MANAGEMENT'S DISCUSSION AND ANALYSIS

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The following Management's Discussion and Analysis ("MD&A") for George Weston Limited ("Weston") and its subsidiaries (collectively, the "Company") should be read in conjunction with the consolidated financial statements and the accompanying notes on pages 51 to 87 of this Financial 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. As a result of implementing Accounting Guideline 15, "Consolidation of Variable Interest Entities", ("AcG 15") effective January 1, 2005, 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. A more comprehensive discussion regarding the implementation of AcG 15 is included in the Accounting Standards Implemented in 2005 section below. A Glossary of terms and ratios used throughout this Financial Report can be found on page 91. The information in this MD&A is current as of March 10, 2006, unless otherwise noted.

FORWARD-LOOKING STATEMENTS

The Annual Report, including this MD&A, contains forward-looking statements which reflect management's expectations regarding the Company's objectives, plans, goals, strategies, future growth, results of operations, performance and business prospects and opportunities. Forward-looking statements are typically identified by words or phrases such as "anticipates", "expects", "believes", "estimates", "intends" and other similar expressions.

These forward-looking statements are not guarantees, but only predictions. Although the Company believes that these statements are based on information and assumptions, which are current, reasonable and complete, these statements are necessarily subject to a number of factors that could cause actual results to vary significantly from the estimates, projections and intentions. Such differences may be caused by factors which include, but are not limited to, changes in consumer spending, preferences and consumers' nutritional and health related concerns, changes in the competitive environment, including changes in pricing and market strategies of the Company's competitors and the entry of new competitors and expansion of current competitors, the availability and cost of raw materials and ingredients, fuels and utilities, the ability to realize anticipated cost savings, including those resulting from restructuring and other cost reduction initiatives, the ability to execute restructuring plans effectively, the Company's relationship with its employees, results of labour negotiations including the terms of future collective bargaining agreements, changes to the regulatory environment in which the Company operates now or in the future, changes in the Company's tax liabilities, either through changes in tax laws or future assessments, performance of third-party service providers, public health events, the ability of the Company to attract and retain key executives, the success rate of the Company in developing and introducing new products and entering new markets and supply and quality control issues with vendors. The Company cautions that this list of factors is not exhaustive. These factors 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 and Financial Risks and Risk Management sections of this MD&A.

The assumptions applied in making the forward-looking statements contained in the Annual Report, including this MD&A, include the following: economic conditions in 2006 do not materially change from those expected, patterns of consumer spending and preferences are reasonably consistent with historical trends, no new significant competitors enter the Company's market nor does any existing competitor significantly increase its presence or change pricing or market strategies, anticipated cost savings from restructuring activities are realized as planned, continuing future restructuring activities are effectively executed, there are no material work stoppages in 2006 and the performance of third-party service providers is in accordance with expectations in the upcoming year.

Potential investors and other readers are urged to consider these factors carefully in evaluating these forward-looking statements and are cautioned not to place undue reliance on them. The forward-looking statements included in the Annual Report, including this MD&A, are made only as of the filing date of the Annual Report and the Company does not undertake to publicly update these forward-looking statements to reflect new information, future events or otherwise. In light of these risks, uncertainties and assumptions, the forward-looking events contained in these forward-looking statements may or may not occur. The Company cannot assure that projected results or events will be achieved.

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. In prior years, the Company reported the Loblaw segment as the Food Distribution segment.

MANAGEMENT'S DISCUSSION AND ANALYSIS

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.

OPERATING AND FINANCIAL STRATEGIES

In order to be successful in delivering long term value and to fulfill its long term objectives of security and growth, the Company employs various operating and financial strategies in order to achieve its long term vision. Each of the Company's two reportable operating segments has its own risk profile and operating risk management strategy.

Weston Foods' long term operating strategies include:

- focusing on core brands, products, customers and markets;
- focusing on the development of new products to grow market share and penetration;
- ensuring its range of products are meeting the nutritional and dietary concerns of consumers;
- ongoing cost reduction initiatives to ensure a low cost operating structure and economies of scale;
- simplifying and removing complexity from both manufacturing and distribution processes;
- targeting strategic acquisitions and relationships to broaden market penetration and expand geographic presence; and
- continuous capital investment to strategically position production facilities across North America to support growth and enhance productivity and efficiencies.

Loblaw's long term operating strategies include:

- using the cash flow generated in its business to invest in its future;
- owning its real estate, where possible, to maximize flexibility for product and business opportunities in the future;
- using a multi-format approach to maximize market share over the longer term;
- focusing on food but serving the consumer's everyday household needs;
- creating customer loyalty and enhancing price competitiveness through a superior control label program;
- implementing and executing plans and programs flawlessly; and
- constantly striving to improve its value proposition.

The Company's financial strategies include:

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

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 time frame, target specific issues in response to 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 continue to fulfill its vision of providing sustainable returns to its shareholders over the long term.

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	2005	2004
Sales growth(2)	**5.3%**	2.7%
Sales growth excluding impact of VIEs(1)	**4.0%**	2.7%
Basic net earnings per common share from continuing operations growth	**16.9%**	(24.0)%
Adjusted basic net earnings per common share from continuing operations growth(1)	**2.5%**	(5.8)%
Net debt (excluding exchangeable debentures)(1) to equity ratio	**1.02:1**	1.26:1
Return on average common shareholders' equity	**16.7%**	14.8%
Common dividend payout ratio	**26.2%**	24.7%

(1) See Non-GAAP Financial Measures beginning on page 44.
(2) Sales growth in 2004 calculated on a 53-week year base in 2003. The extra week in 2003 had a negative impact of approximately 2% on the 2004 sales growth shown in the table above.

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 and market share.

OVERALL FINANCIAL PERFORMANCE

CONSOLIDATED RESULTS OF OPERATIONS

($ millions except where otherwise indicated)	2005	2004	2003
Sales	**$ 31,363**	$ 29,798	$ 29,021
Sales excluding impact of VIEs(1)	**$ 30,985**	$ 29,798	$ 29,021
Operating income	**$ 1,634**	$ 1,782	$ 1,832
Adjusted operating income(1)	**$ 1,894**	$ 1,901	$ 1,881
Interest expense and other financing charges	**$ 187**	$ 438	$ 266
Net earnings from continuing operations	**$ 716**	$ 606	$ 807
Net earnings	**$ 698**	$ 428	$ 792
Basic net earnings from continuing operations per common share ($)	**$ 5.25**	$ 4.49	$ 5.91
Adjusted basic net earnings from continuing operations per common share ($)(1)	**$ 5.64**	$ 5.50	$ 5.84
Basic net earnings per common share ($)	**$ 5.11**	$ 3.11	$ 5.80

(1) See Non-GAAP Financial Measures beginning on page 44.

Sales and Sales Growth Excluding Impact of VIEs(1)

($ millions except where otherwise indicated)	2005	2004	2003
Total sales	**$ 31,363**	$ 29,798	$ 29,021
Less: Sales attributable to the consolidation of VIEs pursuant to AcG 15	**378**		
Sales excluding impact of VIEs(1)	**$ 30,985**	$ 29,798	$ 29,021
Total sales growth(2)	**5.3%**	2.7%	
Less: Positive impact on sales growth attributable to the consolidation of VIEs pursuant to AcG 15	**1.3%**		
Sales growth excluding impact of VIEs(1)	**4.0%**	2.7%	

(1) See Non-GAAP Financial Measures beginning on page 44.
(2) Sales growth in 2004 calculated on a 53-week year base in 2003. The extra week in 2003 had a negative impact of approximately 2% on the 2004 sales growth shown in the table above.

Adjusted Operating Income[1]

($ millions)	2005	2004	2003
Operating income	$ 1,634	$ 1,782	$ 1,832
Add (deduct) impact of the following:			
Restructuring and other charges	118	122	60
Direct costs associated with supply chain disruptions	30		
Goods and Services Tax and provincial sales taxes	40		
Net effect of stock-based compensation and the associated equity derivatives	72	(3)	(11)
Adjusted operating income[1]	$ 1,894	$ 1,901	$ 1,881

(1) See Non-GAAP Financial Measures beginning on page 44.

Adjusted EBITDA[1]

($ millions)	2005	2004	2003
Adjusted operating income[1]	$ 1,894	$ 1,901	$ 1,881
Add (deduct) impact of the following:			
Depreciation and amortization	684	618	537
VIE depreciation and amortization	(26)		
Adjusted EBITDA[1]	$ 2,552	$ 2,519	$ 2,418

(1) See Non-GAAP Financial Measures beginning on page 44.

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

Per common share ($)	2005	2004	2003
Basic net earnings per common share from continuing operations	$ 5.25	$ 4.49	$ 5.91
Add (deduct) impact of the following:			
Restructuring and other charges	0.42	0.58	0.24
Direct costs associated with supply chain disruptions	0.09		
Goods and Services Tax and provincial sales taxes	0.14		
Net effect of stock-based compensation and the associated equity derivatives	0.46	(0.01)	(0.08)
Accounting for Loblaw forward sale agreement	(0.77)	0.51	
Changes in statutory income tax rates	0.02		0.03
Resolution of certain income tax matters		(0.07)	(0.26)
Variable interest entities	0.03		
Adjusted basic net earnings per common share from continuing operations[1]	$ 5.64	$ 5.50	$ 5.84

(1) See Non-GAAP Financial Measures beginning on page 44.

Consolidated 2005 results reflect the 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. Baking industry conditions have changed significantly over the past several years and the Company's North American baking operations have faced a challenging marketplace impacted by changing consumer eating preferences and food shopping patterns and a difficult sales pricing environment, as well as continued inflationary cost pressures. The Company continued to respond to these challenging conditions and execute on opportunities to improve the long term competitive position of its North American baking operations, which has resulted in further restructuring and other charges taken by the Company during 2005.

Results for the Loblaw operating segment were adversely affected by the short term costs associated with the significant transformational initiatives undertaken at Loblaw during 2005. Loblaw's need for this transformative process was driven by its assessments of a fast changing retail environment marked by increased consumer choice, low-cost global retailers and the addition of an increasingly unsustainable amount of industry square footage. Based on this assessment, Loblaw developed a comprehensive strategy designed to fortify its competitive position and to maintain its leadership role in meeting the food and everyday household needs of Canadian consumers. In pursuit of this strategy, Loblaw implemented a number of transformative changes to its organization during 2005, which resulted in certain restructuring and other charges taken by Loblaw. These changes included the restructuring of its supply chain network and the reorganizations involving its merchandising, procurement and operations groups, the establishment of a new national head office and Store Support Centre in Brampton, Ontario, which opened in the third quarter of 2005, and the relocation of general merchandise operations from Calgary, Alberta to the new office. A charge of $86 million was recorded in operating income in 2005 consisting of employee termination benefits resulting from planned involuntary terminations, site closing costs and fixed asset impairment and accelerated depreciation charges associated with these activities. Loblaw encountered challenges during the execution of planned changes to its systems, supply chain and general merchandise areas including certain supply chain systems conversions which were initiated as part of the creation of a national information technology platform and the start-up of a new third-party owned and operated general merchandise warehouse and distribution centre for eastern Canada. These challenges disrupted the flow of inventory to Loblaw's stores and caused Loblaw to incur additional operating costs. Additional incremental direct costs incurred in the handling, storage and movement of inventory resulting from these disruptions amounted to approximately $30 million for the year, which was recognized in operating income. Also in 2005, a charge was recorded relating to an audit and proposed assessment by the Canada Revenue Agency ("CRA") relative to Goods and Services Tax ("GST") on certain products sold during prior fiscal periods on which GST was not appropriately charged and remitted. In light of this proposed assessment, Loblaw assessed and estimated the potential liabilities for GST and provincial sales taxes ("PST") in other areas of its operations. Accordingly, a charge of $40 million was recorded in operating income to reflect the best estimate of such potential tax liabilities of which management is currently aware.

In addition, as previously mentioned in 2004 and consistent with Weston's strategy of focusing primarily on its core business segments, the Company completed the sale of the Fisheries business during 2005.

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

In 2005, consolidated sales increased 5.3% to $31.4 billion from $29.8 billion in 2004. Sales growth for 2005 included a positive impact of approximately 1.3% from the consolidation of certain Loblaw independent franchisees as required by AcG 15. Sales excluding the impact of VIEs(1) increased 4.0% or $1.2 billion over the prior year. In 2004, consolidated sales increased 2.7% from $29.0 billion in 2003. Sales growth in 2004 included a 2% negative impact from the 53rd week in 2003. The 52-week reporting cycle followed by the Company periodically necessitates a 53-week fiscal year, which occurred in 2003. The 2005 consolidated net earnings from continuing operations increased $110 million, or 18.2%, to $716 million from $606 million in 2004. In 2004, consolidated net earnings from continuing operations decreased $201 million, or 24.9%, from $807 million in 2003. Consolidated net earnings increased $270 million, or 63.1%, to $698 million in 2005 from $428 million in 2004. In 2004, consolidated net earnings decreased $364 million, or 46.0%, from $792 million in 2003.

The 2005 basic net earnings per common share from continuing operations of $5.25 increased 16.9% in line with the increase in consolidated net earnings from continuing operations. The increase was primarily due to lower interest expense and other financing charges due to non-cash income of $150 million in 2005 compared to a non-cash charge of $101 million in 2004 relating to the accounting for Weston's 2001 forward sale agreement for 9.6 million Loblaw common shares in accordance with accounting standards amended effective the third quarter of 2004. The 2005 basic net earnings per common share of $5.11 increased by 64.3% compared to $3.11 in 2004. The increase was primarily attributable to lower interest expense and other financing charges as explained above and a lower loss from discontinued operations in 2005.

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 United States dollars affect the Company's 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 the U.S. net investment into Canadian dollars. In 2004 and 2005, due to the significant appreciation in the Canadian dollar relative to the United States dollar, sales, net earnings and the value of the Company's net assets were negatively impacted as a result of foreign currency translation.

(1) See Non-GAAP Financial Measures beginning on page 44.

Over the past two years, the Weston Foods baking operations have operated in a challenging marketplace impacted by changing consumer eating preferences and food shopping patterns and a difficult sales pricing environment, as well as continued inflationary cost pressures. The changing consumer eating preferences, including a focus on health and diet, have negatively impacted Weston Foods sales of traditional white flour based products, in particular white bread and fresh-baked sweet goods. In addition, consumer shopping patterns continue to shift toward alternate format retail channels over traditional, conventional supermarket formats. These continuing trends are more fully discussed under Weston Foods operating results in the Results of Reportable Operating Segments section of this MD&A.

During this two-year period, Weston Foods sales have been positively impacted by its focus on:

- penetrating new sales channels, particularly with alternate format retail channels;
- strong sales growth in the whole grain and higher-priced premium product categories;
- new private label business; and
- the development and introduction of new and expanded convenience and health related product offerings, including "On the Go" individual portioned products as well as Omega-3, no cholesterol, reduced fat, no trans fat and organic products.

In 2005, Weston Foods achieved sales price increases across many of its product categories. These increases helped to partially mitigate the impact of the continued cost inflation experienced across the baking industry. Over the last two years, Weston Foods has continued to restructure its asset base to reduce costs and operate more efficiently. Management continues to review cost reduction and other strategic initiatives, including manufacturing asset and distribution network optimization and a focus on reducing administrative costs, to ensure a low cost operating structure and a continual improvement in its competitive cost position.

Loblaw sales in 2005 increased 6.1% to $27.8 billion from $26.2 billion in 2004. Excluding the impact of VIEs[(1)], sales were $27.4 billion or 4.6% higher than 2004. Sales growth of 3.9% for the full year 2004 included a 2% negative impact from the 53rd week in 2003. Same-store sales increased 0.2% in 2005 and 1.5% in 2004 on an equivalent 52-week basis. National food price inflation as measured by "The Consumer Price Index for Food Purchased from Stores" ("CPI") was approximately 2% for 2005 compared to 1% to 2% in 2004. Loblaw's calculation of food price inflation, which considers Loblaw-specific product mix and pricing strategy was reasonably consistent with that of CPI. Sales growth in 2005 was adversely affected by supply chain disruptions by approximately 0.5% to 0.7% over 2004. Sales were also influenced by a number of other factors, including changes in net retail square footage, expansion into new services and/or departments and the activities of competitors. Over the past two years, an average of $1.2 billion annually in capital was invested, resulting in an increase in net retail square footage of approximately 6.2 million square feet or 14.7%. Corporate store sales per average square foot declined from $605 in 2003 (a 53-week year) to $579 in 2005. The amount of new net retail square footage and the timing of the store openings and closures within any given year may vary. The increase in weighted average net retail square footage was 7.5% in 2005 and 6.4% in 2004. The rollout of *The Real Canadian Superstore* in Ontario, Canada also had an impact on same-store sales in that region by replacing mature, well performing stores that were previously included in same-store sales, and by creating pricing pressure on other Loblaw stores located within the respective trading areas. In pursuit of improving its value proposition, Loblaw has established price leadership in specific markets by adopting everyday low pricing strategies. Consistent with its strategy of focusing on food but serving the consumer's everyday household needs, Loblaw has expanded its general merchandise and drugstore offerings over this period and the retail sales growth realized in those categories continued to surpass retail sales growth of food. Competitor activity varied by market. During the past two years, unprecedented levels of retail square footage, mainly associated with food offerings, have been introduced into certain markets, resulting in pressure on prices and customer retention.

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 2005 consolidated sales increased 5.3% to $31.4 billion from $29.8 billion in 2004, including a positive impact of approximately 1.3% from the consolidation of certain Loblaw independent franchisees as required by AcG 15 and a negative impact of approximately 0.7% from the foreign currency translation of the Weston Foods operating segment.

Consolidated sales growth for 2005 was impacted by each reportable operating segment as follows:

- Positively by 0.1% due to the sales increase of 0.9% at Weston Foods, which included the negative impact of foreign currency translation of approximately 5.1%.
- Positively by 5.3% due to the sales increase of 6.1% at Loblaw, which included the positive impact of approximately 1.5% from the consolidation of certain Loblaw independent franchisees as required by AcG 15. Sales and same-store sales were adversely affected by supply chain disruptions experienced during 2005.

(1) See Non-GAAP Financial Measures beginning on page 44.

The Company's 2004 consolidated sales increased 2.7% to $29.8 billion from $29.0 billion in 2003, including a negative impact of approximately 2% from the 53rd week in 2003 and a negative impact of approximately 1% from the foreign currency translation of the Weston Foods operating segment.

Consolidated sales growth for 2004 was impacted by each reportable operating segment as follows:

- Negatively by 0.6% due to the sales decline of 4.2% at Weston Foods, which included the negative impact of foreign currency translation of approximately 6% and a negative impact of approximately 2% due to the additional week in 2003.
- Positively by 3.4% due to the sales increase of 3.9% at Loblaw, which included the negative impact of approximately 2% due to the additional week in 2003, partially offset by same-store sales growth of 1.5% on an equivalent 52-week basis.

Operating Income The Company's 2005 consolidated operating income decreased $148 million, or 8.3%, to $1,634 million. 2005 consolidated operating income included the negative impact of $260 million as a result of the following:

- a charge of $118 million related to restructuring and other charges for restructuring plans undertaken by both Weston Foods and Loblaw;
- a charge of $30 million related to Loblaw's estimated impact of direct costs associated with supply chain disruptions;
- a charge of $40 million related to Loblaw's estimate of GST and PST charges; and
- a charge of $72 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 dependent upon the number of unexercised, vested stock options and restricted share units, the number of underlying common shares associated with the equity derivatives and the fluctuations in the market price of the underlying common shares.

