



# INNOVATION & EXECUTION

**Loblaws**

COMPANIES LIMITED

LOBLAW COMPANIES LIMITED 2014 ANNUAL REPORT

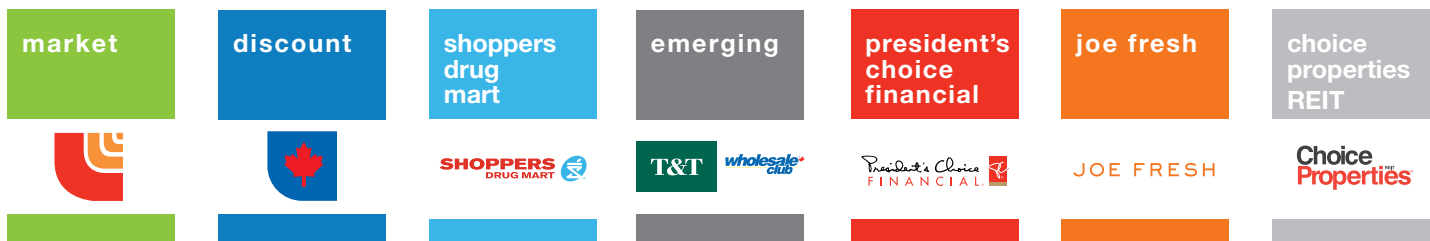


# Loblaw at a Glance

JANUARY 3, 2015

## Loblaw

A portfolio of strong, complementary and independent businesses.

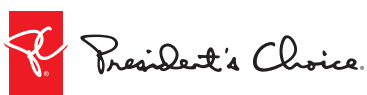


## Our Purpose – *Live Life Well*

Loblaw Companies Limited (“Loblaw” or the “Company”) is Canada’s food and pharmacy leader, the nation’s largest retailer, and the majority unitholder of Choice Properties Real Estate Investment Trust (“Choice Properties”). Loblaw – and its portfolio of grocery, health and beauty, financial services and apparel businesses – provides Canadians with an unparalleled mix of value, assortment and convenience, and offers Canadians two of the country’s most recognized brands – *President’s Choice* and *no name*.

The acquisition of Shoppers Drug Mart, along with the powerful *Life Brand* and *Optimum* brand, has only served to reinforce our leadership position in the marketplace. As well, our *PC Plus* program, omni-channel efforts and multicultural merchandising offerings continued to be points of differentiation for our customer experience.

As a business, we remain committed to our purpose, *Live Life Well* – and as you will see in this report, we took many important steps along this journey in 2014.



JOE FRESH



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### Added new products and store formats

Our long track record of food innovation continued in 2014. We added new products and expanded our *Inspire* store format.



### Creative and successful marketing

We launched the most ambitious advertising campaign in our history with *Crave More*, a new era for the *President's Choice* brand, which invited customers to expect more from their food, now that Canadians care more about the quality, taste, sources, ingredients, value, and excitement of what they eat.

# innovation &



### Wider scope and stronger capabilities

Shoppers Drug Mart maintained its leadership in pharmacy this year. Its pharmacists administered over 800,000 flu shots this year. We opened a Patient Contact Centre, Canada's first, designed to advise patients about their medications and remind them about their refills. This should result in greater patient adherence and better medical outcomes.



### Enhanced capabilities and customer experience

Committed to giving Canadians the best beauty experience in retail, Shoppers Drug Mart opened its fourth enhanced *beautyBOUTIQUE*. These enhanced boutiques feature a wide assortment of prestigious brands and more advice, resulting in an elevated beauty experience for customers.





**Innovation** continues to drive growth at

Loblaw. New products and services attract

customers and enhance our top line. New



ideas have reshaped the Company



including the creation of Choice Properties

and the acquisition of



Shoppers

Drug Mart. However,



getting the most from innovative ideas

depends on how well they are developed

and implemented. Loblaw is building value

through its

focus on



**execution.**





### Offering healthier choices

Loblaws has led the industry with a focus on health and wellness. In 2014, we committed to reducing sodium content levels by an average of 20% across the *President's Choice* line of products.



# & execution



### Information technology system roll-out reached an important milestone

Loblaws completed the introduction of the new information technology system to corporate retail grocery stores – an important step in increasing efficiencies across the Company.



### Bringing two leaders together

After completing the acquisition of Shoppers Drug Mart in March 2014, we immediately began aligning the organization under division presidents, finalized management team members, and made material progress on realizing the expected synergies from the acquisition. We began pilots to enhance the food offer in Shoppers Drug Mart and to optimize the health and beauty offer in a number of grocery stores.

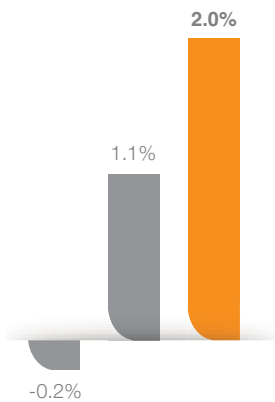


# Delivering solid results.

## 2.0%

Loblaw retail  
same store sales

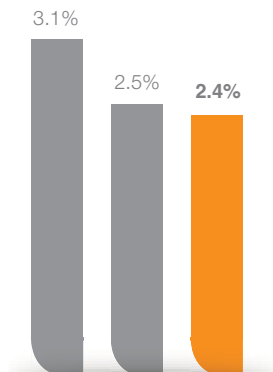
2012 2013 2014



## 2.4%

Shoppers Drug Mart  
front store same store sales

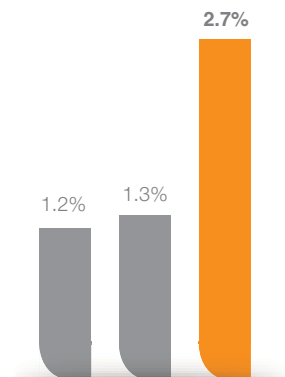
2012 2013 2014



## 2.7%

Shoppers Drug Mart  
pharmacy same store sales

2012 2013 2014



### Forward-Looking Statements

This Annual Report for Loblaw Companies Limited and its subsidiaries (collectively, the “Company” or “Loblaw”) contains forward-looking statements about the Company’s objectives, plans, goals, aspirations, strategies, financial condition, results of operations, cash flows, performance, prospects and opportunities. Specific forward-looking statements in this Annual Report include, but are not limited to, statements with respect to the Company’s anticipated future results and events and plans, synergies and other benefits associated with the acquisition of Shoppers Drug Mart Corporation (“Shoppers Drug Mart”), future liquidity and debt reduction targets, planned capital investments, and status and impact of information technology (“IT”) systems implementation. Forward-looking statements are typically identified by words such as “expect,” “anticipate,” “believe,” “foresee,” “could,” “estimate,” “goal,” “intend,” “plan,” “seek,” “strive,” “will,” “may,” “on track,” and “should” and similar expressions, as they relate to the Company and its management.

Forward-looking statements reflect the Company’s current estimates, beliefs and assumptions, which are based on management’s perception of historical trends, current conditions and expected future developments, as well as other factors it believes are appropriate in the circumstances. The Company’s expectation of operating and financial performance in 2015 is based on certain assumptions, including assumptions about anticipated cost savings, operating efficiencies and continued growth from current initiatives. The Company’s estimates, beliefs and assumptions are inherently subject to significant business, economic, competitive and other uncertainties and contingencies regarding future events and, as such, are subject to change. The Company can give no assurance that such estimates, beliefs and assumptions will prove to be correct.

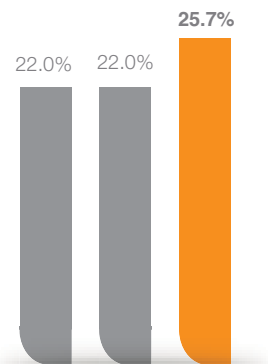
Numerous risks and uncertainties could cause the Company’s actual results to differ materially from those expressed, implied or projected in the forward-looking statements. These risks and uncertainties include, but are not limited to, those discussed in the forward-looking disclaimer found on pages 3 to 4 of the 2014 Annual Report – Financial Review, and the Enterprise Risks and Risk Management section of the Management Discussion and Analysis on pages 33 to 40 of the 2014 Annual Report – Financial Review, and section 4 of the 2014 Annual Information Form.

This is not an exhaustive list of the factors that may affect the Company’s forward-looking statements. Other risks and uncertainties not presently known to the Company or that the Company presently believes are not material could also cause actual results or events to differ materially from those expressed in its forward-looking statements. Additional risks and uncertainties are discussed in the Company’s materials filed with the Canadian securities regulatory authorities from time to time. Readers are cautioned not to place undue reliance on these forward-looking statements, which reflect the Company’s expectations only as of the date of this Annual Report. Except as required by law, the Company does not undertake to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

# 25.7%

Adjusted retail gross margin<sup>1</sup>

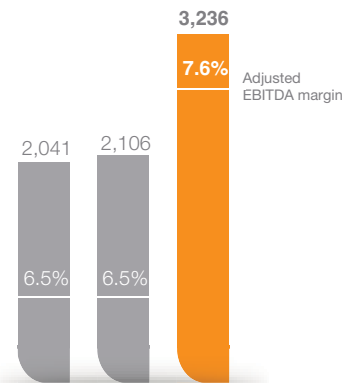
2012 2013 2014



# ↑53.7%

Consolidated adjusted EBITDA<sup>1</sup> and adjusted EBITDA margin<sup>1</sup> (\$ millions)

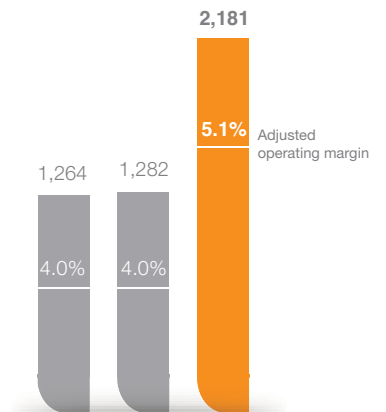
2012 2013 2014



# ↑70.1%

Consolidated adjusted operating income<sup>1</sup> and adjusted operating margin<sup>1</sup> (\$ millions)

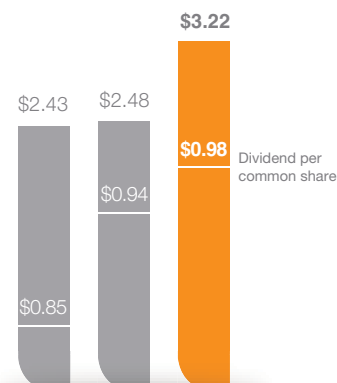
2012 2013 2014



# \$3.22

Adjusted basic EPS<sup>1</sup> and dividend per share

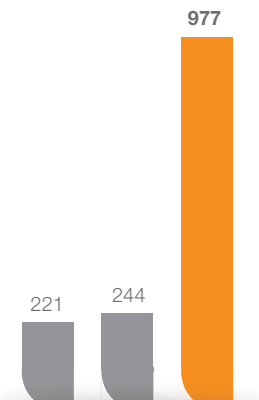
2012 2013 2014



# \$977

Free cash flow<sup>1</sup> (\$ millions)

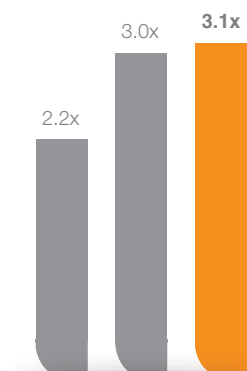
2012 2013 2014



# 3.1x

Adjusted debt<sup>1</sup> to adjusted EBITDA<sup>1</sup>

2012 2013 2014



<sup>1</sup> See Non-GAAP Financial Measures beginning on page 45 of the 2014 Annual Report – Financial Review.

Over the last few years, we strengthened our business by fundamentally improving our customer proposition, investing in price, broadening our offer and improving our stores. We also achieved operating efficiencies, and are well on our way to completing the implementation of our new IT system.

Over the same period, Loblaw fundamentally changed its strategic footprint, moving from a traditional grocer to a portfolio of strong, complementary but independent businesses through the creation of Choice Properties, the acquisition of Shoppers Drug Mart, and the continued growth of President's Choice Financial.

Our progress gives us increased confidence. Our strategic framework is clear, and the entire organization is focused on delivering against it: best in food experience; best in health and beauty; operational excellence; and growth. This strategy is supported by our commitment to stable, consistent trading; realizing synergies and efficiencies in our business; as well as deleveraging the balance sheet.

By delivering the best in health, beauty and food in more than 2,300 convenient locations, we are a trusted leader in achieving our purpose: *Live Life Well.*



## Fellow Shareholders

### **The past year was a significant one for our Company**

In 2014, our Company continued to evolve and grow our diverse portfolio of complementary but distinct businesses. Choice Properties, one of Canada's largest REITs, had its first full year of operations; we completed the acquisition of Shoppers Drug Mart; President's Choice Financial continued to grow; and our grocery business continued to improve, supported by stable business performance in an intensely competitive industry.

On a consolidated basis, we grew revenue by \$10.2 billion to \$42.6 billion, increased our adjusted operating margin by 110 basis points and delivered \$1.2 billion in adjusted net earnings, which generated

over \$975 million in free cash flow. Having completed three quarters since the closing of the Shoppers Drug Mart acquisition, we made excellent progress, including realizing over \$100 million of net synergies.

Our retail businesses performed well, with our core grocery business maintaining positive same store sales and stable gross margin. Shoppers Drug Mart's results were reflected in three quarters of our financials, and they underlined the strength of our front of store offer as well as our resilience in pharmacy.

President's Choice Financial had another strong year. Revenues increased almost 10% and operating income grew by \$22 million as we expanded the breadth and reach of our financial products.

GALEN G. WESTON

EXECUTIVE CHAIRMAN & PRESIDENT



Choice Properties completed its first full year in operation, expanded its portfolio through acquisitions, constructed new square footage, and had solid financial performance.

Loblaw is in a strong financial position, with a solid balance sheet, net assets of \$12.8 billion and adjusted debt of \$10.0 billion.

of our beauty business broadened with the opening of 26 additional *beautyBOUTIQUEs*. We also deepened our product offering and provided a wider assortment of prestige brands.

### **We are executing against our financial plan**

Coupled with our strategic framework, our financial plan is built on four key elements.

# we continue our relentless focus on providing an unsurpassed food experience to our customers

### **Our strategic framework is making us stronger**

Our Company's purpose, *Live Life Well*, is supported by a strategic framework: to be the best in food experience; to be the best in health and beauty; to obtain operational excellence; and to grow. In 2014, we delivered against this strategic framework.

As part of this strategy, we continued our relentless focus on providing an unsurpassed food experience to our customers. Our multi-format strategy offers convenient retail locations and differentiated store formats that fit the lifestyles and budgets of all Canadians. In 2014, we expanded our fresh assortment, added new multicultural products, and continued the introduction of *Inspire* format stores.

At the same time, we grew our unique competitive position in health and beauty. Our pharmacists administered over 1,000,000 flu shots in 2014 and provided additional health services like flu screening and treatment where permitted by law. The reach

The first element is maintaining a stable trading environment. We delivered steady, consistent sales and margin performance across each of our major businesses this year. We believe we are well-positioned competitively and see compelling traction in several major customer initiatives, including *PC Plus*, which has been rolled out across both our market and discount network of grocery stores; increased adoption of an expanded scope of services at our pharmacies; and the continued roll-out of enhanced *beautyBOUTIQUEs*.

Efficiencies, the second element of our financial plan, made meaningful progress at Loblaw with core supply chain, IT and administrative expenses continuing to moderate. Looking forward, we remain committed to achieving efficiencies in our business. A key component of this will be the result of completing the implementation and optimization of our new IT system. We realized an important milestone this year with SAP operating in substantially all of our corporate grocery stores.

The third element is synergies. For 2014, we recorded over \$100 million in net synergies, mostly benefitting cost of goods sold. We remain confident in delivering our target of realizing \$300 million in net synergies by the end of the third year following the close of the Shoppers Drug Mart acquisition.

The final element is deleveraging the balance sheet. We remain on track to achieve our deleveraging target by the first quarter of 2016, and have reduced our adjusted debt by almost \$1.1 billion since closing the acquisition. Despite our focus on debt reduction, we remained committed to a balanced capital return strategy and increased our dividend 3.7%.

### **Innovation and execution lead to long-term competitive advantage**

In 2015 we are making strategic investments in innovation to increase the effectiveness of our pharmacies; unlock additional opportunity in loyalty; offer an enhanced convenience food offering at Shoppers Drug Mart; and continue to grow our eCommerce platform. We believe these investments will result in a strengthened customer proposition, support long-term growth, and create compelling differentiators for us in the industry.

Innovation alone, however, does not translate into results. This year Loblaw also executed consistently, both operationally and financially. Throughout this annual report you will see many examples of how this execution across all of our businesses contributed to our strong performance.

### **Well-positioned for the future**

Looking forward, I am very encouraged by the opportunities we have in our business.

Loblaw is well-positioned as Canada's leader in food, health and beauty. We have a unique set of assets that is unparalleled in Canada which we are capitalizing

on through our portfolio of independent and complementary businesses.

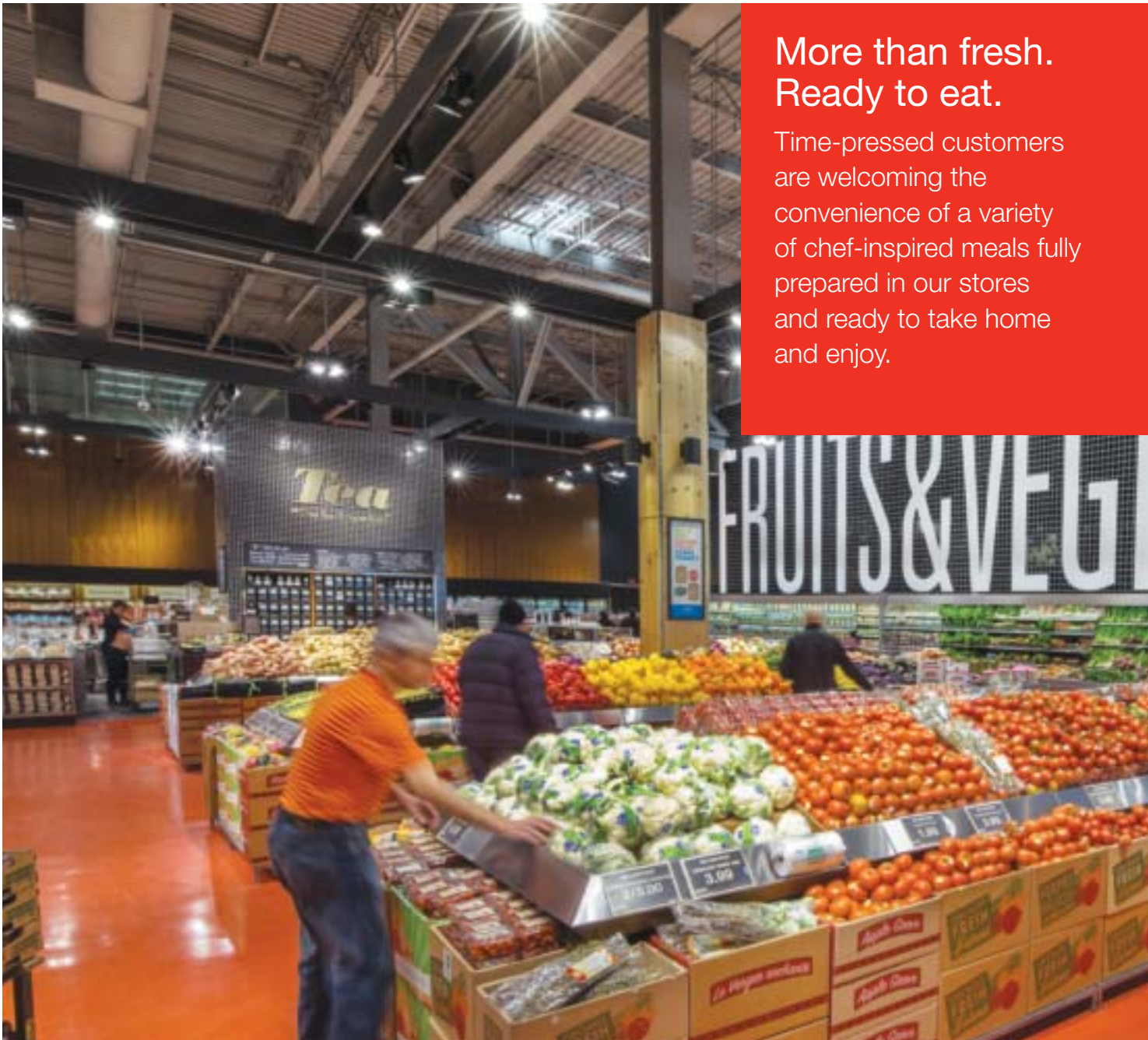
By remaining focused on delivering our purpose of *Live Life Well* and executing on our strategic framework and financial plan, we believe we will accrue long-term value for shareholders.



**GALEN G. WESTON**  
Executive Chairman & President

# Market

Our stores are coast to coast, with our Real Atlantic Superstore, Dominion, Zehrs, Your Independent Grocer and valu-mart banners in our Neighbour format and Loblaws and Provigo Le Marché in traditional and *Inspire* formats. Our mandate is to offer an exceptional fresh offering, breadth of assortment throughout the store and superb service, all of which deliver a competitive value proposition to our customers. With stores tailored to the demographics of each local market and strong ties to their communities, we earned higher net promoter scores for the fourth consecutive year.



**More than fresh.  
Ready to eat.**

Time-pressed customers are welcoming the convenience of a variety of chef-inspired meals fully prepared in our stores and ready to take home and enjoy.



More and more, customers want fresh and nutritious food. Increasingly, they also want *new* and *interesting* food. We are cultivating these food enthusiasts through our *Crave More* campaign,

and delivering a differentiated offering including an in-store chef's program with exclusive recipes from the chefs at the Loblaw's flagship store at Maple Leaf Gardens.\*



## innovation

Expanded our offering in nutritious and fresh food with the introduction of Fresh Juice Bars to over 140 stores and increased our presence in organic and lifestyle offerings.

Introduced ACE™ Bakery destinations to over 140 stores and our in-store chef's program of ready-to-eat products to more than 290 stores.

Helped our customers make smart food choices, by introducing full-time in-store dietitians, and expanded the Guiding Stars® nutrition program to Western and Eastern Canada.

Market stores introduced more products from our own *T&T Supermarket* and *ARZ Fine Foods* brands as we expand our health and multicultural offering.

## execution

We are making strides in growing our Market network of stores in the west. To date we have a total of 22 Market stores in the west, including our recently launched second Loblaw's CityMarket store in British Columbia.

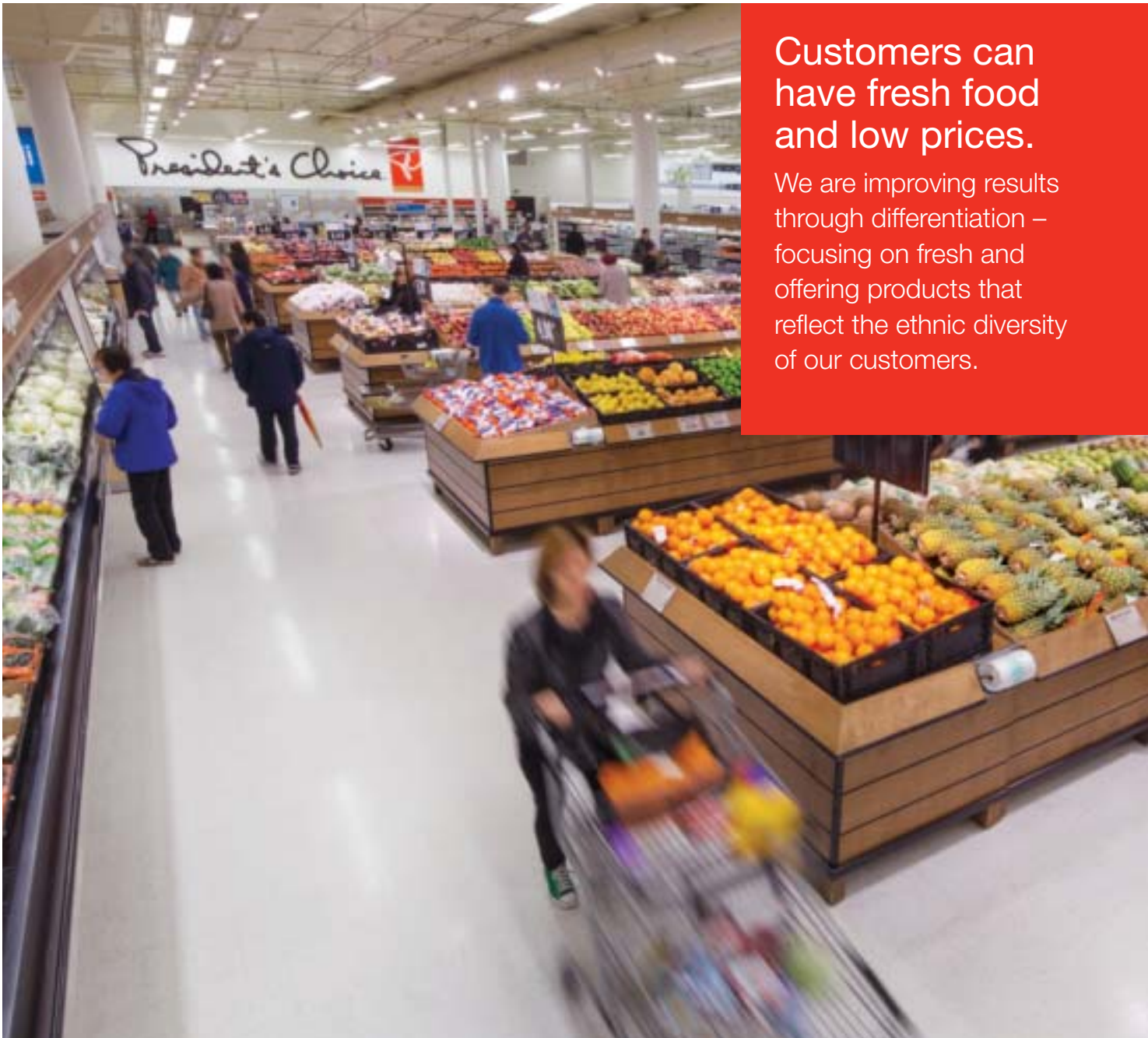
The *Inspire* format continues to drive food discovery with our customers. In 2015 we plan to roll out more than 10 new and renovated stores in the *Inspire* format.

Converted corporate-owned stores to franchises in Quebec, which strengthened the community ties and enhanced performance.

# Discount

Our stores are comprised of hard-discount and our Real Canadian Superstore formats, each delivering a distinct value proposition for consumers.

We are Canada's largest discount operator, with over 500 stores, including *NO FRILLS*, *Maxi*, and *Real Canadian Superstore*. Our mission is to make healthier choices more affordable and appealing, by delivering the lowest price and a differentiated fresh and multicultural offering.



Customers can have fresh food and low prices.

We are improving results through differentiation – focusing on fresh and offering products that reflect the ethnic diversity of our customers.



Leading with fresh, we offer great value on all grocery essentials. Our *NO FRILLS* and *Maxi* stores honour any competitor's advertised prices under our *Won't Be Beat* and

*Imbattable. Point final!* price-matching programs. We offer customers a straightforward shopping experience and cater to diverse lifestyles, including strong multicultural offerings.



## innovation

Introduced the already successful *PC Plus* loyalty program into our Discount format stores, one of the first in Canada.

Launched a project to re-envision our *Real Canadian Superstore* format to better serve the growing multicultural population.

Added a new assortment of products to our *natural-value* section such as gluten-free and organic products that would not be expected in discount stores.

## execution

We increased central sourcing to reduce procurement costs and gained efficiencies in labour.

To meet the growing demand for hard-discount format stores, we opened six more *NO FRILLS* stores in Western Canada.

# Emerging

Our emerging businesses include a range of retail operations and initiatives such as *Real Canadian Wholesale Club* and *Real Canadian Liquorstore* locations. Increasingly, the Emerging business has focused on serving Canada's growing multicultural population through store banners such as *Fortinos* and *T&T Supermarket*. All our stores reflect their surrounding communities; however, our Emerging stores offer specialty products to appeal to those with a taste for authentic cultural foods.



Our *T&T* stores offer authentic Asian products.

*T&T* also offers customers a unique assortment of their private label products in our Market and Discount format stores.



The stores in our Emerging business are growing to meet the needs of new Canadians. *T&T Supermarket* appeals to Asian tastes in fresh and prepared goods. *Fortinos* has a European style

and a focus on fresh meat and produce. In 2014, we acquired *ARZ Fine Foods*, a Toronto-based Middle Eastern bakery and grocery retailer.



## innovation

Our unique take on meals-to-go at *Fortinos* gives customers fresh, authentic take-home options including fresh pasta through the use of a *Pane Fresco* market.

In response to the growing trend in fresh noodles, *T&T* introduced noodle bars in selected stores and has seen positive results.

Introduced the Loblaw *PC Plus* program into our Loblaw Gas Bars.

## execution

*T&T* private label products sold through our other banners doubled in 2014.

The *Real Canadian Wholesale Club* renovation program began, completing the renovations of four stores including the introduction of walk-in meat coolers.

Our *Real Canadian Liquorstore* locations continue to add new control brand products.

# Shoppers Drug Mart

Shoppers Drug Mart/Pharmaprix has been at the forefront of retail pharmacy for over 50 years. Leveraging the strengths of our Associate owners and their pharmacy teams to deliver on the expanded scope of practice, we believe we can contribute to a sustainable health care system for all Canadians through improved patient outcome and greater accessibility.



## More than a drug store.

For Canadians who believe that being healthy means looking and feeling good, Shoppers Drug Mart is the trusted leader in taking care of the whole you by integrating health with beauty in easy and tangible ways.



Shoppers Drug Mart has successfully leveraged its leadership position in pharmacy and its convenient store locations to capture a significant share of the market in front store

merchandise, including over-the-counter medications, health and beauty aids, cosmetics and fragrances, seasonal products and everyday household essentials.



## innovation

Introduced the Patient Contact Centre which allows us to personally contact patients on behalf of their home pharmacy to ensure they are taking their medications as prescribed and help them stay on the appropriate therapy.

Broadened our enhanced *beautyBOUTIQUE* to four stores across Canada, including Calgary and Vancouver.

