

## **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. When a fiscal year such as 2008 contains 53 weeks, the fourth quarter is 13 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.

## 9.1 QUARTERLY FINANCIAL INFORMATION<sup>(1)</sup> (UNAUDITED)

(\$ millions except where otherwise indicated)		First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total (audited)
Sales	<b>2008</b>	<b>\$ 6,835</b>	<b>\$ 7,324</b>	<b>\$ 9,879</b>	<b>\$ 8,050</b>	<b>\$ 32,088</b>
	2007	\$ 6,668	\$ 7,214	\$ 9,497	\$ 7,228	\$ 30,607
Net earnings						
from continuing operations	<b>2008</b>	<b>\$ 84</b>	<b>\$ 87</b>	<b>\$ 118</b>	<b>\$ 356</b>	<b>\$ 645</b>
	2007	\$ 66	\$ 81	\$ 117	\$ 110	\$ 374
Net earnings	<b>2008</b>	<b>\$ 131</b>	<b>\$ 118</b>	<b>\$ 179</b>	<b>\$ 404</b>	<b>\$ 832</b>
	2007	\$ 104	\$ 129	\$ 179	\$ 151	\$ 563
Net earnings per common share						
from continuing operations (\$)						
Basic and diluted	<b>2008</b>	<b>\$ 0.55</b>	<b>\$ 0.60</b>	<b>\$ 0.80</b>	<b>\$ 2.68</b>	<b>\$ 4.63</b>
	2007	\$ 0.41	\$ 0.53	\$ 0.77	\$ 0.75	\$ 2.46
Net earnings per common share (\$)						
Basic and diluted	<b>2008</b>	<b>\$ 0.91</b>	<b>\$ 0.84</b>	<b>\$ 1.28</b>	<b>\$ 3.05</b>	<b>\$ 6.08</b>
	2007	\$ 0.70	\$ 0.90	\$ 1.25	\$ 1.07	\$ 3.92

(1) Results of Weston Foods' U.S. fresh bakery business have been reclassified as discontinued operations.

### Results by Quarter

Consolidated sales and sales growth in 2008 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 2008 compared to 2007. Quarterly same-store sales growth for each of the four quarters of 2008 when compared to 2007 was 2.8%, 0.7%, 3.0% and 10.6%, respectively.

Internal retail food price inflation at Loblaw increased as the year progressed but was lower than the national food price inflation as measured by CPI. In the fourth quarter of 2008, national food price inflation had increased to 8.4% from 0.1% in the first quarter. This measure of inflation does not necessarily reflect the effect of inflation on the specific mix of goods sold in Loblaw stores.

Weston Foods 2008 quarterly sales were positively impacted by price increases across key product categories combined with changes in sales mix. Foreign currency translation negatively impacted sales growth in the first three quarters of 2008 as compared to the same periods in 2007, and positively impacted sales growth in the fourth quarter of 2008.

At Loblaw, fluctuations in quarterly net earnings during 2008 reflect the impact of a number of specific charges including restructuring and other charges and the net effect of stock-based compensation net of the equity forwards. Earnings in the third and fourth quarters of 2008 benefited from Loblaw's cost reduction initiatives, whereas earnings in the first and second quarters of 2008 and the fourth quarter of 2007 were pressured from investments in lower retail pricing. At Weston Foods, pricing, a shift in sales mix to higher margin products and the benefits realized from cost reduction and productivity initiatives more than offset the impact of inflationary cost pressures throughout 2008 and 2007. Quarterly net earnings are also impacted by seasonality and the timing of holidays. The impact of seasonality is greatest in the fourth quarter and least in the first quarter.

Interest expense and other financing charges fluctuate mainly as a result of the accounting for GWL's 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 2008 over 2007 was primarily due to a change in the proportion of taxable income earned across different tax jurisdictions and lower Canadian federal and certain provincial statutory income tax rates relative to 2007, which were partially offset by an increase in income tax accruals relating to certain income tax matters and a 2007 cumulative adjustment of future taxes pursuant to a reduction in the Canadian federal and certain provincial statutory income tax rates. The change in effective tax rates in the fourth quarter of 2008 was also impacted by the impact of non-taxable amounts including capital gains and a charge related to tax on unrealized foreign exchange gains on short term investments.

