate in effect at each balance sheet date. As a result, the Company is exposed to exchange rate gains and losses which are recorded in other comprehensive loss with the offset in the reported Canadian dollar value of the related assets and liabilities included in the U.S. net investment. During 2007, the Canadian dollar appreciated relative to the United States dollar, resulting in a reduction of the Company's U.S. net investment and a corresponding increase in accumulated other comprehensive loss of

$508 million. In addition, revenues and expenses of these self-sustaining foreign operations are translated into Canadian dollars at the average foreign currency exchange rate for the year. An appreciating Canadian dollar relative to the United States dollar will negatively impact year-over-year changes in reported sales, operating income and net earnings, while a depreciating Canadian dollar relative to the United States dollar will have the opposite impact.

Interest Rate

The Company enters into interest rate swaps to manage its current and anticipated exposure to fluctuations in interest rates impacted by market liquidity. Interest rate swaps are transactions in which the Company exchanges interest flows with a counterparty on a specified notional amount for a predetermined period based on agreed-upon fixed and floating interest rates. Notional amounts are not exchanged. The Company monitors market conditions and the impact of interest rate fluctuations on its fixed and floating interest rate exposure mix on an ongoing basis.

Common Share Market Price

Changes in Weston and Loblaw common share prices impact the Company's stock-based compensation costs. The Company strives to manage these exposures by entering into equity swap and forward transactions. In 2007, Weston had cumulative outstanding equity swaps in respect of 1.7 million common shares and Loblaw had cumulative outstanding equity forwards in respect of 4.8 million common shares. These swaps and forwards allow for several methods of settlement including net cash settlement. They change in value as the market prices of the underlying common shares change and provide a partial offset to fluctuations in Weston's and Loblaw's stock-based compensation costs, including the restricted share units plan expense, when the market prices of Weston and Loblaw common shares exceed the exercise price of the related employee stock options. When the market prices of Weston and Loblaw common shares are lower than the exercise price of the related employee stock options, these equity derivatives will provide a partial offset only to the restricted share units plan expense. The amount of net stock-based compensation cost recorded in operating income is mainly dependent upon the number of unexercised stock options and restricted share units and their vesting schedules relative to the number of underlying common shares on the equity derivatives and the level of and fluctuations in the market prices of the underlying common shares.

Changes in the Loblaw common share price impact the Company's interest and other financing charges. In 2001, Weston entered into an equity forward sale agreement based on 9.6 million Loblaw common shares at an original forward price of $48.50 per Loblaw common share which, under the terms of the agreement, had increased to a forward price of $72.06 (2006 – $67.64) per Loblaw common share as at December 31, 2007. The forward matures in 2031 and will be settled in cash as follows: Weston will receive the forward price and will pay the market value of the underlying Loblaw common shares at maturity. The obligation of Weston under this forward is secured by the underlying Loblaw common shares. Weston entered into this forward to partially offset any repayment risk associated with its Series A, 7.00% and Series B Debentures. Weston recognizes a non-cash charge or income, which is included in consolidated interest expense and other financing charges, representing the fair value adjustment of Weston's forward sale agreement for 9.6 million shares. The fair value adjustment in the forward contract is a non-cash item resulting from fluctuations in the market price of the underlying Loblaw shares that Weston owns. Weston does not record any change in the market price associated with the Loblaw shares it owns. At maturity, if the forward price is greater than the market price, Weston will receive a cash amount equal to the difference. If the forward price is less than the market price, Weston will pay a cash amount equal to the difference. Any cash paid under the forward contract could be offset by the sale of Loblaw shares.

Credit

The Company is exposed to credit risk resulting from the possibility that counterparties may default on their financial obligations, or if there is a concentration of transactions carried out with the same counterparty or of financial obligations which have similar economic characteristics such that they could be similarly affected by changes in economic conditions. Exposure to credit risk relates to derivative instruments, cash equivalents and short term investments, amounts receivable from Weston Foods customers and suppliers, *PC* Bank's credit card receivables and accounts receivable from independent franchisees, associates and independent accounts.

The Company may be exposed to losses should any counterparty to the Company's financial or non-financial derivative agreements fail to fulfill its obligations. The Company has sought to minimize potential counterparty risk and losses by conducting transactions for its derivative agreements with counterparties that have at minimum a long term "A" credit rating from a recognized credit rating agency and by placing risk adjusted limits on its exposure to any single counterparty for its financial derivative agreements. The Company has internal policies, controls and reporting processes, which require ongoing assessment and corrective action, if necessary, with respect to its derivative transactions. In addition, principal amounts on cross currency basis swaps and equity swaps and forwards are each netted by agreement and there is no exposure to loss of the original notional principal amounts on the interest rate swaps and equity swaps and forwards.

Credit risk associated with the Company's cash equivalents and short term investments results from the possibility that a counterparty may default on the repayment of a security. The Company attempts to mitigate this risk through policies and guidelines that require issuers of permissible investments to have at minimum a long term "A" credit rating from a recognized credit rating agency and that specify minimum and maximum exposures to specific issuers and that specify the type of instruments to be held by the Company.