After adjusting for the negative impact of the items described above, consolidated adjusted operating income[1] for 2005 was $1,894 million compared to $1,901 million in 2004, a decline of 0.4%.

The Company's 2005 consolidated adjusted operating income[1] was impacted by each of its reportable operating segments as follows:

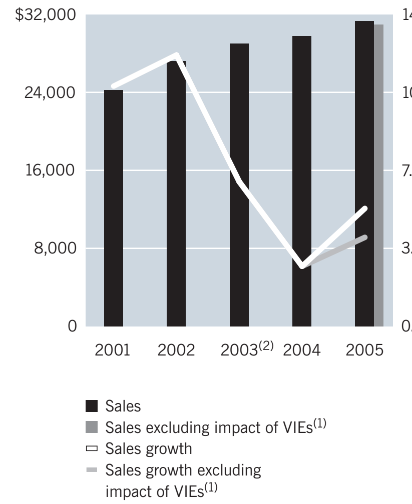
- Positively by 2.4% due to an increase of 18.0% in adjusted operating income[1] at Weston Foods, including the negative impact of foreign currency translation as a result of the appreciation of the Canadian dollar relative to the United States dollar. In addition, Weston Foods operating income was positively impacted by sales growth, including volume, price and sales mix improvements, and by the benefits being realized from restructuring and other cost reduction activities initiated in 2004 and 2005.
- Negatively by 2.8% due to a decrease of 3.2% in adjusted operating income[1] at Loblaw. Softening sales from product supply issues and deliberate delays in program activity in 2005 resulted in lost leverage on the fixed components of operating and administrative expenses.

The Company's 2005 consolidated adjusted operating margin[1] declined to 6.1% from 6.4% in 2004, and consolidated adjusted EBITDA margin[1] declined to 8.2% from 8.5% in 2004. Consolidated adjusted operating margin[1] declined in 2005 primarily due to the lower adjusted operating margin[1] at Loblaw, partially offset by the higher adjusted operating margin[1] at Weston Foods.

(1) See Non-GAAP Financial Measures beginning on page 44.

Sales and Sales Growth

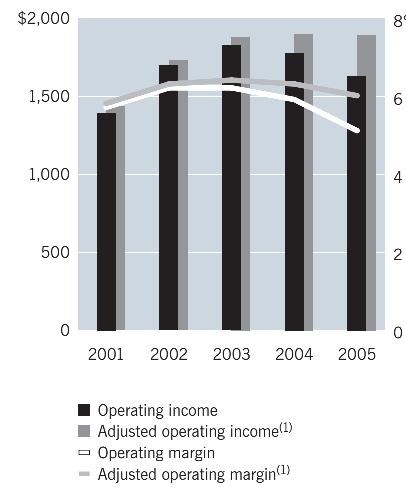
($ millions)



(1) See Non-GAAP Financial Measures beginning on page 44.
(2) 2003 was a 53-week year.

Operating Income and Margin, Adjusted Operating Income[1] and Margin[1]

($ millions)



(1) See Non-GAAP Financial Measures beginning on page 44.

The Company's 2004 consolidated operating income decreased $50 million, or 2.7%, to $1,782 million from $1,832 million in 2003. 2004 consolidated operating income included the net negative impact of $119 million as a result of the following:

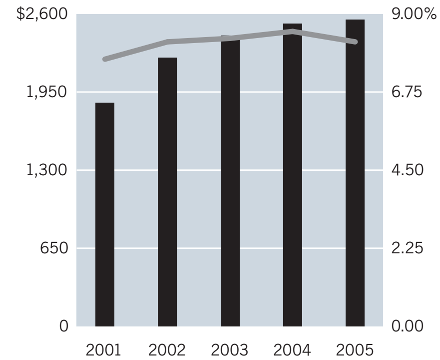
- a charge of $122 million primarily related to restructuring and other charges for restructuring plans undertaken by Weston Foods; and
- income of $3 million for the net effect of stock-based compensation and the associated equity derivatives.

After adjusting for the net negative impact of the items described above, consolidated adjusted operating income[1] for 2004 was $1,901 million compared to $1,881 million in 2003, an increase of 1.1%.

The Company's 2004 consolidated adjusted operating income[1] was impacted by each of its reportable operating segments as follows:

- Negatively by 7.7% due to a decline of 36.3% in adjusted operating income[1] at Weston Foods, primarily due to the significant inflation in ingredient, energy and employee related costs, higher consumer promotions and higher ingredient, production, distribution and product launch costs incurred as a result of the complexities associated with many of the new low-carb product introductions and ongoing changes in product sales mix. In addition, Weston Foods 2004 operating income was negatively impacted by foreign currency translation as a result of the significant appreciation of the Canadian dollar relative to the United States dollar.
- Positively by 8.8% due to an increase of 11.2% in adjusted operating income[1] at Loblaw, primarily due to improvements in operating margins due to buying synergies, a continued focus on administrative cost control and the efficiency resulting from improvements in supply chain operations.

Analysis of Adjusted EBITDA[1] and Margin[1]
($ millions)



(1) See Non-GAAP Financial Measures beginning on page 44.

The Company's 2004 consolidated adjusted operating margin[1] declined to 6.4% from 6.5% in 2003, and consolidated adjusted EBITDA margin[1] increased to 8.5% from 8.3% in 2003. Consolidated adjusted operating margin[1] declined in 2004 primarily due to the lower adjusted operating margin[1] at Weston Foods, partially offset by the higher adjusted operating margin[1] at Loblaw.

Interest Expense and Other Financing Charges Interest expense and other financing charges consist primarily of interest on short and long term debt, the amortization of deferred financing costs, interest and other financing charges on financial derivative instruments, interest earned on short term investments and interest capitalized to fixed assets.

In 2005, interest expense and other financing charges decreased $251 million, or 57.3%, to $187 million from $438 million in 2004. The change is explained as follows:

- Interest expense on long term debt decreased $8 million, or 1.9%, to $404 million from $412 million in 2004 primarily as a result of lower weighted average interest rates.
- Interest on financial derivative instruments, which includes the net positive effect of the Company's interest rate swaps, cross currency basis swaps and equity derivatives, amounted to income of $1 million (2004 – $28 million). The decrease in net interest income was due mainly to the maturity of interest rate swaps during the year and an increase in United States short term interest rates.
- Non-cash income of $150 million (2004 – non-cash charge of $101 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 (the "underlying Loblaw shares"). The fair value adjustment is based on the fluctuations in the market price of the underlying Loblaw shares and is a non-cash item that will ultimately be offset by the recognition of any gain on Weston's disposition of the underlying Loblaw shares (see notes 5 and 20 to the consolidated financial statements for additional information).
- Net short term interest income increased to $25 million (2004 – $7 million) primarily due to higher interest rates on United States dollar denominated cash, cash equivalents and short term investments and lower average short term debt partially offset by an increase in Canadian short term interest rates.
- Interest expense capitalized to fixed assets remained unchanged at $21 million as compared to 2004. Loblaw capitalizes interest incurred on debt related to real estate properties under development.

The 2005 weighted average fixed interest rate on long term debt (excluding capital lease obligations and the Exchangeable Debentures) was 6.6% (2004 – 6.7%) and the weighted average term to maturity was 16 years (2004 – 16 years).

(1) See Non-GAAP Financial Measures beginning on page 44.

In 2004, interest expense and other financing charges increased $172 million, or 64.7%, to $438 million from $266 million in 2003. The change is explained as follows:

- Interest expense on long term debt increased $15 million, or 3.8%, to $412 million from $397 million in 2003 as a result of an increase in average borrowing levels partially offset by lower weighted average interest rates and the impact of the 53rd week in 2003.
- Interest on financial derivative instruments amounted to income of $28 million (2003 – $84 million). The decrease in interest income was mainly due to the termination of currency and interest rate derivatives in late 2003 and the maturity of interest rate swaps during 2004.
- A non-cash charge of $101 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. The Company began recognizing this charge prospectively during the third quarter of 2004 due to the implementation of the amendment to Emerging Issues Committee ("EIC") Abstract 56, "Exchangeable Debentures" ("EIC 56"), which became effective at the beginning of the third quarter of 2004.
- Net short term interest income of $7 million compared to interest expense of $6 million in 2003 due in part to interest income on income tax refunds received in 2004 and lower floating Canadian interest rates, partially offset by lower United States dollar denominated cash, cash equivalents and short term investments.
- Interest expense capitalized to fixed assets amounted to $21 million (2003 – $33 million).

In 2006, interest expense and other financing charges is expected to be relatively consistent with 2005 except for the non-cash income or charge related to the fair value adjustment of Weston's 2001 forward sale agreement for 9.6 million Loblaw common shares, which fluctuates as the market price of Loblaw common shares changes.

Income Taxes The Company's 2005 effective income tax rate increased to 30.6% from 27.4% in 2004. The increase was the result of the following factors:

- a change in the proportion of taxable income earned across different tax jurisdictions, including the jurisdictions in which the income tax impacts of restructuring and other charges and stock-based compensation and the associated equity derivatives occurred;
- Loblaw's successful resolution in 2004 of certain income tax matters from a previous year; and
- a $3 million charge in 2005 for an adjustment to future income tax balances due to statutory income tax rate changes in certain Canadian provinces.

The Company's 2004 effective income tax rate decreased to 27.4% from 27.8% in 2003. The decrease was the result of the following factors:

- a decline in the Canadian federal statutory income tax rate;
- Loblaw's successful resolution in 2004 of certain income tax matters from a previous year of $14 million;
- a change in the proportion of taxable income earned across different tax jurisdictions, including the jurisdictions in which the income tax impacts of restructuring and other charges and stock-based compensation and the associated equity derivatives occurred;
- a $7 million charge in 2003 for an adjustment to future income tax balances due to the increase in corporate income tax rates in Ontario, Canada; and
- a reduction in 2003 of $34 million to the income tax expense due to the favourable resolution of an income tax issue previously accrued for by the Company, which related to the disposition of Weston's forest products business in 1998.

The Company's 2006 effective income tax rate is expected to be reasonably consistent with the 2005 effective tax rate. However, this may change if the proportion of taxable income earned across the different tax jurisdictions changes or if there is any change in tax legislation.

Net Earnings from Continuing Operations Net earnings from continuing operations for 2005 increased $110 million, or 18.2%, to $716 million from $606 million in 2004. Basic net earnings per common share from continuing operations for 2005 increased $0.76, or 16.9%, to $5.25 from $4.49 in 2004. The 2005 basic net earnings per common share from continuing operations of $5.25 included the net negative impact of $0.39 per common share as a result of the following factors:

- a $0.42 per common share charge related to restructuring and other charges for restructuring plans undertaken by both Weston Foods and Loblaw;
- a $0.09 per common share charge related to Loblaw's estimated impact of direct costs associated with supply chain disruptions;
- a $0.14 per common share charge related to Loblaw's estimate of GST and PST charges;
- a $0.46 per common share charge for the net effect of stock-based compensation and the associated equity derivatives;
- $0.77 per common share non-cash income related to the accounting for Weston's 2001 forward sale agreement for 9.6 million Loblaw common shares which is offset on an economic basis;
- a $0.02 per common share charge related to the adjustment to future income tax balances due to the changes in statutory income tax rates in certain Canadian provinces; and
- a $0.03 per common share charge related to the consolidation of VIEs by Loblaw.

(1) See Non-GAAP Financial Measures beginning on page 44.

After adjusting for the above noted items, Weston's 2005 adjusted basic net earnings per common share from continuing operations(1) was $5.64 compared to $5.50 in 2004, an increase of 2.5%.

Net earnings from continuing operations for 2004 decreased $201 million, or 24.9%, to $606 million from $807 million in 2003. Basic net earnings per common share from continuing operations for 2004 decreased $1.42, or 24.0%, to $4.49 from $5.91 in 2003. The 2004 basic net earnings per common share from continuing operations of $4.49 included the net negative impact of $1.01 per common share as a result of the following factors:

- a $0.31 per common share charge related to the impairment of fixed assets and intangible assets associated with the Weston Foods *Entenmann's* operation in the United States;
- a $0.27 per common share charge related to restructuring and other charges for other Weston Foods bakery facilities;
- $0.01 per common share income for the net effect of stock-based compensation and the associated equity derivatives;
- a $0.51 per common share non-cash charge related to the accounting for Weston's 2001 forward sale agreement for 9.6 million Loblaw common shares; and
- $0.07 per common share income related to Loblaw's successful resolution in 2004 of certain income tax matters from a previous year.

After adjusting for the above noted items, Weston's 2004 adjusted basic net earnings per common share from continuing operations(1) was $5.50. This result compares to 2003 adjusted basic net earnings per common share from continuing operations(1) of $5.84 which was adjusted for the net negative impact of restructuring and other charges, stock-based compensation and the associated equity derivatives, changes in statutory income tax rates and the resolution of certain income tax matters from a previous year. Adjusted basic net earnings per common share from continuing operations(1) for 2004 decreased 5.8% compared to 2003.

Discontinued Operations The loss from discontinued operations in 2005 was $18 million compared to a loss of $178 million in 2004. During 2005, the Company completed the sales of the remaining discontinued Fisheries operations. As a result of these sales, the Company will receive total net proceeds of $38 million, of which $12 million will be deferred over the next four years, and recorded an after-tax loss of $24 million as a loss from discontinued operations during 2005.

Subsequent to year end 2005, the Company reached an agreement to settle claims against it relating to certain alleged misrepresentations and warranties arising from the sale of the Company's forest products business in 1998, including tax related representations and warranties dealing with years prior to 1998. The Company did not admit any wrongdoing or liability in connection with the settlement. The net impact of this settlement agreement has been reflected in the 2005 loss from discontinued operations.

The loss from discontinued operations for 2004, net of income taxes, was $178 million, compared to $15 million in 2003, including the charge related to the impairment of assets and the loss on the sale of the operations in Chile incurred in 2004. During 2004, Weston sold all of the Fisheries operations in Chile for cash proceeds of $20 million, which resulted in a loss of $9 million.

For additional information, see note 9 to the consolidated financial statements.

Net Earnings Changes in the Company's net earnings over the past two years were impacted by the factors described above. In addition, the Company implemented several new accounting standards issued by the Canadian Institute of Chartered Accountants ("CICA") that impacted the financial results over the past two years. The following standards were implemented in 2004:

- Section 3063, "Impairment of Long-Lived Assets";
- AcG 13, "Hedging Relationships";
- Section 3110, "Asset Retirement Obligations";
- EIC Abstract 144, "Accounting by a Customer (Including a Reseller) for Certain Consideration Received from a Vendor";
- Amendments to EIC Abstract 56, "Exchangeable Debentures" ("EIC 56"); and
- Section 3461, "Employee Future Benefits" (for enhanced disclosure).

The implementation of these standards did not have a material impact on the Company's financial position or results of operations in 2004, except for EIC 56 as described above.

The new accounting standards implemented in 2005 and the resulting impact on the financial position and results of operations are outlined in the Accounting Standards Implemented in 2005 section of this MD&A.

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

(1) See Non-GAAP Financial Measures beginning on page 44.

CONSOLIDATED FINANCIAL CONDITION

($ millions except where otherwise indicated)		2005		2004[1]		2003[1]
Total assets	$	**18,593**	$	17,769	$	17,278
Total long term debt (excluding amount due within one year)	$	**5,913**	$	6,004	$	5,829
Dividends declared per share ($) – Common share	$	**1.44**	$	1.44	$	1.20
– Preferred share:						
Series I	$	**1.45**	$	1.45	$	1.45
Series II	$	**1.29**	$	1.29	$	1.29
Series III	$	**0.92**				
Series IV	$	**0.54**				

(1) Certain prior years' information was reclassified to conform with the current year's presentation.

The Company's total assets have increased over the past two years. Fixed assets have grown as a result of the capital investment program net of annual depreciation of both the Weston Foods and Loblaw operating segments and the impairment and accelerated depreciation charges taken within both operating segments. In 2004, Weston Foods acquired Boulangerie Gadoua Ltée ("Gadoua") with total assets valued at $75 million. Also in 2004, as a result of the annual impairment test of indefinite life intangible assets, Weston Foods recorded an impairment charge of $18 million related to the *Entenmann's* trademarks and brand names. Loblaw inventory growth resulted primarily from an investment in general merchandise. Loblaw's inventory turns of general merchandise categories are lower than those of food categories, resulting in higher aggregate levels of investment in general merchandise inventories as that business develops. A substantial portion of credit card receivables of President's Choice Bank ("PC Bank"), a wholly owned subsidiary of Loblaw, is sold to an independent trust and the unsecuritized balance net of the allowance for credit losses has increased by $94 million since 2003. The decrease in other assets resulted from a reduction in the Domtar Inc. investment due to exchanges of the 3% Exchangeable Debentures for Domtar Inc. common shares during 2005. In 2005 and 2004, the Company's total assets were reduced by the translation of the Company's U.S. net investment in self-sustaining operations due to the significant strengthening of the Canadian dollar relative to the United States dollar.

Cash flows from operating activities have covered a large portion of the funding requirements for the Company over the past two years. For each of 2005 and 2004, total long term debt issued net of the amounts retired was approximately $100 million. In addition, long term debt increased in 2005 as a result of consolidating $126 million of VIE long term debt ($23 million of which is due within one year) pursuant to AcG 15. The amount of fixed rate debt issued in any given year is intended to continue to preserve the Company's liquidity needs. Cash flows from operating activities in 2005 exceeded the Company's capital investment program of $1.4 billion.

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

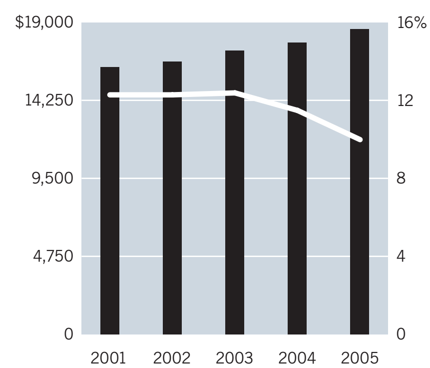
- the capital investment program;
- dividends paid on common and preferred shares;
- defined benefit pension plan contributions;
- non-cash working capital requirements; and
- purchases of Weston and Loblaw common shares pursuant to their respective Normal Course Issuer Bids ("NCIB").

In 2005, 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 decreased shareholders' equity by $114 million (2004 – $213 million). This net change was due to the negative impact of translating the Company's U.S. net investment.

Financial Ratios In 2005, the Company's financial position as measured by its financial ratios, balance sheet and cash flow, continued to be strong. This position is expected to continue in 2006.

The Company's 2005 return on average total assets[1] of 10.0% was lower than the 2004 return of 11.5%. The return was negatively impacted in 2005 by the incremental costs and charges recorded in operating income as outlined above. The Company's 2004 return on average total assets of 11.5% was lower than the 2003 return of 12.4%. This return was negatively impacted in 2004 by the incremental costs and charges recorded in operating income as outlined above.