Launched pilot stores to test the enhanced convenience Food offering.

## execution

Same store pharmacy sales and prescription count grew 2.7% and 4.6%, respectively.

Front store same store sales grew on the back of market share gains.

Administered over 800,000 flu shots across Canada in 2014.

# The Value of Loyalty



**Loyalty programs drive sales.** The Shoppers Drug Mart *Optimum* card is one of Canada’s most successful loyalty programs with over 10 million active members. Digitizing the *Optimum* card – moving away from plastic and coupons and towards a mobile app – will allow for more personalized, one-to-one, marketing.

**The Loblaw *PC Plus* program** offers a technologically advanced loyalty program designed for use through a smart phone. It has grown to more than 8 million members in less than two years. Our *PC Plus* users shop more frequently and with bigger baskets. Our *PC Plus* customers receive personalized one-to-one offers, allowing them to earn points on the items they purchase the most.

Shoppers Drug Mart  
*Optimum* card has  
**10 million+**  
active members

**Loblaw *PC Plus* program**  
has grown to over  
**8 million**  
members in less than 2 years



# President's Choice Financial

Our financial services provide unprecedented value in everyday banking to Canadians. The result is a full range of *President's Choice Financial* services, complete with the *President's Choice Financial MasterCard*®, no fee daily banking and the ability to earn *PC* points.



## innovation

Launched a prepaid, reloadable *President's Choice Financial MasterCard*® and continue to look at opportunities to add even more value for our customers.

Launched an enhanced benefit for our *President's Choice Financial MasterCard*® customers through *PC* travel services, where cardholders can book travel online or by phone and earn more *PC* points.

A digital wallet was introduced with the launch of *UGO* wallet. *UGO* is an open digital wallet application that enables consumers to start replacing credit cards and loyalty cards from their physical wallet with a simple, secure digital payment method on their smart phone.

## execution

We continued to generate strong revenue and income growth.

*President's Choice Financial* continued to grow the volume of its credit card business while maintaining the high quality and creditworthiness of its portfolio.

## innovation

Delivering new styles at more than three times the rate of the industry, *Joe Fresh* continues to attract customers with new and fresh styling.

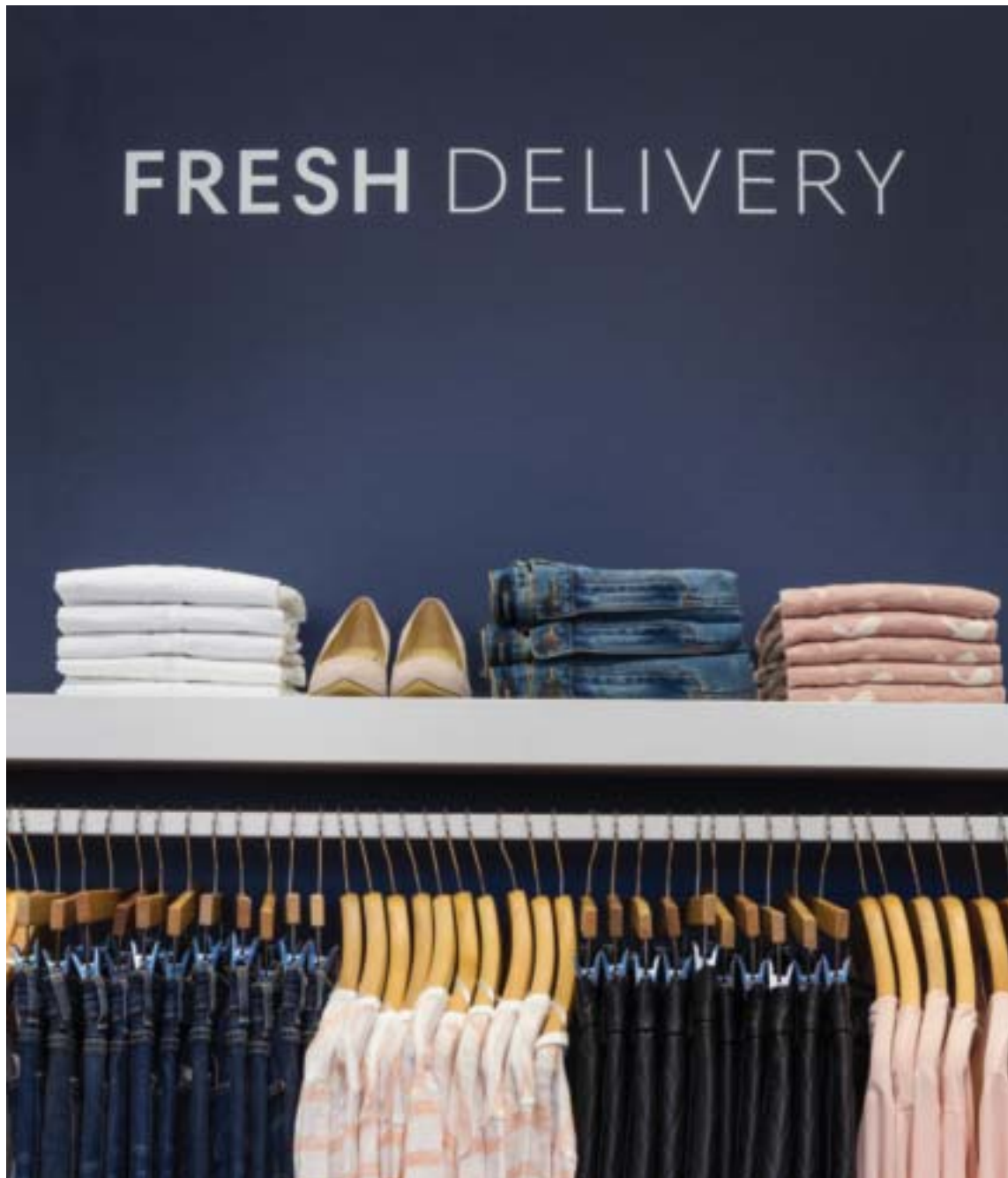
## execution

International expansion was furthered with the opening of *Joe Fresh* stores in three new countries in 2014, with stores slated to open in another two countries in 2015.

Domestic sales have experienced positive growth in 7 of the last 8 years.

# Joe Fresh

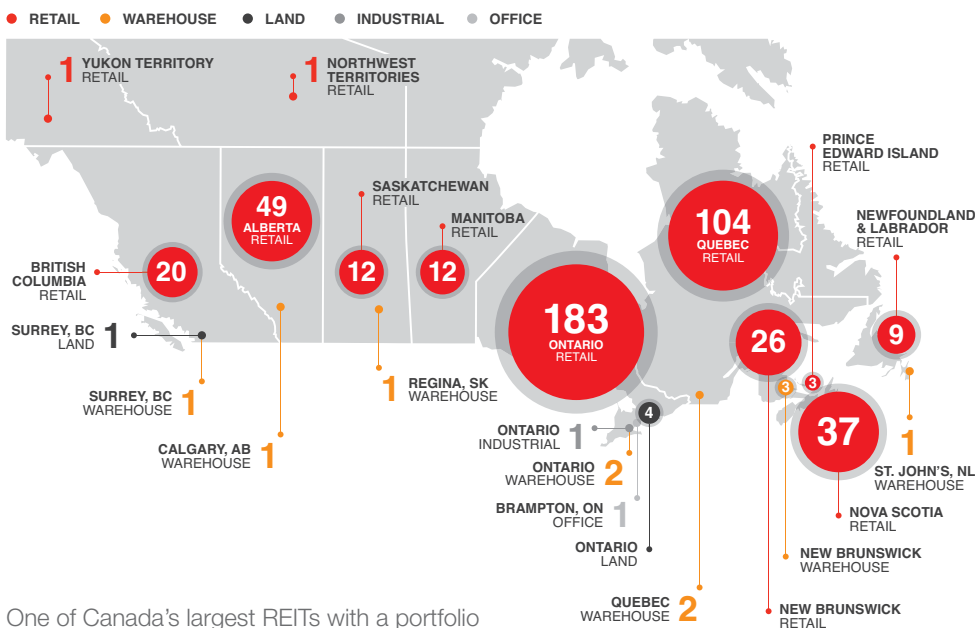
*Joe Fresh* offers stylish and affordable apparel, accessories and beauty for all seasons. It is the answer to consumers' desire for accessible, of-the-moment style. With collections for women, men and children, the label is designed to solve the family's fashion needs and is one of Canada's leading apparel brands.



# Choice Properties

Choice Properties, which is 82.9%-owned by Loblaw, used its first full year as a stand-alone, publicly traded company to build its portfolio and its capabilities. It acquired 37 more properties from Loblaw, taking its total to 472 across Canada, representing 38.9 million square feet at year-end.

## Property Portfolio



One of Canada's largest REITs with a portfolio consisting of **475<sup>1</sup> properties** spanning approximately **39.9<sup>1</sup> million sq. ft.**

<sup>1</sup> Includes acquisitions subsequent to December 31, 2014.

Choice Properties REIT units are listed on the Toronto Stock Exchange under the symbol CHP.UN. For more information, visit [choicereit.ca](http://choicereit.ca) or refer to the 2014 Annual Report of Choice Properties REIT.

## innovation

Choice Properties expanded its growth pipeline through strategic relationships and the acquisition of land. With an expanded team of real estate professionals through internalization, Choice Properties increased efficiency and created a strong platform for future growth.

## execution

Choice Properties expanded its asset base by 2.6 million square feet through acquisitions, and constructed 51,000 square feet of new retail space.

At year-end, Choice Properties' occupancy rate increased to 98%.



# Corporate Social Responsibility

Corporate Social Responsibility (CSR) is reflected in the way we do business at Loblaw, delivering products, services and experiences to our customers, and underpinning our Company purpose – *Live Life Well*.



As Canada's leader

in food and pharmacy, we have a unique opportunity to help Canadians through our strong commitment to Corporate Social Responsibility.

**1,700+**  
pharmacies

**\$15**  
million+  
in contributions  
to children's  
health

**\$9**  
million+  
in contributions  
to women's  
health

**7 billion+**  
fewer plastic  
shopping  
bags

In 2014, our CSR activities included new commitments – sodium reductions across our *President's Choice* products; helping forge a sustainability vision for the beef industry; new animal welfare standards – as well as meaningful advancements in the following long-standing commitments, among others:

- The Guiding Stars® nutrition-rating system was extended nationwide. And, we focused even more on fresh foods, through merchandising and assortments.
- Our Canadian-first sourcing pledge was amplified with the new Near You marketing program, highlighting a broader range of Canadian-grown and -produced fare than in years past.
- We now have rooftop solar panels at 62 facilities, and we completed lighting retrofits in more than 200 stores in 2014. Initiatives like these have driven double-digit declines in store electricity use since 2011.
- Workplace fire and safety standards introduced in 2013 in the wake of the Rana Plaza factory tragedy in Bangladesh were extended to Cambodia, Thailand, Sri Lanka, India and Vietnam, supported by a regional audit oversight team on the ground.
- Our seven-year effort to reduce plastic bag waste marked an important milestone when we surpassed a total of seven billion bags diverted from landfill.



In 2014, Shoppers Drug Mart joined the Loblaw family of companies. Together, our respective commitments to women, children, and the challenges they face position Loblaw to make increasingly meaningful contributions to our national community.

In 2014, *President's Choice* Children's Charity granted \$10.4 million to 2,021 families of children with disabilities and \$5 million to 2,271 child-nutrition programs. The Charity also marked its 25th anniversary, surpassing lifetime-total donations of \$116 million. The Shoppers Drug Mart WOMEN program granted \$9.5 million to various charities and programs supporting women's health and well-being. It continued its flagship event, the Shoppers Drug Mart *Run for WOMEN*, raising awareness and funds in support of local women's mental health organizations in ten communities across Canada.

Our Company purpose – *Live Life Well* – focuses our business and CSR activities on nutrition and wellness. In 2014, we put more dietitians and pharmacists in more communities, to help Canadians avoid, monitor, and manage health conditions ranging from bone health, to hypertension, to diabetes and more.

For more information on our CSR efforts, please visit [Loblaw.ca/csr](http://Loblaw.ca/csr); [pc.ca/charity](http://pc.ca/charity); [shoppersdrugmart.ca/women](http://shoppersdrugmart.ca/women).



# Corporate Governance Practices

The Board of Directors and senior executives of Loblaw Companies Limited are committed to sound corporate governance practices and believe they contribute to the effective management of the Company and its achievement of strategic and operational objectives.

The Governance Committee regularly reviews the Company's corporate governance practices and considers any changes necessary to maintain the Company's high standards of corporate governance in a rapidly changing environment. The Company's website, [loblaw.ca](http://loblaw.ca), sets out additional governance information, including the Company's Code of Conduct (the "Code"), its Disclosure Policy and the Mandates of the Board of Directors (the "Board") and its committees.

## Director independence

The Canadian Securities Administrators' Corporate Governance Guidelines provide that a director is independent if he or she has no material relationship with the Company or its affiliates that could reasonably be expected to interfere with the exercise of the director's independent judgment.

At least 60% of the directors on the Board are independent. The independent directors typically meet separately following each Board meeting and on other occasions as required or desirable.

Information relating to each of the directors, including their independence, committee membership, other public company boards on which they serve, as well as their attendance record for all Board and committee meetings, can be found in the Company's Management Proxy Circular.

## Board leadership

Galen G. Weston is the Executive Chairman of the Board. The Executive Chairman directs the operations of the Board. He chairs each meeting of the Board, is responsible for the management and effective functioning of the Board generally and provides leadership to the Board in all matters. These and other key responsibilities of the Executive Chairman are set out in a position description established by the Board.

The Board has also appointed an independent director, Thomas C. O'Neill, to serve as lead director. The lead director provides leadership to the Board and particularly to the independent directors. He ensures that the Board operates independently of management and that directors have an independent leadership contact.

## Board responsibilities and duties

The Board, directly and through its committees, supervises and oversees the management of the business and affairs of the Company. A copy of the Board's mandate can be found at [loblaw.ca](http://loblaw.ca). The Board reviews the Company's strategic direction, assigns responsibility to management for the achievement of that direction, approves major policy decisions, delegates to management the authority and responsibility of handling day-to-day affairs, and reviews management's performance and effectiveness. The Board's expectations of management are communicated to management directly and through committees of the Board.

The Board regularly receives reports on the operating results of the Company as well as reports on certain non-operational matters, including insurance, pensions, corporate governance, health and safety, legal and treasury matters. The Board also oversees the enterprise risk management (ERM) process, which is designed to assist all areas of the business in managing appropriate levels of risk tolerance by bringing a systematic approach, a methodology and tools for evaluating, measuring and monitoring key risks. The results of the ERM program and other business planning processes are used to identify emerging risks to the Company, prioritize risk management activities and develop a risk-based internal audit plan.



## **Ethical business conduct**

The Code reflects the Company's long-standing commitment to high standards of ethical conduct and business practices. The Code is reviewed annually to ensure it is current and reflects best practices in the area of ethical business conduct and includes a strong "tone from the top" message. All directors, officers and employees of the Company are required to comply with the Code and must acknowledge their commitment to abide by the Code on a periodic basis.

The Company encourages the reporting of violations and potential violations and has established an Integrity Action Line, a toll-free number that any director, officer or employee may use to report conduct which he or she feels violates the Code or otherwise constitutes fraudulent or unethical conduct. A fraud reporting protocol has also been implemented to ensure that fraud is reported to senior management in a timely manner. In addition, the Audit Committee has endorsed procedures for the anonymous receipt, retention and handling of complaints regarding accounting, internal control or auditing matters. These procedures are available at [loblaw.ca](http://loblaw.ca).

## **Board committees**

The following is a brief summary of some of the responsibilities of each committee of the Board.

### **Audit Committee**

The Audit Committee is responsible for supporting the Board in overseeing the quality and integrity of the Company's financial reporting and internal controls over financial reporting, disclosure controls, internal audit function, and compliance with legal and regulatory requirements.

### **Governance, Employee Development, Nominating and Compensation Committee**

The Governance Committee is responsible for the identification of new director nominees for the Board and for the oversight of compensation of directors and executive officers. The Governance Committee is also responsible for developing and maintaining governance

practices consistent with high standards of corporate governance. The Chair of the Governance Committee, who is an independent director, has also been appointed by the Board to serve as lead director.

### **Pension Committee**

The Pension Committee is responsible for reviewing the performance and overseeing the administration of the Company's and its subsidiaries' pension plans and pension funds.

### **Environmental, Health and Safety Committee**

The Environmental, Health and Safety Committee is responsible for reviewing and monitoring environmental affairs, food safety and workplace health and safety policies, procedures, practices and compliance.

### **Finance Committee**

The Finance Committee is responsible for assisting the Board in monitoring and reviewing the capital structure of the Company and the investment and financial risk programs of the Company.

# Board of Directors

Our Board represents the interests of all Loblaw stakeholders. Through its oversight of the management of the Company and its affairs, the Board actively demonstrates Loblaw's commitment to the principles of transparency, accountability and sound corporate governance.

**GALEN G. WESTON**, B.A., M.B.A.

Executive Chairman and President, Loblaw Companies Limited; Chairman and Trustee, Choice Properties Real Estate Investment Trust; Director, Wittington Investments, Limited.

**STEPHEN E. BACHAND**, B.A., M.B.A.<sup>2</sup>

Corporate Director; Retired President and Chief Executive Officer, Canadian Tire Corporation, Limited; Former Director, Canadian Pacific Railway Limited, George Weston Limited, Bank of Montreal.

**PAUL M. BEESTON**, C.M., B.A., F.C.A., F.C.P.A.<sup>1</sup>

President and Chief Executive Officer, Toronto Blue Jays Baseball Team; Former President and Chief Executive Officer, Major League Baseball; Director, President's Choice Bank, Gluskin Sheff & Associates Inc.; Former Chairman, Centre for Addiction and Mental Health; Former Director, Newport Partners Income Fund.

**PAVITER S. BINNING**, F.C.M.A.

President and Director, George Weston Limited; former Executive Vice President, Chief Financial Officer and Chief Restructuring Officer, Nortel Networks Corporation and Nortel Networks Limited; former Director and Chief Financial Officer, Hanson plc and Marconi Corporation plc.

**WARREN BRYANT**, B.S., M.B.A.<sup>1,4</sup>

Corporate Director; Former Chairman, President and Chief Executive Officer of Longs Drug Stores; former Executive of Kroger Co.; Director, Dollar General Corporation, Office Depot (formerly OfficeMax Incorporated); Member of the Executive Advisory Committee, Portland State University Food Industry Leadership Center; Former Director, George Weston Limited; Former Chairman of the Board of Directors and Former member of the Board Executive Committee, National Association of Chain Drug Stores ("NACDS"); Former member of the Board of Directors, California Governor's Council on Physical Fitness and Sports.

**CHRISTIE J.B. CLARK**, B. COMM., M.B.A., F.C.A., F.C.P.A.<sup>1,5</sup>

Corporate Director; Former Chief Executive Officer and Senior Partner, PricewaterhouseCoopers LLP; Trustee, Choice Properties Real Estate Trust; Director, Air Canada; Former Director, Brookfield Office Properties Inc., IGM

Financial Inc.; Chair, Finance Committee of Alpine Canada.

**ANTHONY R. GRAHAM**<sup>2,3</sup>

Vice Chairman and Director, Wittington Investments, Limited; President, Selfridges Group Limited; President and Chief Executive Officer, Sumarria Inc.; Former Vice-Chairman and Director, National Bank Financial; Director, President's Choice Bank, George Weston Limited, Brown Thomas Group Limited, Graymont Limited, Grupo Calidra, S.A. de C.V., Holt, Renfrew & Co., Limited, Power Corporation of Canada, Power Financial Corporation, Selfridges & Co. Ltd.; Director, Art Gallery of Ontario, Canadian Institute for Advanced Research, St. Michael's Hospital, Trans Canada Trail Foundation and Luminato; Chairman, Ontario Arts Foundation and the Shaw Festival Theatre Endowment Foundation.

**HOLGER KLUGE**, B. COMM., M.B.A.<sup>1,3</sup>

Corporate Director; Former President of Personal and Commercial Banking, Canadian Imperial Bank of Commerce; Former Director and Chairman, Shoppers Drug Mart Corporation; Former Director, Husky Energy Inc., Hutchinson Whampoa Limited, Power Assets Holdings Limited.

**JOHN S. LACEY**, B.A.<sup>3\*</sup>

Chairman of the Advisory Board, Brookfield Private Equity Group; Consultant to the Board and to the Board of George Weston Limited; Former President and Chief Executive Officer, the Oshawa Group (now part of Sobeys Inc.); Director, George Weston Limited, Telus Corporation, Ainsworth Lumber Co. Ltd.; Former Chairman, Alderwoods Group, Inc.; Former Director, Canadian Imperial Bank of Commerce.

**NANCY H.O. LOCKHART**, O. ONT.<sup>2,4\*</sup>

Corporate Director; Former Chief Administrative Officer, Frum Development Group; Former Vice President, Shoppers Drug Mart Corporation; Former President, Canadian Club of Toronto; Director, Barrick Gold Corporation, Gluskin Sheff & Associates Inc., Atrium Mortgage Investment Corporation, Centre for Addiction and Mental Health Foundation, Loran Scholars Foundation, The Royal Conservatory of Music; Chair, Crow's Theatre Company; Member, Sotheby's Canada Advisory Board; Former Chair,

Canadian Film Centre, Ontario Science Centre; Former Director, Canada Deposit Insurance Corporation.

**THOMAS C. O'NEILL**, B. COMM., F.C.A., F.C.P.A.<sup>2\*,5\*</sup>

Corporate Director; Chairman, BCE Inc.; Chairman, The Bank of Nova Scotia; Retired Chairman, PricewaterhouseCoopers Consulting; Former Chief Executive Officer and Chief Operating Officer, PricewaterhouseCoopers LLP; Director, Adecco S.A., BCE Inc., The Bank of Nova Scotia; Chair, St. Michael's Hospital; Member, Advisory Board at Queen's University School of Business; Former Vice Chair, Board of Trustees, Queen's University; Former Director of Nexen Inc.

**BETH PRITCHARD**, B.A., M.B.A.<sup>4</sup>

Principal and Strategic Advisor, Sunrise Beauty Studio, LLC; Former North American Advisor, M. H. Alshaya Co.; Former President and Chief Executive Officer and Vice Chairman of Dean & DeLuca, Inc.; Former President and Chief Executive Officer, Bath & Body Works; Former Chief Executive Officer, Victoria's Secret Beauty; Director, Cabela's Incorporated, The Vitamin Shoppe, Inc., Borderfree, Inc.; Former Director, Shoppers Drug Mart Corporation, Zale Corporation.

**SARAH RAISS**, B.S., M.B.A.<sup>2</sup>

Corporate Director; Former Executive, TransCanada Corporation; Director, Canadian Oil Sands Limited, Commercial Metals Company and Vermillion Energy Inc.; Chair, Alberta Electric System Operator Board of Directors; Former Director, Shoppers Drug Mart Corporation.

NOTES

<sup>1</sup> Audit Committee

<sup>2</sup> Governance, Employee Development, Nominating and Compensation Committee

<sup>3</sup> Pension Committee

<sup>4</sup> Environmental, Health and Safety Committee

<sup>5</sup> Finance Committee

\* Chair of the Committee

# Leadership

**GALEN G. WESTON**

Executive Chairman and President

**GRANT FROESE**

Chief Operating Officer

**RICHARD DUFRESNE**

Chief Financial Officer

**SARAH R. DAVIS**

Chief Administrative Officer

**MARK C. BUTLER**

Executive Vice President,  
Business Synergies

**ROBERT CHANT**

Senior Vice President,  
Corporate Affairs and  
Communication

**BARRY K. COLUMB**

President, President's Choice Financial

**GORDON A.M. CURRIE**

Executive Vice President and  
Chief Legal Officer

**MARIO GRAUSO**

President, Joe Fresh

**ANDREW IACOBUCCI**

President, Discount Division

**JUDY A. McCRIE**

Executive Vice President,  
Speed of Change and Culture

**PETER MCLAUGHLIN**

President, Emerging Business

**MIKE MOTZ**

President, Shoppers Drug Mart

**GARRY SENECAI**

President, Market Division

**MARY ALICE VUICIC**

Executive Vice President,  
Human Resources and  
Labour Relations



# Shareholder and Corporate Information

## NATIONAL HEAD OFFICE AND STORE SUPPORT CENTRE

Loblaw Companies Limited  
1 President's Choice Circle, Brampton, Canada L6Y 5S5  
Tel: (905) 459-2500 | Fax: (905) 861-2206 | Internet: loblaw.ca

## STOCK EXCHANGE LISTING AND SYMBOL

The Company's common shares and second preferred shares are listed on the Toronto Stock Exchange and trade under the symbols "L" and "L.PR.A", respectively.

## COMMON SHARES

W. Galen Weston, directly and indirectly, including through his controlling interest in Weston, owns approximately 46% of the Company's common shares.

At year-end 2014, there were 412,480,891 common shares issued and outstanding.

The average daily trading volume of the Company's common shares for 2014 was 751,814.

## PREFERRED SHARES

At year-end 2014, there were 9,000,000 second preferred shares issued and outstanding and available for public trading.

The average daily trading volume of the Company's second preferred shares for 2014 was 4,172.

## TRADEMARKS

Loblaw Companies Limited and its subsidiaries own a number of trademarks. Several subsidiaries are licensees of additional trademarks. These trademarks are the exclusive property of Loblaw Companies Limited or the licensor and, where used in this report, are in italics.

## COMMON DIVIDEND POLICY

The Company's dividend policy states: the declaration and payment of dividends and the amount thereof on the Company's common shares are at the discretion of the Board of Directors, which takes into account the Company's financial results, capital requirements, available cash flow, future prospects of the Company's business and other factors considered relevant from time to time.

## COMMON DIVIDEND DATES

The declaration and payment of quarterly dividends are made subject to approval by the Board of Directors. The anticipated record and payments dates for 2015 are:

RECORD DATE	PAYMENT DATE
March 15	April 1
June 15	July 1
September 15	October 1
December 15	December 30

## PREFERRED SHARE DIVIDEND DATES

The declaration and payment of quarterly dividends are made subject to approval by the Board. The anticipated payment dates for 2015 are January 31, April 30, July 31 and October 31.

## NORMAL COURSE ISSUER BID

The Company has a Normal Course Issuer Bid on the Toronto Stock Exchange.

## VALUE OF COMMON SHARES

For capital gains purposes, the valuation day (December 22, 1971) cost base for the Company is \$0.958 per common share. The value on February 22, 1994 was \$7.67 per common share.

## INVESTOR RELATIONS

Shareholders, security analysts and investment professionals should direct their requests to Sophia Bisoukis, Investor Relations, at the Company's National Head Office or by e-mail at: investor@loblaw.ca

## REGISTRAR AND TRANSFER AGENT

Computershare Investor Services Inc.  
100 University Avenue  
Toronto, Canada M5J 2Y1  
Toll-free: 1-800-564-6253  
(Canada and the U.S.)  
Fax: (416) 263-9394  
Toll-free fax: 1-888-453-0330  
International direct dial: (514) 982-7555

To change your address, eliminate multiple mailings, or for other shareholder account inquiries, please contact Computershare Investor Services Inc.

Additional financial information has been filed electronically with various securities regulators in Canada through the System for Electronic Document Analysis and Retrieval (SEDAR) and with the Office of the Superintendent of Financial Institutions (OSFI) as the primary regulator for the Company's subsidiary, President's Choice Bank.

## INDEPENDENT AUDITORS

KPMG LLP  
Chartered Accountants  
Toronto, Canada

## ANNUAL MEETING

The 2015 Annual Meeting of Shareholders of Loblaw Companies Limited will be held on Thursday, May 7, 2015 at 11:00 a.m. (EST), at the Mattamy Athletic Centre, 50 Carlton Street, Toronto, Canada M5B 1J2.