## Management's Discussion and Analysis

### 9.2 FOURTH QUARTER RESULTS (UNAUDITED)

The following is a summary of selected unaudited consolidated financial information for the fourth quarter of 2008. 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 continuing operations and changes in cash flows in the fourth quarter.

#### Selected Consolidated Information<sup>(1)</sup>

(unaudited)

(\$ millions except where otherwise indicated)

	2008	2007
Sales	\$ 8,050	\$ 7,228
Operating income	\$ 345	\$ 139
Operating margin	4.3%	1.9%
Gain on disposal of business	\$ 335	
Interest expense (income) and other financing charges	\$ 136	\$ (36)
Income taxes	\$ 112	\$ 43
Net earnings from continuing operations	\$ 356	\$ 110
Net earnings	\$ 404	\$ 151
Basic net earnings per common share from continuing operations (\$)	\$ 2.68	\$ 0.75
Basic net earnings per common share (\$)	\$ 3.05	\$ 1.07
EBITDA <sup>(2)</sup>	\$ 484	\$ 287
EBITDA margin <sup>(2)</sup>	6.0%	4.0%
Cash flows from (used in) continuing operations:		
Operating activities	\$ 602	\$ 530
Investing activities	\$ 21	\$ (300)
Financing activities	\$ (498)	\$ (197)

(1) Results of Weston Foods' U.S. fresh bakery business have been reclassified as discontinued operations.

(2) See non-GAAP financial measures beginning on page 46.

#### Sales

Sales in the fourth quarter of 2008 were \$8.1 billion compared to \$7.2 billion for the same period in 2007, an increase of 11.4%, and include the positive impact of approximately 7.8% due to reporting an additional week of results in 2008 (a 13-week period).

#### Operating Income

The Company's consolidated operating income for the fourth quarter of 2008 was \$345 million compared to \$139 million in the same period in 2007, an increase of 148.2%. Consolidated operating margin of 4.3% for the fourth quarter increased compared to 1.9% for the same period in 2007.

Year-over-year changes in the following items influenced the Company's operating income in the fourth quarter of 2008 compared to the same period in 2007:

- income of \$4 million (2007 – a charge of \$38 million) due to lower than anticipated restructuring and other charges for restructuring plans undertaken by both Weston Foods and Loblaw;
- income of \$23 million (2007 – a charge of \$79 million) related to the effect of stock-based compensation net of equity derivatives of both GWL and Loblaw. 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 net of the number of common shares associated with the equity derivatives and the change in the market prices of the underlying common shares;
- a charge of \$5 million (2007 – income of \$4 million) related to the commodity derivatives fair value adjustment at Weston Foods. This commodity derivatives fair value adjustment includes realized and unrealized gains and losses related to future purchases of raw materials;
- income of \$9 million (2007 – \$10 million) related to the income of Weston Foods' dairy and bottling operations;
- income of \$22 million (2007 – nil) related to the gain on the sale of Loblaw's food service business; and
- a charge of nil (2007 – \$1 million) related to the fair value adjustment of the Domtar (Canada) Paper Inc. shares, net of the re-measurement of the GWL 3% Exchangeable Debentures.

Excluding the impact of these specific items, operating income improved compared to the fourth quarter of 2007.

#### ***Gain on Disposal of Business***

In the fourth quarter of 2008, the Company recorded a pre-tax gain of \$335 million (\$281 million, net of tax) on the disposal of Weston Foods' dairy and bottling operations. The effect on basic net earnings per common share for the fourth quarter of 2008 was income of \$2.18.