Total Assets and Return on Average Total Assets[1]
($ millions)



■ Total assets
▭ Return on average total assets[1]

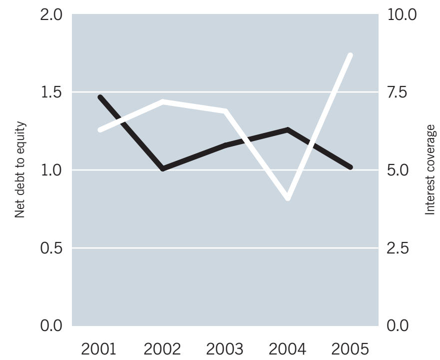
(1) See Non-GAAP Financial Measures beginning on page 44.

(1) See Non-GAAP Financial Measures beginning on page 44.

MANAGEMENT'S DISCUSSION AND ANALYSIS

The Company's 2005 return on average common shareholders' equity of 16.7% increased compared to the 2004 return of 14.8%, primarily due to lower interest expense and other financing charges including the $150 million non-cash income (2004 – non-cash charge of $101 million) related to the fair value adjustment of Weston's 2001 forward sale agreement for 9.6 million Loblaw common shares, partially offset by the incremental costs and charges recorded in operating income as outlined above. The Company's 2004 return on average common shareholders' equity of 14.8% was lower than the 2003 return of 20.0%. This decrease in 2004 was mainly due to lower net earnings from continuing operations, which included the impact of lower Weston Foods operating results and higher interest expense and other financing charges including the $101 million non-cash charge 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 17.9%.

Net Debt[1] to Equity and Interest Coverage



Net debt (excluding exchangable debentures)[1] to equity
Interest coverage

(1) See Non-GAAP Financial Measures beginning on page 44.

The Company's 2005 net debt (excluding exchangeable debentures)[1] to equity ratio was 1.02:1 compared to the 2004 ratio of 1.26:1. The change in this ratio from 2004 was the result of the following factors:

- lower average debt levels;
- the issuance of preferred shares by Weston;
- an increase in United States dollar denominated cash, cash equivalents and short term investments net of the impact of foreign currency translation as a result of the appreciation of the Canadian dollar relative to the United States dollar in 2005;
- higher net earnings primarily due to:
  - the $150 million non-cash income related to the fair value adjustment of Weston's forward sale agreement for 9.6 million Loblaw common shares; and
  - a lower loss from discontinued operations; partially offset by
  - lower Loblaw earnings due to the short term costs associated with the significant transformational initiatives at Loblaw;

offset by:

- the decrease 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 2005.

The Company's 2004 net debt (excluding exchangeable debentures)[1] to equity ratio was 1.26:1 compared to the 2003 ratio of 1.16:1. The change in this ratio from 2003 was the result of the following factors:

- lower net earnings primarily due to:
  - the restructuring and other charges incurred by Weston Foods in 2004;
  - the $101 million non-cash charge related to the fair value adjustment of Weston's forward sale agreement for 9.6 million Loblaw common shares; and
  - the loss from discontinued operations;
- higher average debt levels;
- the purchase of Weston common shares for cancellation pursuant to its NCIB;
- a decrease in United States dollar denominated cash, cash equivalents and short term investments resulting from foreign currency translation and the decrease in shareholders' equity resulting from the translation of the Company's U.S. net investment due to the significant appreciation of the Canadian dollar relative to the United States dollar in 2004; and
- increased funding requirements, primarily due to defined benefit pension plan contributions and working capital requirements.

The 2006 ratio is expected to improve as retained earnings growth is expected to exceed funding requirements.

Pursuant to the requirements of AcG 15, the consolidated balance sheet as at December 31, 2005 includes $126 million of loans payable of VIEs consolidated by the Company, $23 million of which are due within one year. The loans payable represent financing obtained by eligible Loblaw independent franchisees through a structure involving independent trusts to facilitate the purchase of the majority of their inventory and fixed assets, consisting mainly of fixturing and equipment. These loans payable, which have an average term to maturity of 7 years, are due and payable on demand under certain predetermined circumstances and are secured through a general security agreement made by the independent franchisees in favour of the independent funding trust. Interest is charged on a floating rate basis and prepayment of the loans may be made without penalty. The independent funding trust within the structure finances its activities through the issuance of short term asset-backed notes to third-party investors.

(1) See Non-GAAP Financial Measures beginning on page 44.

As disclosed in note 22 to the consolidated financial statements for the year ended December 31, 2005, a standby letter of credit has been provided by a major Canadian bank for the benefit of the independent funding trust equal to approximately 10% of the total principal amount of the loans outstanding at any point in time. Loblaw has agreed to reimburse the issuing bank for any amount drawn on the standby letter of credit. In the event of a default by an independent franchisee, the independent funding trust may assign the loan to Loblaw and draw upon the standby letter of credit. No amount has ever been drawn on the standby letter of credit.

The 2005 interest coverage ratio improved to 8.7 times compared to 4.1 times in 2004 due to lower interest expense and other financing charges, including the $150 million non-cash income recorded in 2005 related to the fair value adjustment of Weston's 2001 forward sale agreement for 9.6 million Loblaw common shares. This non-cash income related to the fair value adjustment of Weston's 2001 forward sale agreement positively impacted the 2005 interest coverage ratio by 3.9 times. The 2004 interest coverage ratio declined to 4.1 times compared to 6.9 times in 2003 due to lower operating income, higher interest expense and other financing charges, including the $101 million non-cash charge related to the fair value adjustment of Weston's 2001 forward sale agreement for 9.6 million Loblaw common shares. The non-cash charge related to the fair value adjustment of Weston's 2001 forward sale agreement negatively impacted the 2004 interest coverage ratio by 1.2 times.

Dividends The Company's common share dividend policy is to maintain a common dividend payment equal to approximately 20% to 25% of the prior year's adjusted basic net earnings per common share from continuing operations(1), giving consideration to the year end cash position, future cash flow requirements and investment opportunities. During 2005, Weston's Board declared quarterly dividends as follows:

($)	2005 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

The 2005 annualized dividend per common share of $1.44 was equal to 26.2% of the 2004 adjusted basic net earnings per common share from continuing operations(1) and was slightly above Weston's common dividend policy range. Subsequent to year end, the Board declared a quarterly dividend per common share of $0.36, payable April 1, 2006 which, on an annualized basis, maintains the 2005 dividend rate per common share.

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	129,038,226
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

For preferred shares Series I, Series II, Series III and Series IV holders, Weston may at any time after issuance, at its option, 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, for preferred shares, Series II holders, on or after July 1, 2009, these outstanding preferred shares are convertible, 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 18 to the consolidated financial statements.

(1) See Non-GAAP Financial Measures beginning on page 44.

MANAGEMENT'S DISCUSSION AND ANALYSIS

RESULTS OF REPORTABLE OPERATING SEGMENTS

The following discussion provides details of the 2005 results of operations of each of the Company's reportable operating segments.

WESTON FOODS OPERATING RESULTS

($ millions except where otherwise indicated)	2005	2004	Change
Sales	**$ 4,376**	$ 4,335	0.9%
Operating income	**$ 241**	$ 138	74.6%
Operating margin	**5.5%**	3.2%	
Adjusted operating income(1)	**$ 302**	$ 256	18.0%
Adjusted operating margin(1)	**6.9%**	5.9%	
Adjusted EBITDA(1)	**$ 428**	$ 401	6.7%
Adjusted EBITDA margin(1)	**9.8%**	9.3%	
Return on average total assets(1)	**6.5%**	3.6%	

(1) See Non-GAAP Financial Measures beginning on page 44.

Adjusted Operating Income(1)

($ millions)	2005	2004
Operating income	**$ 241**	$ 138
Add (deduct) impact of the following:		
Restructuring and other charges	**32**	121
Net effect of stock-based compensation and the associated equity derivatives	**29**	(3)
Adjusted operating income(1)	**$ 302**	$ 256

(1) See Non-GAAP Financial Measures beginning on page 44.

Adjusted EBITDA(1)

($ millions)	2005	2004
Adjusted operating income(1)	**$ 302**	$ 256
Add impact of the following:		
Depreciation and amortization	**126**	145
Adjusted EBITDA(1)	**$ 428**	$ 401

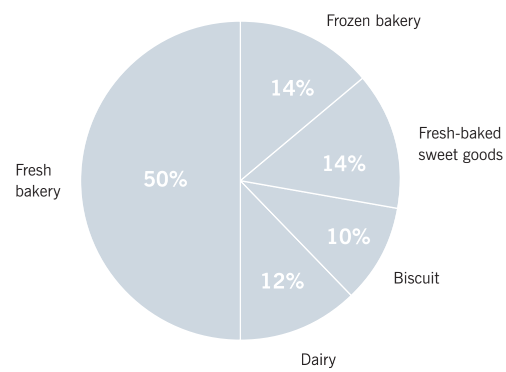
(1) See Non-GAAP Financial Measures beginning on page 44.

Approximately 88% of Weston Foods 2005 sales were generated by the North American baking divisions, with the remaining sales in the Canadian dairy division.

Sales and operating income in 2005 continued to be impacted by some of the same trends experienced in 2004. Most notably:

- Significant cost inflation was experienced in operations in a difficult sales pricing environment.
- Management's focus on cost reduction and growth initiatives resulted in certain restructuring charges in operating income.
- The shift in consumer food shopping patterns toward alternate format retail channels rather than traditional, conventional supermarket formats resulted in strong sales growth with alternate format retailers, specifically mass merchandisers. This shift has also resulted in weaker sales for some traditional food retailers as a result of the difficulties they are experiencing with the emergence of alternate channels for food products. Weston Foods continues its focus on ensuring its products are well aligned to serve the alternate format retail channel while maintaining its important positions with traditional food retailers.

Weston Foods 2005 Sales



- The shift in consumer eating preferences toward healthier and more nutritious offerings, as well as products that are more convenient, portion controlled and that can be consumed away from home continued to grow. Weston Foods has responded to these trends with innovative new and expanded products across its product portfolio. Not all consumer food trends are long lived: the popularity of extreme low-carb diets is declining; however, a more sustained shift in consumer preference for whole grain products rather than white flour based products continued throughout 2005. This trend is expected to continue into 2006. During 2004, Weston Foods launched several new low-carb offerings across many categories in response to anticipated strong consumer and customer demand. While sales volume in these products declined in 2005 over 2004, the trend in whole grain products has shown sustained strength. Weston Foods is well positioned to participate in this growth with investments being made in capacity and expanded product offerings under its *Thomas'*, *Arnold*, *Dutch Country*, *Wonder* and *Country Harvest* brands. Many of Weston Foods brands continue to capitalize on their whole grain heritage.

A detailed discussion on how these trends and other factors impacted sales and operating income in 2005 is set out below:

Sales Weston Foods 2005 reported sales increased 0.9% to $4.4 billion from $4.3 billion in 2004. Sales growth in 2005 was impacted by the following factors:

- Overall volume increases of 3.0% positively impacted sales growth. The acquisition of Gadoua in 2004 contributed 1.6% to overall volume growth.
- Price increases across key product categories combined with changes in sales mix contributed positively to sales growth by 3.0%.
- Foreign currency translation negatively impacted sales growth by 5.1% as a result of the further strengthening of the Canadian dollar relative to the United States dollar during 2005.

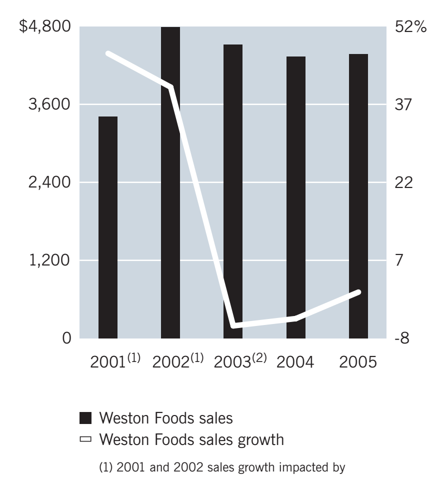
Fresh bakery sales, principally bread, rolls, English muffins and bagels, represented approximately 50% of total Weston Foods sales, up from approximately 48% in 2004. This category contributed positively to overall sales growth in 2005 as a result of a combination of the following:

- Branded volume increases including solid growth in *Thomas'*, *Arnold* and *Dutch Country* in the United States and *Wonder* and *Country Harvest* in Canada.
- Acquisition of Gadoua in 2004 which contributed positively to overall fresh bakery sales growth.
- Introduction of new and expanded product offerings including:
  - *Dutch Country Family Grains* breads;
  - *Thomas'* Mini Bagels and *Thomas' Hearty Grains* English Muffins, supported by a successful media advertising program introduced in 2005;
  - Reformulated *Wonder Fresh* white bread and *Wonder Fresh* 100% whole wheat bread, now made with 100% whole grains, in new foil packaging;
  - *Country Harvest* breads made with 100% whole grains and a source of Omega-3; and
  - Weight Watchers bread and English muffins.
- Although consumption of white flour based products continued to decline, price increases and new private label customers were achieved in this category, contributing positively to overall fresh bakery sales growth.

Fresh-baked sweet goods sales, primarily sold under the *Entenmann's* brand, represented approximately 14% of total Weston Foods sales, down from approximately 15% in 2004. Sales declined slightly over last year as this category continued to experience a challenging sales environment with continued volume declines in full size cake and Danish products. Single-serve and hand-held products such as *Little Bites* and the 2005 newly launched *Enten-minis* continued to provide growth to the overall category.

Frozen bakery sales, principally bread, rolls, bagels, English muffins and sweet goods, represented approximately 14% of total Weston Foods sales, down from approximately 15% in 2004. The frozen bakery category contributed positively to overall sales growth in 2005 with strong growth in sweet goods products offsetting declines in low-carb bread sales. Further improved sales mix and price improvements were realized in 2005.

Weston Foods Sales and Sales Growth
($ millions)



(1) 2001 and 2002 sales growth impacted by acquisition of Bestfoods Baking Co., Inc.
(2) 2003 was a 53-week year.

Biscuit sales, principally cookies, crackers, and ice-cream cones and wafers, represented approximately 10% of total Weston Foods sales, down from approximately 11% in 2004. The biscuit category negatively impacted overall sales growth in 2005 due to lower sales volume. Girl Scout cookie sales declined over 2004, due to a decrease in sales volume. A general weakness in the private label retail cookie business was experienced during 2005 with price increases remaining difficult to achieve.

Dairy sales represented approximately 12% of total Weston Foods sales, up from approximately 11% in 2004. The category contributed positively to overall sales growth in 2005 as a result of volume growth, price increases, and the improvement in sales mix as growth continued in value-added products including the continued success of *Neilson Dairy Oh!* milk enriched with DHA. Continued growth in bottled products was achieved in 2005 and the Ontario bottling facility with aseptic capabilities provides opportunity for future growth in this category.

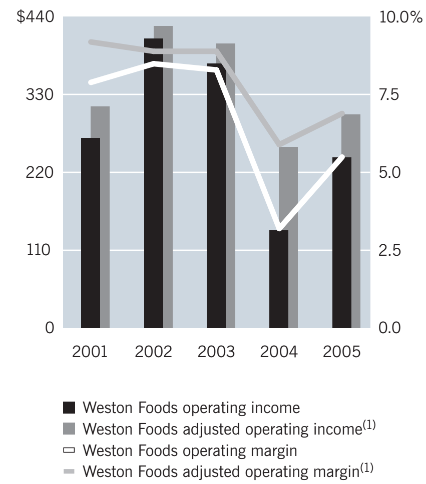
Operating Income Weston Foods operating income increased $103 million, or 74.6%, to $241 million from $138 million in 2004 and was impacted by lower restructuring and other charges and higher net stock-based compensation. Restructuring and other charges in 2005 were $32 million compared to $121 million in 2004 and net stock-based compensation cost was a charge of $29 million in 2005 compared to income of $3 million in 2004. Adjusting for the net impact of restructuring and other charges and stock-based compensation net of the associated equity derivatives, adjusted operating income(1) for 2005 was $302 million, an increase of 18.0% from $256 million in 2004. Adjusted operating margin(1) and adjusted EBITDA margin(1) for 2005 were 6.9% and 9.8%, respectively (2004 – 5.9% and 9.3%). A detailed discussion on the impact of restructuring and other charges is set forth under the "Restructuring and Other Charges" section below. In addition, foreign currency translation negatively impacted 2005 adjusted operating income(1) growth by approximately 5.2%.

Weston Foods 2005 adjusted operating income(1) improved from 2004 and was positively impacted by sales growth, including volume, price and sales mix improvements, and by the benefits being realized from the restructuring and cost reduction activities initiated in 2004 and 2005.

Sales growth during 2005, including volume and sales price improvements, positively impacted 2005 operating income and margin. This was partially offset by the negative impact of inflationary cost pressures related to certain key ingredients and packaging costs, as well as higher energy and employee health related benefit costs, which continue to challenge Weston Foods operating income and margin growth. In addition, during 2005, Weston Foods incurred approximately $4 million of training and other facility start-up related costs. These costs are associated with a biscuit facility being built in Virginia and the investment in a new fresh bakery facility in Florida. These start-up related costs were not included in restructuring and other charges in the consolidated statements of earnings. As anticipated, Weston Foods expects to incur further start-up related costs during 2006 as the ongoing plan to restructure its United States biscuit operations is completed.

Weston Foods Operating Income and Margin, Adjusted Operating Income(1) and Margin(1)

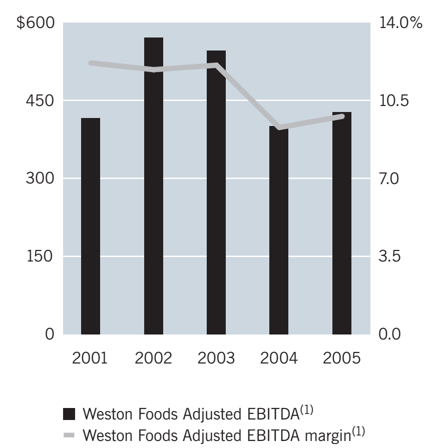
($ millions)



(1) See Non-GAAP Financial Measures beginning on page 44.

Weston Foods Adjusted EBITDA(1) and Margin(1)

($ millions)



(1) See Non-GAAP Financial Measures beginning on page 44.

Weston Foods profitability in the United States fresh-baked sweet goods category improved compared to 2004; however, challenges remain as a result of changing consumer eating and shopping preferences and a high fixed cost manufacturing and distribution structure.

White flour based fresh bakery products remain a significant category for Weston Foods. Volume declines experienced in branded white flour based sales in the United States negatively impacted operating income growth; however, these declines were offset by continued good growth in higher-priced branded whole grain and premium products as well as new private label customer business achieved during 2005. Although the new private label business impacts the sales mix negatively in the short term, it provides Weston Foods the opportunity to grow branded sales in certain customers in the longer term and the ability to efficiently leverage its current fixed overhead costs in manufacturing and distribution.

(1) See Non-GAAP Financial Measures beginning on page 44.

In 2004, the product mix shift toward whole grain products added more variety into the Weston Foods sales mix and created certain manufacturing and distribution complexities. Weston Foods continually works on optimizing its long term operating strategy of simplifying and removing complexity from its manufacturing processes. This includes focusing manufacturing capacity for longer production runs and where appropriate, outsourcing shorter-run products to contract manufacturers. The increased use of contract manufacturers and focused manufacturing facilities generally increases distribution complexity and costs. In 2005, initiatives were implemented to address these complexities in manufacturing and distribution and the work continues to progress. As the shift in sales mix continues, Weston Foods has made good progress on improving manufacturing efficiencies and has invested in new flexible bread capacity in order to produce different varieties of bread more efficiently. Examples of new investment include the new fresh bakery completed in Orlando, Florida as well as recently announced plans to commence construction of a new fresh bakery facility in the Midwest United States. These investments better position supply capacity in Weston Foods' highest potential growth markets.