# INNOVATION & EXECUTION

**Loblaws**  
COMPANIES LIMITED

LOBLAW COMPANIES LIMITED 2014 ANNUAL REPORT –  
FINANCIAL REVIEW



## 2014 Annual Report – Financial Review

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### Footnote Legend

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- (1) For financial definitions and ratios refer to the Glossary of Terms on page 119.
  - (2) See Section 20 “Non-GAAP Financial Measures”.
  - (3) Certain 2012 figures have been restated and amended due to the implementation of revised IAS 19, “Employee Benefits” and to conform with the current year’s presentation, respectively.
  - (4) Certain 2013 figures have been amended to conform with the current year’s presentation. See Section 20 “Non-GAAP Financial Measures” and Section 18.1 “Accounting Standards Implemented in 2014”.
  - (5) For segment presentation purposes, the results are for the periods ended December 31, 2014 and December 31, 2013, consistent with Choice Properties’ fiscal calendar. Adjustments to January 3, 2015 and December 28, 2013 are included in Consolidation and Eliminations. See Section 20 “Non-GAAP Financial Measures”.
  - (6) Results are on an equivalent week basis and exclude the results of Shoppers Drug Mart. For Shoppers Drug Mart fourth quarter of 2014 results, please see Addendum A in the Company’s Fourth Quarter 2014 News Release.
  - (7) For segment presentation purposes, the results are for the period ended December 31, 2014, consistent with Financial Services’ fiscal calendar. Adjustments to January 3, 2015 are included in Consolidation and Eliminations. See Section 20 “Non-GAAP Financial Measures”. This represents a change from the prior year whereby results were presented consistent with the Company’s reporting calendar. The results for 2012 and 2013 have not been restated.
-



# Financial Highlights<sup>(1)</sup>

As at or for the years ended January 3, 2015 and December 28, 2013

(millions of Canadian dollars except where otherwise indicated)

	2014 (53 weeks)	2013 <sup>(4)</sup> (52 weeks)
<b>Consolidated Results of Operations</b>		
Revenue	\$ 42,611	\$ 32,371
Operating income	662	1,321
Adjusted operating income <sup>(2)</sup>	2,181	1,282
EBITDA <sup>(2)</sup>	2,134	2,145
Adjusted EBITDA <sup>(2)</sup>	3,236	2,106
Net interest expense and other financing charges	584	468
Adjusted net interest expense and other financing charges <sup>(2)</sup>	529	354
Net earnings	53	627
Adjusted net earnings <sup>(2)</sup>	1,224	696
<b>Consolidated Financial Position and Cash Flows</b>		
Adjusted debt <sup>(2)</sup>	9,995	6,288
Cash and cash equivalents, short term investments and security deposits	1,027	4,251
Cash flows from operating activities	2,569	1,491
Capital investments	1,086	877
Free cash flow <sup>(2)</sup>	977	244
<b>Consolidated Per Common Share (\$)</b>		
Basic net earnings	0.14	2.23
Adjusted basic net earnings <sup>(2)</sup>	3.22	2.48
<b>Consolidated Financial Measures and Ratios</b>		
Revenue growth	31.6%	2.4%
Adjusted operating margin <sup>(2)</sup>	5.1%	4.0%
Adjusted EBITDA margin <sup>(2)</sup>	7.6%	6.5%
Adjusted debt <sup>(2)</sup> to adjusted EBITDA <sup>(2)</sup>	3.1x	3.0x
<b>Retail Results of Operations</b>		
Sales	\$ 41,731	\$ 31,600
Gross profit	9,734	6,961
Adjusted gross profit <sup>(2)</sup>	10,722	6,961
Operating income	497	1,180
Adjusted operating income <sup>(2)</sup>	2,002	1,138
Adjusted EBITDA <sup>(2)</sup>	3,038	1,947
<b>Retail Operating Statistics</b>		
Same-store sales <sup>(1), (4)</sup> growth	2.0%	1.1%
Adjusted gross profit percentage <sup>(2)</sup>	25.7%	22.0%
Adjusted operating margin <sup>(2)</sup>	4.8%	3.6%
Adjusted EBITDA margin <sup>(2)</sup>	7.3%	6.2%
Total retail square footage (in millions)	70.0	51.9
Number of corporate stores	615	570
Number of franchise stores	527	496
Number of Associate-owned drug stores	1,302	—
<b>Financial Services Results of Operations<sup>(7)</sup></b>		
Revenue	\$ 810	\$ 739
Operating income	164	142
Earnings before income taxes	111	93
<b>Financial Services Operating Measures and Statistics<sup>(7)</sup></b>		
Average quarterly net credit card receivables	\$ 2,535	\$ 2,345
Credit card receivables	2,630	2,538
Allowance for credit card receivables	54	47
Annualized yield on average quarterly gross credit card receivables	13.7%	13.6%
Annualized credit loss rate on average quarterly gross credit card receivables	4.4%	4.2%
<b>Choice Properties Results of Operations<sup>(5)</sup></b>		
Revenue	\$ 683	\$ 319
Operating income	568	370
Net interest expense and other financing charges	369	303
<b>Choice Properties Operating Measure<sup>(5)</sup></b>		
Adjusted funds from operations <sup>(2)</sup>	\$ 285	\$ 131

## Management's Discussion and Analysis

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The following Management's Discussion and Analysis ("MD&A") for Loblaw Companies Limited and its subsidiaries (collectively, the "Company" or "Loblaw") should be read in conjunction with the annual audited consolidated financial statements and the accompanying notes on pages 55 to 117 of this Annual Report – Financial Review ("Annual Report").

The Company's annual audited consolidated financial statements and accompanying notes for the year ended January 3, 2015 have been prepared in accordance with International Financial Reporting Standards ("IFRS" or "GAAP") and include the accounts of the Company and other entities that the Company controls and are reported in Canadian dollars, except where otherwise noted.

The information in this MD&A is current to February 25, 2015, unless otherwise noted. A glossary of terms used throughout this Annual Report can be found on page 119.

Unless otherwise indicated, all comparisons of results for the fourth quarter of 2014 (13 weeks ended January 3, 2015) are against results for the fourth quarter of 2013 (12 weeks ended December 28, 2013) and all comparisons of results for the full year of 2014 (53 weeks ended January 3, 2015) are against the results for the full year of 2013 (52 weeks ended December 28, 2013).

## 1. Forward-Looking Statements

This Annual Report, including this MD&A, for the Company contains forward-looking statements about the Company's objectives, plans, goals, aspirations, strategies, financial condition, results of operations, cash flows, performance, prospects and opportunities. Specific forward-looking statements in this Annual Report include, but are not limited to, statements with respect to the Company's anticipated future results, events and plans, synergies and other benefits associated with the acquisition of Shoppers Drug Mart Corporation ("Shoppers Drug Mart"), future liquidity and debt reduction targets, planned capital investments, and status and impact of information technology ("IT") systems implementation. These specific forward-looking statements are contained throughout this Annual Report including, without limitation, in Section 3 "Strategic Framework", Section 9.2 "Liquidity and Capital Structure" and Section 19 "Outlook" of this MD&A. Forward-looking statements are typically identified by words such as "expect", "anticipate", "believe", "foresee", "could", "estimate", "goal", "intend", "plan", "seek", "strive", "will", "may", "on track" and "should" and similar expressions, as they relate to the Company and its management.

Forward-looking statements reflect the Company's current estimates, beliefs and assumptions, which are based on management's perception of historical trends, current conditions and expected future developments, as well as other factors it believes are appropriate in the circumstances. The Company's expectation of operating and financial performance in 2015 is based on certain assumptions including assumptions about anticipated cost savings, operating efficiencies and continued growth from current initiatives. The Company's estimates, beliefs and assumptions are inherently subject to significant business, economic, competitive and other uncertainties and contingencies regarding future events and as such, are subject to change. The Company can give no assurance that such estimates, beliefs and assumptions will prove to be correct.

Numerous risks and uncertainties could cause the Company's actual results to differ materially from those expressed, implied or projected in the forward-looking statements, including those described in Section 15 "Enterprise Risks and Risk Management" of this MD&A and the Company's Annual Information Form (for the year ended January 3, 2015). Such risks and uncertainties include:

- failure to realize the anticipated strategic benefits or operational, competitive and cost synergies following the acquisition of Shoppers Drug Mart;
- failure to reduce indebtedness associated with the acquisition of Shoppers Drug Mart to bring leverage ratios to a level consistent with investment grade ratings;
- failure to realize benefits from investments in the Company's IT systems, including the Company's IT systems implementation, or unanticipated results from these initiatives;
- failure to realize anticipated results, including revenue growth, anticipated cost savings or operating efficiencies from the Company's major initiatives, including those from restructuring;
- the inability of the Company's IT infrastructure to support the requirements of the Company's business;
- changes in the Company's estimate of inventory cost as a result of its IT system upgrade;
- changes to the regulation of generic prescription drug prices and the reduction of reimbursements under public drug benefit plans and the elimination or reduction of professional allowances paid by drug manufacturers;
- failure to achieve desired results in labour negotiations, including the terms of future collective bargaining agreements, which could lead to work stoppages;
- heightened competition, whether from current competitors or new entrants to the marketplace;
- changes in economic conditions, including the rate of inflation or deflation, changes in interest and currency exchange rates and derivative and commodity prices;



## Management's Discussion and Analysis

- changes in the Company's income, capital, commodity, property and other tax and regulatory liabilities, including changes in tax laws, regulations or future assessments;
- the inability of the Company to manage inventory to minimize the impact of obsolete or excess inventory and to control shrink;
- the risk that the Company would experience a financial loss if its counterparties fail to meet their obligations in accordance with the terms and conditions of their contracts with the Company; and
- the inability of the Company to collect on and fund its credit card receivables.

This is not an exhaustive list of the factors that may affect the Company's forward-looking statements. Other risks and uncertainties not presently known to the Company or that the Company presently believes are not material could also cause actual results or events to differ materially from those expressed in its forward-looking statements. Additional risks and uncertainties are discussed in the Company's materials filed with the Canadian securities regulatory authorities from time to time, including, without limitation, the section entitled "Risks" in the Company's Annual Information Form (for the year ended January 3, 2015). Readers are cautioned not to place undue reliance on these forward-looking statements, which reflect the Company's expectations only as of the date of this MD&A. Except as required by law, the Company does not undertake to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

### 2. Overview

Loblaw Companies Limited includes retail businesses, a bank and a real estate company. The Company has three operating segments: Retail, Financial Services and Choice Properties Real Estate Investment Trust ("Choice Properties"). The Retail segment consists primarily of a discount supermarket business, a full-service supermarket business, an emerging and wholesale business and Shoppers Drug Mart. The Company's Financial Services segment provides retail banking, credit card services, auto, home, travel and pet insurance and wireless mobile products and services. The Company also holds an 82.9% effective interest in Choice Properties, which owns, leases and manages income-producing commercial properties.

### 3. Strategic Framework

The Company's strategic framework is anchored by its vision to help Canadians "*Live Life Well*" and its commitment to produce industry leading financial results through operational excellence. At the core of this framework is our focus on the customer – by providing the best in food experience and the best in health and beauty.

Achieving a "best in food" experience is driven by our desire to lead in fresh selection, drive sustainable and competitive pricing and provide customized assortments across our banners. Achieving "best in health and beauty" is driven by our pharmacies putting customers first, our desire to provide high quality health and wellness products, a diverse and differentiated beauty offering and convenient locations and hours of operations to meet individuals' wellness needs.

The Company's operational excellence goals include driving efficiencies and realizing synergies from its business acquisitions, particularly the acquisition of Shoppers Drug Mart. We are focused on continued growth from President's Choice Financial Services, Choice Properties, product innovation, our emerging businesses and loyalty program initiatives.

#### 4. Key Financial Performance Indicators

The Company has identified key financial performance indicators to measure the progress of short and long term objectives. With the completion of the acquisition of Shoppers Drug Mart, the Company's 2014 results include the consolidation of Shoppers Drug Mart and the associated acquisition-related accounting adjustments. Certain key financial performance indicators are set out below:

As at or for the years ended January 3, 2015 and December 28, 2013 (millions of Canadian dollars except where otherwise indicated)	2014 (53 weeks)	2013 <sup>(4)</sup> (52 weeks)
<b>Consolidated:</b>		
Revenue growth	31.6%	2.4%
EBITDA <sup>(2)</sup>	\$ 2,134	\$ 2,145
Adjusted EBITDA <sup>(2)</sup>	3,236	2,106
Adjusted EBITDA margin <sup>(2)</sup>	7.6%	6.5%
Operating income	\$ 662	\$ 1,321
Adjusted operating income <sup>(2)</sup>	2,181	1,282
Adjusted operating margin <sup>(2)</sup>	5.1%	4.0%
Net earnings	\$ 53	\$ 627
Adjusted net earnings <sup>(2)</sup>	1,224	696
Basic net earnings per common share (\$)	0.14	2.23
Adjusted basic net earnings per common share <sup>(2)</sup> (\$)	3.22	2.48
Cash and cash equivalents, short term investments and security deposits	1,027	4,251
Cash flows from operating activities	2,569	1,491
Adjusted debt <sup>(2)</sup> to adjusted EBITDA <sup>(2)</sup>	3.1x	3.0x
Free cash flow <sup>(2)</sup>	\$ 977	\$ 244
Adjusted debt <sup>(2)</sup>	9,995	6,288
<b>Retail Segment:</b>		
Same-store sales <sup>(1), (6)</sup> growth	2.0%	1.1%
Gross profit	\$ 9,734	\$ 6,961
Adjusted gross profit <sup>(2)</sup>	10,722	6,961
Adjusted gross profit % <sup>(2)</sup>	25.7%	22.0%
Adjusted operating margin <sup>(2)</sup>	4.8%	3.6%
Adjusted EBITDA margin <sup>(2)</sup>	7.3%	6.2%
<b>Financial Services Segment<sup>(7)</sup>:</b>		
Earnings before income taxes	\$ 111	\$ 93
Annualized yield on average quarterly gross credit card receivables	13.7%	13.6%
Annualized credit loss rate on average quarterly gross credit card receivables	4.4%	4.2%
<b>Choice Properties Segment<sup>(5)</sup>:</b>		
Adjusted funds from operations <sup>(2)</sup>	\$ 285	\$ 131

During 2014, the Company introduced two new financial measures to the key financial performance indicators: Retail segment adjusted gross profit<sup>(2)</sup> and Retail segment adjusted gross profit percentage<sup>(2)</sup>, which are both non-GAAP financial measures. Management uses these and other non-GAAP financial measures to exclude the impact of certain expenses and income that must be recognized under GAAP when analyzing consolidated and segment underlying operating performance, as the excluded items are not necessarily reflective of the Company's underlying operating performance and make comparisons between periods difficult. From time to time, the Company may exclude additional items if it believes doing so would result in a more effective analysis of underlying operating performance. The exclusion of certain items does not imply that they are non-recurring. See Section 20 "Non-GAAP Financial Measures" for more information on the Company's non-GAAP financial measures.

## 5. Overall Financial Performance

### 5.1 Significant Accomplishments in 2014

**Acquisition of Shoppers Drug Mart** On March 28, 2014, the Company acquired all of the outstanding shares of Shoppers Drug Mart for total consideration of \$12,273 million, comprised of approximately \$6,600 million of cash and the issuance of approximately 119.5 million common shares of the Company. The cash portion of the acquisition was partially funded by the issuance of \$5,100 million of debt.

During 2014, the Company realized approximately \$101 million of net synergies generated primarily from improved cost of goods sold and from purchasing efficiencies in goods not for resale. Loblaw continues to expect to achieve annualized synergies of \$300 million in the third full year following the close of the acquisition of Shoppers Drug Mart (net of related costs).

**Deleveraging** On closing of the acquisition of Shoppers Drug Mart, adjusted debt<sup>(2)</sup> was \$11,060 million. The Company made significant progress in meeting its debt reduction target by decreasing adjusted debt<sup>(2)</sup> by \$1,065 million since the closing of the acquisition of Shoppers Drug Mart resulting in an outstanding adjusted debt<sup>(2)</sup> balance of \$9,995 million as at January 3, 2015. The reduction in adjusted debt<sup>(2)</sup> since closing included the repayment of a \$350 million medium term note ("MTN") and a repayment of the unsecured term loan facility (net of the replacement of all tranches of inter-corporate debt of Choice Properties initially held by Loblaw and sold to unrelated parties).

**Information Technology and Other Systems Implementations** As of the end of 2014, the Company completed the conversion of substantially all of its corporate grocery locations and associated distribution centres to the new IT systems.

### 5.2 Consolidated Results of Operations

For the years ended January 3, 2015 and December 28, 2013 (millions of Canadian dollars except where otherwise indicated)	2014 (53 weeks)	2013 <sup>(4)</sup> (52 weeks)	\$ Change	% Change
Revenue	\$ 42,611	\$ 32,371	\$ 10,240	31.6 %
<i>Revenue excluding Shoppers Drug Mart</i>	<i>33,561</i>	<i>32,371</i>	<i>1,190</i>	<i>3.7 %</i>
EBITDA <sup>(2)</sup>	\$ 2,134	\$ 2,145	\$ (11)	(0.5)%
Adjusted EBITDA <sup>(2)</sup>	3,236	2,106	1,130	53.7 %
Adjusted EBITDA margin <sup>(2)</sup>	7.6%	6.5%		
<i>Adjusted EBITDA<sup>(2)</sup> excluding Shoppers Drug Mart</i>	<i>\$ 2,248</i>	<i>\$ 2,106</i>	<i>\$ 142</i>	<i>6.7 %</i>
<i>Adjusted EBITDA margin<sup>(2)</sup> excluding Shoppers Drug Mart</i>	<i>6.7%</i>	<i>6.5%</i>		
Operating income	\$ 662	\$ 1,321	\$ (659)	(49.9)%
Adjusted operating income <sup>(2)</sup>	2,181	1,282	899	70.1 %
Adjusted operating margin <sup>(2)</sup>	5.1%	4.0%		
<i>Adjusted operating income<sup>(2)</sup> excluding Shoppers Drug Mart</i>	<i>\$ 1,397</i>	<i>\$ 1,282</i>	<i>\$ 115</i>	<i>9.0 %</i>
<i>Adjusted operating income margin<sup>(2)</sup> excluding Shoppers Drug Mart</i>	<i>4.2%</i>	<i>4.0%</i>		
Net interest expense and other financing charges	\$ 584	\$ 468	\$ 116	24.8 %
Adjusted net interest expense and other financing charges <sup>(2)</sup>	529	354	175	49.4 %
Net earnings	53	627	(574)	(91.5)%
Adjusted net earnings <sup>(2)</sup>	1,224	696	528	75.9 %
Basic net earnings per common share (\$)	0.14	2.23	(2.09)	(93.7)%
Adjusted basic net earnings per common share <sup>(2)</sup> (\$)	3.22	2.48	0.74	29.8 %

With the completion of the acquisition of Shoppers Drug Mart in 2014, the Company's results include the consolidation of Shoppers Drug Mart from the date of acquisition. The Shoppers Drug Mart assets were recognized in the Company's financial results at their fair value, including:

- a fair value increase to Shoppers Drug Mart's inventory on the date of acquisition of \$798 million, which was fully recognized in cost of merchandise inventories sold with a resulting negative impact on gross profit; and
- a \$6,050 million increase for the acquisition of definite life intangible assets, which is being amortized over their estimated useful lives. In 2014, \$417 million of related amortization was recognized in operating income. Annual amortization of approximately \$550 million associated with these intangibles will be recognized over the next ten years and decreasing thereafter.



The Company also recognized acquisition-related costs and a net divestitures loss of \$72 million (2013 – \$6 million) in selling, general and administrative expenses (“SG&A”) and \$15 million (2013 – \$25 million) in net interest expenses and other financing charges related to the acquisition of Shoppers Drug Mart and the divestitures required by the Competition Bureau.

With the upgrade of its IT infrastructure, the Company completed the conversion of substantially all of its corporate grocery locations to a perpetual inventory management system in 2014. As a result, the Company recognized a \$190 million decrease in the value of inventory in gross profit. The implementation of a perpetual inventory system, combined with visibility to integrated costing information provided by the new IT systems enables the Company to estimate the cost of inventory using a more precise system-generated average cost.

In 2014, the Company restructured its fee arrangements with the franchisees of certain franchise banners. These revised arrangements are expected to result in an annual reduction of Retail segment sales of approximately \$150 million and a corresponding decrease in SG&A. As a result of this restructuring, the Company re-evaluated the recoverable amount of franchise-related financial instruments and recorded a reduction in previously recorded impairment of \$40 million.

In 2014, the Company recorded \$46 million (2013 – \$35 million) in restructuring and reorganization costs primarily associated with the reduction of corporate and store-support positions, the departure of certain executives and the realignment of certain of the Company’s central office functions.

The Company’s 2014 financial results also included a charge of \$37 million (2013 – \$25 million), related to the transition of certain grocery stores to more cost effective and efficient operating terms under collective agreements.

**Revenue** Revenue of \$42,611 million in 2014 increased by \$10,240 million compared to 2013, primarily due to Shoppers Drug Mart and the impact of the 53rd week in 2014. Revenue in the 53rd week of 2014 was \$789 million (\$574 million excluding Shoppers Drug Mart). Excluding the impact of Shoppers Drug Mart, consolidated revenue increased by \$1,190 million, or 3.7%. Excluding the impact of Shoppers Drug Mart and the 53rd week of 2014, consolidated revenue increased by \$616 million, or 1.9%.

For the years ended January 3, 2015 and December 28, 2013 (millions of Canadian dollars except where otherwise indicated)	2014 (53 weeks)	2013 <sup>(4)</sup> (52 weeks)	\$ Change	% Change
EBITDA <sup>(2)</sup>	\$ 2,134	\$ 2,145	\$ (11)	(0.5)%
Adjustments to EBITDA <sup>(2)</sup>	1,102	(39)		
Adjusted EBITDA <sup>(2)</sup>	\$ 3,236	\$ 2,106	\$ 1,130	53.7 %
Operating income	\$ 662	\$ 1,321	\$ (659)	(49.9)%
Adjustments to EBITDA <sup>(2)</sup>	1,102	(39)		
Amortization of intangible assets acquired with Shoppers Drug Mart	417			
Adjusted operating income <sup>(2)</sup>	\$ 2,181	\$ 1,282	\$ 899	70.1 %

**EBITDA<sup>(2)</sup>** EBITDA<sup>(2)</sup> of \$2,134 million in 2014 decreased by \$11 million compared to 2013. The decrease in EBITDA<sup>(2)</sup> was negatively impacted by adjustments of \$1,102 million including the full recognition of the fair value increment on the acquired Shoppers Drug Mart inventory sold (\$798 million), the charge related to inventory measurement and other conversion differences associated with the implementation of a perpetual inventory system (\$190 million), increased costs related to the acquisition of Shoppers Drug Mart and a net divestitures loss (\$66 million), year-over-year unfavourable fixed asset and other related impairments (\$48 million), a gain related to defined benefit plan amendments recorded in 2013 (\$51 million), increased restructuring and reorganization costs (\$11 million) and certain other items (\$17 million). These increases were partially offset by restructuring of franchise fees (\$40 million).

After excluding these adjustments, adjusted EBITDA<sup>(2)</sup> of \$3,236 million increased by \$1,130 million compared to 2013. The increase included \$988 million of adjusted EBITDA<sup>(2)</sup> contributed by Shoppers Drug Mart, with the remainder of the increase of \$142 million primarily driven by the Retail segment. The increase was positively impacted by net synergies of \$101 million and the 53rd week in 2014 of \$71 million. Adjusted EBITDA margin<sup>(2)</sup> was 7.6% compared to 6.5% in 2013. Excluding the impact of Shoppers Drug Mart, adjusted EBITDA<sup>(2)</sup> increased by \$142 million, or 6.7%, compared to 2013 and adjusted EBITDA margin<sup>(2)</sup> was 6.7%, compared to 6.5% in 2013.

**Operating Income** Operating income of \$662 million in 2014 decreased by \$659 million compared to 2013, primarily driven by the acquisition-related accounting adjustments of Shoppers Drug Mart. Operating income was negatively impacted by the net adjustments related to EBITDA<sup>(2)</sup> noted above of \$1,102 million and the amortization of intangible assets of \$417 million related to the acquisition of Shoppers Drug Mart.

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After excluding these impacts to operating income, adjusted operating income<sup>(2)</sup> of \$2,181 million increased by \$899 million compared to 2013, including \$784 million of adjusted operating income<sup>(2)</sup> contributed by Shoppers Drug Mart. Adjusted operating margin<sup>(2)</sup> was 5.1% compared to 4.0% in 2013. Excluding the impact of Shoppers Drug Mart, adjusted operating income<sup>(2)</sup> increased by \$115 million and was positively impacted by the increase described in adjusted EBITDA<sup>(2)</sup> noted above of \$142 million, partially offset by an increase in depreciation and amortization<sup>(2)</sup> of \$27 million.

**Net Interest Expense and Other Financing Charges** Net interest expense and other financing charges of \$584 million in 2014 increased by \$116 million compared to 2013, including non-recurring charges incurred in 2013 related to Choice Properties initial public offering ("IPO") transaction costs and early debt settlement costs, and certain other adjustments as set out in Section 20 "Non-GAAP Financial Measures".

After excluding these impacts to net interest expense and other financing charges, adjusted net interest expense and other financing charges<sup>(2)</sup> of \$529 million increased by \$175 million, primarily driven by higher interest on long term debt, primarily as a result of debt incurred to finance the acquisition of Shoppers Drug Mart and distributions paid by Choice Properties on its Units, partially offset by a decrease in net interest on the post-employment and other long term employee benefits.

**Income Taxes** Income tax expense for 2014 was \$25 million and the effective tax rate was 32.1%. Income tax expense for 2013 was \$226 million and the effective tax rate was 26.5%. The increase in the effective tax rate compared to 2013 was primarily attributable to a decrease in certain non-taxable amounts. The adjusted income tax expense<sup>(2)</sup> for 2014 was \$428 million and the adjusted income tax rate<sup>(2)</sup> was 25.9%. The adjusted income tax expense<sup>(2)</sup> for 2013 was \$232 million and the adjusted income tax rate<sup>(2)</sup> was 25.0%. The increase in the adjusted income tax rate<sup>(2)</sup> was primarily attributable to a decrease in certain non-taxable amounts.

In 2012, the Company received indication from the Canada Revenue Agency (the "CRA") that the CRA intends to proceed with reassessments of the tax treatment of the Company's wholly owned subsidiary, Glenhuron Bank Limited ("Glenhuron"). The CRA's position is that certain income earned by Glenhuron in Barbados in respect of the 2000 to 2010 taxation years should be treated, and taxed, as income in Canada.

Based on the proposal letter from the CRA, if the CRA and the relevant provincial tax authorities were to prevail in all of these reassessments, which the Company believes would be unlikely, the estimated total tax and interest for the 2000 to 2010 taxation years would be approximately \$440 million, which would increase as interest accrues. However, the Company is in discussions with the CRA about the amount of taxes in dispute. The Company believes it is likely that the CRA and the relevant provincial tax authorities will issue reassessments for 2011 to 2013 on the same or similar basis. No amount for any reassessments has been provided for in the Company's consolidated financial statements.

Subsequent to the end of 2014, the Company received a letter from the CRA stating that the CRA will be proceeding with the reassessments. The Company expects to receive reassessments from the CRA and the relevant provincial tax authorities sometime in the coming months. The Company strongly disagrees with the CRA's position and intends to vigorously defend its position including appealing the reassessments as and when they are received. The Company will make cash payments or provide other forms of security on a portion of the taxes in dispute. If the Company is successful in defending its position, in whole or in part, some or all of the cash payments or security would be returned to the Company.

**Net Earnings** Net earnings of \$53 million in 2014 decreased by \$574 million compared to 2013, primarily driven by the decrease in operating income and the increase in net interest expense and other financing charges, partially offset by the decrease in income tax expense, described above. Adjusted net earnings<sup>(2)</sup> of \$1,224 million increased by \$528 million compared to 2013, primarily driven by the increase in adjusted operating income<sup>(2)</sup>, primarily as a result of Shoppers Drug Mart, partially offset by the increase in adjusted net interest expense and other financing charges<sup>(2)</sup> and the increase in adjusted income tax expense<sup>(2)</sup>, described above.

**Basic Net Earnings Per Common Share** Basic net earnings per common share were \$0.14 compared to \$2.23 in 2013. Basic net earnings per common share included the negative impact of the full recognition of the Shoppers Drug Mart acquisition-related fair value increment on inventory sold (\$1.55 per share), the amortization of intangible assets acquired with Shoppers Drug Mart (\$0.80 per share), a charge related to inventory measurement and other conversion differences associated with the implementation of a perpetual inventory system (\$0.37 per share), costs and a net divestitures loss associated with the acquisition of Shoppers Drug Mart (\$0.19 per share) and restructuring costs (\$0.09 per share), accelerated amortization of deferred financing costs (\$0.04 per share), fair value adjustment on Trust Unit Liability (\$0.04 per share), fixed asset and other related impairments, net of recoveries (\$0.04 per share) and certain other adjustments (\$0.04 per share) and the positive impact of restructuring of franchise fees (\$0.08 per share).

Adjusted basic net earnings per common share<sup>(2)</sup> were \$3.22 compared to \$2.48 in 2013, primarily due to the increase in adjusted net earnings<sup>(2)</sup> as described above, partially offset by the dilutive effect of the 119.5 million common shares issued as part of the total consideration for the acquisition of Shoppers Drug Mart.

### 5.3 Selected Financial Information

The selected information presented below has been derived from and should be read in conjunction with the annual consolidated financial statements of the Company dated January 3, 2015, December 28, 2013 and December 29, 2012. The analysis of the data contained in the table focuses on the trends and significant events or items affecting the financial condition and results of the Company's operations over the latest three year periods.

For the years ended January 3, 2015 and December 28, 2013 and December 29, 2012 (millions of Canadian dollars except where otherwise indicated)	2014 (53 weeks)	2013 <sup>(4)</sup> (52 weeks)	2012 <sup>(3)</sup> (52 weeks)
Revenue	\$ 42,611	\$ 32,371	\$ 31,604
<i>Revenue excluding Shoppers Drug Mart</i>	<b>33,561</b>	32,371	31,604
EBITDA <sup>(2)</sup>	\$ 2,134	\$ 2,145	\$ 1,972
Adjusted EBITDA <sup>(2)</sup>	<b>3,236</b>	2,106	2,041
<i>Adjusted EBITDA<sup>(2)</sup> excluding Shoppers Drug Mart</i>	<b>2,248</b>	2,106	2,041
Operating income	\$ 662	\$ 1,321	\$ 1,195
Adjusted operating income <sup>(2)</sup>	<b>2,181</b>	1,282	1,264
<i>Adjusted operating income<sup>(2)</sup> excluding Shoppers Drug Mart</i>	<b>1,397</b>	1,282	1,264
Adjusted net interest expense and other financing charges <sup>(2)</sup>	\$ 529	\$ 354	\$ 351
Adjusted income tax rate <sup>(2)</sup>	<b>25.9%</b>	25.0%	25.0%
Net earnings	\$ 53	\$ 627	\$ 634
Adjusted net earnings <sup>(2)</sup>	<b>1,224</b>	696	685
Basic net earnings per common share (\$)	\$ 0.14	\$ 2.23	\$ 2.25
Diluted net earnings per common share (\$)	<b>0.14</b>	2.21	2.23
Adjusted basic net earnings per common share <sup>(2)</sup> (\$)	<b>3.22</b>	2.48	2.43
Dividends declared per common share (\$)	\$ 0.975	\$ 0.940	\$ 0.850
Dividends declared per Second Preferred Share, Series A (\$)	<b>1.49</b>	1.49	1.49

**Revenue** Revenue of \$42,611 million increased by \$10,240 million compared to 2013, primarily due to Shoppers Drug Mart and the impact of the 53rd week in 2014. Revenue in the 53rd week of 2014 was \$789 million. Excluding the impact of Shoppers Drug Mart and the 53rd week of 2014, consolidated revenue increased by \$616 million, or 1.9%. Retail same-store<sup>(6)</sup> sales growth, on a comparable week basis, was 2.0% (2013 – 1.1%) and excluding gas bar, was 2.1% (2013 – 1.0%).

Revenue in 2013 of \$32,371 million increased by \$767 million compared to 2012, primarily due to the increase in the Retail segment. Retail same-store<sup>(6)</sup> sales growth was 1.1% (2012 – decline of 0.2%) and excluding gas bar was 1.0% (2012 – decline of 0.2%).

The Company's Retail segment sales have continued to grow under the pressure of an intensely competitive retail market and uncertain economic environment over the last three years.

**EBITDA<sup>(2)</sup>** EBITDA<sup>(2)</sup> of \$2,134 million in 2014 decreased by \$11 million compared to 2013, primarily driven by a decrease in the Retail segment EBITDA<sup>(2)</sup> due to the acquisition-related accounting adjustments from the acquisition of Shoppers Drug Mart, partially offset by increases in the Financial Services and Choice Properties segments. The 53rd week contributed \$71 million to EBITDA<sup>(2)</sup>.