Weston Foods performs ongoing credit evaluations to assess the financial condition of its new and existing suppliers and customers for amounts receivable from these counterparties.

Loblaw's exposure to credit risk from *PC* Bank's credit card receivables and receivables from independent franchisees, associates and independent accounts results from the possibility that customers may default on their payment obligation. *PC* Bank manages the credit card receivable risk by employing stringent credit scoring techniques, actively monitoring the credit card portfolio and reviewing techniques and technology that can improve the effectiveness of the collection process. In addition, these receivables are dispersed among a large, diversified group of credit card customers.

Loblaw accounts receivable from independent franchisees, associates and independent accounts are actively monitored on an ongoing basis and settled on a frequent basis in accordance with the terms specified in the applicable agreements.

14. RELATED PARTY TRANSACTIONS

Weston's majority shareholder, Wittington Investments, Limited ("Wittington"), and its affiliates are related parties. Weston, in the normal course of business, has routine transactions with these related parties, including the rental of office space at market prices from Wittington. Rental payments amounted to approximately $3 million in 2007 (2006 – $6 million). It is Weston's policy to conduct all transactions and settle balances with related parties on market terms and conditions. For a detailed description of the Company's related party transactions, see note 27 to the consolidated financial statements.

From time to time, the Company and Wittington may make elections that are permitted or required under applicable income tax legislation with respect to affiliated corporations and, as a result, may enter into agreements in that regard. These elections and accompanying agreements do not have any material impact on the Company.

15. CRITICAL ACCOUNTING ESTIMATES

The preparation of financial statements in accordance with Canadian GAAP requires management to make estimates and assumptions that affect the reported amounts and disclosures made in the consolidated financial statements and accompanying notes.

Management continually evaluates the estimates and assumptions it uses. These estimates and assumptions are based on management's historical experience, best knowledge of current events and conditions and activities that the Company may undertake in the future. Actual results could differ from these estimates.

The estimates and assumptions described in this section depend upon subjective or complex judgments about matters that may be uncertain and changes in these estimates and assumptions could materially impact the consolidated financial statements.

Inventories

Certain Loblaw retail store inventories are stated at the lower of cost and estimated net realizable value less normal gross profit margin. Loblaw is required to make significant estimation or judgment in the determination of (i) discount factors used to convert inventory to cost after a physical count at retail has been completed and (ii) estimated inventory losses, or shrinkage, occurring between the last physical inventory count and the balance sheet date.

Inventories counted at retail are converted to cost by applying a discount factor to retail selling prices. This discount factor is determined at a category or department level, is calculated in relation to historical gross margins and is reviewed on a regular basis for reasonableness. Inventory shrinkage, which is calculated as a percentage of sales, is evaluated throughout the year and provides for estimated inventory shortages from the last physical count to the balance sheet date. To the extent that actual losses experienced vary from those estimated, both inventories and operating income may be impacted. Changes or differences in these estimates may result in changes to inventories on the consolidated balance sheet and a charge or credit to operating income in the consolidated statement of earnings.

In the first quarter of 2008, the Company will implement Section 3031, "Inventories", the implications of which are further discussed in the Future Accounting Standards section of this MD&A.

Employee Future Benefits
The cost and accrued benefit plan obligations of the Company's defined benefit pension plans and other benefit plans are accrued based on actuarial valuations which are dependent on assumptions determined by management. These assumptions include the discount rate, the expected long term rate of return on plan assets, the expected growth rate of health care costs, the rate of compensation increase, retirement ages, termination rates and mortality rates. These assumptions are reviewed annually by management and the Company's actuaries.

The discount rate, the expected long term rate of return on plan assets and the expected growth rate in health care costs are the three most significant assumptions.

The discount rates are based on market interest rates, as at the Company's measurement date of September 30 on a portfolio of Corporate AA bonds with terms to maturity that, on average, match the terms of the accrued benefit plan obligations. The discount rates used to determine the 2007 net cost for defined benefit pension and other benefit plans were 5.1% and 5.1%, respectively on a weighted average basis, compared to 5.3% and 5.3%, respectively, in 2006. The discount rates used to determine the net 2008 defined benefit pension and other benefit plans costs increased to 5.5% and 5.3%, respectively, in Canada and increased to 6.0% and 6.0%, respectively, in the United States.

The expected long term rate of return on plan assets is based on current market conditions, the asset mix, the active management of defined benefit pension plan assets and on historical returns. The Company's defined benefit pension plan assets had a 10 year annualized return of 7.2% as at the 2007 measurement date. The actual annual returns within this 10 year period varied with market conditions. The Company has assumed a 7.5% expected long term rate of return on plan assets in Canada and 8.0% on plan assets in the United States in calculating its defined benefit pension plans cost for 2008.

The expected growth rate in health care costs for 2007 was based on external data and the Company's historical trends for health care costs, and in 2008 initial growth rates will be relatively consistent with those of 2007.