Weston Foods continually evaluates its assets with the objective of ensuring an improving competitive fixed cost structure. Weston Foods continues to evaluate cost reduction and other strategic initiatives, particularly related to the fresh-baked sweet goods category in the United States and reducing administrative costs, to ensure a low cost operating structure and an improving competitive cost position. Certain of these initiatives are in progress or nearing completion while others are still in the planning stages. During 2005, major actions implemented included:

- the plan to restructure the United States biscuit operations, which will result in 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;
- plans to exit certain bread and roll manufacturing lines in the United States. All production associated with these lines was transferred to third-party producers or other Weston Foods manufacturing facilities and the exit was completed by the end of 2005; and
- plans to consolidate, relocate and restructure certain administrative offices within North America which are anticipated to be completed by the end of 2006.

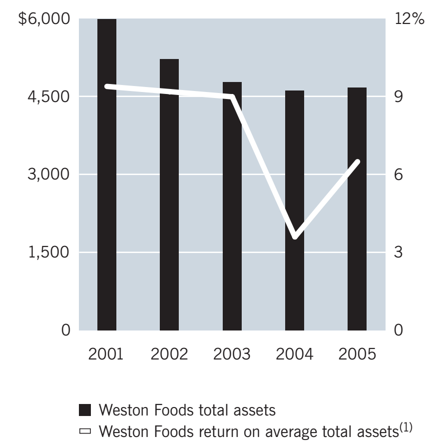
Restructuring and Other Charges

The following table summarizes the restructuring and other charges by plan for 2005 and 2004:

	Employee Termination Benefits and Site Closing and Other Exit Costs	Fixed Asset Impairment and Accelerated Depreciation	Gain on Sale of Fixed Assets	Intangible Asset Impairment	Total
Costs recognized in 2005:					
United States biscuit operations	**$ 28**	**$ 15**	**$ (18)**		**$ 25**
Exit of certain bread and roll lines in the United States	**1**	**4**			**5**
Consolidation and restructuring of administrative offices	**8**				**8**
Completion of prior year plans	**(8)**	**2**			**(6)**
	$ 29	**$ 21**	**$ (18)**		**$ 32**
Costs recognized in 2004:					
Fresh-baked sweet goods impairment		$ 48		$ 18	$ 66
Exit of waffle business in the United States	$ 1	25			26
Closure of production facilities and distribution centres	11	8			19
Completion of prior year plans	5	5			10
	$ 17	$ 86		$ 18	$ 121

During 2005, Weston Foods approved a plan to restructure its United States biscuit operations. This plan will result in the closure of two biscuit facilities located in Elizabeth, New Jersey and Richmond, Virginia by the end of 2006. Employment at both facilities is being phased down as the majority of the production is relocated to a new facility in Virginia and an existing Weston Foods facility already operating in South Dakota. Once completed, this initiative is anticipated to result in lower manufacturing costs and a strengthening of Weston Foods' competitive position within its biscuit operations in the United States. As a result of this restructuring, Weston Foods expects to recognize certain incremental exit and start-up costs of approximately $50 million over 2005 and 2006 including employee related severance, benefit and training costs, production equipment relocations and other facility start-up related costs. In addition, Weston Foods expects to recognize accelerated depreciation on assets currently held-for-use of approximately $25 million over 2005 and 2006. During 2005, Weston Foods recognized $28 million of restructuring charges, $15 million of accelerated depreciation, a gain of $18 million related to the sale and lease-back of the two facilities to be closed associated with this restructuring plan and start-up related costs recognized in operating income of approximately $3 million. Weston Foods received total proceeds of $47 million related to the sale of the two biscuit facilities.

Weston Foods Total Assets and Return on Average Total Assets[1]
($ millions)



(1) See Non-GAAP Financial Measures beginning on page 44.

Also during 2005, the following restructuring activities occurred:

- Weston Foods made further progress on its objective of simplifying and removing cost from its existing manufacturing processes and approved plans to exit certain bread and roll manufacturing lines in the United States. All production associated with these lines was transferred to third-party producers or other Weston Foods manufacturing facilities by the end of 2005. As a result of this decision, Weston Foods recognized $4 million of accelerated depreciation and $1 million of restructuring charges related to this restructuring plan;
- Weston Foods approved plans to consolidate, relocate and restructure certain of its administrative offices within North America, which resulted in an $8 million restructuring charge during 2005; and
- Weston Foods recognized restructuring income of $8 million, primarily related to the reversal of accruals no longer required and accelerated depreciation of $2 million related to restructuring plans approved prior to 2005.

During 2004, restructuring charges of $55 million were recognized relating to the following initiatives:

- completion of the Northlake, Illinois and Buffalo, New York bakery facility closures;
- exiting the fresh waffle business in the United States;
- closure of a frozen bakery production facility in St. Louis, Missouri; and
- closure of three production facilities and one distribution centre in Canada.

Also included in restructuring and other charges in 2004 was $66 million of impairment charges relating to the intangible assets and fixed assets employed in the fresh-baked sweet goods category, which relate primarily to products sold under the *Entenmann's* brand name. Further information on Weston Foods restructuring and other charges is provided in note 3 to the consolidated financial statements.

In 2005, Weston Foods also approved plans to start construction of a new bakery in the Midwestern United States. This new facility will produce fresh bakery products, including bread and English muffins, and is expected to be in commercial production by the end of 2006.

Weston Foods management continues to evaluate strategic and other cost reduction initiatives, particularly related to the fresh-baked sweet goods category in the United States and reducing administrative costs, to ensure a low cost operating structure and an improving competitive cost position. Initiatives currently being evaluated include manufacturing asset and distribution network optimization. Individual actions will be initiated and additional charges may be taken as plans are finalized and approved.

In 2006, Weston Foods expects to see improvements in sales and adjusted operating income[1], on a year-over-year basis, as a result of improvements in volume and pricing and as the benefits of restructuring and cost reduction activities continue to be realized. Operating margins are expected to continue to be pressured by underlying cost inflation, particularly with respect to certain materials, energy and people related benefit costs.

(1) See Non-GAAP Financial Measures beginning on page 44.

LOBLAW OPERATING RESULTS

($ millions except where otherwise indicated)	2005	2004	Change
Sales	**$ 27,801**	$ 26,209	6.1%
Sales excluding impact of VIEs(1)	**$ 27,423**	$ 26,209	4.6%
Operating income	**$ 1,393**	$ 1,644	(15.3)%
Operating margin	**5.0%**	6.3%	
Adjusted operating income(1)	**$ 1,592**	$ 1,645	(3.2)%
Adjusted operating margin(1)	**5.8%**	6.3%	
Adjusted EBITDA(1)	**$ 2,124**	$ 2,118	0.3%
Adjusted EBITDA margin(1)	**7.7%**	8.1%	
Return on average total assets(1)	**11.0%**	14.0%	

(1) See Non-GAAP Financial Measures beginning on page 44.

Sales and Sales Growth Excluding Impact of VIEs(1)

($ millions except where otherwise indicated)	2005	2004
Total sales	**$ 27,801**	$ 26,209
Less: Sales attributable to the consolidation of VIEs pursuant to AcG 15	**378**	
Sales excluding impact of VIEs(1)	**$ 27,423**	$ 26,209
Total sales growth	**6.1%**	
Less: Positive impact on sales growth attributable to the consolidation of VIEs pursuant to AcG 15	**1.5%**	
Sales growth excluding impact of VIEs(1)	**4.6%**	

(1) See Non-GAAP Financial Measures beginning on page 44.

Adjusted Operating Income(1)

($ millions)	2005	2004
Operating income	**$ 1,393**	$ 1,644
Add impact of the following:		
Restructuring and other charges	**86**	1
Direct costs associated with supply chain disruptions	**30**	
Goods and Services Tax and provincial sales taxes	**40**	
Net effect of stock-based compensation and the associated equity derivatives	**43**	
Adjusted operating income(1)	**$ 1,592**	$ 1,645

(1) See Non-GAAP Financial Measures beginning on page 44.

Adjusted EBITDA(1)

($ millions)	2005	2004
Adjusted operating income(1)	**$ 1,592**	$ 1,645
Add (deduct) impact of the following:		
Depreciation and amortization	**558**	473
VIE depreciation and amortization	**(26)**	
Adjusted EBITDA(1)	**$ 2,124**	$ 2,118

(1) See Non-GAAP Financial Measures beginning on page 44.

Loblaw results for 2005 were adversely affected by the short term costs associated with the significant transformational initiatives at Loblaw. The need for this transformative process was driven by Loblaw's assessment of a fast-changing retail environment marked by increased consumer choice, low-cost global retailers, and the addition of an increasingly unsustainable amount of industry square footage.

Based on this assessment, Loblaw developed a comprehensive strategy designed to fortify its competitive position and to maintain its leadership role in meeting the food and everyday household needs of Canadian consumers. In pursuit of this strategy, Loblaw implemented a number of transformative changes to its organization during 2005.

These changes included the restructuring of its supply chain network and the reorganizations involving its merchandising, procurement and operations groups, the establishment of a new national head office and Store Support Centre in Brampton, Ontario, which opened in the third quarter of 2005, and the relocation of general merchandise operations from Calgary, Alberta to the new office. A charge of $86 million was recorded in operating income in 2005 consisting of employee termination benefits resulting from planned involuntary terminations, site closing costs and fixed asset impairment and accelerated depreciation charges associated with these activities.

Loblaw encountered challenges during the execution of planned changes to its systems, supply chain and general merchandise areas including certain supply chain systems conversions which were initiated as part of the creation of a national information technology platform and the start-up of a new third-party owned and operated general merchandise warehouse and distribution centre for eastern Canada. These challenges disrupted the flow of inventory to Loblaw's stores and caused Loblaw to incur additional operating costs. Additional incremental direct costs incurred in the handling, storage and movement of inventory resulting from these disruptions amounted to approximately $30 million for the year, which was recognized in operating income.

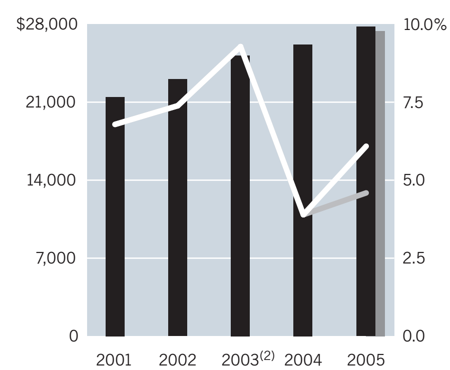
Also in 2005, a charge was recorded relating to an audit and proposed assessment by the CRA relative to GST on certain products sold during prior fiscal periods on which GST was not appropriately charged and remitted. In light of this proposed assessment, Loblaw assessed and estimated the potential liabilities for GST and PST in other areas of its operations. Accordingly, a charge of $40 million was recorded in operating income to reflect the best estimate of such potential tax liabilities of which management is currently aware.

Sales Full year sales in 2005 increased 6.1% to $27.8 billion from $26.2 billion in 2004, including a positive impact of 1.5% or $378 million in sales relating to the consolidation of certain independent franchisees as required by AcG 15. Excluding the impact of the VIEs, 2005 sales increased 4.6% or $1.2 billion over last year.

The following factors further explain the change in sales over the prior year:

- as described earlier, certain initiatives resulted in supply chain disruptions and a drop in service levels and in-stock positions causing an estimated reduction in expected sales growth of approximately 0.5% to 0.7% versus last year;
- retail sales growth in general merchandise and drugstore categories continued to exceed that of food in all regions except in western Canada; general merchandise and drugstore sales in western Canada were most profoundly impacted by the supply chain disruptions;
- *The Real Canadian Superstore* program was positively received in Ontario and has enjoyed significant sales growth;
- strong gas bar sales were partially offset by a decline in tobacco sales;
- same-store sales growth of approximately 0.2%;
- national food price inflation as measured by CPI was approximately 2% for the year, with variances by region; Loblaw's calculation of food price inflation, which considers Loblaw-specific product mix and pricing strategy, was reasonably consistent with that of CPI;
- an increase in net retail square footage of 2.8 million square feet or 6.1% due to the opening of 69 new corporate and franchise stores and the closure of 57 stores including stores which have undergone conversions and major expansions;
- sales per corporate store increased to $32 million in 2005 from $31 million in 2004 reflecting the introduction of larger stores which are expected to become ultimately more productive; and
- sales per average square foot of corporate stores of $579 in 2005 decreased from $592 in 2004 as a result of increases in net retail square footage which outpaced the increase in sales.

Loblaw Sales and Sales Growth
($ millions)



■ Loblaw sales
■ Loblaw sales excluding impact of VIEs(1)
▭ Loblaw sales growth
▬ Loblaw sales growth excluding impact of VIEs(1)

(1) See Non-GAAP Financial Measures beginning on page 44
(2) 2003 was a 53-week year.

Sales of control label products for 2005 amounted to $5.9 billion compared to $5.6 billion in 2004. Control label penetration, which is measured as control label retail sales as a percentage of total retail sales, was 22.4% for 2005, and approximately equal to that of 2004. Loblaw introduced approximately 2,000 new control label products in 2005, including 1,600 new general merchandise products. Loblaw's control label program, which includes *President's Choice, PC, President's Choice Organics, PC Blue Menu, PC Mini Chefs, no name, Club Pack, GREEN, EXACT, Teddy's Choice* and *Life@Home*, provides additional sales growth potential.

Loblaw expects that the following initiatives, coupled with continued investment in pricing, promotions and advertising where appropriate, will generate continued sales growth over the next few years:

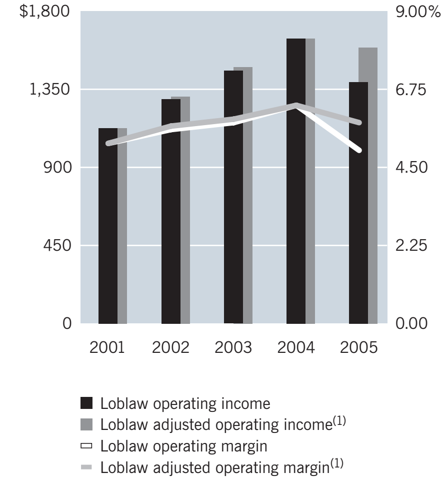
- capital investment in its store network including the planned opening, expansion or renovation of approximately 123 corporate and franchise stores across Canada in 2006;
- additional emphasis on food offerings of great quality and value;
- expansion of general merchandise offerings, including the launch of *Joe Fresh Style* apparel for adults in early 2006, and continued improvement in the execution of its general merchandise and drugstore programs; and
- continued focus on control label products including the development of new products in strategic categories, increased marketing and shortened time to market.

Operating Income Loblaw operating income for 2005 decreased $251 million, or 15.3%, to $1,393 million from $1,644 million in 2004. Operating margin declined to 5.0% in 2005 from 6.3% in 2004. Adjusted EBITDA[1] increased marginally in 2005. Adjusted EBITDA margin[1] was 7.7% in 2005 compared to 8.1% in 2004. In 2005, operating income was adversely impacted by the factors described below.

During the first quarter of 2005, after completion of a detailed assessment of its supply chain network, management of Loblaw approved a comprehensive plan to restructure its supply chain operations nationally. This plan, which is anticipated to be fully implemented by the end of 2007 or early 2008, is expected to reduce future operating costs, provide a smoother flow of products and better service levels to stores and further enable Loblaw to achieve its targeted operating efficiencies. The plan involves the closure of six distribution centres and the relocation of certain activities to new distribution centres. Costs accrued thus far relate primarily to employee termination benefits resulting from planned involuntary terminations. Further costs related to fixed asset impairment and accelerated depreciation and site closure costs as well as additional employee costs will be recognized as appropriate criteria are met. Total costs are expected to approximate $90 million, of which $62 million was recognized in 2005.

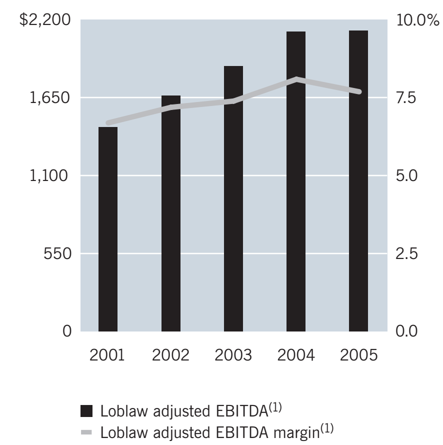
In addition to the restructuring of its supply chain network, Loblaw also reorganized its merchandising, procurement and operations groups, established a new national head office and Store Support Centre in Brampton, Ontario, which opened in the third quarter of 2005, and relocated its general merchandise operations from Calgary, Alberta to the new office. Of the total estimated $25 million cost associated with these initiatives, $24 million was recognized in 2005 resulting in total restructuring and other charges of $86 million in 2005.

Loblaw Operating Income and Margin, Adjusted Operating Income[1] and Margin[1]
($ millions)



(1) See Non-GAAP Financial Measures beginning on page 44.

Loblaw Adjusted EBITDA[1] and Margin[1]
($ millions)



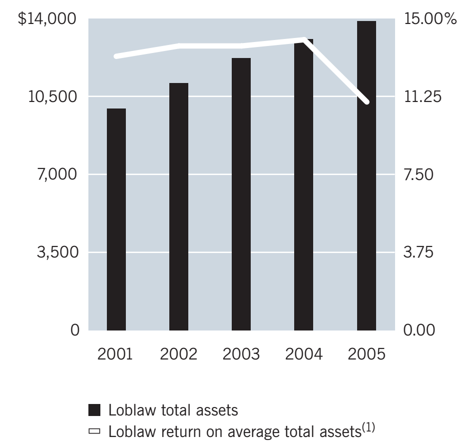
(1) See Non-GAAP Financial Measures beginning on page 44.

($ millions)	**Cost Recognized in 2005**	Total Expected Costs
Supply chain network	**$ 62**	$ 90
Office move and reorganization of the operation support functions	**24**	25
Total restructuring and other charges	**$ 86**	$ 115

See note 3 to the consolidated financial statements for further information.

(1) See Non-GAAP Financial Measures beginning on page 44.

Loblaw Total Assets and Return on Average Total Assets(1)
($ millions)



(1) See Non-GAAP Financial Measures beginning on page 44.

In 2005, operations were also disrupted by certain systems conversions and the start-up of a new third-party owned and operated general merchandise warehouse and distribution centre serving eastern Canada.

As part of the plan to consolidate Loblaw's supply chain operations nationally and to implement a national information technology platform, a number of warehouse systems conversions in western Canada commenced late in the second quarter of 2005 and were scheduled to be completed by year end 2005. Implementation challenges arising from these initiatives were encountered, particularly during the conversion of the Calgary, Alberta general merchandise distribution centre. Service levels, a measure of distribution centre operating efficiency, fell below normal running rates, resulting in recurring out-of-stock positions at retail. This resulted in lost sales and the associated operating income. Given the challenges encountered in the Calgary general merchandise distribution centre, all other planned system conversions for 2005 were delayed and resumed in early 2006.