EBITDA<sup>(2)</sup> in 2013 of \$2,145 million increased by \$173 million compared to 2012, primarily driven by increases in each of the Company's operating segments.

Over the past three years, the Company's consolidated EBITDA<sup>(2)</sup> has been impacted by a number of items which the Company does not consider to be indicative of operational performance. These items have been adjusted in the presentation of adjusted EBITDA<sup>(2)</sup> as set out in Section 20 "Non-GAAP Financial Measures".

**Operating Income** Operating income in 2014 of \$662 million decreased by \$659 million compared to 2013, primarily due to a decrease in the Retail segment operating income. The decrease in the Retail segment is primarily driven by the items as set out in Section 20 "Non-GAAP Financial Measures" and also impacted by the amortization of intangible assets related to the acquisition of Shoppers Drug Mart.

Operating income in 2013 of \$1,321 million increased by \$126 million compared to 2012, primarily driven by increases in each of the Company's operating segments.

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Over the past three years, the Company's consolidated operating income has been impacted by a number of items which the Company does not consider to be indicative of operational performance. These items have been adjusted in the presentation of adjusted operating income<sup>(2)</sup> as set out in Section 20 "Non-GAAP Financial Measures".

**Net Earnings and Basic Net Earnings per Common Share** In 2014, the decreases in net earnings and basic net earnings per common share were primarily due to the decrease in operating income and the increase in net interest expense and other financing charges, partially offset by the decrease in income tax expense. Net interest and other financing charges increased due to increased debt as a result of the acquisition of Shoppers Drug Mart. The decrease in basic net earnings per common share was also impacted by the dilutive effect of the 119.5 million common shares issued as part of the total consideration for the acquisition of Shoppers Drug Mart.

In 2013, the decreases in net earnings and basic net earnings per common share were negatively impacted by an increase in net interest expense and other financing charges, driven by higher interest on long term debt, primarily as a result of debt incurred to finance the acquisition of Shoppers Drug Mart and distributions paid by Choice Properties on its Units, and by a higher effective income tax rate, partially offset by higher operating income.

Over the past three years, the Company's adjusted net earnings<sup>(2)</sup> and adjusted net earnings per common share<sup>(2)</sup> have been impacted by a number of items which the Company does not consider to be indicative of operational performance. These items have been normalized in the presentation of adjusted net earnings<sup>(2)</sup> and adjusted net earnings per common share<sup>(2)</sup> as set out in Section 20 "Non-GAAP Financial Measures".

### Total Assets and Long Term Financial Liabilities

(millions of Canadian dollars)	As at January 3, 2015	As at December 28, 2013	As at December 29, 2012
Total Assets	\$ 33,684	\$ 20,741	\$ 17,961
Long Term Debt	\$ 11,462	\$ 7,680	\$ 5,669
Capital Securities	—	224	223
Trust Unit Liability	722	688	—
Long term financial liabilities	\$ 12,184	\$ 8,592	\$ 5,892

In 2014, total assets of \$33,684 million and long term financial liabilities of \$12,184 million increased by 62.4% and 41.8%, respectively, compared to 2013. These increases were primarily driven by the consolidation of Shoppers Drug Mart balances, the issuance of debt to finance the acquisition of Shoppers Drug Mart, partially offset by debt repayments. In 2014, capital securities became due within one year and were presented in current liabilities.

In 2013, total assets of \$20,741 million and long term financial liabilities of \$8,592 million increased by 15.5% and 45.8%, respectively, compared to 2012. These increases were primarily driven by the Choice Properties IPO, the completed offering of senior unsecured debentures and the financing transactions in preparation for the Shoppers Drug Mart acquisition. Excluding these impacts, the Company's total assets and long term financial liabilities increased marginally over 2012.



## 6. Reportable Operating Segments Results of Operations

### 6.1 Retail Segment

For the years ended January 3, 2015 and December 28, 2013 (millions of Canadian dollars except where otherwise indicated)	2014 (53 weeks)	2013 <sup>(4)</sup> (52 weeks)	\$ Change	% Change
Sales	\$ 41,731	\$ 31,600	\$ 10,131	32.1 %
Gross profit	9,734	6,961	2,773	39.8 %
Adjusted gross profit <sup>(2)</sup>	10,722	6,961	3,761	54.0 %
EBITDA <sup>(2)</sup>	1,950	1,989	(39)	(2.0)%
Adjusted EBITDA <sup>(2)</sup>	3,038	1,947	1,091	56.0 %
Operating income	497	1,180	(683)	(57.9)%
Adjusted operating income <sup>(2)</sup>	2,002	1,138	864	75.9 %

For the years ended January 3, 2015 and December 28, 2013	2014 (53 weeks)	2013 <sup>(4)</sup> (52 weeks)
Same-store sales <sup>(1), (6)</sup> growth	2.0%	1.1%
Adjusted gross profit % <sup>(2)</sup>	25.7%	22.0%
Adjusted EBITDA margin <sup>(2)</sup>	7.3%	6.2%
Adjusted operating margin <sup>(2)</sup>	4.8%	3.6%

### Sales

For the years ended January 3, 2015 and December 28, 2013 (millions of Canadian dollars except where otherwise indicated)	2014 (53 weeks)	2013 <sup>(4)</sup> (52 weeks)	\$ Change	% Change
Retail segment sales	\$ 41,731	\$ 31,600	\$ 10,131	32.1%
Shoppers Drug Mart	9,050			
Excluding Shoppers Drug Mart	\$ 32,681	\$ 31,600	\$ 1,081	3.4%

- Retail segment sales of \$41,731 million in 2014 increased by \$10,131 million compared to 2013, primarily due to Shoppers Drug Mart and the impact of the 53rd week in 2014. Retail segment sales in the 53rd week of 2014 were \$789 million (\$574 million excluding Shoppers Drug Mart). Excluding the impact of Shoppers Drug Mart and the 53rd week of 2014, Retail segment sales increased by \$507 million, or 1.6%, due to the following factors:
  - Same-store sales<sup>(1), (6)</sup> growth, for core grocery and on a comparable week basis, was 2.0% (2013 – 1.1%) and excluding gas bar, was 2.1% (2013 – 1.0%);
  - On a comparable week basis:
    - Sales growth in food was moderate;
    - Sales in drugstore were flat;
    - Sales growth in gas bar was modest;
    - Sales in general merchandise, excluding apparel, were flat; and
    - Sales in retail apparel were modest, while U.S. wholesale apparel sales declined significantly;
  - The Company's average annual internal food price index was slightly higher than (2013 – lower than) the average annual national food price inflation of 2.5% (2013 – 1.1%) as measured by "The Consumer Price Index for Food Purchased from Stores" ("CPI"). CPI does not necessarily reflect the effect of inflation on the specific mix of goods sold in Loblaw stores; and
  - 22 corporate and franchise stores were opened and 12 corporate and franchise stores were closed in the last 12 months, with an additional two franchise grocery stores divested as a result of a Consent Agreement with the Competition Bureau related to the acquisition of Shoppers Drug Mart, resulting in flat square footage growth.

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- Since the acquisition date, Shoppers Drug Mart opened 17 new drug stores and closed 24 drug stores, including 13 drug stores divested in accordance with the Consent Agreement with the Competition Bureau related to the acquisition of Shoppers Drug Mart. As a result, net square footage increased by 0.1 million square feet, or 0.6%.

### Gross Profit

For the years ended January 3, 2015 and December 28, 2013 (millions of Canadian dollars except where otherwise indicated)	2014 (53 weeks)	2013 <sup>(4)</sup> (52 weeks)	\$ Change	% Change
Retail gross profit	\$ 9,734	\$ 6,961	\$ 2,773	39.8%
Adjustments <sup>(2)</sup>	988	—		
Adjusted Retail gross profit <sup>(2)</sup>	\$ 10,722	\$ 6,961	\$ 3,761	54.0%
Adjusted gross profit % <sup>(2)</sup>	25.7%	22.0%		
Shoppers Drug Mart	\$ 3,543			
Excluding Shoppers Drug Mart	\$ 7,179	\$ 6,961	\$ 218	3.1%
Adjusted gross profit % <sup>(2)</sup>	22.0%	22.0%		

- In 2014, gross profit of \$9,734 million increased by \$2,773 million compared to 2013, primarily due to Shoppers Drug Mart and was negatively impacted by adjustments<sup>(2)</sup> of \$988 million including the full recognition of the fair value increment on the acquired Shoppers Drug Mart inventory sold and the charge related to inventory measurement and other conversion differences associated with the implementation of a perpetual inventory system.

After excluding these adjustments<sup>(2)</sup>, adjusted gross profit<sup>(2)</sup> of \$10,722 million increased by \$3,761 million, including \$3,543 million of adjusted gross profit<sup>(2)</sup> contributed by Shoppers Drug Mart. Adjusted gross profit percentage<sup>(2)</sup> was 25.7% compared to 22.0% in 2013.

Excluding Shoppers Drug Mart, adjusted gross profit percentage<sup>(2)</sup> was 22.0%, flat compared to 2013. While flat, adjusted gross profit percentage<sup>(2)</sup> was positively impacted by synergies related to the acquisition and reductions in transportation costs, but were negatively impacted by increased shrink. Excluding Shoppers Drug Mart, adjusted gross profit<sup>(2)</sup> increased by \$218 million, or 3.1%, compared to 2013, driven by higher sales, including the impact of the 53rd week of 2014.

### EBITDA<sup>(2)</sup>

For the years ended January 3, 2015 and December 28, 2013 (millions of Canadian dollars except where otherwise indicated)	2014 (53 weeks)	2013 <sup>(4)</sup> (52 weeks)	\$ Change	% Change
EBITDA <sup>(2)</sup>	\$ 1,950	\$ 1,989	\$ (39)	(2.0)%
Adjustments <sup>(2)</sup>	1,088	(42)		
Adjusted Retail EBITDA <sup>(2)</sup>	\$ 3,038	\$ 1,947	\$ 1,091	56.0 %
Adjusted EBITDA margin <sup>(2)</sup>	7.3%	6.2%		
Shoppers Drug Mart	\$ 988			
Excluding Shoppers Drug Mart	\$ 2,050	\$ 1,947	\$ 103	5.3 %
Adjusted EBITDA margin <sup>(2)</sup>	6.3%	6.2%		

- EBITDA<sup>(2)</sup> of \$1,950 million in 2014 decreased by \$39 million compared to 2013. EBITDA<sup>(2)</sup> was negatively impacted by adjustments of \$1,088 million as set out in Section 20 "Non-GAAP Financial Measures". The significant adjustments during 2014 included the Shoppers Drug Mart acquisition-related costs of the full recognition of the fair value increment on the acquired Shoppers Drug Mart inventory sold and the charge related to inventory measurement and other conversion differences associated with the implementation of a perpetual inventory system.

After excluding these adjustments<sup>(2)</sup>, adjusted EBITDA<sup>(2)</sup> of \$3,038 million increased by \$1,091 million compared to 2013, including \$988 million of adjusted EBITDA<sup>(2)</sup> contributed by Shoppers Drug Mart.

Excluding the impact of Shoppers Drug Mart, adjusted EBITDA<sup>(2)</sup> of \$2,050 million increased by \$103 million, driven by the increase in adjusted gross profit<sup>(2)</sup> of \$218 million, as described above, partially offset by the increase in SG&A of \$115 million. The increase in SG&A was driven by the additional week in 2014 and a \$12 million year-over-year increase in charges related to the transition of certain grocery stores to more cost effective and efficient operating terms under collective agreements. Excluding these impacts, SG&A decreased. This decrease was primarily driven by supply chain efficiencies and changes in the fair value of the Company's franchise investments, partially offset by investments in the Company's emerging business, higher foreign exchange losses, synergy related costs and higher investments in the Company's franchise business.

- Adjusted EBITDA margin<sup>(2)</sup> for 2014 was 7.3%, compared to 6.2% in 2013, primarily driven by Shoppers Drug Mart. Excluding the impact of Shoppers Drug Mart, adjusted EBITDA margin<sup>(2)</sup> was 6.3% compared to 6.2% in 2013.

### Operating Income

For the years ended January 3, 2015 and December 28, 2013 (millions of Canadian dollars except where otherwise indicated)	2014 (53 weeks)	2013 <sup>(4)</sup> (52 weeks)	\$ Change	% Change
Retail operating income	\$ 497	\$ 1,180	\$ (683)	(57.9)%
Adjustments <sup>(2)</sup>	1,505	(42)		
Adjusted Retail operating income <sup>(2)</sup>	\$ 2,002	\$ 1,138	\$ 864	75.9 %
Adjusted operating margin <sup>(2)</sup>	4.8%	3.6%		
Shoppers Drug Mart	\$ 784			
Excluding Shoppers Drug Mart	\$ 1,218	\$ 1,138	\$ 80	7.0 %
Adjusted operating margin <sup>(2)</sup>	3.7%	3.6%		

- Operating income of \$497 million in 2014 decreased by \$683 million compared to 2013, primarily driven by the acquisition-related accounting adjustments of Shoppers Drug Mart. Operating income was negatively impacted by the net adjustments related to EBITDA<sup>(2)</sup> as noted above of \$1,088 million and the amortization of intangible assets related to the acquisition of Shoppers Drug Mart of \$417 million.

After excluding the adjustments to operating income set out in Section 20 "Non-GAAP Financial Measures", adjusted operating income<sup>(2)</sup> of \$2,002 million increased by \$864 million compared to 2013, including \$784 million of adjusted operating income<sup>(2)</sup> contributed by Shoppers Drug Mart. Excluding the impact of Shoppers Drug Mart, adjusted operating income<sup>(2)</sup> increased by \$80 million or 7.0%, driven by the increase in adjusted EBITDA<sup>(2)</sup> described above, partially offset by the increase in retail depreciation and amortization<sup>(2)</sup> of \$23 million.

- Adjusted operating margin<sup>(2)</sup> for 2014 was 4.8%, compared to 3.6% in 2013, primarily driven by the inclusion of Shoppers Drug Mart. Excluding the impact of Shoppers Drug Mart, adjusted operating margin<sup>(2)</sup> was 3.7% compared to 3.6% in 2013.

6.2 Financial Services Segment<sup>(7)</sup>

For the years ended January 3, 2015 and December 28, 2013 (millions of Canadian dollars except where otherwise indicated)	2014 (53 weeks)	2013 (52 weeks)	\$ Change	% Change
Revenue	\$ 810	\$ 739	\$ 71	9.6%
Operating income	164	142	22	15.5%
Earnings before income taxes	111	93	18	19.4%

(millions of Canadian dollars except where otherwise indicated)	As at January 3, 2015	As at December 28, 2013	\$ Change	% Change
Average quarterly net credit card receivables	\$ 2,535	\$ 2,345	\$ 190	8.1%
Credit card receivables	2,630	2,538	92	3.6%
Allowance for credit card receivables	54	47	7	14.9%
Annualized yield on average quarterly gross credit card receivables	13.7%	13.6%		
Annualized credit loss rate on average quarterly gross credit card receivables	4.4%	4.2%		

- Revenue for 2014 of \$810 million increased by \$71 million, or 9.6%, compared to 2013. This increase was primarily driven by higher interest, interchange and other service fee related income as a result of a growth in the credit card receivables portfolio.
- Operating income of \$164 million and earnings before income taxes of \$111 million in 2014 increased by \$22 million and \$18 million, respectively, compared to 2013. These increases were mainly attributable to the higher revenue described above, partially offset by higher operating costs as a result of an increase in the active customer base, higher credit losses from increased credit card receivable balances and higher costs associated with the Financial Services loyalty program.
- As at January 3, 2015, credit card receivables were \$2,630 million, an increase of \$92 million compared to December 28, 2013. This increase was primarily driven by a growth in the active customer base as a result of continued investments in customer acquisitions and marketing initiatives. As at January 3, 2015, the allowance for credit card receivables was \$54 million, an increase of \$7 million compared to December 28, 2013, primarily due to the growth in the credit card receivables portfolio.
- Subsequent to the end of 2014:
  - ▣ The Company, through President's Choice Bank ("PC Bank"), extended the maturity date for certain Other Independent Securitization Trust agreements from the second quarter of 2016 to the second quarter of 2017, with all other terms and conditions remaining substantially the same; and
  - ▣ PC Bank entered into USD foreign exchange forward agreements, which mature by December 2015. The notional amounts of the contracts total USD \$27 million.



### 6.3 Choice Properties Segment<sup>(5)</sup>

For the periods ended January 3, 2015 and December 28, 2013 (millions of Canadian dollars except where otherwise indicated)	2014 (53 weeks)	2013 <sup>(i)</sup> (52 weeks)	\$ Change	% Change
Revenue	\$ 683	\$ 319	\$ 364	114.1%
Operating income	568	370	198	53.5%
Adjusted operating income <sup>(2)</sup>	582	373	209	56.0%
Net interest expense and other financing charges	369	303	66	21.8%
Adjusted funds from operations <sup>(2)</sup>	285	131	154	117.6%

(i) Based on operations beginning July 5, 2013.

- Revenue for 2014 of \$683 million increased by \$364 million, or 114.1%, compared to 2013, and included \$613 million (2013 – \$287 million) primarily related to intersegment revenue from Loblaw retail locations. The increase was primarily driven by the inclusion of a full year of operations in 2014 compared to a partial year in 2013.
- Operating income of \$568 million and adjusted operating income<sup>(2)</sup> of \$582 million in 2014 increased by \$198 million and \$209 million, respectively, compared to 2013. These increases were mainly attributable to a full year of operations in 2014, partially offset by a \$62 million year-over-year unfavourable fair value adjustment on investment properties. The fair value adjustment on investment properties is eliminated on consolidation.
- Adjusted funds from operations<sup>(2)</sup> of \$285 million in 2014 increased by \$154 million compared to 2013. The increase was mainly attributable to a full year of operations and acquisitions of properties from Loblaw.
- During 2014, the Company sold 36 investment properties to Choice Properties for an aggregate purchase price of approximately \$410 million, which was settled through the issuance of 21,957,351 Class B Limited Partnership units, \$179 million in cash and the assumption of a \$4 million mortgage by Choice Properties. In addition, Choice Properties acquired a 40% interest in a limited partnership, which acquired land from the Company, intended for development into a mixed-used property, for approximately \$6 million.
- Choice Properties also acquired in 2014, from a third party, an industrial property in Mississauga, Ontario, for approximately \$16 million, funded by cash. This property is fully leased to a related party.
- In 2014, Choice Properties acquired a 70% interest in a limited partnership, which holds land intended for future retail development, for approximately \$18 million.
- Subsequent to the end of 2014:
  - The Company sold a warehouse to Choice Properties for approximately \$81 million. The warehouse is fully occupied by the Company as the single tenant with a 20-year initial lease term with six five-year renewal options;
  - The Company sold a parcel of land to Choice Properties for approximately \$12 million. Consideration for the acquisition included 265,665 Class B Limited Partnership units, \$7 million in cash and the assumption of a \$2 million obligation. The Class B Limited Partnership units issued to the Company as partial consideration for this transaction did not impact the Company's effective ownership percentage; and
  - Choice Properties issued \$250 million aggregate principal amount of Series E senior unsecured debentures bearing interest at a rate of 2.30% per annum and maturing in 2020. The net proceeds from the issuance were used by Choice Properties to repay existing indebtedness and for general business purposes.
- As of January 3, 2015, the Company's ownership interest in Choice Properties was 82.9%.

## 7. Acquisition of Shoppers Drug Mart Corporation

On March 28, 2014, the Company acquired all of the outstanding shares of Shoppers Drug Mart for total consideration of \$12,273 million, comprised of approximately \$6,600 million of cash and the issuance of approximately 119.5 million common shares of the Company.

The cash portion of the acquisition of Shoppers Drug Mart was financed as follows:

- \$3,500 million was obtained through an unsecured term loan facility bearing interest at a rate equal to the Bankers' Acceptance rate plus 1.75% and maturing March 28, 2019 (the facility was re-priced to Bankers' Acceptance rate plus 1.45% on July 23, 2014);
- \$1,600 million of proceeds from the issuance of unsecured notes in 2013;
- \$500 million was received in consideration of the issuance of 10.5 million common shares to George Weston Limited ("Weston"); and
- approximately \$1,000 million was used from cash on hand.

Based on a preliminary assessment, the Company recognized the following amounts of net tangible assets, goodwill and intangible assets in 2014:

(millions of Canadian dollars except where otherwise indicated)	Estimated Useful Life
<b>Fair Value of Net Tangible Assets Acquired</b>	<b>\$ 548</b>
<b>Goodwill</b>	<b>2,285</b>
Prescription files	5,005      11 years
Brands	3,390      indefinite
Optimum loyalty program	490      18 years
Other	555      5 to 10 years
<b>Total Intangible Assets</b>	<b>9,440</b>
<b>Total Net Assets Acquired</b>	<b>\$ 12,273</b>

As at January 3, 2015, the Company has not yet finalized the above purchase price allocation. In the fourth quarter of 2014, the Company revised its fair value estimate of intangible assets and updated the purchase price equation. The result was to decrease intangible assets by \$35 million to \$9,440 million, decrease deferred income tax liabilities by \$9 million to \$2,252 million and increase goodwill by \$26 million to \$2,285 million. The Company has one year from the date of acquisition to finalize the fair value of net tangible assets, goodwill and intangible assets and any further changes to the amounts presented above will be reflected in the first half of 2015.

Pursuant to a Consent Agreement reached with the Competition Bureau in 2014, the Company was required to divest 16 Shoppers Drug Mart stores, two of the Company's franchise grocery stores and nine in-store pharmacies.

During 2014, two franchise grocery stores and 13 Shoppers Drug Mart stores were sold and nine in-store pharmacies were licensed to unrelated parties, which resulted in a net divestitures loss of \$12 million. The final three Shoppers Drug Mart stores were approved for sale by the Competition Bureau and were sold subsequent to the end of 2014 for estimated proceeds of \$9 million.

The Company has incurred costs of \$75 million (2013 – \$31 million) related to the acquisition of Shoppers Drug Mart, of which \$60 million (2013 – \$6 million) was recorded in SG&A and \$15 million (2013 – \$25 million) was recorded in net interest expense and other financing charges.

Upon closing of the acquisition, all amounts owing on Shoppers Drug Mart's revolving bank credit facility were repaid and the facility was cancelled. In addition, upon closing, the Company guaranteed the outstanding principal amount of Shoppers Drug Mart MTNs of \$500 million, along with accrued interest. The Company has also provided guarantees to various Canadian banks in support of the financing obtained by Shoppers Drug Mart's licensees ("Associates"). An Associate is a pharmacist-owner of a corporation that is licensed to operate a retail drug store at a specific location using Shoppers Drug Mart's trademarks.

## 8. Other Business Matters

**Inventory Valuation** Prior to the second quarter of 2014, the Company valued its merchandise inventories at the lower of cost and net realizable value and used the retail method to measure the cost of the majority of its retail store inventories. The implementation of a perpetual inventory system, combined with visibility to integrated costing information provided by the new IT systems, enables the Company to estimate the cost of inventory using a more precise system-generated average cost.

As of the end of 2014, the Company completed the conversion of substantially all of its corporate grocery locations and associated distribution centres to the new IT systems. As a result of the conversion, the Company recognized a \$190 million charge to cost of merchandise inventories sold and a corresponding reduction in inventory, representing the estimate of the difference between the measurement of the cost of corporate grocery store inventory using a system generated weighted average cost compared to the retail inventory method and other conversion differences associated with the implementation of a perpetual inventory system.

## 9. Liquidity and Capital Resources

### 9.1 Cash Flows

#### *Major Cash Flow Components*

For the years ended January 3, 2015 and December 28, 2013 (millions of Canadian dollars except where otherwise indicated)	2014 (53 weeks)	2013 (52 weeks)	\$ Change	% Change
Cash flows from (used in):				
Operating activities	\$ 2,569	\$ 1,491	\$ 1,078	72.3 %
Investing activities	(5,684)	(1,839)	(3,845)	(209.1)%
Financing activities	1,845	1,521	324	21.3 %

**Cash Flows from Operating Activities** Cash flows from operating activities were \$2,569 million compared to \$1,491 million in 2013. The increase was primarily driven by higher cash earnings, primarily driven by the acquisition of Shoppers Drug Mart and a lower increase in credit card receivables, partially offset by a higher change in non-cash working capital and the settlement of cross currency swaps in 2013. The change in non-cash working capital was due to year-over-year increases in inventory and prepaid expenses, partially offset by a lower year-over-year increase in accounts receivable.

**Cash Flows used in Investing Activities** Cash flows used in investing activities were \$5,684 million compared to \$1,839 million in 2013. The increase in cash flows used in investing activities was primarily due to the acquisition of Shoppers Drug Mart.

Fixed asset purchases in 2014 were \$996 million (2013 – \$865 million). Approximately 22% (2013 – 14%) of this investment was for new store developments, expansions and land, approximately 45% (2013 – 45%) was for store conversions and renovations, and approximately 33% (2013 – 41%) was for infrastructure investments. Intangible asset additions in 2014 were \$90 million (2013 – \$12 million) and primarily related to the acquisition and development of software and the acquisition of prescription files.

During 2014, 22 corporate and franchise stores were opened and 12 corporate and franchise stores were closed, with an additional two franchise grocery stores divested as a result of a Consent Agreement with the Competition Bureau related to the acquisition of Shoppers Drug Mart, resulting in flat square footage growth. Since the acquisition date, Shoppers Drug Mart opened 17 new drug stores and closed 24 drug stores, including 13 drug stores divested in accordance with the Consent Agreement with the Competition Bureau related to the acquisition of Shoppers Drug Mart. As a result, Shoppers Drug Mart's net square footage increased by 0.1 million square feet, or 0.6%.

The Company expects to invest approximately \$1,200 million in capital investments in 2015. Approximately 22% of these funds are expected to be dedicated to investing in IT and supply chain projects, 57% will be spent on retail operations, 14% on Choice Properties' development projects and 7% on other infrastructure projects.

**Capital Investments and Store Activity**

As at or for the years ended January 3, 2015 and December 28, 2013	2014 (53 weeks)	2013 (52 weeks)	% Change
Capital investments (millions of Canadian dollars)	\$ 1,086	\$ 877	23.8 %
Corporate square footage (in millions)	36.8	37.2	(1.1)%
Franchise square footage (in millions)	15.5	14.7	5.4 %
Associate-owned drug store square footage (in millions)	17.7	—	100.0 %
Total retail square footage (in millions)	70.0	51.9	34.9 %
Number of corporate stores <sup>(i)</sup>	615	570	7.9 %
Number of franchise stores	527	496	6.3 %
Number of Associate-owned drug stores	1,302	—	100.0 %
Total number of stores	2,444	1,066	129.3 %
Percentage of corporate real estate owned	72.0%	72.0%	
Percentage of franchise real estate owned	45.0%	45.0%	
Percentage of Associate-owned drug store real estate owned	1.0%	—%	
Average store size (square feet)			
Corporate	59,800	65,300	(8.4)%
Franchise	29,400	29,600	(0.7)%
Associate-owned drug store	13,600	—	100.0 %

(i) 2014 figure includes 68 Shoppers Drug Mart corporate stores.

**Cash Flows from Financing Activities** During 2014, cash flows from financing activities were \$1,845 million compared to cash flows from financing activities of \$1,521 million in 2013. In 2014, cash flows used in financing activities were primarily driven by net issuance of long term debt and proceeds from the issuance of common shares, both primarily used to fund the acquisition of Shoppers Drug Mart. These cash inflows were partially offset by interest and dividend payments, which include one quarter of Shoppers Drug Mart dividends that were declared prior to closing of the acquisition and paid during the second quarter of 2014. Cash flows from financing activities in 2013 were primarily driven by net issuance of long term debt and the issuance of Choice Properties' Trust Units ("Units"), partially offset by repayment of short term debt, as well as interest and dividend payments.

In 2014, net issuances of long term debt included:

- Drawings on the unsecured term loan facility of \$3,500 million and repayments of \$2,271 million for a net outstanding amount of \$1,229 million;
- The issuance and sale to unrelated parties of \$1,500 million of replacement notes related to the Choice Properties Transferor Notes;
- The issuance of \$450 million aggregate principal amount of senior unsecured debentures by Choice Properties;
- The net issuance of \$201 million of Guaranteed Investment Certificates ("GICs");
- The repayment of the Company's \$100 million, 6.0% MTN upon maturity;
- The repayment of the Company's \$350 million, 4.85% MTN upon maturity;
- The repayment of the outstanding \$478 million balance of the Shoppers Drug Mart revolving bank credit facility; and
- Drawings on the \$500 million senior unsecured committed credit facility ("Choice Properties' Credit Facility") of \$122 million.



In 2013, net issuances of long term debt included:

- The issuance of \$1,600 million aggregate principal amount of senior unsecured notes issued to partially fund the acquisition of the outstanding common shares of Shoppers Drug Mart;
- Choice Properties' public offering of \$600 million aggregate principal amount of Debentures;
- The issuance of \$400 million of senior and subordinated term notes by the Independent Securitization Trust, partially offset by the repayment of its \$250 million of senior and subordinated term notes;
- The net issuance of \$125 million of GICs;
- The repayment of the Company's remaining USD \$300 million U.S. Private Placement ("USPP") note; and
- The repayment of the Company's \$200 million, 5.40% MTN upon maturity.

## Free Cash Flow<sup>(2)</sup>

For the years ended January 3, 2015 and December 28, 2013 (millions of Canadian dollars except where otherwise indicated)	2014 (53 weeks)	2013 <sup>(4)</sup> (52 weeks)	\$ Change	% Change
Free cash flow <sup>(2)</sup>	\$ 977	\$ 244	\$ 733	300.4%

For 2014, free cash flow<sup>(2)</sup> was \$977 million compared to \$244 million in 2013. The increase in free cash flow<sup>(2)</sup> for 2014 was primarily due to higher cash flows from operating activities, partially offset by an increase in capital investments as well as higher interest payments.

## 9.2 Liquidity and Capital Structure

The Company expects that cash and cash equivalents, short term investments, future operating cash flows and the amounts available to be drawn against its committed credit facilities will enable the Company to finance its capital investments program and fund its ongoing business requirements, including working capital, pension plan funding requirements, financial obligations and debt reduction commitments over the next 12 months.