Since the three key assumptions discussed above are forward-looking and long term in nature, they are subject to uncertainty and actual results may differ. In accordance with Canadian GAAP, differences between actual experience and the assumptions, as well as the impact of changes in the assumptions, are accumulated as unamortized net actuarial gains and losses and amortized over future periods, affecting the recognized cost of defined benefit pension plans and other benefit plans and the accrued benefit plan obligation in future periods. While the Company believes that its assumptions are appropriate, significant differences in actual experience or significant changes in the Company's assumptions may materially affect its defined benefit pension plans and other benefit plans accrued benefit plan obligations and future costs.

Additional information regarding the Company's pension and other benefit plans, including a sensitivity analysis for changes in key assumptions, is provided in note 16 to the consolidated financial statements and in the Employee Future Benefit Contributions discussion in the Operating Risks and Risk Management section of this MD&A.

Goodwill and Indefinite Life Intangible Assets
Goodwill is not amortized and is assessed for impairment at the reporting unit level at least annually. Any potential goodwill impairment is identified by comparing the fair value of a reporting unit to its carrying value. If the fair value of the reporting unit exceeds its carrying value, goodwill is considered not to be impaired. If the carrying value of the reporting unit exceeds its fair value, a more detailed goodwill impairment assessment must be undertaken. A goodwill impairment charge is recognized to the extent that, at the reporting unit level, the carrying value of goodwill exceeds the implied fair value. Any goodwill impairment will result in a reduction in the carrying value of goodwill on the consolidated balance sheet and in the recognition of a non-cash impairment charge in operating income in the consolidated statement of earnings.

The Company determines the fair value of its reporting units using a discounted cash flow model corroborated by other valuation techniques such as market multiples. The process of determining these fair values requires management to make estimates and assumptions of a long term nature including, but not limited to, projected future sales, earnings and capital investment, discount rates and terminal growth rates. Projected future sales, earnings and capital investment are consistent with strategic plans presented to the Board. Discount rates are based on an industry weighted average cost of capital. These estimates and assumptions may change in the future due to uncertain competitive and economic market conditions or changes in business strategies.

In 2006, the annual goodwill impairment test was performed and it was determined that the carrying value of the goodwill established on the acquisition of Provigo Inc. in 1998 exceeded its respective fair value. As a result, in 2006, Loblaw recorded in operating income a non-cash goodwill impairment charge of $800 million relating to this goodwill. The determination that the fair value of goodwill was less than its carrying value resulted from a decline in market multiples, both from an industry and Loblaw perspective, and a reduction of fair value as determined using the discounted cash flow methodology, incorporating both current Loblaw and market assumptions, which in combination resulted in the goodwill impairment. This $800 million non-cash goodwill impairment charge was finalized in the second quarter of 2007.

During the fourth quarter of 2007, the Company performed its annual goodwill impairment test and determined that there was no impairment of the carrying value of goodwill.

Intangible assets with indefinite useful lives, primarily consisting of certain Weston Foods trademarks and brand names, are assessed for impairment at least annually. Any potential intangible asset impairment is identified by comparing the fair value of the indefinite life intangible asset to its carrying value. If the fair value of the intangible asset exceeds its carrying value, the intangible asset is considered not to be impaired. If the carrying value of the intangible asset exceeds its fair value, impairment is identified as the difference between the fair value and the carrying value and will result in a reduction in the carrying value of the intangible assets on the consolidated balance sheet and the recognition of a non-cash impairment charge in operating income in the consolidated statement of earnings.

The Company determines the fair value of its trademarks and brand names by using the "Relief from Royalty Method", a discounted cash flow model. The process of determining the fair values requires management to make assumptions of a long term nature regarding projected future sales, terminal growth rates, royalty rates and discount rates. Projected future sales are consistent with strategic plans presented to Weston's Board and discount rates are based on an industry after-tax cost of equity. These estimates and assumptions may change in the future due to uncertain competitive and economic market conditions or changes in business strategies.

During the fourth quarters of 2007 and 2006, the Company performed the annual indefinite life intangible assets impairment tests and determined that there was no impairment of the carrying values of indefinite life intangible assets.

Income Taxes

Future income tax assets and liabilities are recognized for the future income tax consequences attributable to temporary differences between the financial statement carrying values of assets and liabilities and their respective income tax bases. Future income tax assets or liabilities are measured using enacted or substantively enacted income tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The calculation of current and future income taxes requires management to make estimates and assumptions and to exercise judgment regarding the financial statement carrying values of assets and liabilities which are subject to accounting estimates inherent in those balances, the interpretation of income tax legislation across various jurisdictions, expectations about future operating results, the timing of reversal of temporary differences and possible audits of income tax filings by the regulatory authorities. Management believes it has adequately provided for income taxes based on currently available information.

At each balance sheet date, future income tax assets are reviewed to determine whether a valuation allowance is required. Such an allowance is required when it is deemed unlikely that projected future taxable income will be sufficient to realize the future income tax benefits.

Changes or differences in the underlying estimates or assumptions may result in changes to the current or future income tax balances on the consolidated balance sheet, a charge or credit to income tax expense in the consolidated statement of earnings and may result in cash payments or receipts.