In Ontario, the general merchandise warehouse and distribution activities were transitioned to a new facility owned and operated by a third party. Complexities were experienced during the start-up phase and as a result, service levels were below expectations in the second half of the year. This resulted in some out-of-stock positions in Ontario and a delay in the transition of volume into the third-party facility from existing Loblaw distribution centres, which in turn, placed additional pressure on existing Loblaw distribution centres. Productivity declined in certain Loblaw distribution centres during 2005 as a result of the announced restructuring.

Higher direct and indirect operating costs resulting from the supply chain disruptions were significant during the last two quarters of 2005. While it was possible to quantify the direct costs at approximately $30 million for the year, the indirect cost of lost sales, poor service levels and resultant higher operating costs was difficult to quantify.

During the third quarter of 2005, Loblaw also recorded a charge relating to an audit and proposed assessment by the CRA relating to GST on certain products sold between 2000 and 2002 on which GST was not appropriately charged and remitted. In light of this proposed assessment, Loblaw assessed and estimated the potential liabilities for GST and PST in other areas of its operations for various periods up to the end of 2004. Accordingly, a charge of $40 million was recorded in operating income to reflect management's best estimate of such potential tax liabilities of which management is currently aware. Approximately $15 million of this amount was settled during the fourth quarter of 2005. 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. An internal review of the procedures and controls surrounding the process of charging and remitting these taxes has been substantially completed and recommendations are in the process of being implemented to avoid the recurrence of similar charges subsequent to the periods currently accounted for.

An incremental charge of $43 million over last year was also recorded in operating income in 2005 for the net effect of stock-based compensation and the associated equity derivatives.

After adjusting for the above-noted items, adjusted operating income(1) in 2005 was $1,592 million compared to $1,645 million in 2004. Adjusted operating margin(1) was 5.8% in 2005 compared to 6.3% in 2004. Inventory shrink in the general merchandise categories was higher than normal throughout 2005 and showed some progress back to more normal levels in the fourth quarter. Improved buying synergies and product mix offset this increase in shrink, resulting in a gross margin in 2005 that was approximately equal to that of 2004. Softening sales from product supply issues and deliberate delays in program activity in 2005 resulted in lost leverage on the fixed components of operating and administrative expenses.

Loblaw expects to see improvement in adjusted operating income(1) on a year-over-year basis during the second half of 2006. The emphasis in the early part of 2006 will be on improving service levels, particularly in the general merchandise and drugstore areas, and ensuring that product is available at the store level to support merchandising programs. Loblaw expects some lowering of prices in certain formats to encourage more customer traffic and build sales.

(1) See Non-GAAP Financial Measures beginning on page 44.

LIQUIDITY AND CAPITAL RESOURCES

MAJOR CASH FLOW COMPONENTS

($ millions)	2005	2004	Change
Cash flows from operating activities of continuing operations	**$ 1,812**	$ 1,576	$ 236
Cash flows used in investing activities of continuing operations	**$ (1,092)**	$ (1,335)	$ 243
Cash flows used in financing activities of continuing operations	**$ (176)**	$ (87)	$ (89)

Cash Flows from Operating Activities of Continuing Operations Cash flows from operating activities of continuing operations increased in 2005 to $1.8 billion from $1.6 billion in 2004. The increase over 2004 was primarily attributable to the improvement in the change in non-cash working capital.

The Company's 2006 cash flows from operating activities of continuing operations are expected to increase at a rate consistent with net earnings growth and are expected to fund a large portion of the Company's anticipated 2006 funding requirements, including its planned capital investment activity of approximately $1.2 billion.

Cash Flows used in Investing Activities of Continuing Operations Cash flows used in investing activities of continuing operations in 2005 were $1.1 billion compared to $1.3 billion in 2004. The decrease of $243 million is primarily due to the shortening term to maturity profile of the Company's short term investment portfolio. The shortening term to maturity profile of the Company's short term investment portfolio resulted in a shift from short term investments to cash and cash equivalents and an increase in cash flows from short term investments of $202 million.

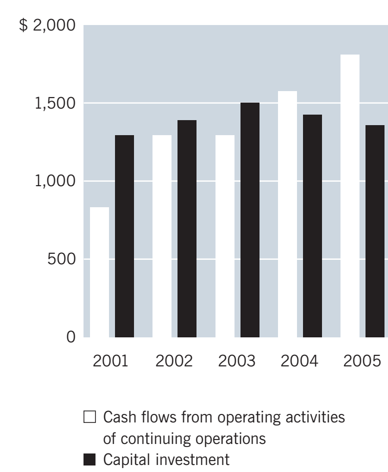
Capital investment amounted to $1.4 billion (2004 – $1.4 billion), reflecting the Company's continuing commitment to maintain and renew its asset base and invest for growth across North America. Weston Foods capital investment was $202 million (2004 – $167 million). The capital was directed toward the construction of three new plants, facility improvements and the upgrade 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 $1.2 billion (2004 – $1.3 billion). Approximately 82% (2004 – 83%) of Loblaw's capital investment was for new stores, renovations or expansions. The continued capital investment activity benefited all regions in 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. The remaining 18% (2004 – 17%) of the capital investment was for the warehouse and distribution network, information systems and other infrastructure required to support store growth. Loblaw's 2005 corporate and franchised store capital investment program, which includes the impact of store openings and closures, resulted in an increase in net retail square footage of 6.1% over 2004. During 2005, 69 (2004 – 86) new corporate and franchised stores were opened and 77 (2004 – 82) underwent renovation or minor expansion. The 69 new stores, net of 57 (2004 – 71) store closures, added 2.8 million square feet of retail space (2004 – 3.4 million). The 2005 average corporate store size increased 4.7% to 56,100 square feet (2004 – 53,600) and the average franchised store size increased 4.2% to 27,100 square feet (2004 – 26,000).

The Company also generated $170 million (2004 – $118 million) from fixed asset sales, including proceeds of $47 million from the sale of two Weston Foods biscuit facilities.

The Company expects to continue its capital investment pace in 2006. Capital investment in 2006 is estimated at $1.2 billion (approximately $200 million for Weston Foods and $1.0 billion for Loblaw). Weston Foods' 2006 capital investment will focus on the completion of two new bakery facilities in the United States and the streamlining of production and distribution assets to be more efficient. In 2005, Weston Foods approved plans to start construction of a new bakery in the Midwestern United States. This new facility will produce fresh bakery products, including bread and English muffins, and is expected to be in commercial production by the end of 2006. In addition, as part of the plan to restructure the United States biscuit operations, a new biscuit facility in Virginia will be completed during 2006. Loblaw plans to open, expand or renovate more than 123 corporate and franchised stores throughout Canada in a geographic investment pattern similar to that of 2005 which is expected to result in a net increase of approximately 1.8 million square feet and should generate additional sales growth.

Cash Flows from Operating Activities and Capital Investment
($ millions)



Cash Flows used in Financing Activities of Continuing Operations Cash flows used in financing activities of continuing operations were $176 million in 2005 compared to $87 million in 2004.

During 2005, Weston and Loblaw completed the following financing activities:

- Loblaw issued $300 million of Medium Term Notes ("MTN");
- Weston issued $36 million of Series B Debentures;
- Loblaw repaid $200 million of MTN;
- commercial paper decreased $342 million;
- Weston issued 8.0 million preferred shares, Series III for total proceeds of $194 million;
- Weston issued 8.0 million preferred shares, Series IV for total proceeds of $195 million; and
- Loblaw purchased for cancellation 226,100 of its common shares for $16 million, pursuant to its NCIB.

During 2004, Weston and Loblaw completed the following financing activities:

- issued a total of $400 million of MTN;
- Weston issued $35 million of Series B Debentures;
- Weston repaid $200 million of Series A Debentures;
- Loblaw repaid $100 million of Series 1997 Provigo Inc. Debenture;
- commercial paper increased $144 million;
- Weston purchased for cancellation 587,200 of its common shares for $59 million, pursuant to its NCIB; and
- Loblaw purchased for cancellation 576,100 of its common shares for $35 million, pursuant to its NCIB.

See notes 6, 16 and 18 to the consolidated financial statements for the terms and details of the debt and share capital transactions.

Weston intends to renew its NCIB to purchase on the Toronto Stock Exchange or enter into equity derivatives to purchase up to 5% of its common shares outstanding.

During 2005, Weston's 2003 Base Shelf Prospectus expired and a new base shelf prospectus under which it may issue preferred shares and MTN in an aggregate amount not to exceed $1 billion was filed. During 2005, Loblaw's 2003 Base Shelf Prospectus expired and a new base shelf prospectus allowing the issue of up to $1 billion of aggregate MTN was filed.

The following tables present the amounts of preferred shares and MTN available to issue under the Weston and Loblaw programs:

Weston Preferred Shares and Medium Term Notes Program

($ millions)	**Base Shelf Prospectus dated April 11, 2005**	Base Shelf Prospectus dated May 16, 2003
Preferred shares and MTN issue limit	**$ 1,000**	$ 750
MTN issued in 2004		200
Preferred shares, Series III issued in 2005	**200**	
Preferred shares, Series IV issued in 2005	**200**	
MTN issue expired		$ 550
MTN capacity available, year end 2005	**$ 600**	

Loblaw Medium Term Notes Program

($ millions)	**Base Shelf Prospectus dated June 20, 2005**	Base Shelf Prospectus dated May 12, 2003
MTN issue limit	**$ 1,000**	$ 1,000
MTN issued in 2003(1)		455
MTN issued in 2004		200
MTN issued in 2005		300
MTN issue expired		$ 45
MTN capacity available, year end 2005	**$ 1,000**	

(1) In 2003, an additional $200 of MTN was issued pursuant to a Base Shelf Prospectus dated May 24, 2001

SOURCES OF LIQUIDITY

The Company can obtain its short term financing through a combination of cash generated from operating activities, cash, cash equivalents, short term investments, bank indebtedness and commercial paper programs. Weston's cash, cash equivalents and short term investments, as well as $268 million in uncommitted credit facilities and $300 million in committed credit facilities extended by several banks, support Weston's $500 million commercial paper program. Loblaw's cash, cash equivalents and short term investments, as well as $845 million in uncommitted operating lines of credit extended by several banks, support its $1.2 billion commercial paper program. Weston's and Loblaw's commercial paper borrowings generally mature less than 90 days from the date of issuance, although the term can be up to 364 days.

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 an independent trust. PC Bank securitized $225 million of credit card receivables during 2005 (2004 – $227 million). In 2006, PC Bank finalized the restructuring of its securitization program, which was undertaken in part to accommodate growth in the credit card program. Information on PC Bank's credit card receivables and securitization is provided in notes 11 and 22 to the consolidated financial statements and in the Off-Balance Sheet Arrangements section of this MD&A.

The Company obtains its long term financing primarily through MTN and preferred share programs. The Company plans to refinance the Weston $200 million of 5.25% MTN and the Loblaw $125 million 8.70% Series 1996 Provigo Inc. Debenture as they mature.

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 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 $547 million (2004 – $463 million), against which the Company had $632 million (2004 – $628 million) in credit facilities available to draw on.

The Company has the following sources from which it can fund its 2006 cash requirements: cash flows generated from operating activities, cash, cash equivalents, short term investments, bank indebtedness, commercial paper programs, preferred shares and MTN programs, and additional credit card receivable securitizations from future growth in the PC Bank credit card operations.

In 2006, the Company anticipates no difficulty in obtaining external financing in view of its current credit ratings, its past experience in the capital markets and general market conditions. The Company's credit ratings are outlined in the table below:

Credit Ratings (Canadian Standards)	Dominion Bond Rating Service ("DBRS")	Standard & Poor's ("S&P")
Commercial paper	R-1 (low)	A-1 (low)
Medium term notes	A (low)	A–
Exchangeable debentures	BBB (high)	
Preferred shares	Pfd-2 (low)	P-2
Other notes and debentures	A (low)	A–

The rating organizations listed above base their credit ratings on quantitative and qualitative considerations. In January 2006, S&P changed their outlook on the trend of the Company's long term debt and preferred shares from "stable" to "negative". In addition, DBRS and S&P changed their outlook on the trend of Loblaw's long term debt from "stable" to "negative". These credit ratings are intended to give an indication of the risk that Weston will not fulfill its obligations in a timely manner.

CONTRACTUAL OBLIGATIONS

The following illustrates certain of the Company's significant contractual obligations and discusses other obligations as at December 31, 2005:

Summary of Contractual Obligations

	Payments due by year						
($ millions)	2006	2007	2008	2009	2010	Thereafter	Total
Long term debt (including capital lease obligations)	$ 361	$ 24	$ 407	$ 390	$ 314	$ 4,916	$ 6,412
Operating leases(1)	234	215	189	163	140	860	1,801
Contracts for purchase of real property and capital investment projects(2)	299		9				308
Purchase obligations(3)	874	820	761	720	659	1,320	5,154
Total contractual obligations	$ 1,768	$ 1,059	$ 1,366	$ 1,273	$ 1,113	$ 7,096	$ 13,675

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

(2) These obligations include agreements for the purchase of real property. 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.

(3) These include material contractual obligations 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. While estimates of anticipated financial commitments were made for the purpose of this disclosure, the amount of actual payments may vary.

The purchase obligations presented in the above table do not include purchase orders issued in the ordinary course of business for goods which are meant for resale, nor do they include any contracts which may be terminated on relatively short notice 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. The Company believes such excluded contracts do not have a material impact on its liquidity.

At year end, the Company had other long term liabilities which included accrued benefit plan liability, future income tax liability, stock-based compensation liability, accrued insurance liability and an equity derivative liability. 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 the share appreciation value on employee stock options depend on whether employees exercise their stock options, the market prices of Weston and Loblaw common shares on the exercise date and the manner in which they exercise those stock options;
- future payments of restricted share units depend on the market prices of Weston's and Loblaw's common shares;
- future payments of insurance claims can extend over several years and depend on the timing of anticipated settlements and results of litigation; and
- future payments relating to the settlement of the equity forward obligation based on 9.6 million Loblaw common shares which matures in 2031 (see note 20 to the consolidated financial statements) will depend on the market price of Loblaw common shares at the time of maturity; further, the market value of the 9.6 million Loblaw common shares that Weston has used to secure this obligation exceeds the amount owing under the forward contract, and a portion of the proceeds from a future sale of these shares may be used to satisfy the obligation under this forward contract upon termination or maturity.

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 is approximately $143 million (2004 – $104 million);
- the securitization of a portion of PC Bank's credit card receivables through independent trusts;
- a standby letter of credit to an independent funding trust which provides loans to Loblaw's franchisees for their purchase of inventory and fixed assets;
- guarantees; and
- financial derivative instruments in the form of interest rate swaps.

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 and in relation to third-party financing made available to the Company's 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 22 to the consolidated financial statements.

Securitization of Credit Card Receivables Loblaw, through its wholly owned subsidiary PC Bank, securitizes credit card receivables through an independent trust administered by a major Canadian bank. In these securitizations, PC Bank sells a portion of its credit card receivables to the trust in exchange for cash. The trust funds these purchases by issuing debt securities in the form of asset-backed commercial paper 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 trust 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 trust, the financial results of the trust have not been included in the Company's consolidated financial statements.

When Loblaw sells credit card receivables to the trust, it no longer has access to the receivables but continues to maintain credit card customer account relationships and servicing obligations. Loblaw does not receive a servicing fee from the trust for its servicing obligations. When a sale occurs, PC Bank retains a subordinated interest consisting of rights to future cash flows after obligations to the investors in the trust have been met, which is considered to be a retained interest. The 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 bank for 9% (2004 – 15%) 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 carrying value of the retained interests is periodically reviewed and when a decline in value is identified that is other than temporary, the carrying value is written down to fair value.

As at year end 2005, the total amount of securitized credit card receivables outstanding which PC Bank continues to service was $1 billion (2004 – $785 million) and the associated retained interests amounted to $5 million (2004 – $12 million). The standby letter of credit supporting these securitized receivables amounted to approximately $91 million (2004 – $118 million). During 2005, PC Bank received income of $106 million (2004 – $83 million) in securitization revenue from the independent trust 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 11 and 22 to the consolidated financial statements.

In October 2005, Eagle Credit Card Trust ("Eagle"), an independent trust, was established for the purpose of issuing notes backed by credit card receivables originated and serviced by PC Bank. Subsequent to year end, Eagle issued $500 million, five year notes at a weighted average rate of 4.5%, due 2011, to finance the purchase of credit card receivables, previously securitized by PC Bank, from an independent trust. PC Bank will continue to service the credit card receivables on behalf of Eagle, but will not receive any fee for its servicing obligations and has a retained interest in the securitized receivables represented by the right to future cash flows after obligations to investors have been met. In accordance with Canadian GAAP, the financial statements of Eagle will not be consolidated with those of the Company.

Independent Funding Trust Franchisees of Loblaw may obtain financing through a structure involving independent trusts, that was created to provide loans to the franchisees to facilitate their purchase of inventory and fixed assets, consisting mainly of fixturing and equipment. These trusts are administered by a major Canadian bank. The independent funding trust within the structure finances its activities through the issuance of short term asset-backed notes to third-party investors. The total amount of loans issued to Loblaw's franchisees outstanding as at year end 2005 was $420 million (2004 – $394 million) including $126 million of loans payable of VIEs consolidated by the Company in 2005. 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 for approximately 10% of the principal amount of the loans outstanding at any point in time, or $42 million (2004 – $42 million) as of year end 2005. This credit enhancement allows the independent funding trust to provide favourable financing terms to Loblaw's franchisees. In the event that a 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 may 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. No amount has ever been drawn on the standby letter of credit. Loblaw is confident it would be able to fully recover from the franchisee any amounts it had reimbursed to the issuing bank. Neither the independent funding trust nor Loblaw can voluntarily terminate the agreement prior to December 2009, and only upon six months' prior notice following that date. Automatic termination of the agreement can only occur if specific, pre-determined events occur and are not remedied within the time periods required. If the arrangement is terminated, the franchisees would be required to replace the loans provided by the independent funding trust with alternative financing. The Company is under no contractual obligation to provide funding to franchisees under such circumstances. In accordance with Canadian GAAP, the financial statements of the independent funding trust are not consolidated with those of the Company.

Derivative Instruments The Company uses off-balance sheet financial derivative instruments to manage its exposure to changes in interest rates. For a detailed description of the Company's off-balance sheet derivative instruments and the related accounting policies, see notes 1 and 20 to the consolidated financial statements.

During 2005, Weston terminated its interest rate swaps with a notional value of $200 million which were designated as a fair value hedge of the $200 million of 5.05% MTN due 2014. The gain realized on the termination of these swaps of $5 million, will be deferred over the remaining term of the initial hedge and recognized in interest expense and other financing charges.

QUARTERLY RESULTS OF OPERATIONS

The 52-week reporting cycle followed by the Company is divided into equal 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.