**Adjusted Debt<sup>(2)</sup>** On closing of the acquisition of Shoppers Drug Mart, adjusted debt<sup>(2)</sup> was \$11,060 million. The Company made significant progress in meeting its debt reduction target by decreasing adjusted debt<sup>(2)</sup> by \$1,065 million since the closing of the acquisition of Shoppers Drug Mart resulting in an outstanding adjusted debt<sup>(2)</sup> balance of \$9,995 million as at January 3, 2015. The reduction in adjusted debt<sup>(2)</sup> since closing included the repayment of a \$350 million MTN and a repayment of the unsecured term loan facility (net of the replacement of all tranches of inter-corporate debt of Choice Properties initially held by Loblaw and sold to unrelated parties).

Under the terms of the unsecured term loan facility, the proceeds from the store divestitures required pursuant to the Consent Agreement must be used to repay the facility. Of the total amount repaid under the facility in 2014, \$57 million related to these proceeds.

## Adjusted Debt<sup>(2)</sup> to Adjusted EBITDA<sup>(2)</sup>

	As at January 3, 2015	As at December 28, 2013 <sup>(4)</sup>
Adjusted debt <sup>(2)</sup> to adjusted EBITDA <sup>(2)</sup>	3.1x	3.0x

The adjusted debt<sup>(2)</sup> to adjusted EBITDA<sup>(2)</sup> ratio increased at the end of 2014 compared to the end of 2013 as a result of the \$3,500 million unsecured term loan facility used to partially fund the cash portion of the Shoppers Drug Mart acquisition, and the assumption of Shoppers Drug Mart outstanding debt, partially offset by the increase in adjusted EBITDA<sup>(2)</sup> due to the inclusion of Shoppers Drug Mart adjusted EBITDA<sup>(2)</sup> and the debt reduction progress since the acquisition. The Company will continue to target leverage ratios consistent with those of investment grade ratings.

**Unsecured Term Loan Facility** In connection with the financing of the acquisition of Shoppers Drug Mart, \$3,500 million was obtained through an unsecured term loan facility bearing interest at a rate equal to the Bankers' Acceptance rate plus 1.75% maturing March 28, 2019. Loblaw used the proceeds from the sale of \$1,500 million of Transferor Notes to third parties, mentioned below, to partially repay the \$3,500 million unsecured term loan facility. The overall consolidated impact was neutral to adjusted debt<sup>(2)</sup>. However, this repayment combined with the \$771 million in unsecured term loan facility repayments during the year reduced the term loan facility balance to approximately \$1,229 million as at January 3, 2015.

## Management's Discussion and Analysis

In 2014, the Company reached an agreement to re-price the interest rate on its unsecured term loan facility, obtained to finance the acquisition of Shoppers Drug Mart, to reduce the rate from Bankers' Acceptance rate plus 1.75% to Bankers' Acceptance rate plus 1.45%.

**Committed Credit Facility** In 2014, effective on the closing of the acquisition of Shoppers Drug Mart, the Company's \$800 million committed credit facility ("Credit Facility") was increased to \$1,000 million and the term was extended to December 31, 2018, with all other terms and conditions remaining substantially the same. The Credit Facility contains certain financial covenants with which the Company was in compliance throughout the year and as at the end of 2014. As at January 3, 2015 and December 28, 2013, there were no amounts drawn under the Credit Facility.

**PC Bank Securities Portfolio** In 2014, the Office of the Superintendent of Financial Institutions ("OSFI") released the final Guideline on Liquidity Adequacy Requirements ("LARs"). The LARs guideline establishes standards based on the Basel III framework, including a Liquidity Coverage Ratio ("LCR") standard effective January 1, 2015 and a Net Stable Funding Ratio standard effective January 1, 2018. The LCR standard specifies the level of liquid securities that PC Bank is required to maintain to meet its financial liabilities.

**Choice Properties** Choice Properties expects to obtain its long term financing, for the acquisition of accretive properties, primarily through the issuance of equity and unsecured debentures.

In 2014, Choice Properties Limited Partnership entered into a Master Trust Indenture agreement with Computershare Trust Company of Canada to create supplemental indentures in order to facilitate the replacement of all tranches of Transferor Notes held by Loblaw, with Series 5 to Series 10 notes containing the same principal amounts, interest rates and maturity dates. These replacement notes bear fixed interest rates between 3.00% and 3.60% and mature during 2016 through 2022. The remaining terms and conditions were substantially similar to the original notes. Loblaw subsequently sold the replacement notes to unrelated parties and received net proceeds of \$1,500 million.

In 2014, Choice Properties issued \$250 million principal amount of Series C senior unsecured debentures with a 7-year term and a coupon rate of 3.50% per annum and \$200 million principal amount of Series D senior unsecured debentures with a 10-year term and a coupon rate of 4.29% per annum, under its Short Form Base Shelf Prospectus. The majority of the proceeds were used to repay \$440 million of Transferor Notes held by Loblaw.

Subsequent to the end of the year, Choice Properties issued \$250 million aggregate principal amount of Series E senior unsecured debentures bearing interest at a rate of 2.30% per annum and maturing in 2020. The net proceeds from the issuance were used by Choice Properties to repay existing indebtedness and for general business purposes.

In 2013, Choice Properties entered into an agreement for the Choice Properties Credit Facility, provided by a syndicate of lenders. In 2014, Choice Properties extended the maturity date of the Choice Properties Credit Facility to July 5, 2019. The facility contains certain financial covenants with which Choice Properties was in compliance throughout the year and as at the end of 2014. As at January 3, 2015, Choice Properties had drawn \$122 million (2013 – nil) under the Choice Properties Credit Facility.

**Prospectus** Subsequent to the end of 2014, the Company received approval from its Board of Directors ("Board") to file a Short Form Base Shelf Prospectus which allows for the issuance of up to \$1,500 million of unsecured debentures and/or preference shares subject to the availability of funding in capital markets.

### 9.3 Credit Ratings

The Company guaranteed the outstanding MTNs of Shoppers Drug Mart (see Section 7, "Acquisition of Shoppers Drug Mart" of this MD&A). As a result, Standard & Poor's changed its credit rating of the outstanding Shoppers Drug Mart MTNs to BBB with "Stable" outlook and DBRS changed its rating to BBB with a "Stable" trend, in each case consistent with the credit ratings of the Company. In the fourth quarter of 2014, Dominion Bond Rating Service reaffirmed Loblaw's credit ratings and trends.

The following table sets out the current credit ratings of the Company:

Credit Ratings (Canadian Standards)	Dominion Bond Rating Service		Standard & Poor's	
	Credit Rating	Trend	Credit Rating	Outlook
Issuer rating	BBB	Stable	BBB	Stable
Medium term notes	BBB	Stable	BBB	n/a
Other notes and debentures	BBB	Stable	BBB	n/a
Preferred shares	Pfd-3	Stable	P-3 (high)	n/a

The following table sets out the current credit ratings of Choice Properties:

Credit Ratings (Canadian Standards)	Dominion Bond Rating Service		Standard & Poor's	
	Credit Rating	Trend	Credit Rating	Outlook
Issuer rating	BBB	Stable	BBB	Stable
Senior unsecured debentures	BBB	Stable	BBB	n/a

#### 9.4 Other Sources of Funding

**Independent Securitization Trusts** The Company, through PC Bank, participates in various securitization programs that provide the primary source of funds for the operation of its credit card business. PC Bank sells and repurchases credit card receivables with independent securitization trusts, including *Eagle Credit Card Trust*<sup>®</sup> ("*Eagle*") and Other Independent Securitization Trusts, from time to time, depending on PC Bank's financing requirements. As at January 3, 2015, the amount of credit card receivables securitized to *Eagle* was \$750 million (December 28, 2013 – \$750 million) and \$605 million (December 28, 2013 – \$605 million) were securitized to Other Independent Securitization Trusts.

Letters of credit for the benefit of independent securitization trusts with respect to the securitization programs of PC Bank have been issued by major financial institutions. These standby letters of credit can 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. The Company has agreed to reimburse the issuing banks for any amount drawn on the standby letters of credit.

As at January 3, 2015, the aggregate gross potential liability under these arrangements for the Other Independent Securitization Trusts was \$61 million (December 28, 2013 – \$54 million), which represented 10% (2013 – 9%) of the securitized credit card receivables amount. As at January 3, 2015, the aggregate gross potential liability under these arrangements for *Eagle* was \$68 million (December 28, 2013 – nil), which represented 9% (2013 – nil) of the *Eagle* notes outstanding.

In 2014, PC Bank extended the maturity date for one of its Other Independent Securitization Trust agreements from the third quarter of 2015 to the third quarter of 2016, with all other terms and conditions remaining substantially the same. In addition, PC Bank extended the maturity date for two of its Other Independent Securitization Trust agreements from the second quarter of 2015 to the second quarter of 2016, with all other terms and conditions remaining substantially the same. Subsequent to the end of the year, PC Bank extended the maturity date for certain Other Independent Securitization Trust agreements from the second quarter of 2016 to the second quarter of 2017, with all other terms and conditions remaining substantially the same.

The undrawn commitments on facilities available from the Other Independent Securitization Trusts as at January 3, 2015 were \$120 million (December 28, 2013 – \$120 million).

**Independent Funding Trusts** The Company has a revolving committed credit facility that is the source of funding to the independent funding trusts. As at January 3, 2015, the independent funding trusts had drawn \$498 million (December 28, 2013 – \$475 million).

In 2014, the Company renewed the revolving committed credit facility and extended the maturity date to May 6, 2017, with terms and conditions remaining substantially the same.

The Company provides credit enhancement in the form of a standby letter of credit for the benefit of the independent funding trusts representing not less than 10% of the principal amount of the loans outstanding. As at January 3, 2015, the Company had provided a letter of credit in the amount of \$50 million (December 28, 2013 – \$48 million). This credit enhancement allows the independent funding trusts to provide financing to the Company's independent franchisees. As well, each independent franchisee provides security to the independent funding trusts for its obligations by way of a general security agreement. In the event that an independent franchisee defaults on its loan and the Company has not, within a specified time period, assumed the loan, or the default is not otherwise remedied, the independent funding trusts would assign the loan to the Company and draw upon this standby letter of credit. This standby letter of credit has never been drawn upon. The Company has agreed to reimburse the issuing bank for any amount drawn on the standby letter of credit.

**Guaranteed Investment Certificates** The following table summarizes PC Bank's GICs activity, before commissions, for the years ended 2014 and 2013:

(millions of Canadian dollars)	2014	2013
Balance, beginning of year	\$ 430	\$ 303
GICs issued	261	167
GICs matured	(57)	(40)
Balance, end of year	\$ 634	\$ 430

As at January 3, 2015, \$29 million in GICs were recorded as long term debt due within one year (December 28, 2013 – \$52 million).

**Associate Guarantees** The Company has arranged for its Shoppers Drug Mart Associates to obtain financing to facilitate their inventory purchases and fund their working capital requirements by providing guarantees to various Canadian chartered banks that support Associate loans. As at January 3, 2015, the Company's maximum obligation in respect of such guarantees was \$570 million with an aggregate amount of \$476 million in available lines of credit allocated to the Associates by the various banks. As at January 3, 2015, Associates had drawn an aggregate amount of \$162 million against these available lines of credit. Any amounts drawn by the Associates are included in bank indebtedness on the Company's consolidated balance sheet. As recourse in the event that any payments are made under the guarantees, the Company holds a first-ranking security interest on all assets of Associates, subject to certain prior-ranking statutory claims.

## 9.5 Share Capital

**Outstanding Share Capital and Capital Securities** The following table details the outstanding common shares and preferred shares as at January 3, 2015:

	Authorized	Outstanding
Common Shares	Unlimited	412,480,891
First Preferred Shares	1,000,000	nil
Second Preferred Shares, Series A <sup>(i)</sup>	12,000,000	9,000,000

(i) The Second Preferred Shares, Series A are presented as capital securities on the consolidated balance sheet.

**Common Shares (authorized – unlimited)** Common shares issued are fully paid and have no par value. The activity in the common shares issued and outstanding during 2014 and 2013 were as follows:

(number of common shares)	2014	2013
Issued and outstanding, beginning of year	282,311,573	281,680,157
Issued for settlement of stock options	3,536,489	2,131,416
Issued for acquisition of Shoppers Drug Mart <sup>(i)</sup>	119,471,382	—
Issued to controlling shareholder <sup>(i)</sup>	10,515,247	—
Purchased for cancellation	(3,353,800)	(1,500,000)
Issued and outstanding, end of year	412,480,891	282,311,573
Shares held in trust, beginning of year	(1,067,323)	—
Purchased for future settlement of RSUs and PSUs	—	(1,103,500)
Released for settlement of RSUs and PSUs	512,277	36,177
Shares held in trust, end of year	(555,046)	(1,067,323)
Issued and outstanding, net of shares held in trust, end of year	411,925,845	281,244,250
Weighted average outstanding, net of shares held in trust	380,540,877	281,123,452

(i) See Section 7 "Acquisition of Shoppers Drug Mart Corporation".



**Dividends** The declaration and payment of dividends on the Company's common shares and the amount thereof are at the discretion of the Board, which takes into account the Company's financial results, capital requirements, available cash flow, future prospects of the Company's business and other factors considered relevant from time to time. Over time, it is the Company's intention to increase the amount of the dividend while retaining appropriate free cash flow to reduce debt and finance future growth.

The following table summarizes the Company's cash dividends declared for 2014 and 2013:

	2014 <sup>(i)</sup> (53 weeks)	2013 (52 weeks)
Dividends declared per share (\$):		
Common share	\$ 0.975	\$ 0.940
Second Preferred Share, Series A <sup>(ii)</sup>	\$ 1.49	\$ 1.49

- (i) The fourth quarter dividends of \$0.245 per share declared on common shares were paid on December 30, 2014. The fourth quarter dividends of \$0.37 per share declared on Second Preferred Shares, Series A were paid on January 31, 2015.
- (ii) Dividends on Second Preferred Share, Series A are presented in net interest and other financing charges on the consolidated statements of earnings.

Subsequent to the end of the year, the Board declared a quarterly dividend of \$0.245 per common share, payable April 1, 2015, and declared a quarterly dividend of \$0.37 per Second Preferred Share, Series A, payable April 30, 2015. At the time such dividends are declared, the Company identifies on its website, [loblaw.ca](http://loblaw.ca), the designation of eligible and ineligible dividends in accordance with the administrative position of the CRA.

**Normal Course Issuer Bid** The activity under the Company's Normal Course Issuer Bid ("NCIB") is summarized as follows:

(millions of Canadian dollars except where otherwise indicated)	2014 (53 weeks)	2013 (52 weeks)
Shares repurchased under the NCIB for cancellation (number of shares)	3,353,800	1,500,000
Cash consideration paid	\$ 178	\$ 73
Premium charged to Retained Earnings	115	64
Reduction in common shares	63	9
Shares repurchased under the NCIB and held in trusts (number of shares)	—	1,103,500
Cash consideration paid	\$ —	\$ 46
Premium charged to Retained Earnings	—	40
Reduction in common shares	—	6

In 2014, the Company renewed its NCIB to purchase on the Toronto Stock Exchange ("TSX") or to enter into equity derivatives to purchase up to 20,636,596 of the Company's common shares, representing approximately 5% of the common shares outstanding after taking into account shares issued in connection with the acquisition of Shoppers Drug Mart. In accordance with the rules and by-laws of the TSX, the Company may purchase its common shares from time to time at the then market price of such shares.

## 9.6 Contractual Obligations

The following illustrates certain of the Company's significant contractual obligations and discusses other obligations as at January 3, 2015:

### Summary of Contractual Obligations

(millions of Canadian dollars)	Payments due by year						Total
	2015	2016	2017	2018	2019	Thereafter	
Long term debt (including interest payments <sup>(i)</sup> )	\$ 911	\$ 1,445	\$ 1,278	\$ 1,767	\$ 2,920	\$ 8,263	\$ 16,584
Operating leases <sup>(ii)</sup>	674	654	620	573	529	2,818	5,868
Contracts for purchases of investment projects <sup>(iii)</sup>	191	1	—	—	—	—	192
Purchase obligations <sup>(iv)</sup>	124	68	36	23	1	5	257
<b>Total contractual obligations</b>	<b>\$ 1,900</b>	<b>\$ 2,168</b>	<b>\$ 1,934</b>	<b>\$ 2,363</b>	<b>\$ 3,450</b>	<b>\$ 11,086</b>	<b>\$ 22,901</b>

- (i) Fixed interest payments are based on the maturing face values and annual interest for each instrument, including GICs, long term independent securitization trusts and an independent funding trust, as well as annual payment obligations for Consolidated Structured Entities, mortgages and finance lease obligations. Variables interest payments are based on the forward rates as of January 3, 2015.
- (ii) Represents the minimum or base rents payable. Amounts are not offset by any expected sub-lease income.
- (iii) These obligations include agreements for the purchase of real property and capital commitments for construction, expansion and renovation of buildings. These agreements may contain conditions that may or may not be satisfied. If the conditions are not satisfied, it is possible the Company will no longer have the obligation to proceed with the underlying transactions.
- (iv) Include contractual obligations to purchase goods or services of a material amount where the contract prescribes fixed or minimum volumes to be purchased or payments to be made within a fixed period of time for a set or variable price. These are only estimates of anticipated financial commitments under these arrangements and the amount of actual payments will vary. These purchase obligations do not include purchase orders issued or agreements made in the ordinary course of business which are solely for goods which are meant for resale, nor do they include any contracts which may be terminated on relatively short notice or with relatively insignificant cost or liability to the Company.

At year end, the Company had additional long term liabilities which included post-employment and other long term employee benefit plan liabilities, deferred vendor allowances, deferred income tax liabilities, Trust Unit Liability and provisions, including insurance liabilities. These long term liabilities have not been included above as the timing and amount of future payments are uncertain.

## 10. Financial Derivative Instruments

The following describes the financial derivative instruments that were terminated in 2013:

**Cross Currency Swaps** In 2013, Glenhuron unwound its cross currency swaps and received a net cash settlement of \$76 million, representing the cumulative fair value gain on the swaps. The swaps were offset by the effect of translation gains and losses relating to USD cash and cash equivalents, short term investments and security deposits.

In 2013, the Company settled its USD \$300 million USPP cross currency swaps in conjunction with the settlement of the underlying USD \$300 million USPP debt.

The following table summarizes the 2013 impact to operating income resulting from changes in the fair value of the cross currency swaps and the underlying exposures:

(millions of Canadian dollars)	<u>Glenhuron</u> <u>Cross Currency</u> <u>Swaps</u> December 28, 2013 (52 weeks)	<u>USPP</u> <u>Cross Currency</u> <u>Swaps</u> December 28, 2013 (52 weeks)
	Fair value loss (gain) related to swaps <sup>(i)</sup>	\$ 37
Translation (gain) loss related to the underlying exposures	(33)	14

- (i) The impact to USPP cross currency swaps excludes the \$7 million gain on derecognized derivative instruments, before income taxes, reclassified from accumulated other comprehensive income.

**Interest Rate Swaps** During 2013, the Company settled its notional \$150 million in interest rate swaps and recognized a \$5 million fair value gain in operating income related to these swaps.

**Trust Unit Liability** As at January 3, 2015, the fair value of the Trust Unit Liability of \$722 million (December 28, 2013 – \$688 million) was recorded on the consolidated balance sheet. In 2014, the Company recorded a fair value loss of \$17 million (2013 – \$27 million), in net interest expense and other financing charges related to Choice Properties' Units.

## 11. Off-Balance Sheet Arrangements

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

**Letters of Credit** Standby and documentary letters of credit are used in connection with certain obligations mainly related to real estate transactions, benefit programs, purchase orders and performance guarantees, securitization of PC Bank's credit card receivables and third party financing made available to the Company's independent franchisees. The aggregate gross potential liability related to the Company's letters of credit is approximately \$586 million (December 28, 2013 – \$470 million).

As at January 3, 2015, the Company had agreements to cash collateralize certain of these letters of credit up to an amount of \$141 million (December 28, 2013 – \$136 million), of which \$7 million (December 28, 2013 – \$102 million) was deposited with major financial institutions and classified as security deposits.

**Guarantees** In addition to the letters of credit mentioned above, the Company has entered into various guarantee arrangements including obligations to indemnify third parties in connection with leases, business dispositions and other transactions in the normal course of business, some of which are discussed in section 9 "Liquidity and Capital Resources."

In addition, the Company has provided a guarantee on behalf of PC Bank to MasterCard® International Incorporated ("MasterCard®") for accepting PC Bank as a card member and licensee of MasterCard®. As at January 3, 2015, the guarantee on behalf of PC Bank to MasterCard® was USD \$170 million (December 28, 2013 – USD \$170 million).

## 12. Quarterly Results of Operations

### 12.1 Results by Quarter

Under an accounting convention common in the retail industry, the Company follows a 52-week reporting cycle which periodically necessitates a fiscal year of 53 weeks. Fiscal year 2014 is 53 weeks and fiscal year 2013 is 52 weeks. When a fiscal year such as 2014 contains 53 weeks, the fourth quarter is 13 weeks in duration. The 52-week reporting cycle is divided into four quarters of 12 weeks each except for the third quarter, which is 16 weeks in duration.

The following is a summary of selected consolidated financial information derived from the Company's unaudited interim period condensed consolidated financial statements for each of the eight most recently completed quarters:

### Summary of Consolidated Quarterly Results

(millions of Canadian dollars except where otherwise indicated)	2014					2013 <sup>(4)</sup>				
	First Quarter (12 weeks)	Second Quarter (12 weeks)	Third Quarter (16 weeks)	Fourth Quarter (13 weeks)	Total (audited) (53 weeks)	First Quarter (12 weeks)	Second Quarter (12 weeks)	Third Quarter (16 weeks)	Fourth Quarter (12 weeks)	Total (audited) (52 weeks)
Revenue	\$ 7,292	\$ 10,307	\$ 13,599	\$ 11,413	\$ 42,611	\$ 7,202	\$ 7,520	\$ 10,009	\$ 7,640	\$ 32,371
Net earnings (loss)	\$ 120	\$ (456)	\$ 142	\$ 247	\$ 53	\$ 186	\$ 177	\$ 150	\$ 114	\$ 627
Net earnings (loss) per common share:										
Basic (\$)	\$ 0.43	\$ (1.13)	\$ 0.34	\$ 0.60	\$ 0.14	\$ 0.66	\$ 0.63	\$ 0.53	\$ 0.41	\$ 2.23
Diluted (\$)	\$ 0.42	\$ (1.13)	\$ 0.34	\$ 0.59	\$ 0.14	\$ 0.65	\$ 0.62	\$ 0.53	\$ 0.40	\$ 2.21
Average national food price inflation (as measured by CPI)	1.2%	2.5%	2.8%	3.5%	2.5%	1.4%	1.5%	0.9%	0.9%	1.1%
Retail same-store sales <sup>(1), (6)</sup> growth	0.9%	1.8%	2.6%	2.4%	2.0%	2.8%	1.1%	0.4%	0.6%	1.1%

CPI does not necessarily reflect the effect of inflation on the specific mix of goods sold in Loblaw stores.

## Management's Discussion and Analysis

Over the past eight quarters, net retail square footage increased by 0.4 million square feet to 51.9 million square feet, excluding Shoppers Drug Mart.

Fluctuations in quarterly net earnings reflect the underlying operations of the Company and are impacted by seasonality, which is greatest in the fourth quarter and least in the first quarter, the timing of holidays and were impacted by the items set out in Section 20 "Non-GAAP Financial Measures" of the MD&A as well as the following significant items:

- Transition of certain stores to more cost effective and efficient operating terms under collective agreements; and
- Equity-based compensation, net of equity forwards.

### 12.2 Fourth Quarter Results

The following is a summary of selected consolidated unaudited financial information for the fourth quarter of 2014:

For the periods ended January 3, 2015 and December 28, 2013 (millions of Canadian dollars except where otherwise indicated)	2014 (13 weeks)	2013 <sup>(4)</sup> (12 weeks)	\$ Change	% Change
Revenue	\$ 11,413	\$ 7,640	\$ 3,773	49.4 %
<i>Revenue excluding Shoppers Drug Mart</i>	<i>8,359</i>	<i>7,640</i>	<i>719</i>	<i>9.4 %</i>
EBITDA <sup>(2)</sup>	\$ 900	\$ 492	\$ 408	82.9 %
Adjusted EBITDA <sup>(2)</sup>	950	489	461	94.3 %
Adjusted EBITDA margin <sup>(2)</sup>	8.3%	6.4%		
<i>Adjusted EBITDA<sup>(2)</sup> excluding Shoppers Drug Mart</i>	<i>\$ 598</i>	<i>\$ 489</i>	<i>\$ 109</i>	<i>22.3 %</i>
<i>Adjusted EBITDA margin<sup>(2)</sup> excluding Shoppers Drug Mart</i>	<i>7.2%</i>	<i>6.4%</i>		
Operating income	\$ 507	\$ 296	\$ 211	71.3 %
Adjusted operating income <sup>(2)</sup>	681	293	388	132.4 %
Adjusted operating margin <sup>(2)</sup>	6.0%	3.8%		
<i>Adjusted operating income<sup>(2)</sup> excluding Shoppers Drug Mart</i>	<i>\$ 391</i>	<i>\$ 293</i>	<i>\$ 98</i>	<i>33.4 %</i>
<i>Adjusted operating margin<sup>(2)</sup> excluding Shoppers Drug Mart</i>	<i>4.7%</i>	<i>3.8%</i>		
Net interest expense and other financing charges	\$ 169	\$ 141	\$ 28	19.9 %
Adjusted net interest expense and other financing charges <sup>(2)</sup>	144	92	52	56.5 %
Net earnings	247	114	133	116.7 %
Adjusted net earnings <sup>(2)</sup>	396	161	235	146.0 %
Basic net earnings per common share (\$)	\$ 0.60	\$ 0.41	\$ 0.19	46.3 %
Adjusted basic net earnings per common share <sup>(2)</sup> (\$)	0.96	0.57	0.39	68.4 %
Cash flows from (used in):				
Operating activities	\$ 952	\$ 738	\$ 214	29.0 %
Investing activities	(363)	471	(834)	(177.1)%
Financing activities	(575)	(387)	(188)	(48.6)%
Dividends declared per common share (\$)	\$ 0.245	\$ 0.240	\$ 0.005	2.1 %
Dividends declared on Second Preferred Share, Series A (\$)	0.37	0.37	—	— %

**Revenue** Revenue of \$11,413 million in the fourth quarter of 2014 increased by \$3,773 million compared to the fourth quarter of 2013, primarily due to Shoppers Drug Mart and the impact of the 13th week of the fourth quarter of 2014. Revenue in the 13th week of the fourth quarter of 2014 was \$789 million (\$574 million excluding Shoppers Drug Mart). Excluding the impact of Shoppers Drug Mart, consolidated revenue increased by \$719 million, or 9.4%. Excluding the impact of Shoppers Drug Mart and the 13th week of the fourth quarter of 2014, consolidated revenue increased by \$145 million, or 1.9%.



**EBITDA<sup>(2)</sup>** EBITDA<sup>(2)</sup> of \$900 million in the fourth quarter of 2014 increased by \$408 million compared to the fourth quarter of 2013, primarily driven by Shoppers Drug Mart. The increase in EBITDA<sup>(2)</sup> was positively impacted by adjustments of \$50 million including restructuring of franchise fees (\$40 million) and restructuring costs incurred in 2013 (\$32 million), that were not incurred in 2014. The increases were partially offset by the net loss on divestitures related to the acquisition of Shoppers Drug Mart (\$7 million), the recognition of the fair value increment on the acquired Shoppers Drug Mart inventory sold (\$69 million), increased fixed asset and other related impairments (\$43 million), the fair value adjustment on fuel and foreign currency contracts (\$4 million) and the fair value adjustment on Shoppers Drug Mart's equity-based compensation liability (\$2 million).

After excluding these adjustments, adjusted EBITDA<sup>(2)</sup> of \$950 million increased by \$461 million compared to the fourth quarter of 2013. The increase included \$352 million of adjusted EBITDA<sup>(2)</sup> contributed by Shoppers Drug Mart, with the remainder of the increase of \$109 million primarily driven by the Retail segment. The increase was positively impacted by net synergies of \$49 million and the 13th week of the fourth quarter of 2014 of \$71 million. Adjusted EBITDA margin<sup>(2)</sup> was 8.3% for the fourth quarter of 2014 compared to 6.4% in the same quarter in 2013. Excluding the impact of Shoppers Drug Mart, adjusted EBITDA<sup>(2)</sup> increased by \$109 million, or 22.3%, compared to the fourth quarter of 2013 and adjusted EBITDA margin<sup>(2)</sup> was 7.2% compared to 6.4% in the same quarter in 2013.

**Synergies** During the fourth quarter of 2014, the Company realized approximately \$49 million of net synergies associated with the acquisition of Shoppers Drug Mart, primarily in cost of goods sold.

**Operating Income** Operating income of \$507 million in the fourth quarter of 2014 increased by \$211 million compared to the fourth quarter of 2013, primarily driven by Shoppers Drug Mart. Operating income was negatively impacted by the net adjustments related to EBITDA<sup>(2)</sup> noted above of \$50 million and by the amortization of intangible assets of \$124 million related to the acquisition of Shoppers Drug Mart.

After excluding these impacts to operating income, adjusted operating income<sup>(2)</sup> of \$681 million increased by \$388 million compared to the fourth quarter of 2013, including \$290 million of adjusted operating income<sup>(2)</sup> contributed by Shoppers Drug Mart. Adjusted operating margin<sup>(2)</sup> was 6.0% compared to 3.8% in the fourth quarter of 2013. Excluding the impact of Shoppers Drug Mart, adjusted operating income<sup>(2)</sup> increased by \$98 million and was positively impacted by the increase in adjusted EBITDA<sup>(2)</sup> noted above of \$109 million, partially offset by an increase in depreciation and amortization<sup>(2)</sup> of \$11 million.

**Net Interest Expense and Other Financing Charges** Net interest expense and other financing charges of \$169 million in the fourth quarter of 2014 increased by \$28 million compared to the fourth quarter of 2013, including a lower fair value adjustment related to the Trust Unit Liability for the change in the fair value of Choice Properties' Units held by unitholders other than the Company, Shoppers Drug Mart acquisition-related costs incurred in the fourth quarter of 2013 and certain other adjustments as set out in Section 20 "Non-GAAP Financial Measures".