Fixed Assets

Fixed assets to be held and used are reviewed for impairment annually and when events or circumstances indicate that their carrying value exceeds the sum of the undiscounted cash flows expected from their use and eventual disposition. An impairment loss is measured as the amount by which the fixed assets carrying value exceeds the fair value. As discussed in notes 4 and 14 to the consolidated financial statements, the Company reviewed certain fixed assets for impairment in the Weston Foods and Loblaw operating segments due to circumstances that indicated that their carrying values may not be recovered. The factor that most significantly influences the impairment assessments and calculations is estimates of future cash flows. The Company uses its internal plans in estimating future cash flows. These plans reflect the Company's current best estimate of future cash flows but may change in the future due to uncertain competitive and economic market conditions or changes in business strategies. Changes or differences in these estimates may result in changes to fixed assets on the consolidated balance sheet and a charge to operating income on the statement of earnings.

Goods and Services Tax and Provincial Sales Taxes

During 2005, Loblaw recorded a charge relating to an audit and proposed assessment by the Canada Revenue Agency relating to GST on certain products sold on which GST was not appropriately charged and remitted. In light of this proposed assessment, the Company assessed and estimated the potential liabilities for GST and PST in other areas of its operations for various periods. Accordingly, a charge of $40 million was recorded in operating income in 2005. Approximately $4 million was paid in 2007 (2006 – $1 million) and approximately $20 million remains accrued as at year end 2007. The ultimate remaining amount paid will depend on the outcome of audits performed by or settlements reached with the various tax authorities, and therefore may differ from this estimate. Management will continue to assess the remaining accrual as progress towards resolution with the various tax authorities is made and will adjust the remaining accrual accordingly. Changes in this accrual may result in a charge or credit to operating income in the consolidated statement of earnings.

16. ACCOUNTING STANDARDS IMPLEMENTED IN 2007

During the year, the Company implemented the following accounting standards issued by the Canadian Institute of Chartered Accountants ("CICA"):

On January 1, 2007, the Company implemented the CICA Handbook Section 3855, "Financial Instruments – Recognition and Measurement", Section 3865, "Hedges", Section 1530, "Comprehensive Income", Section 3251, "Equity" and Section 3861, "Financial Instruments – Disclosure and Presentation". The transitional adjustments resulting from these standards are recognized in the opening balance of retained earnings and opening accumulated other comprehensive loss. Prior periods have not been restated except to reclassify unrealized foreign currency translation losses on net investments in self-sustaining foreign operations to accumulated other comprehensive loss.

The new accounting standards require that all financial instruments be classified into a defined category, namely, held-for-trading financial assets or financial liabilities, held-to-maturity investments, loans and receivables, available-for-sale financial assets, or other financial liabilities. The financial instruments within scope, including derivative instruments, are included on the Company's balance sheet and measured at fair value except for loans and receivables, held-to-maturity financial assets and other financial liabilities which are measured at cost or amortized cost except for the Weston's 3% Exchangeable Debentures as more fully discussed in note 2 to the consolidated financial statements. Held-for-trading financial assets and financial liabilities are measured at fair value with gains and losses recognized in net earnings in the period in which they arise. Available-for-sale financial assets are measured at fair value, with unrealized gains and losses, including changes in foreign exchange rates, recognized in other comprehensive income until the financial asset is derecognized or impaired, at which time any unrealized gains or losses are recorded in net earnings. In cash flow hedges, the effective portion of the change in fair value of the hedging item is recorded in other comprehensive income. To the extent the change in fair value of the derivative instrument is not completely offset by the change in fair value of the hedged item, the ineffective portion of the hedging relationship is recorded immediately in net earnings.

Upon implementation of these standards, the Company has recorded the following transitional adjustments:

($ millions)	Balance as Reported, Dec. 31, 2006	Transitional Adjustments	Opening Balance Jan. 1, 2007
Other assets	$ 1,459	$ (101)	$ 1,358
Accounts payable and accrued liabilities	$ 3,176	$ 1	$ 3,177
Long term debt	$ 5,918	$ (11)	$ 5,907
Future income taxes	$ 366	$ (41)	$ 325
Other liabilities	$ 688	$ 41	$ 729
Retained earnings	$ 4,506	$ (100)	$ 4,406
Accumulated other comprehensive loss	$ (503)	$ 9	$ (494)

For further details of the specific accounting changes and related impacts, see note 2 to the consolidated financial statements.

17. FUTURE ACCOUNTING STANDARDS

The Company closely monitors new accounting standards to assess the impact, if any, on its consolidated financial statements.

In 2008, the Company will be reviewing the implications of the following standards and implementing the recommendations as required.

In December 2006, the CICA issued three new accounting standards: Section 1535, "Capital Disclosures", ("Section 1535"), Section 3862, "Financial Instruments – Disclosures" ("Section 3862") and Section 3863, "Financial Instruments – Presentation" ("Section 3863"). Section 1535 establishes guidelines for the disclosure of information regarding a company's capital and how it is managed. Enhanced disclosures with respect to the objectives, policies and processes for managing capital and quantitative disclosure about what a company regards as capital are required. Section 3862 and Section 3863 replace Section 3861 "Financial Instruments – Disclosure and Presentation". Section 3862 requires increased disclosures regarding the risks associated with financial instruments and how these risks are managed. Section 3863 carries forward standards for presentation of financial instruments and non-financial derivative instruments and provides additional guidance for the classification of financial instruments, from the perspective of the issuer, between liabilities and equity. These standards are effective for fiscal years beginning on or after October 1, 2007 and therefore the Company will implement them in the first quarter of 2008.