QUARTERLY FINANCIAL INFORMATION[1] (UNAUDITED)

($ millions except where otherwise indicated)		First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total (audited)
Sales	**2005**	**$ 6,972**	**$ 7,273**	**$ 9,737**	**$ 7,381**	**$ 31,363**
	2004	$ 6,551	$ 6,915	$ 9,260	$ 7,072	$ 29,798
Net earnings from continuing operations	**2005**	**$ 101**	**$ 179**	**$ 196**	**$ 240**	**$ 716**
	2004	$ 125	$ 142	$ 185	$ 154	$ 606
Net earnings (loss)	**2005**	**$ 100**	**$ 153**	**$ 196**	**$ 249**	**$ 698**
	2004	$ 121	$ 140	$ 168	$ (1)	$ 428
Net earnings per common share from continuing operations ($)						
Basic	**2005**	**$ .73**	**$ 1.33**	**$ 1.41**	**$ 1.78**	**$ 5.25**
	2004	$ .91	$ 1.06	$ 1.37	$ 1.15	$ 4.49
Diluted	**2005**	**$ .73**	**$ 1.33**	**$ 1.41**	**$ 1.78**	**$ 5.25**
	2004	$ .91	$ 1.06	$ 1.37	$ 1.14	$ 4.48
Net earnings (loss) per common share ($)						
Basic	**2005**	**$ .72**	**$ 1.13**	**$ 1.41**	**$ 1.85**	**$ 5.11**
	2004	$ .88	$ 1.04	$ 1.24	$ (.05)	$ 3.11
Diluted	**2005**	**$ .72**	**$ 1.13**	**$ 1.41**	**$ 1.85**	**$ 5.11**
	2004	$ .88	$ 1.04	$ 1.24	$ (.06)	$ 3.10

(1) During 2005, the Company implemented AcG 15 retroactively without restatement as described in the "Accounting Standards Implemented in 2005" section below. The implementation of EIC 144 in the third quarter of 2004 on a retroactive basis with restatement did not result in a material change in the quarterly net earnings.

Results by Quarter 2005 quarterly sales growth was impacted by various factors including Loblaw sales growth as well as sales from the consolidation of certain Loblaw independent franchisees and the impact of Weston Foods foreign currency translation. Adjusting for the quarterly impacts of foreign currency translation, Weston Foods 2005 quarterly sales were impacted positively by volume increases as a result of the introduction of new products and a sales mix shift to higher-priced premium products throughout the year as well as sales price increases. During 2005, incremental sales as a result of the acquisition of Gadoua in the third quarter of 2004 positively impacted Weston Foods sales growth. Loblaw 2005 sales included sales of VIEs consolidated by Loblaw and accounted for quarterly sales growth of between 1.2% and 1.7% when compared to their respective quarters in 2004. Loblaw sales growth during the last two quarters of 2005 continued to be negatively impacted by supply chain disruptions which started earlier in the year. Net retail square footage increased by 2.8 million square feet in 2005 and was somewhat weighted over the last two quarters. Same-store sales growth declined during the year from 2.4% in the first quarter to a decline of approximately 0.7% in the fourth quarter. Overall national food price inflation, as measured by CPI, during 2005 was approximately 2%, trending downwards in the last quarter of the year. Holidays such as Easter, Thanksgiving and Christmas impact the Company's sales volumes and have fallen within the same quarters year over year except for Easter, which was in the first quarter in 2005 compared to the second quarter in 2004. In addition, Weston Foods is impacted by the timing of seasonal sales items such as pies, buns, rolls, Girl Scout cookies and ice cream cones and wafers. The sales timing of these seasonal items generally occurs in the same quarters year over year.

2005 quarterly operating income was positively impacted by higher operating margins at Weston Foods due to sales growth, including volume, price and sales mix improvements, and by the benefits realized from the restructuring and other cost reduction activities initiated in 2004 and 2005. In addition, Weston Foods quarterly operating income was impacted by restructuring and other charges incurred in 2005 and 2004. Loblaw's quarterly operating income reflected the impact of restructuring and other charges resulting from the ongoing transformative changes. In addition, quarter-to-quarter variability in consolidated operating income was also caused by the following:

- fluctuations in stock-based compensation net of the impact of the associated equity derivatives as a result of changes in the market price of Weston's and Loblaw's common shares;
- $30 million of direct costs in 2005 related to the handling, storage and movement of inventory from Loblaw's supply chain disruptions, of which $20 million was recorded in the third quarter and an additional $10 million was incurred in the fourth quarter;
- $40 million in GST and PST related charges recorded by Loblaw in the third quarter of 2005; and
- higher than normal inventory shrink in Loblaw's general merchandise categories throughout 2005 with some progress back to more normal levels in the fourth quarter.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Interest expense and other financing charges incurred on a quarterly basis in 2005 as compared to the prior year were generally impacted by decreases in average borrowing levels outstanding and higher short term interest income, offset by the lower positive impact of interest on financial derivative instruments as a result of the maturity of interest rate swaps during the year and an increase in United States and Canadian short term interest rates. In addition interest expense and other financing charges included non-cash income or a non-cash charge relating to the accounting for Weston's 2001 forward sale agreement for 9.6 million Loblaw common shares which fluctuates as the market price of Loblaw common shares changes.

The change in the quarterly effective income tax rate for 2005 over 2004 was primarily due to the change in the proportion of taxable income earned in each tax jurisdiction in which the Company operated, including the jurisdiction in which the income tax impact of stock-based compensation and the associated equity derivatives occurred. In addition, the income tax expense for the first quarter of 2004 included a reversal of $14 million due to Loblaw's successful resolution of certain income tax matters from a previous year.

Net earnings were impacted by the items described above as well as the negative impact of discontinued operations, which was lower this year as compared to last year.

FOURTH QUARTER RESULTS

The following is a summary of selected information for the fourth quarter of 2005 extracted from the Company's preliminary unaudited consolidated financial statements. This information was prepared in accordance with Canadian GAAP and is reported in Canadian dollars.

($ millions except where otherwise indicated)	**2005**	2004
Sales	**$ 7,381**	$ 7,072
Sales excluding impact of VIEs[1]	**$ 7,294**	$ 7,072
Adjusted EBITDA[1]	**$ 669**	$ 733
Operating income	**$ 440**	$ 524
Adjusted operating income[1]	**$ 509**	$ 584
Interest expense and other financing charges	**$ (47)**	$ 164
Net earnings from continuing operations	**$ 240**	$ 154
Net earnings (loss)	**$ 249**	$ (1)
Basic net earnings per common share from continuing operations ($)	**$ 1.78**	$ 1.15
Adjusted basic net earnings per common share from continuing operations[1] ($)	**$ 1.55**	$ 1.81

(1) See Non-GAAP Financial Measures beginning on page 44.

Sales and Sales Growth Excluding Impact of VIEs[1]

($ millions except where otherwise indicated)	**2005**	2004
Total sales	**$ 7,381**	$ 7,072
Less: Sales attributable to the consolidation of VIEs pursuant to AcG 15	**87**	
Sales excluding impact of VIEs[1]	**$ 7,294**	$ 7,072
Total sales growth	**4.4%**	
Less: Positive impact on sales growth attributable to the consolidation of VIEs pursuant to AcG 15	**1.3%**	
Sales growth excluding impact of VIEs[1]	**3.1%**	

(1) See Non-GAAP Financial Measures beginning on page 44.

Sales Sales for the fourth quarter of 2005 increased 4.4% to $7.4 billion, with a positive impact of approximately 1.3% from the consolidation of certain Loblaw independent franchisees as required by AcG15.

Operating Income Operating income of $440 million for the fourth quarter of 2005 declined 16.0% compared to $524 million in 2004. Fourth quarter operating income included a $7 million (2004 – $77 million) charge for restructuring and other charges, a $10 million charge related to Loblaw's estimated impact of direct costs associated with supply chain disruptions, a $48 million (2004 – income of $17 million) charge related to net stock-based compensation net of the impact of the associated equity derivatives and a negative $4 million VIE impact. Adjusting for the net negative impact of these items, consolidated adjusted operating income(1) for the fourth quarter of 2005 was $509 million compared to $584 million in 2004, a decline of 12.8%. Consolidated adjusted operating margin(1) for the fourth quarter of 2005 was 7.0% compared to 8.3% in 2004 and was adversely affected by the short term costs associated with the significant transformational initiatives at Loblaw.

Interest Expense and Other Financing Charges Interest expense and other financing charges for the fourth quarter of 2005 decreased $211 million resulting in interest income of $47 million from a charge of $164 million in 2004, primarily as a result of non-cash income of $122 million (2004 – non-cash charge of $83 million), reflecting the accounting for Weston's 2001 forward sale agreement for 9.6 million Loblaw common shares.

Income Taxes The effective income tax rate increased to 34.9% from 21.4% in the fourth quarter of 2004, primarily due to the change in the proportion of taxable income earned across the different tax jurisdictions in which the Company operated, including the jurisdictions in which the income tax impact of stock-based compensation and the associated equity derivatives occurred.

Net Earnings from Continuing Operations Net earnings from continuing operations for the fourth quarter of 2005 increased $86 million, or 55.8%, to $240 million from $154 million in 2004. Basic net earnings per common share from continuing operations for the fourth quarter of 2005 increased $0.63, or 54.8% to $1.78 from $1.15 in 2004. Basic net earnings per common share from continuing operations included the net positive impact of $0.23 per common share for the fourth quarter as a result of the following factors:

- a $0.02 per common share charge related to restructuring and other charges for restructuring plans undertaken by both Weston Foods and Loblaw;
- a $0.03 per common share charge related to Loblaw's estimated impact of direct costs associated with supply chain disruptions;
- a $0.31 per common share charge for the net effect of stock-based compensation and the associated equity derivatives;
- $0.63 per common share non-cash income related to the accounting for Weston's 2001 forward sale agreement for 9.6 million Loblaw common shares which is offset on an economic basis;
- a $0.02 per common share charge related to the adjustment to future income tax balances due to the changes in statutory income tax rates in certain Canadian provinces; and
- a $0.02 per common share charge related to the consolidation of VIEs by Loblaw.

After adjusting for the above noted items, Weston's 2005 adjusted basic net earnings per common share from continuing operations(1) was $1.55 for the fourth quarter. These results compare to 2004 adjusted basic net earnings per common share from continuing operations(1) of $1.81, which were adjusted for the net negative impact of restructuring and other charges, stock-based compensation and the associated equity derivatives and the accounting for Weston's 2001 forward sale agreement for 9.6 million Loblaw common shares. Adjusted basic net earnings per common share from continuing operations(1) for the fourth quarter of 2005 decreased 14.4% compared to 2004, adversely affected by the short term financial costs associated with the significant transformational initiatives at Loblaw.

Discontinued Operations The gain from discontinued operations for the fourth quarter of 2005 was $9 million compared to a loss from discontinued operations of $155 million in 2004.

Subsequent to quarter end, the Company reached an agreement to settle claims against it relating to certain alleged misrepresentations and warranties arising from the sale of the Company's forest products business in 1998. The Company did not admit any wrongdoing or liability in connection with the settlement. The net impact of this settlement agreement has been reflected in the 2005 fourth quarter loss from discontinued operations.

Net Earnings Net earnings for the fourth quarter of 2005 increased $250 million to $249 million from a net loss of $1 million in 2004. Basic net earnings per common share for the fourth quarter of 2005 increased $1.90 to $1.85 from a basic net loss per common share of $0.05 in 2004 as a result of the factors discussed above.

(1) See Non-GAAP Financial Measures beginning on page 44.

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

($ millions except where otherwise indicated)	**2005**	2004
Sales	**$ 980**	$ 916
Adjusted EBITDA[1]	**$ 98**	$ 96
Operating income	**$ 48**	$ (4)
Adjusted operating income[1]	**$ 70**	$ 64

(1) See Non-GAAP Financial Measures beginning on page 44.

Sales for the fourth quarter of 2005 increased 7.7% but were offset by the negative impact of foreign currency translation, which reduced Weston Foods sales growth by approximately 0.7% and resulted in reported sales of $1.0 billion, an increase of 7.0% compared to 2004. Sales growth for the fourth quarter of 2005 was also impacted by the following:

- overall volume growth of approximately 2.8%;
- price increases in key product categories combined with changes in sales mix contributed positively to sales growth by approximately 4.9%;
- fresh bakery sales continued to experience strong growth and contributed positively to overall sales growth, driven by both volume growth and price increases. Volume growth was experienced in branded products including solid growth in *Thomas'*, *Arnold* and *Dutch Country* in the United States and *Wonder* and *Country Harvest* in Canada. The introduction of new and expanded products, continued growth in whole grain products and new private label business also contributed to fresh bakery sales growth;
- sales in the fresh-baked sweet goods category, primarily sold under the *Entenmann's* brand, increased as compared to 2004 while this category continued to experience a challenging sales environment. Growth in single serve and hand held products, including the introduction of *Enten-minis* products during the second half of 2005, was offset by a decline in sales of full size cake products;
- frozen bakery sales contributed positively to overall sales growth as a result of improvements in sales mix and price increases;
- dairy sales contributed positively to overall sales growth as a result of volume growth, sales price increases and the improvement in sales mix as growth continued in value-added products; and
- the biscuit category negatively impacted overall sales growth primarily due to lower sales volumes.

Operating income for the fourth quarter of 2005 was $48 million compared to an operating loss of $4 million in 2004. Fourth quarter operating income included a $1 million (2004 – $77 million) charge for restructuring and other charges and a $21 million (2004 – income of $9 million) charge related to net stock-based compensation net of the impact of the associated equity derivatives. Adjusting for the net negative impact of restructuring and other charges and stock-based compensation net of the associated equity derivatives, adjusted operating income[1] for the fourth quarter of 2005 was $70 million, an increase of 9.4% compared to $64 million in 2004. Adjusted operating margin[1] and adjusted EBITDA margin[1] for the fourth quarter of 2005 were 7.1% and 10.0%, respectively (2004 – 7.0% and 10.5%). Adjusted operating income[1] for the fourth quarter of 2005 was impacted by the following:

- operating income and margin was positively impacted by sales growth, including volume, price and sales mix improvements, and by the benefits realized from the restructuring and cost reduction activities initiated in 2004 and 2005;
- inflationary cost pressures, related to certain key ingredients and packaging costs, as well as higher energy and employee health related benefit costs, continue to challenge Weston Foods operating income and margin growth; and
- during the fourth quarter of 2005, Weston Foods incurred approximately $4 million of training and other facility start-up related costs primarily associated with the new biscuit facility in Virginia, resulting from the ongoing plan to restructure the United States biscuit operations, and the investment in a new fresh bakery facility in Florida. These start-up related costs were not included in restructuring and other charges in the consolidated statements of earnings. As anticipated, Weston Foods expects to incur further start-up related costs during 2006 as the ongoing plan to restructure its United States biscuit operations is completed.

As previously discussed, Weston Foods approved several restructuring plans in 2005. During the fourth quarter of 2005, Weston Foods recognized $1 million of restructuring and other charges in connection with these restructuring plans.

(1) See Non-GAAP Financial Measures beginning on page 44.

LOBLAW

($ millions except where otherwise indicated)	2005	2004
Sales	**$ 6,588**	$ 6,329
Sales excluding impact of VIEs[1]	**$ 6,501**	$ 6,329
Adjusted EBITDA[1]	**$ 571**	$ 637
Operating income	**$ 392**	$ 528
Adjusted operating income[1]	**$ 439**	$ 520

(1) See Non-GAAP Financial Measures beginning on page 44.

Sales and Sales Growth Excluding Impact of VIEs[1]

($ millions except where otherwise indicated)	2005	2004
Total sales	**$ 6,588**	$ 6,329
Less: Sales attributable to the consolidation of VIEs pursuant to AcG 15	**87**	
Sales excluding impact of VIEs[1]	**$ 6,501**	$ 6,329
Total sales growth	**4.1%**	
Less: Positive impact on sales growth attributable to the consolidation of VIEs pursuant to AcG 15	**1.4%**	
Sales growth excluding impact of VIEs[1]	**2.7%**	

(1) See Non-GAAP Financial Measures beginning on page 44.

Loblaw sales for the fourth quarter of 2005 increased 4.1% or $259 million to $6.6 billion from the $6.3 billion reported in the fourth quarter of 2004, including an increase of 1.4% or $87 million related to the consolidation of certain independent franchisees. Sales in the fourth quarter continued to be negatively impacted by the supply chain disruptions which started earlier in 2005. Some improved stability has been realized in the latter part of the quarter but significant improvements are not expected to be felt until mid-2006. *The Real Canadian Superstore* program has been positively received in Ontario and has enjoyed growth in both absolute and same-store sales.

Fourth quarter same-store sales in 2005 declined approximately 0.7% when compared to the same period last year. Expected sales growth was also negatively impacted by approximately 0.9% to 1.2% for the quarter due to supply chain disruptions and a drop in service levels. During the quarter, 17 new corporate and franchised stores were opened and 9 stores were closed, resulting in a net increase of 0.8 million square feet of retail square footage. Loblaw's calculation of food price inflation was reasonably consistent with the national food price inflation as measured by CPI, which was approximately 1% for the quarter.

Operating income for the fourth quarter of 2005 decreased $136 million or 25.8% from the fourth quarter of 2004, to $392 million. Operating margin declined to 6.0% from 8.3% in the comparable period of 2004. Fourth quarter operating income in 2005 included a $6 million charge for restructuring and other charges and incremental direct costs of approximately $10 million related to the supply chain disruptions. A charge of $27 million related to stock-based compensation net of the impact of the associated equity forwards was also recorded in the fourth quarter and compared to $8 million income in 2004. These items, in addition to the negative $4 million VIE impact, accounted for a decline in operating margin of approximately 0.8 of a percentage point for the quarter.

Liquidity and Capital Resources

Cash flows from operating activities of continuing operations Fourth quarter cash flows from operating activities of continuing operations were $902 million in 2005 compared to $1,017 million in the comparable period of 2004.

Cash flows used in investing activities of continuing operations Fourth quarter 2005 cash flows used in investing activities of continuing operations were $494 million in 2005 compared to $410 million in 2004. Capital investment for the fourth quarter amounted to $390 million (2004 – $373 million). New Loblaw retail stores account for the significant portion of this investment.

Cash flows used in financing activities of continuing operations Fourth quarter 2005 cash flows used in financing activities of continuing operations were $395 million in 2005 compared to $480 million in 2004, decreasing mainly due to the repayment of Loblaw's $100 million 6.35% Series 1997 Provigo Inc. Debenture as it matured during the fourth quarter of 2004.

Further discussion and analysis of the fourth quarter results was provided in the Company's 2005 Fourth Quarter News Release which is available online at www.sedar.com.

MANAGEMENT'S DISCUSSION AND ANALYSIS

DISCLOSURE CONTROLS AND PROCEDURES

Based on an evaluation of the Company's disclosure controls and procedures, the Company's President and Chief Financial Officer have concluded that these controls and procedures were effective as of December 31, 2005.

OPERATING RISKS AND RISK MANAGEMENT

In the normal course of its business, the Company's reportable operating segments are exposed to operating risks that have the potential to negatively affect its financial performance. Each operating segment has insurance programs and its own operating and risk management strategies to help minimize these operating risks.

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

Both operating segments evaluate the markets they operate in and will enter new markets and review acquisitions when opportunities arise, and will also exit a particular market and reallocate assets elsewhere when there is a strategic advantage to doing so. With any acquisition, there is inherent risk related to the Company's ability to integrate the acquired business and to achieve the anticipated operating improvements. Weston Foods' strategy to operate on a North American scale allows it to effectively manage and minimize its exposure to industry risk.