After excluding these impacts to net interest expense and other financing charges, adjusted net interest expense and other financing charges<sup>(2)</sup> of \$144 million increased by \$52 million, primarily driven by higher interest on long term debt, primarily as a result of debt incurred to finance the acquisition of Shoppers Drug Mart.

**Income Taxes** Income tax expense for the fourth quarter of 2014 was \$91 million and the effective tax rate was 26.9%. Income tax expense for the fourth quarter of 2013 was \$41 million and the effective tax rate was 26.5%. The marginal increase in the effective tax rate was primarily attributable to an increase in certain non-deductible amounts. The adjusted income tax expense<sup>(2)</sup> for the fourth quarter was \$141 million and the adjusted income tax rate<sup>(2)</sup> was 26.3%. The adjusted income tax expense<sup>(2)</sup> for the fourth quarter of 2013 was \$40 million and the adjusted income tax rate<sup>(2)</sup> was 19.9%, which reflects an increase in certain non-taxable amounts.

**Net Earnings** Net earnings of \$247 million in the fourth quarter of 2014 increased by \$133 million compared to the fourth quarter of 2013, primarily driven by the increase in operating income, partially offset by the increase in net interest expense and other financing charges and by the increase in the income tax expense, described above.

Adjusted net earnings<sup>(2)</sup> of \$396 million increased by \$235 million compared to the fourth quarter of 2013, primarily driven by the increase in adjusted operating income<sup>(2)</sup>, primarily as a result of Shoppers Drug Mart, partially offset by the increase in adjusted net interest expense and other financing charges<sup>(2)</sup> and the increase in the adjusted income tax expense<sup>(2)</sup>, described above.

**Basic Net Earnings Per Common Share** Basic net earnings per common share were \$0.60 compared to \$0.41 in the fourth quarter of 2013. Basic net earnings per common share included the negative impacts of amortization of intangible assets (\$0.22 per share), the recognition of a portion of the Shoppers Drug Mart acquisition-related fair value adjustments for inventory sold (\$0.12 per share), the divestiture of certain stores related to the acquisition of Shoppers Drug Mart (\$0.02 per share), certain other adjustments (\$0.07 per share), partially offset by restructuring of franchise fees (\$0.07 per share).

## Management's Discussion and Analysis

Adjusted basic net earnings per common share<sup>(2)</sup> were \$0.96 in the fourth quarter of 2014 compared to \$0.57 in the fourth quarter of 2013. This increase was primarily due to the increase in adjusted net earnings<sup>(2)</sup> as described above, partially offset by the dilutive effect of the 119.5 million common shares issued as partial consideration for the acquisition of Shoppers Drug Mart.

**Capital Investments** In the fourth quarter of 2014, the Company invested \$400 million (2013 – \$304 million) in fixed asset purchases and intangible asset additions.

**Free Cash Flow<sup>(2)</sup>** For the fourth quarter of 2014, free cash flow<sup>(2)</sup> was \$439 million compared to \$336 million in the fourth quarter of 2013. The increase in free cash flow<sup>(2)</sup> in the fourth quarter of 2014 was primarily due to higher cash flows from operating activities, partially offset by an increase in capital investments as well as higher interest payments.

**Adjusted Debt<sup>(2)</sup>** On closing of the acquisition of Shoppers Drug Mart, adjusted debt<sup>(2)</sup> was \$11,060 million. The Company made significant progress in meeting its debt reduction target by decreasing adjusted debt<sup>(2)</sup> by \$421 million in the fourth quarter of 2014 and by \$1,065 million since the closing of the acquisition of Shoppers Drug Mart resulting in an outstanding adjusted debt<sup>(2)</sup> balance of \$9,995 million as at January 3, 2015. The reduction in adjusted debt<sup>(2)</sup> since closing included the repayment of a \$350 million MTN and a repayment of the unsecured term loan facility (net of the replacement of all tranches of inter-corporate debt of Choice Properties initially held by Loblaw and sold to unrelated parties).

**Cash Flows from Operating Activities** Cash flows from operating activities for the fourth quarter of 2014 were \$952 million compared to \$738 million in 2013. The increase was primarily driven by higher cash earnings, primarily driven by the acquisition of Shoppers Drug Mart, partially offset by a higher change in non-cash working capital and the settlement of cross currency swaps in the fourth quarter of 2013. The change in non-cash working capital was due to a quarter over quarter lower increase in accounts payable and decrease in prepaid expenses, partially offset by a decrease in inventory.

**Cash Flows (used in) from Investing Activities** Cash flows used in investing activities for the fourth quarter of 2014 were \$363 million compared to cash flows from investing activities of \$471 million in 2013. The decrease in cash flows from investing activities was primarily due to a reduction in short term investments and the release of funds from security deposits in the fourth quarter of 2013 for the repayment of *Eagle* notes.

**Cash Flows used in Financing Activities** Cash flows used in financing activities for the fourth quarter of 2014 were \$575 million compared to \$387 million in 2013. In the fourth quarter of 2014, cash flows used in financing activities were primarily driven by net repayment of long term debt, change in bank indebtedness acquired with the Shoppers Drug Mart acquisition, as well as interest and dividend payments. In the same period in 2013, cash flows used in financing activities were primarily due to the repayment of short term debt and interest payments.

### Retail Segment Fourth Quarter Results of Operations

For the periods ended January 3, 2015 and December 28, 2013 (millions of Canadian dollars except where otherwise indicated)	2014 (13 weeks)	2013 <sup>(4)</sup> (12 weeks)	\$ Change	% Change
Sales	\$ 11,164	\$ 7,419	\$ 3,745	50.5%
Gross profit	2,925	1,625	1,300	80.0%
Adjusted gross profit <sup>(2)</sup>	2,994	1,625	1,369	84.2%
EBITDA <sup>(2)</sup>	847	443	404	91.2%
Adjusted EBITDA <sup>(2)</sup>	897	440	457	103.9%
Operating income	459	252	207	82.1%
Adjusted operating income <sup>(2)</sup>	633	249	384	154.2%

For the periods ended January 3, 2015 and December 28, 2013	2014 (13 weeks)	2013 <sup>(4)</sup> (12 weeks)
Same-store sales <sup>(1), (6)</sup> growth	2.4%	0.6%
Adjusted gross profit % <sup>(2)</sup>	26.8%	21.9%
Adjusted EBITDA margin <sup>(2)</sup>	8.0%	5.9%
Adjusted operating margin <sup>(2)</sup>	5.7%	3.4%

For a discussion of Shoppers Drug Mart results, please see Addendum A on page 29 of the Company's fourth quarter of 2014 News Release.

## Sales

For the periods ended January 3, 2015 and December 28, 2013 (millions of Canadian dollars except where otherwise indicated)	2014 (13 weeks)	2013 <sup>(4)</sup> (12 weeks)	\$ Change	% Change
Retail segment sales	\$ 11,164	\$ 7,419	\$ 3,745	50.5%
Shoppers Drug Mart	3,054			
Excluding Shoppers Drug Mart	\$ 8,110	\$ 7,419	\$ 691	9.3%

- Retail segment sales of \$11,164 million in the fourth quarter of 2014 increased by \$3,745 million compared to the fourth quarter of 2013, primarily due to Shoppers Drug Mart and the impact of the 13th week of the fourth quarter of 2014. Retail segment sales in the 13th week of the fourth quarter of 2014 were \$789 million (\$574 million excluding Shoppers Drug Mart). Excluding the impact of Shoppers Drug Mart and the 13th week of the fourth quarter of 2014, Retail segment sales increased by \$117 million, or 1.6%, due to the following factors:
  - Same-store sales<sup>(1, 6)</sup> growth, for core grocery, was 3.3% for the quarter, excluding gas bar (0.5%) and the negative impact of a change in distribution model by a tobacco supplier (0.4%). On a comparable basis, same-store sales<sup>(1, 6)</sup> growth was 2.4% (2013 – 0.6%);
  - On a comparable week basis:
    - Sales growth in food was strong, primarily driven by inflation;
    - Sales in drugstore were flat, with increases in health and beauty, offset by declines in pharmacy;
    - Sales in gas bar declined, primarily driven by a decline in gas prices;
    - Sales in general merchandise, excluding apparel, were flat; and
    - Sales in retail apparel were flat, while U.S. wholesale apparel sales declined significantly;
  - The Company's average quarterly internal food price index was slightly higher than (2013 – lower than) the average quarterly national food price inflation of 3.5% (2013 – 0.9%) as measured by CPI. CPI does not necessarily reflect the effect of inflation on the specific mix of goods sold in Loblaw stores; and
  - 22 corporate and franchise stores were opened and 12 corporate and franchise stores were closed in the last 12 months, with an additional two franchise grocery stores divested as a result of a Consent Agreement with the Competition Bureau related to the acquisition of Shoppers Drug Mart, resulting in flat square footage growth.
- Since the acquisition date, Shoppers Drug Mart opened 17 new drug stores and closed 24 drug stores, including 13 drug stores divested in accordance with the Consent Agreement with the Competition Bureau related to the acquisition of Shoppers Drug Mart. As a result, net square footage increased by 0.1 million square feet, or 0.6%.

## Gross Profit

For the periods ended January 3, 2015 and December 28, 2013 (millions of Canadian dollars except where otherwise indicated)	2014 (13 weeks)	2013 <sup>(4)</sup> (12 weeks)	\$ Change	% Change
Retail gross profit	\$ 2,925	\$ 1,625	\$ 1,300	80.0%
Adjustments <sup>(2)</sup>	69	—		
Adjusted Retail gross profit <sup>(2)</sup>	\$ 2,994	\$ 1,625	\$ 1,369	84.2%
Adjusted gross profit % <sup>(2)</sup>	26.8%	21.9%		
Shoppers Drug Mart	\$ 1,221			
Excluding Shoppers Drug Mart	\$ 1,773	\$ 1,625	\$ 148	9.1%
Adjusted gross profit % <sup>(2)</sup>	21.9%	21.9%		

- In the fourth quarter of 2014, gross profit of \$2,925 million increased by \$1,300 million compared to 2013, primarily due to Shoppers Drug Mart and was negatively impacted by the recognition of the fair value increment on the acquired Shoppers Drug Mart inventory sold (\$69 million).  
After excluding this adjustment<sup>(2)</sup>, adjusted gross profit<sup>(2)</sup> of \$2,994 million increased by \$1,369 million, including \$1,221 million of adjusted gross profit<sup>(2)</sup> contributed by Shoppers Drug Mart. Adjusted gross profit percentage<sup>(2)</sup> was 26.8% compared to 21.9% in the fourth quarter of 2013.
- Excluding Shoppers Drug Mart, adjusted gross profit percentage<sup>(2)</sup> was 21.9%, flat compared to 2013. While flat, adjusted gross profit percentage<sup>(2)</sup> was positively impacted by synergies related to the acquisition and reductions in transportation costs, but negatively impacted by increased shrink. Excluding Shoppers Drug Mart, adjusted gross profit<sup>(2)</sup> increased by \$148 million, or 9.1%, compared to 2013, driven by higher sales, including the impact of the 13th week in the fourth quarter of 2014.

**EBITDA<sup>(2)</sup>**

For the periods ended January 3, 2015 and December 28, 2013 (millions of Canadian dollars except where otherwise indicated)	2014 (13 weeks)	2013 <sup>(4)</sup> (12 weeks)	\$ Change	% Change
EBITDA <sup>(2)</sup>	\$ 847	\$ 443	\$ 404	91.2%
Adjustments <sup>(2)</sup>	50	(3)		
Adjusted Retail EBITDA <sup>(2)</sup>	\$ 897	\$ 440	\$ 457	103.9%
Adjusted EBITDA margin <sup>(2)</sup>	8.0%	5.9%		
Shoppers Drug Mart	\$ 352			
Excluding Shoppers Drug Mart	\$ 545	\$ 440	\$ 105	23.9%
Adjusted EBITDA margin <sup>(2)</sup>	6.7%	5.9%		

- EBITDA<sup>(2)</sup> of \$847 million in the fourth quarter of 2014 increased by \$404 million compared to the fourth quarter of 2013, primarily driven by Shoppers Drug Mart. EBITDA<sup>(2)</sup> was negatively impacted by adjustments of \$50 million as set out in Section 20 "Non-GAAP Financial Measures". The significant adjustments during the fourth quarter of 2014 included restructuring of franchise fees, the recognition of the fair value increment on the acquired Shoppers Drug Mart inventory sold and net divestitures loss related to the acquisition of Shoppers Drug Mart.

After excluding these adjustments<sup>(2)</sup>, adjusted EBITDA<sup>(2)</sup> of \$897 million increased by \$457 million compared to the fourth quarter of 2013, including \$352 million of adjusted EBITDA<sup>(2)</sup> contributed by Shoppers Drug Mart.

Excluding the impact of Shoppers Drug Mart, adjusted EBITDA<sup>(2)</sup> of \$545 million increased by \$105 million, driven by the increase in adjusted gross profit<sup>(2)</sup> of \$148 million, as described above, partially offset by the increase in SG&A of \$43 million. The increase in SG&A was driven by the 13th week in the fourth quarter of 2014. Excluding the 13th week of the fourth quarter of 2014, SG&A decreased. This decrease was primarily driven by supply chain efficiencies, changes in the fair value of the Company's franchise investments and lower administrative and other operating costs, partially offset by higher foreign exchange losses, higher investments in the Company's franchise business and synergy related costs.

- For the fourth quarter of 2014, adjusted EBITDA margin<sup>(2)</sup> was 8.0% compared to 5.9% in 2013, primarily driven by Shoppers Drug Mart. Excluding the impact of Shoppers Drug Mart, adjusted EBITDA margin<sup>(2)</sup> was 6.7% compared to 5.9% in 2013.

**Operating Income**

For the periods ended January 3, 2015 and December 28, 2013 (millions of Canadian dollars except where otherwise indicated)	2014 (13 weeks)	2013 <sup>(4)</sup> (12 weeks)	\$ Change	% Change
Retail operating income	\$ 459	\$ 252	\$ 207	82.1%
Adjustments <sup>(2)</sup>	174	(3)		
Adjusted Retail operating income <sup>(2)</sup>	\$ 633	\$ 249	\$ 384	154.2%
Adjusted operating margin <sup>(2)</sup>	5.7%	3.4%		
Shoppers Drug Mart	\$ 290			
Excluding Shoppers Drug Mart	\$ 343	\$ 249	\$ 94	37.8%
Adjusted operating margin <sup>(2)</sup>	4.2%	3.4%		

- Operating income of \$459 million in the fourth quarter of 2014 increased by \$207 million compared to the fourth quarter of 2013, primarily driven by the acquisition-related accounting adjustments of Shoppers Drug Mart. Operating income was negatively impacted by the amortization of intangible assets related to the acquisition of \$124 million and the net adjustments related to EBITDA<sup>(2)</sup> of \$50 million, as noted above.

After excluding the adjustments to operating income set out in Section 20 "Non-GAAP Financial Measures", adjusted operating income<sup>(2)</sup> of \$633 million increased by \$384 million compared to the fourth quarter of 2013, including \$290 million of adjusted operating income<sup>(2)</sup> contributed by Shoppers Drug Mart. Excluding the impact of Shoppers Drug Mart, adjusted operating income<sup>(2)</sup> increased by \$94 million, or 37.8%, driven by the increase in adjusted EBITDA<sup>(2)</sup> described above, partially offset by the increase in retail depreciation and amortization<sup>(2)</sup> of \$11 million.

- For the fourth quarter of 2014, adjusted operating margin<sup>(2)</sup> was 5.7% compared to 3.4% in 2013, primarily driven by the inclusion of Shoppers Drug Mart. Excluding the impact of Shoppers Drug Mart, adjusted operating margin<sup>(2)</sup> was 4.2% compared to 3.4% in 2013.



## Financial Services Segment Fourth Quarter Results of Operations<sup>(7)</sup>

For the periods ended January 3, 2015 and December 28, 2013 (millions of Canadian dollars except where otherwise indicated)	2014 (13 weeks)	2013 (12 weeks)	\$ Change	% Change
Revenue	\$ 231	\$ 204	\$ 27	13.2%
Operating income	49	43	6	14.0%
Earnings before income taxes	35	29	6	20.7%

(millions of Canadian dollars except where otherwise indicated)	As at January 3, 2015	As at December 28, 2013	\$ Change	% Change
Average quarterly net credit card receivables	\$ 2,535	\$ 2,345	\$ 190	8.1%
Credit card receivables	2,630	2,538	92	3.6%
Allowance for credit card receivables	54	47	7	14.9%
Annualized yield on average quarterly gross credit card receivables	13.7%	13.6%		
Annualized credit loss rate on average quarterly gross credit card receivables	4.4%	4.2%		

- Revenue for the fourth quarter of 2014 of \$231 million increased by \$27 million, or 13.2%, compared to the fourth quarter of 2013. This increase was primarily driven by higher interest and interchange income as a result of growth in the credit card receivables portfolio.
- Operating income of \$49 million increased by \$6 million and earnings before income taxes of \$35 million in the fourth quarter of 2014 increased by \$6 million, respectively, compared to the fourth quarter of 2013. These increases were primarily driven by higher revenue described above, partially offset by higher costs associated with the Financial Services loyalty program, higher credit losses from increased credit card receivable balances and higher operating costs as a result of an increase in the active customer base.
- As at January 3, 2015, credit card receivables were \$2,630 million, an increase of \$92 million compared to December 28, 2013. This increase was primarily driven by a growth in the active customer base as a result of continued investments in customer acquisitions and marketing initiatives. As at January 3, 2015, the allowance for credit card receivables was \$54 million, an increase of \$7 million compared to December 28, 2013, primarily due to the growth in the credit card receivables portfolio.
- Subsequent to the end of 2014:
  - The Company, through PC Bank, extended the maturity date for certain Other Independent Securitization Trust agreements from the second quarter of 2016 to the second quarter of 2017, with all other terms and conditions remaining substantially the same; and
  - PC Bank entered into USD foreign exchange forward agreements, which mature by December 2015. The notional amounts of the contracts total USD \$27 million.

Choice Properties Segment Fourth Quarter Results of Operations<sup>(5)</sup>

For the periods ended January 3, 2015 and December 28, 2013 (millions of Canadian dollars)	2014 (13 weeks)	2013 <sup>(4)</sup> (12 weeks)	\$ Change	% Change
Revenue	\$ 175	\$ 165	\$ 10	6.1 %
Operating income	223	186	37	19.9 %
Adjusted operating income <sup>(2)</sup>	223	186	37	19.9 %
Net interest expense and other financing charges	137	193	(56)	(29.0)%
Adjusted funds from operations <sup>(2)</sup>	74	65	9	13.8 %

- Revenue for the fourth quarter of 2014 of \$175 million increased by 10 million, or 6.1%, compared to 2013, and included \$157 million (2013 – \$148 million) generated from tenants within the Retail segment. The increase was primarily driven by revenue from properties acquired since the IPO.
- Operating income and adjusted operating income<sup>(2)</sup> of \$223 million in the fourth quarter of 2014 increased by \$37 million compared to the fourth quarter of 2013 and included a \$29 million year-over-year favourable fair value adjustment on investment properties. The fair value adjustment on investment properties is eliminated on consolidation.
- Adjusted funds from operations<sup>(2)</sup> of \$74 million in the fourth quarter of 2014 increased by \$9 million compared to the fourth quarter of 2013. The increase was mainly attributable to an increase in net property income and the decrease in sustaining property and leasing capital expenditures, normalized, partially offset by increased general and administrative expenses and interest and other financing charges.
- In the fourth quarter of 2014:
  - The Company sold 16 properties to Choice Properties for an aggregate price of approximately \$210 million. Consideration for the properties included 10,698,143 Class B Limited Partnership units, \$98 million in cash and the assumption of a \$4 million mortgage by Choice Properties. In addition, Choice Properties acquired a 40% interest in a limited partnership, which acquired land from the Company, intended for development into a mixed-used property, for approximately \$6 million; and
  - Choice Properties acquired a 70% interest in a limited partnership, which holds land intended for future retail development, for approximately \$18 million.
- Subsequent to the end of 2014:
  - The Company sold a warehouse to Choice Properties for approximately \$81 million. The warehouse is fully occupied by the Company as the single tenant with a 20-year initial lease term with six five-year renewal options;
  - The Company sold a parcel of land to Choice Properties for approximately \$12 million. Consideration for the acquisition included 265,665 Class B Limited Partnership units, \$7 million in cash and the assumption of a \$2 million obligation. The Class B Limited Partnership units issued to the Company as partial consideration for this transaction did not impact the Company's effective ownership percentage; and
  - Choice Properties issued \$250 million aggregate principal amount of Series E senior unsecured debentures bearing interest at a rate of 2.30% per annum and maturing in 2020. The net proceeds from the issuance were used by Choice Properties to repay existing indebtedness and for general business purposes.
- As of January 3, 2015, the Company's ownership interest in Choice Properties was 82.9%.

### 13. Disclosure Controls and Procedures

Management is responsible for establishing and maintaining a system of disclosure controls and procedures to provide reasonable assurance that all material information relating to the Company and its subsidiaries is gathered and reported to senior management on a timely basis so that appropriate decisions can be made regarding public disclosure.

As required by National Instrument 52-109 (Certification of Disclosure in Issuers' Annual and Interim Filings), the President, as the Chief Executive Officer ("CEO"), and the Chief Financial Officer ("CFO") have caused the effectiveness of the disclosure controls and procedures to be evaluated. Based on that evaluation, they have concluded that the design and operation of the system of disclosure controls and procedures were effective as at January 3, 2015.

### 14. Internal Control over Financial Reporting

Management is also responsible for establishing and maintaining adequate internal controls over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial reports for external purposes in accordance with IFRS.

As required by National Instrument 52-109 (Certification of Disclosure in Issuers' Annual and Interim Filings), the President, as CEO, and the CFO have caused the effectiveness of the internal controls over financial reporting to be evaluated using the framework established in 'Internal Control – Integrated Framework (COSO Framework)' published by The Committee of Sponsoring Organizations of the Treadway Commission (COSO), 2013. Based on that evaluation, they have concluded that the design and operation of the Company's internal controls over financial reporting were effective as at January 3, 2015.

In designing such controls, it should be recognized that due to inherent limitations, any controls, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives and may not prevent or detect misstatements. Projections of any evaluations of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate. Additionally, management is required to use judgment in evaluating controls and procedures.

**Changes in Internal Control over Financial Reporting** There were no changes in the Company's internal controls over financial reporting in the fourth quarter of 2014 that materially affected, or are reasonably likely to materially affect the Company's internal control over financial reporting, except as noted below:

In accordance with the provisions of National Instrument 52-109 – Certification of Disclosure in Issuers' Annual and Interim Filings, management, including the CEO and CFO, have limited the scope of their design of the Company's disclosure controls and procedures and internal control over financial reporting to exclude controls, policies and procedures of Shoppers Drug Mart. Loblaw acquired the net assets of Shoppers Drug Mart and its subsidiaries on March 28, 2014.

Shoppers Drug Mart's contribution to the Company's consolidated financial statements for the year ended January 3, 2015 was approximately 20 percent of consolidated revenues and approximately 35 percent of consolidated adjusted operating income. Additionally, Shoppers Drug Mart's current assets and current liabilities were approximately 30 percent and 25 percent of consolidated current assets and liabilities, respectively, and its long term assets and long term liabilities were approximately 55 percent and 20 percent of consolidated long term assets and long term liabilities, respectively.

The scope limitation is primarily based on the time required to assess Shoppers Drug Mart's disclosure controls and procedures (DC&P) and internal controls over financial reporting in a manner consistent with the Company's other operations. The assessment on the design effectiveness of DC&P and internal controls over financial reporting is on track for completion by the second quarter of 2015 and the assessment of operating effectiveness will be completed by fourth quarter of 2015.

Further details related to the acquisition of Shoppers Drug Mart are disclosed in Section 7 "Acquisition of Shoppers Drug Mart Corporation" of this MD&A and in the notes to the Company's annual audited consolidated financial statements for the fiscal year ended January 3, 2015.

### 15. Enterprise Risks and Risk Management

The Company is committed to maintaining a framework that ensures risk management is an integral part of its activities. To ensure the continued growth and success of the Company, risks are identified and managed through an Enterprise Risk Management ("ERM") program. The Board has approved an ERM policy and oversees the ERM program through approval of the Company's risks and risk prioritization. The ERM program assists all areas of the business in managing appropriate levels of risk tolerance by bringing a systematic approach, methodology and tools for evaluating, measuring and monitoring key risks. The results of the ERM program and other business planning processes are used to identify emerging risks to the Company, prioritize risk management activities and develop a risk-based internal audit plan.

## Management's Discussion and Analysis

Risks are not eliminated through the ERM program. Risks are identified and managed within understood risk tolerances. The ERM program is designed to:

- promote a culture of awareness of risk management and compliance within the Company;
- facilitate corporate governance by providing a consolidated view of risks across the Company and insight into the methodologies for identification, assessment, measurement and monitoring of the risks;
- assist in developing consistent risk management methodologies and tools across the organization; and
- enable the Company to focus on its key risks in the business planning process and reduce harm to financial performance through responsible risk management.

Risk identification and assessments are important elements of the Company's ERM framework. An annual ERM assessment is completed to assist in the update and identification of internal and external risks, which may be both strategic and operational in nature. Key risks affecting the Company are prioritized under five categories: financial, operational, regulatory, human capital and reputational risks. The annual ERM assessment is carried out through interviews, surveys and facilitated workshops with management and the Board. Risks are assessed and evaluated based on the Company's vulnerability to the risk and the potential impact that the underlying risks would have on the Company's ability to execute its strategies and achieve its objectives. Risk owners are assigned relevant risks and key risk indicators are developed. Management provides a semi-annual update to a committee of the Board on the status of the key risks based on significant changes from the prior update, anticipated impacts in future quarters and significant changes in key risk indicators. In addition, the long term risk level is assessed to monitor potential long term risk impacts, which may assist in risk mitigation planning activities. Accountability for oversight of the management of each risk is allocated by the Board either to the full Board or to a committee of the Board.

Operating and financial risks which are reasonably likely to affect the Company's future performance are discussed below. Any of these risks has the potential to negatively affect the Company and its financial performance. The Company has risk management strategies, including insurance programs, controls and contractual arrangements. However, there can be no assurance that the associated risks will be mitigated or will not materialize or that events or circumstances will not occur that could adversely affect the Company's financial condition or performance. The risks included below should be read in conjunction with the risks included in the Company's AIF (for the year ended January 3, 2015).

### 15.1 Operating Risks and Risk Management

The following is a summary of the Company's key operating risks which are discussed in detail below:

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Acquisition of Shoppers Drug Mart Corporation	Competitive Environment
IT Systems Implementations	Regulatory and Tax
Pharmacy Industry Regulations	Legal Proceedings
Inventory Management	Vendor Management and Third Party Service Providers
Information Integrity and Reliability	Franchisee Independence and Relationships
Availability, Access and Security of Information Technology	Associate-owned Drug Store Network and Relationships with Associates
Product Safety and Public Health	Alternative Arrangements for Sourcing Generic Drug Products
Labour Relations	Multi-Employer Pension Plans

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#### Discussion of Operating Risks and Risk Management Strategies

**Acquisition of Shoppers Drug Mart Corporation** On March 28, 2014, the Company acquired all of the outstanding shares of Shoppers Drug Mart. The realization of the anticipated strategic benefits associated with this acquisition will depend on several factors and will require significant effort on the part of management of the Company. Failure to realize the anticipated strategic benefits or operational, competitive and cost synergies associated with this acquisition could adversely affect the reputation, operations or financial performance of the Company.



**IT Systems Implementations** The Company continues to undertake a major upgrade of its IT infrastructure. Completing the IT systems deployment will require continued focus and investment. Failure to successfully migrate from legacy systems to the new IT systems or a significant disruption in the Company's current IT systems during the implementation of the new systems could result in a lack of accurate data to enable management to effectively manage day-to-day operations of the business or achieve its operational objectives, causing significant disruptions to the business and potential financial losses. Failure to successfully adopt the new IT systems or to implement appropriate processes to support them could result in inefficiencies and duplication in processes, which could in turn adversely affect the reputation, operations and financial performance of the Company. Failure to realize the anticipated strategic benefits including revenue growth, anticipated cost savings or operating efficiencies associated with the new IT systems could adversely affect the reputation, operations or financial performance of the Company.

**Pharmacy Industry Regulation** With the acquisition of Shoppers Drug Mart, the Company is reliant on prescription drug sales for a more significant portion of its sales and profits. Prescription drugs and their sales are subject to numerous federal, provincial, territorial and local laws and regulations. Changes to these laws and regulations, or non-compliance with these laws and regulations, could adversely affect the reputation, operations or financial performance of the Company.

Federal and provincial laws and regulations that establish public drug plans typically regulate prescription drug coverage, patient eligibility, pharmacy reimbursement, drug product eligibility and drug pricing and may also regulate manufacturer allowance funding that is provided to or received by pharmacy or pharmacy suppliers. With respect to pharmacy reimbursement, such laws and regulations typically regulate the allowable drug cost of a prescription drug product, the permitted mark-up on a prescription drug product and the professional or dispensing fees that may be charged on prescription drug sales to patients eligible under the public drug plan. With respect to drug product eligibility, such laws and regulations typically regulate the requirements for listing the manufacturer's products as a benefit or partial benefit under the applicable governmental drug plan, drug pricing and, in the case of generic prescription drug products, the requirements for designating the product as interchangeable with a branded prescription drug product. In addition, other federal, provincial, territorial and local laws and regulations govern the approval, packaging, labeling, sale, marketing, advertising, handling, storage, distribution, dispensing and disposal of prescription drugs.

Sales of prescription drugs, pharmacy reimbursement and drug prices may be affected by changes to the health care industry, including legislative or other changes that impact patient eligibility, drug product eligibility, the allowable cost of a prescription drug product, the mark-up permitted on a prescription drug product, the amount of professional or dispensing fees paid by third-party payers or the provision or receipt of manufacturer allowances by pharmacy and pharmacy suppliers.