In June 2007, the CICA issued Section 3031, "Inventories", that will replace existing Section 3030 of the same title. The new standard requires inventories to be measured at the lower of cost and net realizable value with more specific guidance of costs to include in the cost of inventory. Costs such as storage costs and administrative overhead that do not contribute to bringing inventories to their present location and condition are specifically excluded from the cost of inventories and expensed in the period incurred. This standard is effective for fiscal years beginning on or after January 1, 2008 and will be implemented by the Company in the first quarter of 2008 to the opening inventory for the period with an adjustment to opening retained earnings, net of income taxes and applicable minority interest, for the difference in measurement of the opening inventory with no prior periods restated. Loblaw expects to record, upon implementation of this standard, a decrease in the measurement of its opening inventory of less than 4% of its inventory value resulting in a corresponding decrease to opening retained earnings of less than $31 million net of income taxes and minority interest on the consolidated balance sheet. The impact of the Weston Foods adjustment to inventory and retained earnings is not expected to be material to the consolidated balance sheet. In addition to the changes in the cost of inventory, the Company is reviewing the additional presentation and disclosure requirements which will be required in the consolidated financial statements and/or in the accompanying notes.

In November 2007, the CICA issued amendments to Section 1000, "Financial Statement Concepts", and AcG 11, "Enterprises in the Development Stage", issued a new Handbook Section 3064, "Goodwill and Intangible Assets" ("Section 3064") to replace Section 3062, "Goodwill and Other Intangible Assets", withdrew Section 3450, "Research and Development Costs" and amended EIC 27, "Revenues and Expenditures During the Pre-operating Period" to not apply to entities that have adopted Section 3064. These amendments provide guidance for the recognition of internally developed intangible assets, including assets developed from research and development activities, ensuring consistent treatment of all intangible assets, whether separately acquired or internally developed. The amendments are effective for annual and interim financial statements relating to fiscal years beginning on or after October 1, 2008 and therefore the Company will implement them in the first quarter of 2009, retroactively with restatement of the comparative periods for the current and prior year. The impact of implementing these amendments on the Company's financial statements is currently being assessed.

The Canadian Accounting Standards Board will require all public companies to adopt International Financial Reporting Standards ("IFRS") for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011. Companies will be required to provide IFRS comparative information for the previous fiscal year. The transition from Canadian GAAP to IFRS will be applicable for the Company for the first quarter of 2011 when the Company will prepare both the current and comparative financial information using IFRS. The Company expects the transition to IFRS to impact financial reporting, business processes and information systems. The Company will assess the impact of the transition to IFRS and will continue to invest in training and resources throughout the transition period to facilitate a timely conversion.

For further details on the above future accounting standards see note 1 to the consolidated financial statements.

18. OUTLOOK

The outlook for the consolidated results of George Weston Limited for 2008 reflects the underlying results of its operating segments as discussed below. The consolidated results continue to reflect the changes undertaken by both the Weston Foods and Loblaw operating segments in order to position them for strong growth in the future.

In 2008, Weston Foods anticipates challenging market conditions as unprecedented increases for ingredient and other input costs are expected. Weston Foods plans to offset these higher input costs by ongoing cost reduction initiatives and pricing as necessary.

Loblaw's sales volumes have been positively responding to its investments in lower prices to give value to its customers. Loblaw expects this to continue in 2008. Investments in price will also continue. However, Loblaw expects that cost reductions in 2008 will help to support its profitability. Sales, margins and profitability in the first half of 2008 in relation to 2007 may be affected by more difficult comparables.

This outlook should be read in conjunction with the Forward-Looking Statements section of the MD&A on page 5.

19. NON-GAAP FINANCIAL MEASURES

The Company reports its financial results in accordance with Canadian GAAP. However, the Company has included certain non-GAAP financial measures and ratios, which it believes provide useful information to both management and readers of this Annual Report, in measuring the financial performance and financial condition of the Company for the reasons set out below. These measures do not have a standardized meaning prescribed by Canadian GAAP and, therefore, may not be comparable to similarly titled measures presented by other publicly traded companies, nor should they be construed as an alternative to other financial measures determined in accordance with Canadian GAAP.

Sales and Sales Growth Excluding the Impact of Tobacco Sales and VIEs

These financial measures exclude the impact on sales from the decrease in tobacco sales and from the consolidation by the Company of certain independent franchisees. Tobacco sales continued to decrease through the end of third quarter 2007 as a result of a major tobacco supplier shipping directly to certain customers of Loblaw's Cash & Carry and wholesale club network commencing in the third quarter of 2006. These impacts on sales are excluded because the Company believes this allows for a more effective analysis of the operating performance of the Company. A reconciliation of the financial measures to the Canadian GAAP financial measures is included in the table "Sales and Sales Growth Excluding the Impact of Tobacco Sales and VIEs" on pages 8, 24, 36 and 40 of this MD&A. Loblaw same-store sales growth and same-store sales growth excluding the impact of decreased tobacco sales are included in the table "Sales and Sales Growth Excluding the Impact of Tobacco Sales and VIEs" on pages 24 and 40 of this MD&A.