Loblaw pursues a strategy of enhancing profitability on a market-by-market basis by using a multi-format approach. By operating across Canada through corporate stores, franchised stores and associated stores and by servicing independent accounts, Loblaw strategically minimizes and balances its exposure to industry risk.

Competitive Environment 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, 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' brands provide it with a strategic advantage over its competitors. Its premium and popular 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.

As a result of the difficult sales environment being experienced by United States traditional food retailers, coupled with the continuing cost pressures being experienced by the industry, Weston Foods anticipates that competitive business restructuring will continue in 2006. Although the outcome and the impact, if any, on the Company's consolidated financial results from this anticipated restructuring is uncertain, Weston Foods will closely monitor the United States food retail market and, if required, adjust its strategies and programs as necessary.

Loblaw's control label program represents a significant competitive advantage because it enhances customer loyalty by offering superior value and provides some protection against national brand pricing strategies. Loblaw faces increasing competition from many types of non-traditional competitors, such as mass merchandisers, warehouse clubs, drugstores, limited assortment stores, discount stores, convenience stores and specialty stores, all of which continue to increase their offerings of products typically associated with traditional supermarkets. In order to compete effectively and efficiently, Loblaw is developing and operating new departments and services that complement the traditional supermarket layout, as well as enhancing its product and service offerings. Loblaw is also subject to competitive pressures from new entrants into the marketplace and from the potential consolidation of existing competitors. These competitors may have extensive resources, which will allow them to compete effectively with Loblaw in the long term.

In order to remain competitive by having an optimal cost structure, the Company continuously evaluates and implements various cost saving initiatives. The Company may not always achieve the expected cost savings and other benefits of these initiatives. Accordingly, the Company's competitive position and financial results could be negatively impacted.

Increased competition could adversely affect the Company's ability to achieve its objectives. The Company'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 competitors' pricing activities. Accordingly, the Company's position and financial performance could be negatively impacted.

Food Safety and Public Health The Company is subject to potential liabilities connected with its business operations, including potential exposures 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 Loblaw's control label products, in relation to the production, packaging and design of products.

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 ensure that potentially harmful products are removed from inventories immediately. Food safety related liability exposures are insured by the Company's insurance program. In addition, the Company has food safety policies 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 is intensifying the campaign for consumer awareness of safe food handling and consumption.

In the event of a significant public health crisis, such as a flu or other type of pandemic, it is possible that significant numbers of customers may choose to limit their activities outside of their home, including shopping trips, thereby negatively impacting the Company's sales. Furthermore, it may not be possible to adequately staff the Company's businesses during such an event. The Company is in the process of preparing a plan for its approach to such an event.

Labour A significant portion of the Company's workforce is unionized. Renegotiating collective agreements might 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 2005 as 79 collective agreements expired and another 80 collective agreements were successfully negotiated which represented a combination of agreements expiring in 2005, those carried over from prior years and those negotiated early. In 2006, 99 collective agreements affecting approximately 43,000 employees will expire, with the single largest agreement covering approximately 14,300 employees. The Company will also continue to negotiate the 41 collective agreements carried over from 2003 to 2005 and anticipates no labour disruption with respect to these negotiations. 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, making it more difficult for the Company to compete.

Commodity Prices Weston Foods operating results are directly impacted by fluctuations in the price of commodities such as wheat, flour, sugar, vegetable oil and cocoa. Increases in the price of these commodities could adversely affect the Company's financial performance. In order to minimize the effect of these fluctuations on current operating results and to lessen the resulting uncertainty of future financial results, the Company hedges a portion of its anticipated commodity purchases. As at year end 2005, Weston Foods had entered into commodity future contracts that mitigate price fluctuations on some commodities for approximately 6 months, on average, into 2006.

Employee Future Benefit Contributions Although the Company's registered funded defined benefit pension plans are currently adequately funded and returns on defined benefit pension plan assets are in line with expectations, 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 registered funded defined benefit pension plans in excess of those currently contemplated, which in turn could have a negative effect on its financial performance.

During 2005, the Company contributed $103 million (2004 – $85 million) to its registered funded defined benefit pension plans. During 2006, the Company expects to contribute approximately $103 million to these plans. In 2006, the Company also expects to make a contribution of $17 million to the funded long term disability benefit plan in addition to contributions 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.

In addition to the Company-sponsored pension plans, the Company participates in various multi-employer pension plans, providing pension benefits in which approximately 40% (2004 – 41%) of employees of the Company and of its 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. Pension cost for these plans is recognized as contributions are paid. The Financial Services Commission of Ontario has recently issued a report concerning one of these multi-employer pension plans. This report deals with alleged breaches of the Ontario pension and benefits legislation in connection with certain of the investments of the plan under review and its governance practices.

Third-Party Service Providers Certain aspects of the Company's business are significantly affected by third parties. 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, which are among the most recognized brands in Canada, are manufactured under contract by third-party vendors, and in order to preserve the brands' equity, these vendors are held to high standards of quality. Loblaw also uses third-party logistic services including those in connection with a dedicated warehouse and distribution centre in Pickering, Ontario and third-party common carriers. Any disruption in these services could interrupt the delivery of merchandise to the stores 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 credit and fraud for the *President's Choice Financial* MasterCard®. In order to minimize operating risk, PC Bank and Loblaw actively manage and monitor their relationship with all third-party service providers. PC Bank has developed a vendor management policy, approved by its Board of Directors, and 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.

Real Estate The availability and conditions affecting the acquisition and development of real estate properties may impact Loblaw's ability to execute its planned real estate program on schedule and therefore, its ability to achieve its sales targets. Real estate development plans may be contingent on successful negotiation of labour agreements with respect to same-site expansion or redevelopment. As Loblaw expands its general merchandise offering, 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 allowing it to introduce new departments and services that could be precluded under operating leases. At year end 2005, Loblaw owned 72% (2004 – 70%) of its corporate store 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. As Loblaw expands the breadth of its general merchandise offering, it may increase the number of seasonal products offered and its operations may therefore be subject to more seasonal fluctuations.

Leadership Development and Employee Retention Effective leadership is essential to sustaining the growth and success of the Company. The Company continues to focus on the development of leaders at all levels and across all regions, by executing tailored leadership development programs that provide the knowledge and skills necessary to drive positive change and ensure effective execution. The degree to which the Company is effective in developing its leaders and retaining key employees could affect its ability to execute its strategies, efficiently run its operations and meet its goals for financial performance.

Loblaw opened a new head office and Store Support Centre in Brampton, Ontario in the third quarter of 2005 combining several administrative and operating offices from across southern Ontario and the general merchandise operations from Calgary, Alberta. In addition, Loblaw's internal reorganizations involving the merchandising, procurement and operations groups took effect. These initiatives may result in further short term employee turnover and disruption as certain employees may assume new roles and responsibilities.

Utility and Fuel Prices The Company is a significant consumer of electricity, other utilities and fuel. Unanticipated cost increases in these items could negatively affect the Company's financial performance.

Insurance The Company limits its exposure to risk 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, which provide the appropriate level of retained and insured risks. 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 to reduce and manage the risk it retains.

Environmental, Health and Safety 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 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 an adverse 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 legislative concerns and related communication efforts.

Ethical Business Conduct Any failure of the Company to adhere to its policies, the law or ethical business practices could significantly affect its reputation and brands and could therefore, negatively impact the Company's financial performance. The Company has adopted a Code of Business Conduct which employees of the Company are required to acknowledge and agree to comply with on a regular basis. The Company has established an Ethics and Business Conduct Committee 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. 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.

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. 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.

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.

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 and the market prices of Weston and Loblaw common shares. 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.

Derivative Instruments The Company uses over-the-counter financial derivative instruments, specifically cross currency basis swaps, interest rate swaps, equity forwards and swaps, and commodity futures and options, to minimize the risks and costs associated with its financing activities, stock-based compensation plans and future purchases of commodities. 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 prevent it from using any derivative instrument for trading or speculative purposes. See notes 1 and 20 to the consolidated financial statements for additional information on the Company's derivative instruments.

Foreign Currency Exchange Rate The Company enters into currency derivative agreements 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 in United States dollars are exchanged against the receipt of floating interest payments and principal 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.

Interest Rate The Company enters into interest rate swaps to manage its current and anticipated exposure to fluctuations in interest rates and 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 The Company enters into equity derivative agreements to manage its current and anticipated exposure to fluctuations in its stock-based compensation cost as a result of changes in the market prices of Weston and Loblaw common shares. These equity derivative agreements change in value as the market prices of the underlying common shares change, which effectively results in a partial offset to fluctuations in the Company's stock-based compensation cost. The partial offset between the Company's stock-based compensation costs and the equity derivatives exists as long as the market prices of Weston and Loblaw common shares exceed the exercise price of employee stock options. The amount of net stock-based compensation cost recorded in operating income is 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 fluctuations in the market price of the underlying common shares. As at year end 2005, 1,927,640 Weston stock options and share appreciation rights and 2,254,639 Loblaw stock options had exercise prices which were greater than the respective market price of Weston and Loblaw common shares at year end. The fair value of Weston's equity forward sale agreement based on 9.6 million Loblaw common shares is based on fluctuations in the market price of Loblaw common shares, and is a non-cash item that will ultimately be offset by the recognition of any gain on Weston's disposition of the 9.6 million Loblaw common shares.

Counterparty Over-the-counter financial derivative instruments are subject to counterparty risk. Counterparty risk arises from the possibility that market changes may affect a counterparty's position unfavourably and that the counterparty defaults on its obligations to the Company. 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 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 forwards.

Credit The Company's exposure to credit risk relates to the Company's cash equivalents and short term investments, Weston Foods' trade accounts receivables and Loblaw's credit card receivables and accounts receivable from franchisees, associates and independent accounts.

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. This risk is mitigated by the established 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.

Weston Foods performs ongoing credit evaluations of new and existing customers' financial condition and reviews the collectibility of its trade accounts receivables in order to mitigate any possible credit losses.

Loblaw's exposure to credit risk relates to PC Bank's credit card receivables. PC Bank manages the *President's Choice Financial* MasterCard®. PC Bank grants credit to its customers on *President's Choice Financial* MasterCard® with the intention of increasing the loyalty of those customers and Loblaw profitability. Credit risk results from the potential for loss due to those customers defaulting on their payment obligations. In order to minimize the associated credit risk, PC Bank employs stringent credit scoring techniques, actively monitors the credit card portfolio and reviews techniques and technology that can improve the effectiveness of its collection process. In addition, these receivables are dispersed among a large, diversified group of credit card customers. Loblaw also has accounts receivable from its franchisees, associates and independent accounts, mainly as a result of sales to these customers. Loblaw actively monitors the balances on an ongoing basis and collects funds from its franchisees on a frequent basis in accordance with terms specified in the applicable agreements.

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 rates from Wittington. Rental payments amounted to approximately $5 million in 2005 (2004 – $4 million). In 2004, a one time payment of $8 million for a property designated for future development was also made. 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 23 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.

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.

Valuation of 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.

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 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 2005 net cost for defined benefit pension and other benefit plans were 6.2% and 6.1% respectively on a weighted average basis, compared to 6.3% and 6.1% respectively in 2004. Certain defined benefit pension plans and other benefit plans affected by the plan to restructure Weston Foods' United States biscuit operations, the plan to restructure Loblaw's supply chain operations nationally and the plan to exit certain of Weston Foods' United States bread lines were remeasured as at March 1, 2005, March 31, 2005 and August 1, 2005 respectively. For these plans, costs subsequent to these dates were determined using discount rates of 5.75%, 5.75% and 5.50% respectively. The majority of the resulting curtailment gains were offset against net unamortized actuarial losses for those plans. A net curtailment loss of $2 million for defined benefit pension plans, a net curtailment gain of $2 million for other benefit plans and additional defined benefit pension costs were recorded in restructuring and other charges in the consolidated statement of earnings. The discount rates used to determine the net 2006 defined benefit pension and other benefit plans costs decreased and as a result, the Company expects an increase in these costs in 2006.

The expected long term rate of return on plan assets is based on historical returns, on the asset mix and on the active management of defined benefit pension plan assets. The Company's defined benefit pension plan assets had a 10 year annualized return of 9.1% as at the 2005 measurement date. The actual annual returns within this 10 year period varied with market conditions. Consistent with 2005, the Company has assumed an 8.0% expected long term rate of return on plan assets in calculating its defined benefit pension plans cost for 2006.

The expected growth rate in health care costs for 2005 was based on external data and the Company's historical trends. Higher initial growth rates were used in 2006, when compared to 2005.

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. Differences between actual experience and the assumptions and changes in the assumptions may result in changes to the accrued benefit plan asset and liability presented in the consolidated balance sheet and the defined benefit pension and other benefit plans cost recognized in the consolidated statement of earnings.

In accordance with Canadian GAAP, the difference between actual results and assumptions are accumulated in net actuarial gain or loss. The magnitude of any immediate impact to the Company's operating income is mitigated by the fact that the excess net accumulated actuarial gain or loss over 10% of the greater of the accrued benefit plan obligation or the fair value of the plan assets at the beginning of the year is amortized over the expected average remaining service period of the active employees. As at September 30, 2005, the unamortized net actuarial loss was $433 million (2004 – $283 million) for defined benefit pension plans and $179 million (2004 – $119 million) for other benefit plans.

Additional information regarding the Company's pension and other benefit plans, including a sensitivity analysis for changes in key assumptions, is provided in note 15 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 loss would be recognized to the extent that, at the reporting unit level, the carrying value of goodwill exceeds the implied fair value. Fair value of goodwill is estimated in the same manner as goodwill is determined at the date of acquisition in a business acquisition, that is, the excess of the fair value of the reporting unit over the fair value of the identifiable net assets of the reporting unit. 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.

Intangible assets with indefinite 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 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 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 quarter of 2005, the Company performed the annual goodwill and indefinite life intangible assets impairment tests and it was determined that the fair value of each of the reporting units exceeded its respective carrying value and therefore, no impairment of goodwill or indefinite life intangible assets was identified.

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 and the timing of reversal of temporary differences and possible audits of tax filings by regulatory authorities. Management believes it has adequately provided for income taxes based on current available information.

On an ongoing basis, future income tax assets are reviewed to determine if a valuation allowance is required and if it is deemed more likely than not that the future income tax assets will not be realized based on taxable income projections, a valuation allowance is recorded. As at December 31, 2005, total valuation allowances amounted to $54 million.

Changes or differences in these 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 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 3 and 12 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 Company made assumptions about the sum of the undiscounted cash flows of certain fixed assets and determined they were less than their carrying value, resulting in the recognition of an impairment loss. The Company uses its internal plans in estimating future cash flows. These plans reflect the Company's best estimate but may change in the future due to uncertain competitive and economic market conditions or changes in business strategies.

Goods and Services Tax and Provincial Sales Taxes During the third quarter of 2005, Loblaw recorded a charge relating to an audit and proposed assessment by the CRA relating to GST on certain products sold between 2000 and 2002 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 up to the end of 2004. Accordingly, a charge of $40 million was recorded in operating income in the third quarter to reflect management's best estimate of such potential tax liabilities of which management is currently aware. Approximately $15 million of this amount was settled during the fourth quarter of 2005. 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.

ACCOUNTING STANDARDS IMPLEMENTED IN 2005

Effective January 1, 2005, the Company implemented the following accounting standards issued by the CICA:

- Accounting Guideline 15, "Consolidation of Variable Interest Entities", issued by the CICA in June 2003 and amended in September 2004, requires the consolidation of certain entities that are subject to control on a basis other than through ownership of a majority of voting interests.

  AcG 15 defines a variable interest entity as an entity that either does not have sufficient equity at risk to finance its activities without subordinated financial support or where the holders of the equity at risk lack the characteristics of a controlling financial interest. AcG 15 requires the primary beneficiary to consolidate VIEs. AcG 15 considers an entity to be the primary beneficiary of a VIE if it holds variable interests that expose it to a majority of the VIE's expected losses or that entitle it to receive a majority of the VIE's expected residual returns or both.

  Prior to AcG 15, the Company consolidated all entities that it controlled through ownership of a majority of voting interests. Effective January 1, 2005, the Company implemented AcG 15 retroactively without restatement of prior periods and as a result, the Company consolidates entities in which it has control through ownership of a majority of the voting interests as well as all significant VIEs for which it is the primary beneficiary.

Upon implementation of AcG 15, the Company identified the following significant VIEs:

Independent Franchisees Loblaw enters into various forms of franchise agreements that generally require the independent franchisee to purchase inventory from Loblaw and pay certain fees in exchange for services provided by Loblaw and for the right to use certain trademarks and licences owned by Loblaw. Independent franchisees generally lease the land and building from Loblaw, and when eligible, may obtain financing through a structure involving independent trusts to facilitate the purchase of the majority of their inventory and fixed assets, consisting mainly of fixturing and equipment. These trusts are administered by a major Canadian bank. Under the terms of certain franchise agreements, Loblaw may also lease equipment to independent franchisees. Independent franchisees may also obtain financing through operating lines of credit with traditional financial institutions or through issuing preferred shares or notes payable to Loblaw. Loblaw monitors the financial condition of its independent franchisees and provides for estimated losses or write-downs on its accounts and notes receivable or investments when appropriate. Upon implementation of AcG 15, the Company determined that 121 of Loblaw's independent franchisee stores met the criteria for VIEs that require consolidation by the Company pursuant to AcG 15.

Warehouse and Distribution Agreement Loblaw has entered into a warehousing and distribution agreement with a third party to provide to Loblaw distribution and warehousing services from a dedicated facility. Loblaw has no equity interest in this third party; however, the terms of the agreement with the third party are such that the Company has determined that the third party meets the criteria for a VIE that requires consolidation by the Company. As a result of the fee structure agreed to with this third party, the impact of the consolidation of this warehouse and distribution entity was not material.

Accordingly, the Company has included the results of these independent franchisees and this third-party entity that provides distribution and warehousing services in its consolidated financial statements effective January 1, 2005.

Details of the amounts recorded upon implementation and the effect on the opening consolidated balance sheet as at January 1, 2005 are summarized below and include the impact of both the independent franchisees and the warehouse and distribution entity:

CONDENSED CONSOLIDATED BALANCE SHEET AS AT JANUARY 1, 2005

($ millions)	Condensed consolidated balance sheet as at January 1, 2005 before AcG 15 impact	Impact of the implementation of AcG 15	Condensed consolidated balance sheet as at January 1, 2005 after AcG 15 impact
Cash and cash equivalents	$ 1,008	$ 20	$ 1,028
Short term investments	388		388
Accounts receivable	920	(73)	847
Inventories	1,979	78	2,057
Other current assets	250	4	254
Total current assets	4,545	29	4,574
Fixed assets	8,256	136	8,392
Goodwill and intangible assets	3,456	3	3,459
Other assets	1,512	(51)	1,461
Total assets	$ 17,769	$ 117	$ 17,886
Total current liabilities	$ 4,352	$ 48	$ 4,400
Long term debt	6,004	96	6,100
Other liabilities	967	(8)	959
Minority interest	2,066	(1)	2,065
Total liabilities	13,389	135	13,524
Common share capital	614		614
Retained earnings	4,170	(18)	4,152
Cumulative foreign currency translation adjustment	(404)		(404)
Total liabilities and shareholders' equity	$ 17,769	$ 117	$ 17,886

The impact of AcG 15 on the opening consolidated balance sheet can be further explained as follows:

- An after-tax, one-time charge of $18 million (net of income taxes of $12 million and minority interest of $11 million) was recorded upon implementation and resulted mainly from delaying the recognition of vendor monies to when the related inventories of the independent franchisees are sold to their customers, the excess of the independent franchisees' accumulated losses over the allowance for doubtful accounts previously recorded by the Company and the reversal of initial franchise fees initially recognized upon the sale of franchises to third parties.
- Accounts receivable due from the independent franchisees and the investment in preferred shares of the independent franchisees were eliminated upon consolidation; cash and cash equivalents, inventories and fixed assets financed by long term debt (a portion of which is due within one year) were recorded.
- An increase in fixed assets and total current liabilities in respect of the warehouse and distribution entity.
- Minority interest representing the common stakeholder's equity in the respective VIEs.