The majority of prescription drug sales are reimbursed or paid by third-party payers, such as governments, insurers or employers. These third-party payers have pursued and continue to pursue measures to manage the costs of their drug plans. Each provincial jurisdiction has implemented legislative and/or other measures directed towards managing pharmacy service costs and controlling increasing drug costs incurred by public drug plans and private payers which impact pharmacy reimbursement levels and the availability of manufacturer allowances. Legislative measures to control drug costs include lowering of generic drug pricing, restricting or prohibiting the provision of manufacturer allowances and placing limitations on private label prescription drug products. Other measures that have been implemented by certain government payers include restricting the number of interchangeable prescription drug products which are eligible for reimbursement under provincial drug plans. Additionally, the Council of the Federation, an institution created by the provincial Premiers in 2003 to collaborate on intergovernmental relations, continues its work regarding cost reduction initiatives for pharmaceutical products and services.

Legislation in certain provincial jurisdictions establish listing requirements that ensure that the selling price for a prescription drug product will not be higher than any selling price established by the manufacturer for the same prescription drug product under other provincial drug insurance programs. In some provinces, elements of the laws and regulations that impact pharmacy reimbursement and manufacturer allowances for sales to the public drug plans are extended by legislation to sales in the private sector. Also, private third-party payers (such as corporate employers and their insurers) are looking or may look to benefit from any measures implemented by government payers to reduce prescription drug costs for public plans by attempting to extend these measures to prescription drug plans they own or manage. Accordingly, changes to pharmacy reimbursement and manufacturer allowances for a public drug plan could also impact pharmacy reimbursement and manufacturer allowances for private sector sales. In addition, private third-party payers could reduce pharmacy reimbursement for prescription drugs provided to their members or could elect to reimburse members only for products included on closed formularies or available from preferred providers.

## Management's Discussion and Analysis

Ongoing changes impacting pharmacy reimbursement programs, prescription drug pricing and manufacturer allowance funding, legislative or otherwise, are expected to continue to put downward pressure on prescription drug sales. These changes may have a material adverse impact on the Company's business, sales and profitability. In addition, the Company could incur significant costs in the course of complying with any changes in the regulatory regime affecting prescription drugs. Non-compliance with any such existing or proposed laws or regulations, particularly those that provide for the licensing and conduct of wholesalers, the licensing and conduct of pharmacists, the regulation and ownership of pharmacies, the advertising of pharmacies and prescription services, the provision of information concerning prescription drug products, the pricing of prescription drugs and restrictions on manufacturer allowance funding, could result in audits, civil or regulatory proceedings, fines, penalties, injunctions, recalls or seizures, any of which could adversely affect the reputation, operations and financial performance of the Company.

**Inventory Management** The Company is subject to risks associated with managing its inventory. Failure to successfully manage such risks could result in shortages of inventory, or excess or obsolete inventory which cannot be sold profitably or increases in levels of inventory shrink. Any of these outcomes could negatively affect the financial results of the Company. The Company is continuing to convert its grocery stores to a new IT system, and in doing so is gaining increased visibility to integrated costing and sales information at store level. With this increased visibility, the Company will have more precise information to better identify and assess risks relating to inventory, however this will not eliminate such risks.

**Information Integrity and Reliability** Management depends on relevant and reliable information for decision making purposes, including key performance indicators and financial reporting. A lack of relevant and reliable information necessary to manage the business could preclude the Company from optimizing its overall performance. Any significant loss of data or failure to maintain reliable data could adversely affect the reputation, operations or financial performance of the Company.

**Availability, Access and Security of Information Technology** The Company is reliant on the continuous and uninterrupted operations of its IT systems. Point of sale availability, 24/7 user access and security of all IT systems, including distribution of prescription drugs and reimbursement by third-party payors, are critical elements to the operations of the Company. Protection against cyber security incidents and cloud security, and security of all of the Company's IT systems are critical to the operations of the Company. Any IT failure pertaining to availability, access or system security could result in disruption for the customer and could adversely affect the reputation, operations or financial performance of the Company.

**Product Safety and Public Health** The Company is subject to risks associated with product safety and defects, including the Company's control brand products. The Company could be adversely affected in the event of a significant outbreak of food-borne illness or other public health concerns related to food, health and wellness, including pharmaceuticals, or general merchandise products. The occurrence of such events or incidents could result in harm to customers, negative publicity or damage to the Company's brands and could lead to unforeseen liabilities from legal claims or otherwise. Failure to trace or locate any contaminated or defective products could affect the Company's ability to be effective in a recall situation. Any of these events, as well as the failure to maintain the cleanliness and health standards at store level, could adversely affect the reputation, operations or financial performance of the Company.

**Labour Relations** The Company's workforce is comprised of both unionized and non-unionized colleagues. With respect to those colleagues that are covered by collective agreements, there can be no assurance as to the outcome of any labour negotiations or the timing of their completion. Failure to renegotiate collective agreements could result in strikes, work stoppages or business interruptions, and if any of these events were to occur, they could adversely affect the reputation, operations or financial performance of the Company. If non-unionized colleagues become unionized, the terms of the resulting collective agreements would have implications for the affected operations and those implications could be material.

**Competitive Environment** The retail industry in Canada is highly competitive. If the Company is ineffective in responding to consumer trends or in executing its strategic plans, its financial performance could be adversely affected.

The Company's competitors include supermarket and retail drug store operators, as well as mass merchandisers, warehouse clubs, on-line retailers, mail order prescription drug distributors, limited assortment stores, discount stores, convenience stores and specialty stores. Many of these competitors now offer a selection of food, drug store and general merchandise. Others remain focused on supermarket-type merchandise. The Company is subject to competitive pressures from new entrants into the marketplace and from the expansion or renovation of existing competitors, particularly those expanding into the grocery market. The Company's inability to effectively predict market activity or compete effectively with its current or future competitors could result in, among other things, reduced market share and lower pricing in response to its competitors' pricing activities. Failure by the Company to sustain its competitive position could adversely affect the financial performance of the Company.

**Regulatory and Tax** Changes to any of the laws, rules, regulations or policies (collectively, "laws") applicable to the Company's business, including laws affecting all types of taxes, and laws affecting the production, processing, preparation, distribution, packaging and labelling of products, could have an adverse impact on the financial or operational performance of the Company. In the course of complying with such changes, the Company could incur significant costs. Changing laws or interpretations of such laws or enhanced enforcement of existing laws could restrict the Company's operations or profitability and thereby threaten the Company's competitive position and ability to efficiently conduct business. Failure by the Company to comply with applicable laws and orders could subject the Company to civil or regulatory actions, investigations or proceedings, including fines, assessments, injunctions, recalls or seizures, which in turn could adversely affect the reputation, operations or financial performance of the Company.

The Company is subject to tax audits from various government and regulatory agencies on an ongoing basis. As a result, from time to time, taxing authorities may disagree with the positions and conclusions taken by the Company in its tax filings or legislation could be amended or interpretations of current legislation could change, any of which events could lead to reassessments. These reassessments could have a material impact on the Company.

In 2012, the Company received indication from the CRA that the CRA intends to proceed with reassessments of the tax treatment of the Company's wholly owned subsidiary, Glenhuron. The CRA's position is that certain income earned by Glenhuron in Barbados in respect of the 2000 to 2010 taxation years should be treated, and taxed, as income in Canada.

Based on the proposal letter from the CRA, if the CRA and the relevant provincial tax authorities were to prevail in all of these reassessments, which the Company believes would be unlikely, the estimated total tax and interest for the 2000 to 2010 taxation years would be approximately \$440 million, which would increase as interest accrues. However, the Company is in discussions with the CRA about the amount of taxes in dispute. The Company believes it is likely that the CRA and the relevant provincial tax authorities will issue reassessments for 2011 to 2013 on the same or similar basis. No amount for any reassessments has been provided for in the Company's consolidated financial statements.

Subsequent to the end of 2014, the Company received a letter from the CRA stating that the CRA will be proceeding with the reassessments. The Company expects to receive reassessments from the CRA and the relevant provincial tax authorities sometime in the coming months. The Company strongly disagrees with the CRA's position and intends to vigorously defend its position including appealing the reassessments as and when they are received. The Company will make cash payments or provide other forms of security on a portion of the taxes in dispute. If the Company is successful in defending its position, in whole or in part, some or all of the cash payments or security would be returned to the Company. If the CRA were to ultimately prevail with respect to the proposed reassessment or if the CRA were to successfully pursue other reassessments, the outcome could have a negative material impact on the Company's reputation, results of operations and financial position of the Company in the year(s) of resolution.

As part of the review undertaken by the Competition Bureau of the acquisition by the Company of Shoppers Drug Mart, it expressed concerns about practices that the Company has in place with certain suppliers. In connection with this review, the Competition Bureau issued requests for documents from 12 suppliers of the Company. The Company has and will continue to cooperate with the Competition Bureau in its review of these practices. At this stage of the review, it is not possible to predict when the review will be completed or the outcome of such review. If the Competition Bureau is not satisfied that the Company's practices satisfy the Competition Bureau's objectives of maintaining competitive markets, then the Competition Bureau may pursue remedies that could have a negative material impact on the Company's reputation, results of operations and financial position of the Company.

PC Bank operates in a highly regulated environment and a failure by it to comply, understand, acknowledge and effectively respond to applicable regulators could result in monetary penalties, regulatory intervention and reputational damage.

Choice Properties is currently classified as a "unit trust" and a "mutual fund trust" under the *Income Tax Act*. It also qualifies for the Real Estate Investment Trust Exception under the *Income Tax Act* and as such is not subject to specified investment flow-through rules. If Choice Properties ceases to qualify for these and other classifications and exceptions, the taxation of Choice Properties and unitholders, including Loblaw, could be materially adversely different in certain respects, which in turn could materially adversely affect the trading price of the Units.

**Legal Proceedings** As part of its normal course of operations, the Company is involved in and potentially subject to a variety of legal claims and proceedings. With the acquisition of Shoppers Drug Mart, the Company is the subject of a class action brought by two licensed Associate-owners. The claim seeks damages in the amount of \$500 million based on alleged breaches of the Associate Agreement with Shoppers Drug Mart. At this stage of the proceeding any potential liability and the quantum of any loss cannot be determined. Since litigation is inherently uncertain, the outcome of this class action, and all other litigation proceedings and claims remains uncertain. However, based on information currently available, these matters, individually and in the aggregate, are not expected to have a material impact on the Company. In the event that management's assessment of materiality of current claims and proceedings proves inaccurate or litigation that is material arises in the future, there may be a material adverse effect on the Company's operations, revenues or financial performance.

**Vendor Management and Third Party Service Providers** The Company relies on vendors, including offshore vendors in both mature and developing markets, to provide the Company with goods and services. Offshore sourcing increases certain risks to the Company, including risks associated with food safety and general merchandise product defects, non-compliance with ethical and safe business practices and inadequate supply of products. The Company has no direct influence over how vendors are managed. Negative events affecting vendors or inefficient, ineffective or incomplete vendor management strategies, policies and/or procedures could adversely impact the Company's reputation and impair the Company's ability to meet customer needs or control costs and quality, which could adversely affect the reputation, operations and financial performance of the Company.

The Company also uses third party suppliers, carriers, logistic service providers and operators of warehouses and distribution facilities, including for product development, design and sourcing of the Company's control brand apparel products. Ineffective selection, contract terms or relationship management could impact the Company's ability to source control brand products, to have products available for customers, to market to customers or to operate efficiently and effectively. Disruption in services from third party suppliers could interrupt the delivery of merchandise to stores, thereby adversely affecting the operations or financial performance of the Company.

*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 operationalize certain risk management strategies for the *President's Choice Financial MasterCard*®. A significant disruption in the services provided by the chartered bank or by third party service providers would adversely affect the financial performance of PC Bank and the Company.

The Company relies on third parties for investment management, custody and other services for its cash equivalents, short term investments, security deposits and pension assets. Any disruption in the services provided by these suppliers could adversely affect the return on these assets or liquidity of the Company.

**Franchisee Independence and Relationships** A substantial portion of the Company's revenues and earnings comes from amounts paid by franchisees of its grocery store operations. Franchisees are independent businesses and, as a result, their operations may be negatively affected by factors beyond the Company's control, which in turn could negatively affect the Company's reputation, operations and financial performance. Revenues and earnings could also be negatively affected, and the Company's reputation could be harmed, if a significant number of franchisees were to experience operational failures, health and safety exposures or were unable to pay the Company for products, rent or fees. The Company's franchise system is also subject to franchise legislation enacted by a number of provinces. Any new legislation or failure to comply with existing legislation could negatively affect operations and could add administrative costs and burdens, any of which could affect the Company's relationship with its franchisees. Relationships with franchisees could pose significant risks if they are disrupted, which could negatively affect the reputation, operations and financial performance of the Company. Supply chain or system changes by the Company could cause or be perceived to cause disruptions to franchise operations and could result in negative effects on franchisee financial performance. Reputational damage or adverse consequences for the Company, including litigation and disruption to revenue from franchise stores could result.

**Associate-owned Drug Store Network and Relationships with Associates** The success of the Company and the reputation of its brands are closely tied to the performance of the Shoppers Drug Mart Associate-owned drug stores. Accordingly, the Company relies on Associates to successfully operate, manage and execute retail programs and strategies at their respective drug store locations. Associates are independent business operators and the success of the operations and financial performance of their respective drug stores may be beyond the Company's control. In addition, Associates operate in the same regulatory framework as described above under "Franchisee Independence and Relationships". Disruptions to the Company's relationships with Shoppers Drug Mart Associate-owned drug stores or changes in legislation could negatively affect revenue from Associates, which in turn, could adversely affect the reputation, operations or financial performance of the Company.

**Alternative Arrangements for Sourcing Generic Drug Products** As the utilization rate of generic prescription drugs increases, the Company is pursuing alternative sourcing and procurement models for generic prescription drug products. As part of this alternative sourcing and procurement initiative, the Company has entered into contracts for the fabrication of private label generic prescription drug products. These alternative sourcing and procurement models contain certain additional risks beyond those associated with the Company's conventional procurement strategy. The most significant of these additional risks are product liability and intellectual property infringement. Product liability claims may arise in the event that the use of the Company's products cause, or are alleged to have caused, any injury to consumers. Intellectual property infringement claims may arise in the event that the Company's products infringe or violate, or are alleged to infringe or violate, the patents or other intellectual property rights of any third parties, including the brand manufacturer. Both product liability and intellectual property infringement claims could be costly to defend and could result in significant liabilities and monetary damages. Failure to successfully implement these alternative sourcing and procurement models could adversely affect the reputation, operations or financial performance of the Company.



In addition, the market for generic prescription drug products and eligibility for reimbursement from governmental and other third-party payers will depend on the extent to which the products are designated as interchangeable with the branded products and are included as a benefit on the public drug plans in Canada. These interchangeability designations and benefit listings are highly regulated and will be dependent on the products and the procurement model meeting the regulatory requirements. If the demand for generic products is negatively affected by fewer designations, it could adversely affect the reputation, operations or financial performance of the Company.

**Multi-Employer Pension Plans** In addition to the Company-sponsored pension plans, the Company participates in various multi-employer pension plans, providing pension benefits to union employees pursuant to provisions of collective bargaining agreements. Approximately 27% (2013 – 39%) of employees of the Company, and of its franchisees and Associates, participate in these plans. These plans are administered by independent boards of trustees generally consisting of an equal number of union and employer representatives. In some circumstances, the Company has a representative on the board of trustees of these plans. The Company's responsibility to make contributions to these plans is limited by the amounts established pursuant to its collective agreements; however, poor performance of these plans could have an adverse impact on the Company's employees and former employees who are members of these plans or could result in changes to the terms and conditions of participation in these plans, which in turn could adversely affect the financial performance of the Company.

The Company, together with its franchisees, is the largest participating employer in the Canadian Commercial Workers Industry Pension Plan ("CCWIPP"), with approximately 52,000 (2013 – 53,000) employees as members. In 2014, the Company contributed approximately \$54 million (2013 – \$54 million) to CCWIPP. The recent actuarial reports filed for CCWIPP indicate that the Plan is underfunded with the accrued benefit obligations exceeding the value of CCWIPP assets. Any benefit reductions would negatively affect the retirement benefits of the Company's employees, which in turn could negatively affect their morale and productivity and, in turn, could adversely affect the reputation of the Company.

## 15.2 Financial Risks and Risk Management

The Company is exposed to a number of financial risks, including those associated with financial instruments, which have the potential to affect its operating and financial performance. The Company uses over-the-counter derivative instruments to offset certain of these risks. Policies and guidelines prohibit the use of any derivative instrument for trading or speculative purposes. The fair value of derivative instruments is subject to changing market conditions which could adversely affect the financial performance of the Company.

The following is a list of the Company's financial risks which are discussed in detail below:

Level of Indebtedness	Foreign Currency Exchange Rates
Liquidity	Interest Rates
Choice Properties' Capital Availability	Credit
Commodity Prices	Choice Properties Unit Price

### Discussion of Financial Risks

**Level of Indebtedness** To fund the cash portion of the acquisition of Shoppers Drug Mart, the Company utilized excess cash and significantly increased its indebtedness. Although the Company has made progress in reducing its indebtedness subsequent to the acquisition of Shoppers Drug Mart, there can be no assurance that the Company will generate sufficient free cash flow to significantly further reduce indebtedness and maintain adequate cash reserves. A failure to achieve these objectives could adversely affect the Company's credit ratings and its cost of funding.

If the Company, PC Bank or Choice Properties' financial performance and condition deteriorate or downgrades in the Company's or Choice Properties' current credit ratings occur, their ability to obtain funding from external sources could be restricted, which could adversely affect the financial performance of the Company.

**Liquidity** Liquidity risk is the risk that the Company is unable to generate or obtain sufficient cash or its equivalents in a cost effective manner to fund its obligations as they come due. The Company is exposed to liquidity risk through, among other areas, PC Bank and its credit card business, which requires a reliable source of funding for its credit card business. PC Bank relies on its securitization programs and the acceptance of GIC deposits to fund the receivables of its credit cards. The Company would experience liquidity risks if it fails to maintain appropriate levels of cash and short term investments, it is unable to access sources of funding or it fails to appropriately diversify sources of funding. If any of these events were to occur, they would adversely affect the financial performance of the Company.

Liquidity risk is mitigated by maintaining appropriate levels of cash and cash equivalents and short term investments, actively monitoring market conditions, and by diversifying sources of funding, including the Company's committed credit facility, and maintaining a well-diversified maturity profile of debt and capital obligations.

**Choice Properties' Capital Availability** The real estate industry is highly capital intensive. Choice Properties requires access to capital to maintain its properties, refinance its indebtedness as well as to fund its growth strategy and certain capital expenditures from time to time. Although Choice Properties expects to have access to its credit facility, there can be no assurance that it will otherwise have sufficient capital or access to capital on acceptable terms for future property acquisitions, refinancing indebtedness, financing or refinancing properties, funding operating expenses or for other purposes. Further, in certain circumstances, Choice Properties may not be able to borrow funds due to certain limitations. Failure by Choice Properties to access required capital could have a material adverse effect on the Company's ability to pay its financial or other obligations. An inability to access capital could also impact Choice Properties' ability to make distributions which could have a material adverse effect on the trading price of Units which would adversely affect the financial performance of the Company.

**Commodity Prices** The Company is exposed to increases in the prices of commodities in operating its stores and distribution networks, as well as to the indirect effect of changing commodity prices on the price of consumer products. Rising commodity prices could adversely affect the financial performance of the Company and the impact could be material. To manage a portion of this exposure, the Company uses purchase commitments for a portion of its need for certain consumer products that are commodities based. The Company enters into exchange traded futures contracts and forward contracts to minimize cost volatility related to energy.

**Foreign Currency Exchange Rates** The Company is exposed to foreign currency exchange rate variability, primarily on its USD denominated based purchases in trade payables and other liabilities. A depreciating Canadian dollar relative to the USD will have a negative impact on year-over-year changes in reported operating income and net earnings, while an appreciating Canadian dollar relative to the USD will have the opposite impact.

**Interest Rates** The Company is exposed to interest rate risk from fluctuations in interest rates on its floating rate debt and financial instruments, net of cash and cash equivalents, short term investments and security deposits. An increase in interest rates could adversely affect the financial performance of the Company. The Company manages interest rate risk by monitoring the respective mix of fixed and floating rate debt, net of cash and cash equivalents, short term investments and security deposits, and by taking action as necessary to maintain an appropriate balance considering current market conditions.

**Credit** The Company is exposed to credit risk resulting from the possibility that counterparties could default on their financial obligations to the Company. Exposure to credit risk relates to derivative instruments, cash and cash equivalents, short term investments, security deposits, PC Bank's credit card receivables, franchise loans receivable, pension assets held in the Company's defined benefit plans and accounts receivable, including amounts due from independent franchisees, government, prescription sales and third-party drug plans, independent accounts and amounts owed from vendors. Failure to manage credit risk could adversely affect the financial performance of the Company.

The risk related to derivative instruments, cash and cash equivalents, short term investments and security deposits is reduced by policies and guidelines that require that the Company enters into transactions only with counterparties or issuers that have a minimum long term "A-" credit rating from a recognized credit rating agency and place minimum and maximum limits for exposures to specific counterparties and instruments.

Choice Properties mitigates the risk of credit loss relating to rent receivables by evaluating the creditworthiness of new tenants, obtaining security deposits wherever permitted by legislation, ensuring its tenant mix is diversified and by limiting its exposure to any one tenant except Loblaw. Choice Properties establishes an allowance for doubtful accounts that represents the estimated losses with respect to rents receivable. The allowance is determined on a tenant-by-tenant basis based on the specific factors related to the tenant.

PC Bank manages its credit card receivable risk by employing stringent credit scoring techniques, actively monitoring the credit card portfolio and reviewing techniques and technology that can improve the effectiveness of the collection process. In addition, these receivables are dispersed among a large, diversified group of credit card customers.

Franchise loans receivable and accounts receivable, including amounts due from independent franchisees, governments, prescription sales covered by third-party drug plans, independent accounts and amounts owed from vendors, are actively monitored on an ongoing basis and settled on a frequent basis in accordance with the terms specified in the applicable agreements.

**Choice Properties Unit Price** The Company is exposed to market price risk as a result of Choice Properties' Units that are held by unitholders other than the Company. These Units are presented as a liability on the Company's consolidated balance sheets as they are redeemable for cash at the option of the holder. The liability is recorded at fair value at each reporting period based on the market price of Units. The change in the fair value of the liability negatively impacts net earnings when the Unit price increases and positively impacts net earnings when the Unit price declines.

## 16. Related Party Transactions

The Company's controlling shareholder is Weston, which owns, directly and indirectly, 187,815,136 of the Company's common shares, representing approximately 46% of the Company's outstanding common shares. Mr. W. Galen Weston controls Weston, directly and indirectly through private companies which he controls, including Wittington Investments, Limited ("Wittington") who owns a total of 80,746,099 of Weston's common shares, representing approximately 63% of Weston's outstanding common shares. Mr. Weston also beneficially owns 5,096,189 of the Company's common shares, representing approximately 1% of the Company's outstanding common shares. The Company's policy is to conduct all transactions and settle all balances with related parties on market terms and conditions.

### Transactions with Related Parties

(millions of Canadian dollars)	Transaction Value	
	2014 (53 weeks)	2013 (52 weeks)
<b>Included in Cost of Merchandise Inventories Sold</b>		
Inventory purchases from a subsidiary of Weston	\$ 615	\$ 601
Inventory purchases from a related party <sup>(i)</sup>	24	22
<b>Operating Income</b>		
Cost sharing agreements with Parent <sup>(ii)</sup>	\$ 20	\$ 9
Net administrative services provided by Parent <sup>(iii)</sup>	18	13
Choice Properties distributions to Parent <sup>(iv)</sup>	14	6
Lease of office space from a subsidiary of Wittington	3	3

- (i) Associated British Foods plc is a related party by virtue of Mr. W. Galen Weston being a director of such entity's parent company. Total balance outstanding owing to Associated British Foods plc as at January 3, 2015 was \$3 million (December 28, 2013 – \$4 million).
- (ii) Weston and the Company have each entered into certain contracts with third parties for administrative and corporate services, including telecommunication services and IT related matters on behalf of itself and the related party. Through cost sharing agreements that have been established between the Company and Weston concerning these costs, the Company has agreed to be responsible to Weston for the Company's proportionate share of the total costs incurred.
- (iii) The Company and Weston have entered into an agreement whereby certain administrative services are provided by one party to the other. The services to be provided under this agreement include those related to commodity management, pension and benefits, tax, medical, travel, information system, risk management, treasury and legal. Payments are made quarterly based on the actual costs of providing these services. Where services are provided on a joint basis for the benefit of the Company and Weston together, each party pays the appropriate proportion of the costs. Fees paid under this agreement are reviewed each year by the Audit Committee.
- (iv) Weston is a unitholder of Choice Properties and is entitled to receive distributions declared by the trust. Unitholders who elect to participate in the Choice Properties Distribution Reinvestment Plan ("DRIP") receive a further distribution, payable in Units, equal in value to 3% of each cash distribution. In 2014, Choice Properties issued 1,306,847 Units (2013 – 107,810 Units) to Weston under its DRIP at a weighted average price of \$10.30 (2013 – \$10.05) per Unit.

The net balances due to Weston are comprised as follows:

(millions of Canadian dollars)	As at January 3, 2015	As at December 28, 2013
Trade payables and other liabilities	\$ 7	\$ 27

**Joint Venture** In 2014, a joint venture, formed between Choice Properties and Wittington, completed the acquisition of property from Loblaw. The joint venture intends to develop the acquired site into a mixed-used property, anchored by a Loblaw food store. As at January 3, 2015, the joint venture did not have any operating activity. Choice Properties uses the equity method of accounting to record its 40% interest in the joint venture, which is included in other assets.

**Post-Employment Benefit Plans** The Company sponsors a number of post-employment plans, which are related parties. Contributions made by the Company to these plans are disclosed in the notes to the consolidated financial statements.

**Income Tax Matters** From time to time, the Company, Weston and its affiliates may enter into agreements to make elections that are permitted or required under applicable income tax legislation with respect to affiliated corporations. In 2014, these elections and accompanying agreements did not have a material impact on the Company.

**Key Management Personnel** The Company's key management personnel are comprised of the Board and certain members of the executive team of the Company, as well as both the Board and certain members of the executive team of Weston and Wittington to the extent that they have the authority and responsibility for planning, directing and controlling the day-to-day activities of the Company.

**Compensation of Key Management Personnel** Annual compensation of key management personnel that is directly attributable to the Company was as follows:

(millions of Canadian dollars)	2014 (53 weeks)	2013 (52 weeks)
Salaries, director fees and other short term employee benefits	\$ 9	\$ 8
Equity-based compensation	3	6
Total compensation	\$ 12	\$ 14

## 17. Critical Accounting Estimates and Judgments

The preparation of the consolidated financial statements requires management to make estimates and judgments in applying the Company's accounting policies that affect the reported amounts and disclosures made in the consolidated financial statements and accompanying notes.

Within the context of this Annual Report, a judgment is a decision made by management in respect of the application of an accounting policy, a recognized or unrecognized financial statement amount and/or note disclosure, following an analysis of relevant information that may include estimates and assumptions. Estimates and assumptions are used mainly in determining the measurement of balances recognized or disclosed in the consolidated financial statements and are based on a set of underlying data that may include management's historical experience, knowledge of current events and conditions and other factors that are believed to be reasonable under the circumstances. Management continually evaluates the estimates and judgments it uses.

The following are the accounting policies subject to judgments and key sources of estimation uncertainty that the Company believes could have the most significant impact on the amounts recognized in the consolidated financial statements.

### 17.1 Consolidation

**Judgments Made in Relation to Accounting Policies Applied** The Company uses judgment in determining the entities that it controls and therefore consolidates. The Company controls an entity when the Company has the existing rights that give it the current ability to direct the activities that significantly affect the entities' returns. The Company consolidates all of its wholly owned subsidiaries. Judgment is applied in determining whether the Company controls the entities in which it does not have ownership rights or does not have full ownership rights. Most often, judgment involves reviewing contractual rights to determine if rights are participating (giving power over the entity) or protective rights (protecting the Company's interest without giving it power).

### 17.2 Inventories

**Key Sources of Estimation** Inventories are carried at the lower of cost and net realizable value which requires the Company to utilize estimates related to fluctuations in shrink, future retail prices, the impact of vendor rebates on cost, seasonality and costs necessary to sell the inventory.

### 17.3 Impairment of Non-Financial Assets (Goodwill, Intangible Assets, Fixed Assets and Investment Properties)

**Judgments Made in Relation to Accounting Policies Applied** Management is required to use judgment in determining the grouping of assets to identify their cash generating units ("CGUs") for the purposes of testing fixed assets for impairment. Judgment is further required to determine appropriate groupings of CGUs, for the level at which goodwill and intangible assets are tested for impairment. The Company has determined that each location is a separate CGU for purposes of fixed asset impairment testing. For the purpose of goodwill and indefinite life intangible impairment testing, CGUs are grouped at the lowest level at which goodwill and intangibles are monitored for internal management purposes. In addition, judgment is used to determine whether a triggering event has occurred requiring an impairment test to be completed.

**Key Sources of Estimation** In determining the recoverable amount of a CGU or a group of CGUs, various estimates are employed. The Company determines fair value less costs to sell using such estimates as market rental rates for comparable properties, recoverable operating costs for leases with tenants, non-recoverable operating costs, discount rates, capitalization rates and terminal capitalization rates. The Company determines value in use by using estimates including projected future sales, earnings and capital investment consistent with strategic plans presented to the Board. Discount rates are consistent with external industry information reflecting the risk associated with the specific cash flows.

#### 17.4 Franchise Loans Receivable and Certain Other Financial Assets

**Judgments Made in Relation to Accounting Policies Applied** Management reviews franchise loans receivable, trade receivables and certain other assets relating to the Company's franchise business at each balance sheet date utilizing judgment to determine whether a triggering event has occurred requiring an impairment test to be completed.

**Key Sources of Estimation** Management determines the initial fair value of its franchise loans and certain other financial assets using discounted cash flow models. The process of determining these fair values requires management to make estimates of a long term nature regarding discount rates, projected revenues, and margins, as applicable, derived from past experience, actual operating results, budgets and the Company's five year forecast.

#### 17.5 Loyalty Programs

**Key Sources of Estimation** The Company defers revenue equal to the fair value of the award points earned by loyalty program members at the time of award. The Company determines fair value using such estimates as breakage (the amount of points that will never be redeemed) and the estimated retail value per point on redemption. The trends in breakage are reviewed on an ongoing basis and the estimated retail value per point is adjusted based on expected future activity.