Adjusted Operating Income and Margin

The following table reconciles operating income (loss) and adjusted operating income to Canadian GAAP net earnings (loss) from continuing operations for the quarters ended December 31, 2007 and December 31, 2006 and the years ended December 31 as indicated. For each of its reportable operating segments, the tables on pages 19 and 24 of this MD&A reconcile segment adjusted operating income to segment operating income. Items listed in these reconciliations are excluded because the Company believes adjusted operating income allows for a more effective analysis of the operating performance of the Company. In addition, the excluded items affect the comparability of the financial results and could potentially distort the analysis of trends. The exclusion of these items does not imply they are non-recurring. Adjusted operating income and margin are useful to management in assessing the Company's performance and in making decisions regarding the ongoing operations of its business.

Adjusted operating margin is calculated as adjusted operating income divided by sales excluding the impact of tobacco sales and VIEs.

CONSOLIDATED

($ millions)	**Quarter ended Dec. 31, 2007 (unaudited)**	Quarter ended Dec. 31, 2006 (unaudited)	**Year ended Dec. 31, 2007**	Year ended Dec. 31, 2006	Year ended Dec. 31, 2005	Year ended Dec. 31, 2004	Year ended Dec. 31, 2003
Net earnings (loss) from continuing operations	**$ 151**	$ (428)	**$ 563**	$ 110	$ 716	$ 606	$ 807
Add (deduct) impact of the following:							
Minority interest	**22**	(289)	**130**	(82)	288	370	324
Income taxes	**46**	(3)	**236**	256	443	368	435
Interest (income) expense and other financing charges	**(38)**	90	**165**	253	187	438	266
Operating income (loss)	**$ 181**	$ (630)	**$ 1,094**	$ 537	$ 1,634	$ 1,782	$ 1,832
Add (deduct) impact of the following:							
Restructuring and other charges	**39**	51	**227**	90	118	122	60
Net effect of stock-based compensation and the associated equity derivatives	**77**	(11)	**109**	60	72	(3)	(11)
Commodity futures fair value adjustment	**6**	(3)	**(19)**		(3)		
Inventory liquidation	**3**	68	**15**	68			
VIEs	**(4)**		**(11)**	(8)			
Curtailment of post-retirement plan			**(7)**				
Loblaw goodwill impairment charge		800		800			
Ontario collective labour agreement		84		84			
Departure entitlement charge				12			
Goods and Services Tax and provincial sales taxes					40		
Direct costs associated with supply chain disruptions					30		
Adjusted operating income	**302**	359	**1,408**	1,643	1,891	1,901	1,881
Add (deduct) impact of the following:							
Depreciation and amortization	**162**	159	**704**	705	684	618	537
VIE depreciation and amortization	**(6)**	(5)	**(33)**	(24)	(26)		
Adjusted EBITDA	**$ 458**	$ 513	**$ 2,079**	$ 2,324	$ 2,549	$ 2,519	$ 2,418

WESTON FOODS

($ millions)	Quarter ended Dec. 31, 2007 (unaudited)	Quarter ended Dec. 31, 2006 (unaudited)	Year ended Dec. 31, 2007	Year ended Dec. 31, 2006	Year ended Dec. 31, 2005	Year ended Dec. 31, 2004	Year ended Dec. 31, 2003
Operating income	**$ 49**	$ 67	**$ 366**	$ 256	$ 241	$ 138	$ 374
Add (deduct) impact of the following:							
Restructuring and other charges	**3**	16	**5**	46	32	121	35
Net effect of stock-based compensation and the associated equity derivatives	**25**	(5)	**37**	23	29	(3)	(7)
Commodity futures fair value adjustment	**6**	(3)	**(19)**		(3)		
Curtailment of post-retirement plan			**(7)**				
Adjusted operating income	**83**	75	**382**	325	299	256	402
Add impact of the following:							
Depreciation and amortization	**28**	26	**116**	115	126	145	144
Adjusted EBITDA	**$ 111**	$ 101	**$ 498**	$ 440	$ 425	$ 401	$ 546

LOBLAW

($ millions)	Quarter ended Dec. 31, 2007 (unaudited)	Quarter ended Dec. 31, 2006 (unaudited)	Year ended Dec. 31, 2007	Year ended Dec. 31, 2006	Year ended Dec. 31, 2005	Year ended Dec. 31, 2004	Year ended Dec. 31, 2003
Operating income (loss)	**$ 132**	$ (697)	**$ 728**	$ 281	$ 1,393	$ 1,644	$ 1,458
Add (deduct) impact of the following:							
Restructuring and other charges	**36**	35	**222**	44	86	1	25
Net effect of stock-based compensation and the associated equity derivatives	**52**	(6)	**72**	37	43		(4)
Inventory liquidation	**3**	68	**15**	68			
VIEs	**(4)**		**(11)**	(8)			
Goodwill impairment charge		800		800			
Ontario collective labour agreement		84		84			
Departure entitlement charge				12			
Goods and Services Tax and provincial sales taxes					40		
Direct costs associated with supply chain disruptions					30		
Adjusted operating income	**219**	284	**1,026**	1,318	1,592	1,645	1,479
Add (deduct) impact of the following:							
Depreciation and amortization	**134**	133	**588**	590	558	473	393
VIE depreciation and amortization	**(6)**	(5)	**(33)**	(24)	(26)		
Adjusted EBITDA	**$ 347**	$ 412	**$ 1,581**	$ 1,884	$ 2,124	$ 2,118	$ 1,872