#### ***Interest Expense (Income) and Other Financing Charges***

Interest expense and other financing charges for the fourth quarter of 2008 increased \$172 million to \$136 million from income of \$36 million in the fourth quarter of 2007. This increase was primarily due to a non-cash charge relating to the accounting for GWL's forward sale agreement of 9.6 million Loblaw common shares of \$52 million, compared to non-cash income of \$110 million in 2007. Also impacting the year-over-year increase in the fourth quarter were dividends on capital securities offset by lower levels of net debt<sup>(1)</sup>

#### ***Income Taxes***

The effective income tax rate decreased to 20.6% in the fourth quarter of 2008 compared to 24.6% in the fourth quarter of 2007. The decrease in the fourth quarter of 2008 when compared to the same period in 2007 was primarily due to non-taxable amounts including capital gains, a change in the proportion of taxable income earned across different tax jurisdictions, lower Canadian federal and certain provincial statutory income tax rates relative to the fourth quarter of 2007 and a decrease in income tax accruals relating to certain income tax matters, which were partially offset by a charge of \$11 million related to tax on unrealized foreign exchange gains on short term investments and a 2007 cumulative adjustment of future taxes pursuant to a reduction in Canadian federal and certain provincial statutory income tax rates.

#### ***Net Earnings from Continuing Operations***

Net earnings from continuing operations for the fourth quarter of 2008 increased \$246 million, or 223.6%, to \$356 million from \$110 million in the same period in 2007. Basic net earnings per common share from continuing operations for the fourth quarter of 2008 increased \$1.93, or 257.3%, to \$2.68 from \$0.75 in the same period in 2007.

Basic net earnings per common share from continuing operations were affected in the fourth quarter of 2008 compared to the fourth quarter of 2007 by the following factors:

- \$0.02 per common share income (2007 – \$0.12 per common share charge) due to lower than anticipated restructuring and other charges for restructuring plans undertaken by both Weston Foods and Loblaw;
- \$0.08 per common share income (2007 – \$0.41 per common share charge) related to the effect of stock-based compensation net of equity derivatives of both GWL and Loblaw;
- a \$0.03 per common share charge (2007 – \$0.02 per common share income) related to the commodity derivatives fair value adjustment at Weston Foods;
- \$0.05 per common share income (2007 – \$0.06) related to the income of Weston Foods' dairy and bottling operations;
- \$0.07 per common share income (2007 – nil) related to the gain on the sale of Loblaw's food service business;
- \$2.18 per common share income (2007 – nil) related to the gain on disposal of Weston Foods' dairy and bottling operations;
- a \$0.30 per common share non-cash charge (2007 – \$0.64 per common share non-cash income) related to the accounting for GWL's forward sale agreement for 9.6 million Loblaw common shares;
- nil per common share (2007 – \$0.01 per common share charge) related to the income tax effect of the fair value adjustment of the Domtar (Canada) Paper Inc. shares, net of the re-measurement of the GWL 3% Exchangeable Debentures; and
- nil per common share (2007 – \$0.15 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.

#### ***Discontinued Operations***

Net earnings from discontinued operations for the fourth quarter of 2008 were \$48 million, compared to \$41 million in the same period in 2007.

#### ***Net Earnings***

Net earnings for the fourth quarter of 2008 of \$404 million increased \$253 million compared to net earnings of \$151 million in the same period in 2007. Basic net earnings per common share for the fourth quarter of 2008 of \$3.05 increased \$1.98 compared to basic net earnings per common share of \$1.07 in 2007, including earnings from discontinued operations per common share of \$0.37 compared to \$0.32 in the same period in 2007.

(1) See non-GAAP financial measures beginning on page 46.

## Management's Discussion and Analysis

### 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)

	2008	2007
Sales	\$ 507	\$ 468
Operating income	\$ 30	\$ 7
EBITDA <sup>(1)</sup>	\$ 45	\$ 21

(1) See non-GAAP financial measures beginning on page 46.

Weston Foods sales for the fourth quarter of 2008 of \$507 million increased 8.3% compared to the same period in 2007. The results of its dairy and bottling operations negatively impacted reported sales growth by approximately 14.4%, while the additional week of operating results in 2008 and foreign currency translation positively impacted sales by approximately 7.0% and 6.7%, respectively. Price increases across key product categories combined with changes in sales mix contributed positively to sales growth by 8.9% for the fourth quarter of 2008. Volume declined 11.5% for the fourth quarter of 2008 when compared to the same period in 2007 and was negatively impacted by 18.1% due to the results of the dairy and bottling operations, while the additional week of operating results in 2008 positively impacted volume growth by approximately 6.5%.