As at December 31, 2005, 123 of Loblaw's independent franchise stores met the criteria for a VIE and were consolidated pursuant to AcG 15. The impact from the consolidation of these VIEs on the consolidated balance sheet as at December 31, 2005 was not significantly different than the impact on the opening consolidated balance sheet as outlined above. The impact on the consolidated statement of earnings for the year ended December 31, 2005 was predominantly an increase in sales as quantified in the table "Sales and Sales Growth Excluding Impact of VIEs" included on pages 3 and 19. The impact on basic net earnings per common share from continuing operations for 2005 was a decline of approximately $0.03.

The consolidation of these VIEs by the Company does not result in any change to its tax, legal or credit risks nor does it result in the Company assuming any obligations of these third parties.

Independent Trust Loblaw has also identified that it holds a variable interest, by way of a standby letter of credit, in an independent trust which is used to securitize credit card receivables for PC Bank. In these securitizations, PC Bank sells a portion of its credit card receivables to the independent trust in exchange for cash. Although this independent trust has been identified as a VIE, it was determined that Loblaw is not the primary beneficiary and therefore this VIE is not subject to consolidation by the Company. The Company's maximum exposure to loss as a result of its involvement with this independent trust is disclosed in the Off-Balance Sheet Arrangements section of this MD&A and in notes 11 and 22 to the consolidated financial statements.

- EIC Abstract 150, "Determining Whether an Arrangement Contains a Lease" ("EIC 150"), addresses arrangements comprising a transaction or a series of transactions that do not take the legal form of a lease but convey a right to use a tangible asset in return for a payment or a series of payments. EIC 150 provides guidance for determining whether these types of arrangements contain a lease within the scope of CICA section 3065, "Leases", and should be accounted for accordingly. The assessment should be based on whether the fulfillment of the arrangement is dependent on the use of specific tangible assets and whether the arrangement conveys the right to control the use of the tangible assets. This assessment should be made at inception of the arrangement and only reassessed if certain conditions are met. EIC 150 is effective for arrangements entered into or modified as of the beginning of 2005 and did not have any impact during 2005. The Company will continue to monitor whether EIC 150 is applicable to transactions undertaken by the Company.

- EIC Abstract 154, "Accounting for Pre-Existing Relationships Between the Parties of a Business Combination" ("EIC 154"), issued on May 31, 2005, requires that a business combination between parties that have a pre-existing relationship be evaluated to determine if a settlement of a pre-existing contract has occurred which would require separate accounting from the business combination. The settlement of the pre-existing contract should be measured at the settlement amount as defined within the standard. In addition, EIC 154 requires that certain reacquired rights, including the rights to the acquirer's trade name under a franchise agreement, be recognized as an intangible asset separate from goodwill.

  The Company has determined that acquisitions by the Company of independent franchisees are within the scope of EIC 154. The adoption of EIC 154 by the Company on a prospective basis did not have a material impact on net earnings.

FUTURE ACCOUNTING STANDARDS

The Company closely monitors new accounting standards to assess the impact, if any, on its consolidated financial statements. In 2006, the Company will be reviewing the implications of the following standards and implementing the recommendations as required.

- In 2005, the Accounting Standards Board finalized its strategic plan for financial reporting in Canada whereby Canadian GAAP will converge with International Financial Reporting Standards over a five-year period. After this transitional period, Canadian GAAP will cease to exist as a separate, distinct basis of financial reporting. The Company will continue to monitor the changes resulting from this transition.

- EIC Abstract 156, "Accounting for Consideration by a Vendor to a Customer (Including a Reseller of the Vendor's products)", issued in September 2005 addresses cash consideration, including a sales incentive, given by a vendor to a customer. This consideration is presumed to be a reduction of the selling price of the vendor's products and should therefore be classified as a reduction of sales in the vendor's income statement. These recommendations are effective for all interim and annual financial statements for fiscal years beginning on or after January 1, 2006. The Company is currently assessing the impact of these recommendations and will implement them in the first quarter of 2006.
- Section 3855, "Financial Instruments – Recognition and Measurement", Section 3865, "Hedges" and Section 1530 "Comprehensive Income" issued in January 2005:
- Section 3855, "Financial Instruments – Recognition and Measurement" establishes standards for recognizing and measuring financial assets, financial liabilities and non-financial derivatives. All financial instruments must be classified into a defined category, namely, held-to-maturity investments, held for trading, loans and receivables, available-for-sale financial assets and other liabilities. This classification will determine how each instrument is measured and how gains and losses are recognized. In addition, the recommendations define derivatives to include non-financial derivatives and embedded derivatives which meet certain criteria. All such derivatives must be classified as held for trading and therefore recorded at fair value unless they are designated in a hedging relationship.
- Section 3865, "Hedges", replaces AcG 13, "Hedging Relationships" and the guidance formerly in Section 1650, "Foreign Currency Translation". The recommendations of this section are optional and are only required if the entity is applying hedge accounting. This section establishes standards for the accounting treatment of qualifying hedge relationships and the necessary disclosures.
- Section 1530, "Comprehensive Income", introduces a statement of comprehensive income which will be included in the full set of interim and annual financial statements. Comprehensive income will represent the change in equity during a period from transactions and other events and circumstances from non-owner sources and will include all changes in equity other than those resulting from investments by owners and distributions to owners.

  These standards are effective for interim and annual financial statements for fiscal years beginning on or after October 1, 2006. The Company is currently assessing the impact of these recommendations and will implement them in the first quarter of 2007 prospectively.

OUTLOOK

The outlook for 2006 for Weston Foods is for continued growth in sales as a result of continued volume and price improvements. Adjusted operating income(1) growth is expected to continue, with operating margins being pressured by underlying cost inflation, particularly with respect to certain materials, energy and people related benefits costs.

Loblaw continues to expect that the negative impact of its transformative process will be absorbed by the end of the second quarter of 2006. This includes an anticipated decline in adjusted basic net earnings per common share(1) in the first quarter of 2006 compared to the same period in 2005. This decline is expected to be consistent with the relative decline in adjusted basic net earnings per common share(1), experienced in the fourth quarter of 2005. Loblaw expects that adjusted basic net earnings per common share(1) performance will improve during the second half of 2006. Further information on Loblaw's outlook regarding its sales and adjusted basic earnings per common share(1) growth can be found in Loblaw's 2005 Annual Report, which is available at www.sedar.com and at www.loblaw.ca.

Loblaw remains confident that its strategic plan is appropriate given the increased competitive landscape. It believes that the transformation will provide the benefits of being a national organization while operating locally in each community. Loblaw expects these initiatives will better position Loblaw to meet the food and everyday household needs of Canadian consumers, and make Loblaw more aligned, streamlined and efficient so that it can continue to offer customers the best value in the form of lower prices and better service.

The outlook for the consolidated results is consistent with those of the operating segments as discussed above. The consolidated results continue to reflect the transformational changes undertaken by both the Weston Foods and Loblaw operating businesses in order to position them for strong growth in the future.

This outlook should be read in conjunction with the Forward-Looking Statements section of the MD&A on page 1.

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 the Annual Report, including this Financial 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.

(1) See Non-GAAP Financial Measures beginning on page 44.

Sales and Sales Growth Excluding the Impact of VIEs These financial measures exclude the impact of the increase in sales from the consolidation by the Company of Loblaw independent franchisees which resulted from the implementation of AcG 15 retroactively without restatement effective January 1, 2005. These sales are excluded because they affect the comparability of the financial results and could potentially distort the analysis of trends. A reconciliation of the financial measures to the Canadian GAAP financial measures is included in the tables *"Sales and Sales Growth Excluding Impact of VIEs"* included on pages 3, 19, 30 and 33 of this MD&A.

Adjusted Operating Income and Margin The following table reconciles adjusted operating income to Canadian GAAP operating income reported in the consolidated statements of earnings for the quarters ended December 31, 2005 and December 31, 2004 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 operating income and margin are useful to management in assessing the Company's performance and in making decisions regarding the ongoing operation of its business.

CONSOLIDATED	**Quarter ended Dec. 31, 2005**	Quarter ended Dec. 31, 2004	**Year ended Dec. 31, 2005**	Year ended Dec. 31, 2004	Year ended Dec. 31, 2003	Year ended Dec. 31, 2002	Year ended Dec. 31, 2001
Operating income	**$ 440**	$ 524	**$ 1,634**	$ 1,782	$ 1,832	$ 1,704	$ 1,397
Add (deduct) impact of the following:							
Restructuring and other charges	**7**	77	**118**	122	60		44
Direct costs associated with supply chain disruptions	**10**		**30**				
Goods and Services Tax and provincial sales taxes			**40**				
Net effect of stock-based compensation and the associated equity derivatives	**48**	(17)	**72**	(3)	(11)	32	
Variable interest entities	**4**						
Adjusted operating income	**$ 509**	$ 584	**$ 1,894**	$ 1,901	$ 1,881	$ 1,736	$ 1,441

WESTON FOODS	**Quarter ended Dec. 31, 2005**	Quarter ended Dec. 31, 2004	**Year ended Dec. 31, 2005**	Year ended Dec. 31, 2004	Year ended Dec. 31, 2003	Year ended Dec. 31, 2002	Year ended Dec. 31, 2001
Operating income	**$ 48**	$ (4)	**$ 241**	$ 138	$ 374	$ 409	$ 269
Add (deduct) impact of the following:							
Restructuring and other charges	**1**	77	**32**	121	35		44
Net effect of stock-based compensation and the associated equity derivatives	**21**	(9)	**29**	(3)	(7)	18	
Adjusted operating income	**$ 70**	$ 64	**$ 302**	$ 256	$ 402	$ 427	$ 313

LOBLAW	**Quarter ended Dec. 31, 2005**	Quarter ended Dec. 31, 2004	**Year ended Dec. 31, 2005**	Year ended Dec. 31, 2004	Year ended Dec. 31, 2003	Year ended Dec. 31, 2002	Year ended Dec. 31, 2001
Operating income	**$ 392**	$ 528	**$ 1,393**	$ 1,644	$ 1,458	$ 1,295	$ 1,128
Add (deduct) impact of the following:							
Restructuring and other charges	**6**		**86**	1	25		
Direct costs associated with supply chain disruptions	**10**		**30**				
Goods and Services Tax and provincial sales taxes			**40**				
Net effect of stock-based compensation and the associated equity derivatives	**27**	(8)	**43**		(4)	14	
Variable interest entities	**4**						
Adjusted operating income	**$ 439**	$ 520	**$ 1,592**	$ 1,645	$ 1,479	$ 1,309	$ 1,128

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

MANAGEMENT'S DISCUSSION AND ANALYSIS

Adjusted EBITDA and Margin The following table reconciles adjusted EBITDA to adjusted operating income which is reconciled to Canadian GAAP measures reported in the consolidated statements of earnings for the quarters ended December 31, 2005 and December 31, 2004 and the years ended December 31 as indicated. 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.

CONSOLIDATED	**Quarter ended Dec. 31, 2005**	Quarter ended Dec. 31, 2004	**Year ended Dec. 31, 2005**	Year ended Dec. 31, 2004	Year ended Dec. 31, 2003	Year ended Dec. 31, 2002	Year ended Dec. 31, 2001
Adjusted operating income	**$ 509**	$ 584	**$ 1,894**	$ 1,901	$ 1,881	$ 1,736	$ 1,441
Add (deduct) impact of the following:							
Depreciation and amortization	**168**	149	**684**	618	537	498	418
VIE depreciation and amortization	**(8)**		**(26)**				
Adjusted EBITDA	**$ 669**	$ 733	**$ 2,552**	$ 2,519	$ 2,418	$ 2,234	$ 1,859

WESTON FOODS	**Quarter ended Dec. 31, 2005**	Quarter ended Dec. 31, 2004	**Year ended Dec. 31, 2005**	Year ended Dec. 31, 2004	Year ended Dec. 31, 2003	Year ended Dec. 31, 2002	Year ended Dec. 31, 2001
Adjusted operating income	**$ 70**	$ 64	**$ 302**	$ 256	$ 402	$ 427	$ 313
Add (deduct) impact of the following:							
Depreciation and amortization	**28**	32	**126**	145	144	144	103
Adjusted EBITDA	**$ 98**	$ 96	**$ 428**	$ 401	$ 546	$ 571	$ 416

LOBLAW	**Quarter ended Dec. 31, 2005**	Quarter ended Dec. 31, 2004	**Year ended Dec. 31, 2005**	Year ended Dec. 31, 2004	Year ended Dec. 31, 2003	Year ended Dec. 31, 2002	Year ended Dec. 31, 2001
Adjusted operating income	**$ 439**	$ 520	**$ 1,592**	$ 1,645	$ 1,479	$ 1,309	$ 1,128
Add (deduct) impact of the following:							
Depreciation and amortization	**140**	117	**558**	473	393	354	315
VIE depreciation and amortization	**(8)**		**(26)**				
Adjusted EBITDA	**$ 571**	$ 637	**$ 2,124**	$ 2,118	$ 1,872	$ 1,663	$ 1,443

Adjusted EBITDA margin is calculated as adjusted EBITDA divided by sales excluding impact of 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 per common share from continuing operations reported in the consolidated statements of earnings for the quarters ended December 31, 2005 and December 31, 2004 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 operation of its business.

CONSOLIDATED

	Quarter ended Dec. 31, 2005	Quarter ended Dec. 31, 2004	**Year ended Dec. 31, 2005**	Year ended Dec. 31, 2004	Year ended Dec. 31, 2003	Year ended Dec. 31, 2002	Year ended Dec. 31, 2001
Basic EPS from continuing operations	**$ 1.78**	$ 1.15	**$ 5.25**	$ 4.49	$ 5.91	$ 5.19	$ 4.58
Add (deduct) impact of the following:							
Restructuring and other charges	**0.02**	0.37	**0.42**	0.58	0.24		0.21
Direct costs associated with supply chain disruptions	**0.03**		**0.09**				
Goods and Services Tax and provincial sales taxes			**0.14**				
Net effect of stock-based compensation and the associated equity derivatives	**0.31**	(0.13)	**0.46**	(0.01)	(0.08)	0.15	
Accounting for Loblaw forward sale agreement	**(0.63)**	0.42	**(0.77)**	0.51			
Changes in statutory income tax rates	**0.02**		**0.02**		0.03		
Resolution of certain income tax matter				(0.07)	(0.26)		
Variable interest entities	**0.02**		**0.03**				
Gain on sale of Loblaw shares							(0.89)
Goodwill							0.27
Adjusted Basic EPS from continuing operations	**$ 1.55**	$ 1.81	**$ 5.64**	$ 5.50	$ 5.84	$ 5.34	$ 4.17

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 with the Company's investment in Domtar common shares included in other assets.

($ millions)	**Dec. 31, 2005**	Dec. 31, 2004	Dec. 31, 2003	Dec. 31, 2002	Dec. 31, 2001
Bank indebtedness	**$ 113**	$ 123	$ 108	$ 61	$ 152
Commercial paper	**498**	840	696	715	466
Short term bank loans	**138**	102	67	33	1,367
Long term debt due within one year	**361**	222	307	110	82
Long term debt	**5,913**	6,004	5,829	5,387	4,905
Less: Cash and cash equivalents	**1,540**	1,008	965	1,157	743
Short term investments	**50**	388	545	398	518
Net debt	**5,433**	5,895	5,497	4,751	5,711
Less: Exchangeable debentures	**225**	373	374	374	375
Net debt excluding exchangeable debentures	**$ 5,208**	$ 5,522	$ 5,123	$ 4,377	$ 5,336

MANAGEMENT'S DISCUSSION AND ANALYSIS

Total Assets The following table reconciles 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 investment from the total assets used in this ratio.

				As at December 31, 2005
($ millions)	**Weston Foods**	**Loblaw**	**Discontinued Operations**	**Consolidated**
Total assets	**$ 4,675**	**$ 13,906**	**$ 12**	**$ 18,593**
Less:				
Cash and cash equivalents	**624**	**916**		**1,540**
Short term investments	**46**	**4**		**50**
Long term assets of operations held for sale			**12**	**12**
Domtar investment	**220**			**220**
Total assets	**$ 3,785**	**$ 12,986**	**$ –**	**$ 16,771**

				As at December 31, 2004
($ millions)	Weston Foods	Loblaw	Discontinued Operations	Consolidated
Total assets(1)	$ 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 operations held for sale			62	62
Long term assets of operations held for sale			11	11
Domtar investment	365			365
Total assets	$ 3,677	$ 12,258	$ –	$ 15,935

(1) Certain prior years' information was reclassified to conform with the current year's presentation.

				As at December 31, 2003
($ millions)	Weston Foods	Loblaw	Discontinued Operations	Consolidated
Total assets(1)	$ 4,780	$ 12,230	$ 268	$ 17,278
Less:				
Cash and cash equivalents	347	618		965
Short term investments	167	378		545
Current assets of operations held for sale			179	179
Long term assets of operations held for sale			89	89
Domtar investment	367			367
Total assets	$ 3,899	$ 11,234	$ –	$ 15,133

(1) Certain prior years' information was reclassified to conform with the current year's presentation.

As at December 31, 2002

($ millions)	Weston Foods	Loblaw	Discontinued Operations	Consolidated
Total assets[1]	$ 5,228	$ 11,104	$ 292	$ 16,624
Less:				
Cash and cash equivalents	334	823		1,157
Short term investments	94	304		398
Current assets of operations held for sale			207	207
Long term assets of operations held for sale			85	85
Domtar investment	367			367
Total assets	$ 4,433	$ 9,977	$ –	$ 14,410

(1) Certain prior years' information was reclassified to conform with the current year's presentation.

As at December 31, 2001

($ millions)	Weston Foods	Loblaw	Discontinued Operations	Consolidated
Total assets[1]	$ 5,995	$ 9,972	$ 320	$ 16,287
Less:				
Cash and cash equivalents	168	575		743
Short term investments	92	426		518
Current assets of operations held for sale	934		195	1,129
Long term assets of operations held for sale			125	125
Domtar investment	368			368
Total assets	$ 4,433	$ 8,971	$ –	$ 13,404

(1) Certain prior years' information was reclassified to conform with the current year's presentation.

The following table provides additional financial information.

	As at December 31, 2005	As at December 31, 2004	As at December 31, 2003
Market price per common share ($)	**$ 86.31**	$ 109.71	$ 103.71
Actual common shares outstanding (in millions)	**129.0**	128.9	129.4
Weighted average common shares outstanding (in millions)	**129.0**	128.9	131.9

ADDITIONAL INFORMATION

Additional information 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.

March 10, 2006
Toronto, Canada