Adjusted EBITDA and Margin

The table on page 56 of this MD&A reconciles adjusted earnings before interest, income taxes, depreciation and amortization ("EBITDA") to Canadian GAAP net earnings (loss) from continuing operations for the quarters ended December 31, 2007 and December 31, 2006 and the years ended December 31 as indicated. For each of its reportable operating segments, the tables on pages 19 and 24 of this MD&A reconcile segment adjusted EBITDA to segment operating income. Adjusted EBITDA is useful to management in assessing the Company's performance of its ongoing operations and its ability to generate cash flows to fund its cash requirements, including the Company's capital investment program.

Adjusted EBITDA margin is calculated as adjusted EBITDA divided by sales excluding the impact of tobacco sales and VIEs.

Adjusted Basic Net Earnings per Common Share from Continuing Operations

The following table reconciles adjusted basic net earnings per common share from continuing operations to Canadian GAAP basic net earnings (loss) per common share from continuing operations reported in the consolidated statements of earnings for the quarters ended December 31, 2007 and December 31, 2006 and the years ended December 31 as indicated. Items listed in the reconciliation below are excluded because the Company believes this allows for a more effective analysis of the operating performance of the Company. In addition, they affect the comparability of the financial results and could potentially distort the analysis of trends. The exclusion of these items does not imply that they are non-recurring. Adjusted basic net earnings per common share from continuing operations is useful to management in assessing the Company's performance and in making decisions regarding the ongoing operations of its business.

CONSOLIDATED

Per common share ($)	**Quarter ended Dec. 31, 2007 (unaudited)**	Quarter ended Dec. 31, 2006 (unaudited)	**Year ended Dec. 31, 2007**	Year ended Dec. 31, 2006	Year ended Dec. 31, 2005	Year ended Dec. 31, 2004	Year ended Dec. 31, 2003
Basic net earnings (loss) per common share from continuing operations	**$ 1.07**	$ (3.42)	**$ 3.92**	$ 0.43	$ 5.25	$ 4.49	$ 5.91
Add (deduct) impact of the following:							
Restructuring and other charges	**0.13**	0.20	**0.72**	0.36	0.42	0.58	0.24
Net effect of stock-based compensation and the associated equity derivatives	**0.41**	(0.03)	**0.63**	0.38	0.46	(0.01)	(0.08)
Commodity futures fair value adjustment	**0.02**	(0.01)	**(0.10)**		(0.02)		
Inventory liquidation		0.21	**0.04**	0.21			
VIEs	**0.05**		**0.04**		0.03		
Curtailment of post-retirement plan			**(0.03)**				
Loblaw goodwill impairment charge		3.84		3.84			
Ontario collective labour agreement		0.26		0.26			
Departure entitlement charge				0.04			
Direct costs associated with supply chain disruptions					0.09		
Goods and Services Tax and provincial sales taxes					0.14		
Accounting for Loblaw forward sale agreement	**(0.64)**	0.09	**(0.81)**	(0.40)	(0.77)	0.51	
Changes in statutory income tax rates	**(0.15)**		**(0.15)**	(0.14)	0.02		0.03
Resolution of certain income tax matters						(0.07)	(0.26)
Adjusted basic net earnings per common share from continuing operations	**$ 0.89**	$ 1.14	**$ 4.26**	$ 4.98	$ 5.62	$ 5.50	$ 5.84

Net Debt

The following table reconciles net debt excluding Exchangeable Debentures to Canadian GAAP measures reported in the consolidated balance sheets as at the years ended as indicated. The Company calculates net debt as the sum of long term debt and short term debt less cash, cash equivalents and short term investments and believes this measure is useful in evaluating the amount of leverage employed. The Company calculates net debt excluding Exchangeable Debentures as net debt (as calculated above) less Exchangeable Debentures and believes this measure is also useful in evaluating the amount of leverage employed as the Exchangeable Debentures can be settled by the delivery of common shares of Domtar Corporation (see note 18 to the consolidated financial statements).