In the fourth quarter, the following sales analysis inclusive of the 53rd week excludes the impact of foreign currency translation and the results of the dairy and bottling operations:

- fresh bakery sales, including fresh-baked sweet goods, increased by approximately 14.5% driven by price increases in key product categories combined with changes in sales mix. Volume increases were positively impacted by the additional week of operating results. Sales growth in whole grain and whole wheat products exceeded the sales growth of white flour based products. The introduction of new products, such as *D'Italiano Thintini*, *Gadoua Vitalité*, *Wonder + Headstart*, *Country Harvest Plus* and products under the *Weight Watchers*<sup>®</sup> licensed brand contributed positively to branded sales growth;
- frozen bakery sales increased by approximately 18.2% driven mainly by price increases combined with changes in sales mix. Positive volume growth was driven by increases in certain categories and the additional week of operating results; and
- biscuit sales, principally wafers, ice-cream cones, cookies and crackers, increased by approximately 17.0% due to higher sales volumes in all categories.

Weston Foods operating income increased \$23 million to \$30 million in the fourth quarter of 2008 from \$7 million in the same period in 2007. Operating margin was 5.9% for the fourth quarter of 2008 compared to 1.5% in 2007.

The year-over-year change in the following items influenced operating income for the fourth quarter of 2008 compared to the fourth quarter of 2007:

- a charge of \$4 million (2007 – \$2 million) related to restructuring and other charges;
- income of \$6 million (2007 – a charge of \$27 million) related to the effect of stock-based compensation net of equity derivatives;
- a charge of \$5 million (2007 – income of \$4 million) related to the commodity derivatives fair value adjustment;
- income of \$9 million (2007 – \$10 million) related to the income of the dairy and bottling operations; and
- a charge of nil (2007 – \$1 million) related to the fair value adjustment of the Domtar (Canada) Paper Inc. shares, net of the re-measurement of the GWL 3% Exchangeable Debentures.

Excluding the specific items described above, operating income increased in the fourth quarter of 2008 compared to the same period in 2007. Operating income was positively impacted by sales growth primarily due to price increases combined with changes in sales mix, the additional week of operating results and the benefits realized from the continued focus on cost reduction initiatives and restructuring activities. Pricing and other actions mitigated the impact of higher fuel costs and the inflationary cost pressures related to certain ingredients, primarily flour, oils and sugar. Gross margin decreased in the fourth quarter of 2008 mainly as a result of the commodity derivatives fair value adjustment.

EBITDA<sup>(1)</sup> increased \$24 million to \$45 million in the fourth quarter of 2008 compared to \$21 million in 2007. EBITDA margin<sup>(1)</sup> increased in the fourth quarter of 2008 to 8.9% from 4.5% in 2007.

(1) See non-GAAP financial measures beginning on page 46.

**LOBLAW**(unaudited)  
(\$ millions)

	2008	2007
Sales	\$ 7,745	\$ 6,967
Operating income	\$ 315	\$ 132
EBITDA <sup>(1)</sup>	\$ 439	\$ 266

(1) See non-GAAP financial measures beginning on page 46.

Sales in the fourth quarter increased 11.2% to \$7.7 billion compared to \$7.0 billion in the fourth quarter of 2007. The following factors explain the major components in the change in sales for the fourth quarter of 2008 compared to the fourth quarter of 2007:

- same-store sales growth of 10.6% including an increase in sales and same-store sales growth of 7.9% due to the extra selling week in the fourth quarter of 2008;
- a shift of the Thanksgiving holiday to the fourth quarter of 2008 resulted in higher sales and same-store sales growth of approximately 0.8% during the fourth quarter of 2008;
- sales and same-store sales growth were negatively impacted by 1.0% due to a strike in certain *Maxi* stores in Quebec;
- on an equivalent 12-week basis, total sales growth in both food and drugstore was strong;
- on an equivalent 12-week basis, apparel sales growth was strong in the fourth quarter but this did not offset the decline in core general merchandise sales growth, which primarily declined due to reductions in assortment and square footage;
- on an equivalent 12-week basis, item count growth declined marginally, while customer count growth remained flat versus the fourth quarter of 2007;
- on an equivalent 12-week basis, gas bar sales growth was negative as a result of lower fuel prices;
- Loblaw's analysis indicated that internal retail food price inflation was higher than the year-to-date trend, but lower than the national food price inflation of 8.4% as measured by CPI. In the fourth quarter of 2007, Loblaw experienced internal retail food price deflation; and
- during the fourth quarter of 2008, 16 new corporate and franchised stores were opened and 10 were closed, resulting in a net increase of 0.2 million square feet or 0.5%.

Operating income of \$315 million for the fourth quarter of 2008 increased \$183 million, or 138.6%, compared to operating income of \$132 million in 2007. Operating margin was 4.1% compared to 1.9% in the fourth quarter of 2007. The increase in operating income was mainly due to lower restructuring and net stock-based compensation costs, higher sales, and cost reduction initiatives.

The year-over-year change in the following items influenced operating income for the fourth quarter of 2008 compared to the fourth quarter of 2007:

- income of \$8 million (2007 – a charge of \$36 million) related to lower than anticipated restructuring and other charges;
- income of \$17 million (2007 – a charge of \$52 million) related to the effect of stock-based compensation net of equity forwards; and
- income of \$22 million (2007 – nil) related to the gain on the sale of Loblaw's food service business.

Included in 2008 fourth quarter operating income is a fixed asset impairment charge of \$29 million (2007 – \$33 million). In the fourth quarter of 2007, an \$11 million gain was realized related to the sale of an office building in Calgary, Alberta. On an equivalent 12-week basis and excluding the above items, operating income in the fourth quarter of 2008 improved compared to the fourth quarter of 2007.

Loblaw experienced higher store labour costs in the fourth quarter of 2008 as a result of higher sales. Labour productivity decreased slightly in the fourth quarter of 2008 compared to the same period in 2007 as a result of investments in training and Loblaw's commitment to improve customer service during the holiday season. Labour productivity has improved on a year-over-year basis.

EBITDA<sup>(1)</sup> increased \$173 million, or 65.0%, to \$439 million in the fourth quarter of 2008 compared to \$266 million in the fourth quarter of 2007. EBITDA margin<sup>(1)</sup> increased in the fourth quarter of 2008 to 5.7% compared to 3.8% in 2007. The increases in EBITDA<sup>(1)</sup> and EBITDA margin<sup>(1)</sup> were due to lower restructuring charges, lower net stock-based compensation costs, higher sales and cost reduction initiatives.

(1) See non-GAAP financial measures beginning on page 46.

## Management's Discussion and Analysis

### Liquidity and Capital Resources

#### ***Cash flows from operating activities of continuing operations***

The Company's fourth quarter 2008 cash flows from operating activities of continuing operations were \$602 million compared to \$530 million in the comparable period in 2007. The increase for the fourth quarter was mainly due to an increase in net earnings from continuing operations before minority interest, excluding the impact of the gain on disposal of business, restructuring and other charges, and the fair value adjustment of GWL's forward sale agreement.

#### ***Cash flows from (used in) investing activities of continuing operations***

The Company's fourth quarter 2008 cash flows from investing activities of continuing operations were \$21 million compared to cash flows used in investing activities of continuing operations of \$300 million in 2007. The primary reasons for the change include the \$467 million of proceeds from the fourth quarter 2008 disposition of Weston Foods' dairy and bottling operations and a decrease in the cash flows used in credit card receivables, after securitization. Offsetting these changes was an increase in capital spending primarily associated with Loblaw's investment in its infrastructure, and reduced proceeds from asset sales when compared to the same period in 2007. Capital investment for the fourth quarter amounted to \$383 million (2007 – \$185 million).

#### ***Cash flows used in financing activities of continuing operations***

The Company's fourth quarter 2008 cash flows used in financing activities of continuing operations were \$498 million compared to \$197 million in 2007. This increase was primarily due to an increase in cash flows used in short term borrowings, largely driven by the reduction in GWL's committed credit facility, as well as an increase in dividends paid in the quarter, which was due to the timing of payment.