($ millions)	**Dec. 31, 2007**	Dec. 31, 2006	Dec. 31, 2005	Dec. 31, 2004	Dec. 31, 2003
Bank indebtedness	**$ 85**	$ 99	$ 113	$ 123	$ 108
Commercial paper	**609**	838	498	840	696
Short term bank loans	**250**	178	138	102	67
Long term debt due within one year	**432**	27	361	222	307
Long term debt	**5,494**	5,918	5,913	6,004	5,829
Less: Cash and cash equivalents	**1,353**	1,219	1,540	1,008	965
Short term investments	**603**	610	50	388	545
Net debt	**4,914**	5,231	5,433	5,895	5,497
Less: Exchangeable Debentures	**157**	220	225	373	374
Net debt excluding Exchangeable Debentures	**$ 4,757**	$ 5,011	$ 5,208	$ 5,522	$ 5,123

Total Assets

The following tables reconcile total assets used in the return on average total assets measure to Canadian GAAP measures reported in the consolidated balance sheets as at the years ended as indicated. The Company believes the return on average total assets ratio is useful in assessing the performance of operating assets and therefore excludes cash, cash equivalents, short term investments, assets of operations held for sale and the Domtar/Domtar (Canada) Paper Inc. investment (see note 18 to the consolidated financial statements) from the total assets used in this ratio.

				As at December 31, 2007
($ millions)	**Weston Foods**	**Loblaw**	**Discontinued Operations**	**Consolidated**
Total assets	**$ 4,574**	**$ 13,814**	**$ –**	**$ 18,388**
Less: Cash and cash equivalents	**679**	**674**		**1,353**
Short term investments	**300**	**303**		**603**
Domtar (Canada) Paper Inc. investment	**157**			**157**
Total assets	**$ 3,438**	**$ 12,837**	**$ –**	**$ 16,275**

				As at December 31, 2006
($ millions)	Weston Foods	Loblaw	Discontinued Operations	Consolidated
Total assets	$ 4,969	$ 13,626	$ –	$ 18,595
Less: Cash and cash equivalents	550	669		1,219
Short term investments	283	327		610
Domtar investment	215			215
Total assets	$ 3,921	$ 12,630	$ –	$ 16,551

Management's Discussion and Analysis

As at December 31, 2005

($ millions)	Weston Foods	Loblaw	Discontinued Operations	Consolidated
Total assets	$ 4,680	$ 13,901	$ 12	$ 18,593
Less: Cash and cash equivalents	624	916		1,540
Short term investments	46	4		50
Long term assets of discontinued operations			12	12
Domtar investment	220			220
Total assets	$ 3,790	$ 12,981	$ –	$ 16,771

As at December 31, 2004

($ millions)	Weston Foods	Loblaw	Discontinued Operations	Consolidated
Total assets	$ 4,614	$ 13,082	$ 73	$ 17,769
Less: Cash and cash equivalents	459	549		1,008
Short term investments	113	275		388
Current assets of discontinued operations			62	62
Long term assets of discontinued operations			11	11
Domtar investment	365			365
Total assets	$ 3,677	$ 12,258	$ –	$ 15,935

As at December 31, 2003

($ millions)	Weston Foods	Loblaw	Discontinued Operations	Consolidated
Total assets	$ 4,780	$ 12,230	$ 268	$ 17,278
Less: Cash and cash equivalents	347	618		965
Short term investments	167	378		545
Current assets of discontinued operations			179	179
Long term assets of discontinued operations			89	89
Domtar investment	367			367
Total assets	$ 3,899	$ 11,234	$ –	$ 15,133

Free Cash Flow

The following table reconciles free cash flow to Canadian GAAP measures reported in the consolidated cash flow statements for the quarters ended December 31, 2007 and December 31, 2006 and the years ended December 31 as indicated. The Company calculates free cash flow as cash flows from operating activities of continuing operations less fixed asset purchases and dividends. The Company believes free cash flow is a useful measure of the Company's cash available for additional funding and investing activities.

($ millions)	**Quarter ended Dec. 31, 2007 (unaudited)**	Quarter ended Dec. 31, 2006 (unaudited)	**Year ended Dec. 31, 2007**	Year ended Dec. 31, 2006	Year ended Dec. 31, 2005	Year ended Dec. 31, 2004	Year ended Dec. 31, 2003
Cash flows from operating activities of continuing operations	**$ 602**	$ 889	**$ 1,673**	$ 1,452	$ 1,812	$ 1,576	$ 1,294
Less: Fixed asset purchases	**206**	307	**722**	1,121	1,358	1,425	1,502
Dividends	**3**	3	**331**	304	308	285	241
Free cash flow	**$ 393**	$ 579	**$ 620**	$ 27	$ 146	$ (134)	$ (449)

The following table provides additional financial information.

	As at December 31, 2007	As at December 31, 2006	As at December 31, 2005
Market price per common share ($)	**$ 54.08**	$ 75.60	$ 86.31
Actual common shares outstanding (in millions)	**129.1**	129.1	129.0
Weighted average common shares outstanding (in millions)	**129.1**	129.0	129.0

20. ADDITIONAL INFORMATION

Additional information about the Company, including its Annual Information Form and other disclosure documents, has been filed electronically with various securities regulators in Canada through the System for Electronic Document Analysis and Retrieval (SEDAR) and is available online at www.sedar.com.

This Annual Report includes selected information on Loblaw Companies Limited, a 62%-owned public reporting company with shares trading on the Toronto Stock Exchange. For information regarding Loblaw, readers should also refer to the materials filed by Loblaw with the Canadian securities regulatory authorities from time to time.

Toronto, Canada
March 12, 2008