#### 17.6 Income and Other Taxes

**Judgments Made in Relation to Accounting Policies Applied** The calculation of current and deferred income taxes requires management to make certain judgments regarding the tax rules in jurisdictions where the Company performs activities. Application of judgments is required regarding the classification of transactions and in assessing probable outcomes of claimed deductions including expectations about future operating results, the timing and reversal of temporary differences and possible audits of income tax and other tax filings by the tax authorities.

### 18. Accounting Standards

#### 18.1 Accounting Standards Implemented in 2014 and Changes to Significant Accounting Policies

The Company implemented the amendments to International Accounting Standards ("IAS") 32, "Financial Instruments: Presentation" and International Financial Reporting Interpretations Committee ("IFRIC") 21, "Levies" retrospectively in 2014. There was no significant impact on the Company's annual audited consolidated financial statements as a result of the implementation of these standards.

**Vendor Allowances** The timing of recognition of vendor allowances requires judgment to determine the point at which the Company has earned the allowance. In conjunction with the acquisition of Shoppers Drug Mart, management reviewed the timing of recognition of certain vendor allowances and has determined that it would be appropriate to align the policies of both companies. The Company has implemented the change retrospectively in 2014, as follows:

Consolidated Statement of Earnings and Comprehensive Income			
Increase (Decrease)	December 28, 2013		December 28, 2013
(millions of Canadian dollars except where otherwise indicated)	(12 weeks)		(52 weeks)
Cost of Merchandise Inventories Sold	\$	18	\$ 5
Operating Income	\$	(18)	\$ (5)
Earnings Before Income Taxes	\$	(18)	\$ (5)
Income taxes		(5)	(2)
Net Earnings	\$	(13)	\$ (3)
Total Comprehensive Income	\$	(13)	\$ (3)
Net Earnings per Common Share (\$)			
Basic	\$	(0.04)	\$ (0.01)
Diluted	\$	(0.05)	\$ (0.01)



Consolidated Balance Sheets

Increase (Decrease) (millions of Canadian dollars)	As at December 28, 2013	As at December 30, 2012
Accounts receivable	\$ (39)	\$ (32)
Inventories	13	11
Deferred Income Tax Assets	8	6
<b>Total Equity Attributable to Shareholders of the Company</b>	<b>\$ (18)</b>	<b>\$ (15)</b>

## 18.2 Future Accounting Standards

In May 2014, the International Accounting Standards Board ("IASB") issued IFRS 15, "Revenue from Contracts with Customers" ("IFRS 15"). The new standard provides a comprehensive framework for the recognition, measurement and disclosure of revenue from contracts with customers, excluding contracts within the scope of the accounting standards on leases, insurance contracts and financial instruments. IFRS 15 becomes effective for annual periods beginning on or after January 1, 2017, and is to be applied retrospectively. Early adoption is permitted. The Company is currently assessing the impact of the new standard on its consolidated financial statements.

In July 2014, the IASB issued IFRS 9, "Financial Instruments", replacing IAS 39, "Financial Instruments: Recognition and Measurement." The standard had three main phases: classification and measurement, impairment, and general hedging. The standard becomes effective for annual periods beginning on or after January 1, 2018 and is to be applied retrospectively with the exception of the general hedging phase which is applied prospectively. Early adoption is permitted. The Company is currently assessing the impact of the new standard on its consolidated financial statements.

In December 2014, the IASB issued amendments to IAS 1, "Presentation of Financial Statements" ("IAS 1 amendments"). The IAS 1 amendments provide guidance on the application of judgment in the preparation of financial statements and disclosures. The IAS 1 amendments are effective for annual periods beginning on or after January 1, 2016. Early adoption is permitted. The Company is currently assessing the impact of the IAS 1 amendments on its consolidated financial statements.

## 19. Outlook

Loblaw's strategic framework is focused on delivering the best in food, best in health and beauty, operational excellence and growth. This strategic framework is supported by a financial strategy of maintaining a stable trading environment which targets positive same-store sales<sup>(3), (6)</sup> and stable gross margin; surfacing efficiencies; delivering synergies as a result of its acquisition of Shoppers Drug Mart; and deleveraging the balance sheet.

On a full year comparative basis, reflecting 2014 financial results for Loblaw and Shoppers Drug Mart, in 2015 the Company expects to:

- Maintain positive same-store sales<sup>(3), (6)</sup> and stable gross margin (excluding synergies) in its Retail segment;
- Achieve net synergies as a result of the acquisition of Shoppers Drug Mart approaching \$200 million;
- Continue to drive net efficiencies across the core grocery business by achieving reductions in supply chain, administrative functions and IT, while still investing in key areas, like eCommerce;
- Grow adjusted operating income in its core grocery business, excluding synergies;
- Experience a decline in adjusted operating income<sup>(2)</sup> in its core pharmacy business, excluding synergies, as a result of investments in key projects and other factors;
- Grow consolidated adjusted net earnings<sup>(2)</sup> (including synergies) relative to 2014, with adjusted basic net earnings per common share<sup>(2)</sup> being moderated due to a significantly increased weighted average share count (approximately 412 million in 2015 versus approximately 380 million in 2014);
- Target a capital expenditure program of approximately \$1,200 million; and
- Remain on track with its deleveraging target, expecting to meet its target in the first quarter of 2016.

The Company's expectations for 2015 also include the following:

- Competitive intensity expected to remain high, but relatively stable as industry square footage growth in supermarket-type merchandise moderates; and
- Continued pressure in our pharmacy business from the ongoing impact of healthcare reform.

## 20. Non-GAAP Financial Measures

The Company uses the following non-GAAP financial measures: EBITDA, adjusted EBITDA, adjusted EBITDA margin, adjusted operating income, adjusted operating margin, adjusted net earnings, adjusted basic net earnings per common share, free cash flow, adjusted debt and adjusted debt to adjusted EBITDA and with respect to Choice Properties: adjusted funds from operations. In 2014, the Company has introduced five new financial measures: adjusted net interest expense and other financing charges, adjusted income taxes, adjusted income tax rate, Retail segment adjusted gross profit and Retail segment adjusted gross profit percentage. The Company believes these non-GAAP financial measures provide useful information to both management and investors in measuring the financial performance and financial condition of the Company for the reasons outlined below.

Management uses these and other non-GAAP financial measures to exclude the impact of certain expenses and income that must be recognized under GAAP when analyzing consolidated and segment underlying operating performance, as the excluded items are not necessarily reflective of the Company's underlying operating performance and make comparisons of underlying financial performance between periods difficult. From time to time, the Company may exclude additional items if it believes doing so would result in a more effective analysis of underlying operating performance. The exclusion of certain items does not imply that they are non-recurring.

The Company enters into exchange traded futures contracts and forward contracts to minimize cost volatility relating to fuel prices and foreign exchange rates. Pursuant to the Company's derivative instruments accounting policy, changes in the fair value of these instruments are recorded in operating income. With significant fluctuations in fuel and foreign exchange rates, commencing in the fourth quarter of 2014 the Company has excluded the fair value adjustment on fuel and foreign currency contracts in calculating adjusted operating income.

In 2014, the Company restructured its fee arrangements with the franchisees of certain franchise banners. As a result of the restructuring, the Company re-evaluated the recoverable amount of the franchise-related financial instruments and recorded a reduction in previously recorded impairment.

The Company has adjusted for Choice Properties' general and administrative costs incurred in the first half of 2014. As Choice Properties' operations commenced on July 5, 2013, there were no comparative amounts.

With the acquisition of Shoppers Drug Mart, the Company converted certain Shoppers Drug Mart cash-settled equity-based compensation awards to cash-settled awards based on the Company's common shares. The Company is exposed to market price fluctuations in its common share price as these awards are settled in cash and the associated liability is recorded at fair value at each reporting date based on the market price of the Company's common shares. The Company excludes the fair value adjustment when calculating adjusted operating income. On November 10, 2014, the Company amended these compensation awards to be settled in shares and is no longer exposed to market price fluctuations.

As of the second quarter of 2014, the Company no longer excludes net interest expense incurred in connection with the financing related to the acquisition of Shoppers Drug Mart when analyzing consolidated underlying operating performance. These amounts were excluded from adjusted net earnings and adjusted basic net earnings per common share in periods prior to the closing of the acquisition of Shoppers Drug Mart.

Beginning in 2014, the Company no longer excludes the impact of equity-settled equity-based compensation when analyzing consolidated and segment underlying operating performance. As a result, prior year adjusted EBITDA and adjusted EBITDA margin, adjusted operating income and adjusted operating margin, and adjusted net earnings and adjusted basic net earnings per common share were restated to conform with the current year's presentation.

These measures do not have a standardized meaning prescribed by GAAP and therefore they may not be comparable to similarly titled measures presented by other publicly traded companies and should not be construed as an alternative to other financial measures determined in accordance with GAAP.

**Retail Segment Adjusted Gross Profit and Retail Segment Adjusted Gross Profit Percentage** The following table reconciles Retail segment adjusted gross profit to gross profit measures reported in the consolidated statements of earnings for the periods ended January 3, 2015 and December 28, 2013. The Company believes that Retail segment adjusted gross profit is useful in assessing the Retail segment's underlying operating performance and in making decisions regarding the ongoing operations of the business.

Retail segment adjusted gross profit percentage is calculated as adjusted Retail segment gross profit divided by Retail segment sales.

(millions of Canadian dollars)	2014 (13 weeks)	2013 <sup>(4)</sup> (12 weeks)	2014 (53 weeks)	2013 <sup>(4)</sup> (52 weeks)
Retail segment gross profit	\$ 2,925	\$ 1,625	\$ 9,734	\$ 6,961
Add impact of the following:				
Recognition of fair value increment on inventory sold	69	—	798	—
Charge related to inventory measurement and other conversion differences	—	—	190	—
Retail segment adjusted gross profit	\$ 2,994	\$ 1,625	\$ 10,722	\$ 6,961

**Recognition of fair value increment on inventory sold** In connection with the acquisition of Shoppers Drug Mart, acquired assets and liabilities were recorded on the Company's consolidated balance sheets at their fair value. This resulted in a fair value adjustment to Shoppers Drug Mart inventory on the date of acquisition representing the difference between inventory cost and its fair value. This difference was recognized in cost of sales as the inventory was sold, with a resulting negative impact on gross profit. In the fourth quarter of 2014, \$69 million (2013 – nil) and year-to-date \$798 million (2013 – nil), was recognized in gross profit and operating income, representing the full amount of the fair value adjustment.

**Charge related to inventory measurement and other conversion differences for the Company's corporate grocery stores** As of the end of 2014, the Company had completed the conversion of substantially all of its corporate grocery locations and associated distribution centres to the new IT systems. The implementation of a perpetual inventory system, combined with visibility to integrated costing information provided by the new IT systems, enabled the Company to estimate the cost of inventory using a more precise system-generated average cost. The impact was estimated to be a \$190 million (2013 – nil) decrease in the value of the inventory, which was recognized in gross profit and operating income in 2014. The Company is undertaking the conversion of its remaining grocery locations during 2015 and additional impacts may result.

**EBITDA, Adjusted EBITDA, Adjusted EBITDA Margin, Adjusted Operating Income and Adjusted Operating Margin** The following tables reconcile earnings before income taxes, net interest expense and other financing charges and depreciation and amortization ("EBITDA"), adjusted EBITDA and adjusted operating income to operating income, which is reconciled to GAAP net earnings measures reported in the consolidated statements of earnings for the periods ended January 3, 2015 and December 28, 2013. The Company believes that adjusted EBITDA is useful in assessing the performance of its ongoing operations and its ability to generate cash flows to fund its cash requirements, including the Company's capital investments program. The Company also believes that adjusted operating income is useful in assessing the Company's underlying operating performance and in making decisions regarding the ongoing operations of the business.

Adjusted EBITDA margin is calculated as adjusted EBITDA divided by revenue. Adjusted operating margin is calculated as adjusted operating income divided by revenue.

(millions of Canadian dollars)	2014 (13 weeks)					2013 <sup>(4)</sup> (12 weeks)				
	Retail	Financial Services <sup>(7)</sup>	Choice Properties <sup>(5)</sup>	Consolidation and Eliminations	Consolidated	Retail	Financial Services	Choice Properties <sup>(5)</sup>	Consolidation and Eliminations	Consolidated
Net earnings					\$ 247					\$ 114
Add impact of the following:										
Net interest expense and other financing charges					169					141
Income taxes					91					41
Operating income	\$ 459	\$ 49	\$ 223	\$ (224)	\$ 507	\$ 252	\$ 43	\$ 186	\$ (185)	\$ 296
Depreciation and amortization	388	2	—	3	393	191	2	—	3	196
EBITDA	\$ 847	\$ 51	\$ 223	\$ (221)	\$ 900	\$ 443	\$ 45	\$ 186	\$ (182)	\$ 492
Operating income	\$ 459	\$ 49	\$ 223	\$ (224)	\$ 507	\$ 252	\$ 43	\$ 186	\$ (185)	\$ 296
Add (deduct) impact of the following:										
Amortization of intangible assets acquired with Shoppers Drug Mart	124	—	—	—	124	—	—	—	—	—
Recognition of fair value increment on inventory sold	69	—	—	—	69	—	—	—	—	—
Restructuring of franchise fees	(40)	—	—	—	(40)	—	—	—	—	—
Shoppers Drug Mart acquisition-related costs and net divestitures loss	14	—	—	—	14	7	—	—	—	7
Fair value adjustment on fuel and foreign currency contracts	4	—	—	—	4	—	—	—	—	—
Fair value adjustment on Shoppers Drug Mart's equity-based compensation liability	2	—	—	—	2	—	—	—	—	—
Fixed asset and other related impairments, net of recoveries	1	—	—	—	1	(42)	—	—	—	(42)
Restructuring costs	—	—	—	—	—	32	—	—	—	32
Adjusted operating income	\$ 633	\$ 49	\$ 223	\$ (224)	\$ 681	\$ 249	\$ 43	\$ 186	\$ (185)	\$ 293
Depreciation and amortization	388	2	—	3	393	191	2	—	3	196
Less: Amortization of intangible assets acquired with Shoppers Drug Mart	(124)	—	—	—	(124)	—	—	—	—	—
Adjusted EBITDA	\$ 897	\$ 51	\$ 223	\$ (221)	\$ 950	\$ 440	\$ 45	\$ 186	\$ (182)	\$ 489

## Management's Discussion and Analysis

(millions of Canadian dollars)	2014 (53 weeks)					2013 <sup>(i)</sup> (52 weeks)				
	Retail	Financial Services <sup>(7)</sup>	Choice Properties <sup>(8)</sup>	Consolidation and Eliminations	Consolidated	Retail	Financial Services	Choice Properties <sup>(9),(i)</sup>	Consolidation and Eliminations	Consolidated
Net earnings					\$ 53					\$ 627
Add impact of the following:										
Net interest expense and other financing charges					584					468
Income taxes					25					226
Operating income	\$ 497	\$ 164	\$ 568	\$ (567)	\$ 662	\$1,180	\$ 142	\$ 370	\$ (371)	\$ 1,321
Depreciation and amortization	1,453	7	—	12	1,472	809	9	—	6	824
EBITDA	\$1,950	\$ 171	\$ 568	\$ (555)	\$ 2,134	\$1,989	\$ 151	\$ 370	\$ (365)	\$ 2,145
Operating income	\$ 497	\$ 164	\$ 568	\$ (567)	\$ 662	\$1,180	\$ 142	\$ 370	\$ (371)	\$ 1,321
Add (deduct) impact of the following:										
Recognition of fair value increment on inventory sold	798	—	—	—	798	—	—	—	—	—
Amortization of intangible assets acquired with Shoppers Drug Mart	417	—	—	—	417	—	—	—	—	—
Charge related to inventory measurement and other conversion differences	190	—	—	—	190	—	—	—	—	—
Shoppers Drug Mart acquisition-related costs and net divestitures loss	72	—	—	—	72	6	—	—	—	6
Restructuring costs	44	—	2	—	46	35	—	—	—	35
Restructuring of franchise fees	(40)	—	—	—	(40)	—	—	—	—	—
Fixed asset and other related impairments, net of recoveries	15	—	1	—	16	(32)	—	—	—	(32)
Choice Properties general and administrative costs	(2)	—	11	—	9	—	—	—	—	—
Fair value adjustment on Shoppers Drug Mart's equity-based compensation liability	7	—	—	—	7	—	—	—	—	—
Fair value adjustments on fuel and foreign currency contracts	4	—	—	—	4	—	—	—	—	—
Defined benefit plan amendments	—	—	—	—	—	(51)	—	—	—	(51)
Choice Properties start-up costs	—	—	—	—	—	—	—	3	—	3
Adjusted operating income	\$2,002	\$ 164	\$ 582	\$ (567)	\$ 2,181	\$1,138	\$ 142	\$ 373	\$ (371)	\$ 1,282
Depreciation and amortization	1,453	7	—	12	1,472	809	9	—	6	824
Less: Amortization of intangible assets acquired with Shoppers Drug Mart	(417)	—	—	—	(417)	—	—	—	—	—
Adjusted EBITDA	\$3,038	\$ 171	\$ 582	\$ (555)	\$ 3,236	\$1,947	\$ 151	\$ 373	\$ (365)	\$ 2,106

(i) Based on operations beginning July 5, 2013.



**Amortization of intangible assets acquired with Shoppers Drug Mart** The acquisition of Shoppers Drug Mart in the second quarter of 2014 included approximately \$6,050 million of definite life intangible assets, which are being amortized over their estimated useful lives. During the fourth quarter of 2014, \$124 million and year-to-date \$417 million of amortization were recognized in operating income. Annual amortization associated with the acquired intangibles will be approximately \$550 million over the next ten years, and will decrease thereafter.

**Shoppers Drug Mart acquisition-related costs and net divestitures loss** In connection with the agreement to acquire all of the outstanding common shares of Shoppers Drug Mart, in the fourth quarter of 2014, the Company excluded nil (2013 – \$7 million) and year-to-date \$60 million (2013 – \$16 million) of acquisition-related costs in operating income. The Company recorded a net loss related to the completed divestitures in the fourth quarter of 2014 of \$14 million and year-to-date of \$12 million (grouped with acquisition-related costs). Although no further significant acquisition-related costs are anticipated, further adjustments for divestitures gain or loss will be made when the remaining three Shoppers Drug Mart stores are sold. In the third quarter of 2013, in connection with the issuance of \$1,600 million of unsecured notes, the Company hedged its exposure to interest rates for the period prior to issuance. As the hedge did not qualify for hedge accounting, the resulting \$10 million gain on settlement was recorded in operating income.

**Restructuring costs** In the fourth quarter of 2014 and year-to-date, the Company recorded a charge of nil (2013 – \$32 million) and \$46 million (2013 – \$35 million), respectively, of restructuring and reorganization costs primarily associated with the reduction of corporate and store-support positions, the departure of certain executives and the realignment of certain of the Company's central office functions.

**Restructuring of franchise fees** In the fourth quarter and year-to-date of 2014, the Company restructured its fee arrangements with the franchisees of certain franchise banners. As a result of this restructuring, the Company re-evaluated the recoverable amount of franchise-related financial instruments and recorded a reduction in previously recorded impairment of \$40 million (2013 – nil).

**Fixed asset and other related impairments, net of recoveries** At each balance sheet date, the Company assesses and, when required, records impairments and recoveries of previous impairments related to the carrying value of its fixed assets, investment properties and intangible assets. In the fourth quarter of 2014, the Company recorded an impairment of \$1 million (2013 – recovery of \$42 million) and year-to-date \$16 million (2013 – recovery of \$32 million) related to fixed asset and other related impairments.

**Choice Properties general and administrative costs** During the fourth quarter of 2014, the Company recorded nil and year-to-date \$9 million of general and administrative costs incurred by Choice Properties in operating income. The Company has adjusted for Choice Properties' general and administrative costs incurred in the first half of 2014. As Choice Properties' operations commenced on July 5, 2013, there were no comparative amounts.

**Fair value adjustment on Shoppers Drug Mart's equity-based compensation liability** In the second quarter of 2014, in conjunction with the acquisition, the Company converted certain Shoppers Drug Mart cash-settled equity-based compensation awards to cash-settled awards based on the Company's common shares. The Company is exposed to market price fluctuations in its common share price as these awards are settled in cash and the associated liability is recorded at fair value at each reporting date based on the market price of the Company's common shares. In the fourth quarter and year-to-date of 2014, the Company recorded a loss of \$2 million (2013 – nil) and a loss of \$7 million (2013 – nil), respectively. On November 10, 2014, the Company amended these compensation awards to be settled in shares and is no longer exposed to market price fluctuations.

**Fair value adjustment on fuel and foreign currency contracts** The Company enters into exchange traded futures contracts and forward contracts to minimize cost volatility relating to fuel prices and foreign exchange rates. Pursuant to the Company's derivative instruments accounting policy, changes in the fair value of these instruments are recorded in operating income. With significant fluctuations in fuel and foreign exchange rates, commencing in the fourth quarter of 2014, the Company has excluded the fair value adjustment on fuel and foreign currency contracts in calculating adjusted operating income. In the fourth quarter and year-to-date of 2014, the Company recorded a net fair value adjustment loss on these fuel and foreign currency contracts of \$4 million (2013 – nil).

**Defined benefit plan amendments** In the first quarter of 2013, the Company announced amendments to certain of its defined benefit plans that impact certain employees retiring after January 1, 2015. As a result, the Company recorded a gain of \$51 million in the first quarter of 2013.

**Choice Properties start-up costs** In connection with the IPO of Choice Properties, the Company incurred certain costs to facilitate the start-up of the new entity. For the year ended 2013, the Company recorded \$3 million of Choice Properties' start-up costs in operating income.

**Adjusted Net Interest Expense and Other Financing Charges** The following table reconciles adjusted net interest expense and other financing charges to net interest and other financing charges in the consolidated statements of earnings for the periods ended January 3, 2015 and December 28, 2013. The Company believes that adjusted net interest expense and other financing charges is useful in assessing the Company's underlying financial performance and in making decisions regarding the financial operations of the business.

(millions of Canadian dollars)	2014 (13 weeks)	2013 <sup>(4)</sup> (12 weeks)	2014 (53 weeks)	2013 <sup>(4)</sup> (52 weeks)
Net interest expense and other financing charges	\$ 169	\$ 141	\$ 584	\$ 468
Deduct impact of the following:				
Accelerated amortization of deferred financing costs	(5)	—	(23)	—
Fair value adjustment on Trust Unit Liability	(20)	(34)	(17)	(27)
Shoppers Drug Mart acquisition-related costs and net divestitures loss	—	(14)	(15)	(25)
Choice Properties IPO transaction costs	—	(1)	—	(44)
Early debt settlement costs	—	—	—	(18)
Adjusted net interest expense and other financing charges	\$ 144	\$ 92	\$ 529	\$ 354

**Accelerated amortization of deferred financing costs** In the fourth quarter of 2014, the Company recorded a \$5 million charge and year-to-date a \$23 million charge related to the accelerated amortization of deferred financing costs due to the repayment of \$321 million and \$2,271 million year-to-date of the unsecured term loan facility.

**Fair value adjustment on Trust Unit Liability** The Company is exposed to market price fluctuations as a result of the Units held by unitholders other than the Company. These Units are presented as a liability on the Company's consolidated balance sheets as they are redeemable for cash at the option of the holder, subject to certain restrictions. This liability is recorded at fair value at each reporting date based on the market price of Units at the end of the period. In the fourth quarter of 2014, the Company recorded a loss of \$20 million (2013 – \$34 million) and year-to-date a loss of \$17 million (2013 – \$27 million) related to the fair value adjustment on the Trust Unit Liability.

**Shoppers Drug Mart acquisition-related costs and net divestitures loss** In addition to the acquisition-related costs and net divestitures loss recorded in operating income noted above, during the first quarter and year-to-date of 2014, \$15 million and during the fourth quarter and year-to-date of 2013, \$14 million and \$25 million, respectively, of additional net interest expense were incurred in connection with the financing related to the acquisition of Shoppers Drug Mart. As of the acquisition date, these costs are no longer excluded from adjusted net interest expense and other financing charges as they are now part of ongoing business operations.

**Choice Properties IPO transaction costs** In addition to the start-up costs recorded in operating income noted above, in the fourth quarter and year-to-date of 2013, \$1 million and \$44 million, respectively, of transaction costs were incurred related directly to the Choice Properties IPO.

**Early debt settlement costs** In the third quarter of 2013, the Company settled its remaining USD \$150 million USPP note in advance of its May 29, 2015 maturity date and settled the related cross currency swap. The Company incurred early-settlement costs related to the prepayment of \$18 million.

**Adjusted Income Tax Expense and Adjusted Income Tax Rate** The Company believes the adjusted income tax expense is useful in assessing the underlying operating performance and in making decisions regarding the ongoing operations of its business.

(millions of Canadian dollars)	2014 (13 weeks)	2013 <sup>(4)</sup> (12 weeks)	2014 (53 weeks)	2013 <sup>(4)</sup> (52 weeks)
Adjusted operating income <sup>(i)</sup>	\$ 681	\$ 293	\$ 2,181	\$ 1,282
Adjusted net interest and other financing charges <sup>(i)</sup>	144	92	529	354
Adjusted earnings before taxes	\$ 537	\$ 201	\$ 1,652	\$ 928
Income taxes	\$ 91	\$ 41	\$ 25	\$ 226
Tax impact of items included in adjusted earnings before taxes <sup>(ii)</sup>	50	(1)	403	6
Adjusted income taxes	\$ 141	\$ 40	\$ 428	\$ 232
Effective tax rate	26.9%	26.5%	32.1%	26.5%
Adjusted income tax rate	26.3%	19.9%	25.9%	25.0%

(i) See reconciliations of adjusted operating income and adjusted net interest and other financing charges above.

(ii) See the EBITDA, adjusted EBITDA and adjusting operating income table and the adjusted net interest and other financing charges table above for a complete list of items included in adjusted earnings before taxes.

Adjusted income tax rate is calculated as adjusted income taxes divided by the sum of adjusted operating income less adjusted net interest expense and other financing charges.

**Adjusted Net Earnings and Adjusted Basic Net Earnings Per Common Share** The Company believes adjusted net earnings and adjusted basic net earnings per common share are useful in assessing the Company's underlying operating performance and in making decisions regarding the ongoing operations of its business.

The following table reconciles adjusted net earnings and adjusted basic net earnings per common share to GAAP net earnings and basic net earnings per common share reported for the periods ended January 3, 2015 and December 28, 2013:

(millions of Canadian dollars/Canadian dollars)	2014 (13 weeks)		2013 <sup>(4)</sup> (12 weeks)		2014 (53 weeks)		2013 <sup>(4)</sup> (52 weeks)	
	Net Earnings	Basic Net Earnings Per Common Share	Net Earnings	Basic Net Earnings Per Common Share	Net Earnings	Basic Net Earnings Per Common Share	Net Earnings	Basic Net Earnings Per Common Share
	\$ 247	\$ 0.60	\$ 114	\$ 0.41	\$ 53	\$ 0.14	\$ 627	\$ 2.23
Add (deduct) impact of the following:								
Recognition of fair value increment on inventory sold	50	0.12	—	—	586	1.55	—	—
Amortization of intangible assets acquired with Shoppers Drug Mart	90	0.22	—	—	306	0.80	—	—
Charge related to inventory measurement and other conversion differences	—	—	—	—	139	0.37	—	—
Shoppers Drug Mart acquisition-related costs and net divestitures loss	9	0.02	17	0.05	73	0.19	27	0.10
Restructuring costs	—	—	24	0.09	34	0.09	26	0.09
Restructuring of franchise fees	(30)	(0.07)	—	—	(30)	(0.08)	—	—
Fair value adjustment on Trust Unit Liability <sup>(i)</sup>	20	0.05	34	0.12	17	0.04	27	0.10
Accelerated amortization of deferred financing costs	4	0.01	—	—	17	0.04	—	—
Fixed asset and other related impairments, net of recoveries	2	—	(29)	(0.10)	14	0.04	(22)	(0.08)
Choice Properties general and administrative costs	—	—	—	—	7	0.02	—	—
Fair value adjustment on Shoppers Drug Mart's equity-based compensation liability	1	—	—	—	5	0.01	—	—
Fair value adjustment on fuel and foreign currency contracts	3	0.01	—	—	3	0.01	—	—
Defined benefit plan amendments	—	—	—	—	—	—	(37)	(0.13)
Choice Properties start-up costs and IPO transaction costs	—	—	1	—	—	—	35	0.12
Early debt settlement costs	—	—	—	—	—	—	13	0.05
<b>Adjusted</b>	<b>\$ 396</b>	<b>\$ 0.96</b>	<b>\$ 161</b>	<b>\$ 0.57</b>	<b>\$ 1,224</b>	<b>\$ 3.22</b>	<b>\$ 696</b>	<b>\$ 2.48</b>

(i) Gains or losses related to the fair value adjustment on Trust Unit Liability are not subject to tax.

**Free Cash Flow** The following table reconciles free cash flow used in assessing the Company's financial condition to GAAP measures for the periods ended week periods ended January 3, 2015 and December 28, 2013. In the fourth quarter of 2014, the Company refined its definition of free cash flow as cash flows from operating activities less intangible asset additions, fixed asset purchases and interest paid. The Company believes that free cash flow is the appropriate measure in assessing the Company's cash available for additional financing and investing activities.

(millions of Canadian dollars)	2014 (13 weeks)	2013 (12 weeks)	2014 (53 weeks)	2013 (52 weeks)
Cash flows from operating activities	\$ 952	\$ 738	\$ 2,569	\$ 1,491
Less:				
Intangible asset additions	42	—	90	12
Fixed asset purchases	358	304	996	865
Interest paid	113	98	506	370
Free cash flow	\$ 439	\$ 336	\$ 977	\$ 244

**Adjusted Debt** The following table reconciles adjusted debt, used in the adjusted debt to adjusted EBITDA ratio, to GAAP measures reported as at the periods ended as indicated. The Company believes that adjusted debt is relevant in assessing the amount of financial leverage employed. The Company changed its definition of adjusted debt in the second quarter of 2014 to include capital securities to better align with management's definition for deleveraging purposes. In the table below, the Company has also presented adjusted debt as at March 28, 2014, the date of the acquisition of Shoppers Drug Mart, as this is the baseline for the Company's debt reduction targets.

(millions of Canadian dollars)	As at January 3, 2015	As at March 28, 2014 (unaudited)	As at December 28, 2013
Bank indebtedness	\$ 162	\$ 295	\$ —
Short term debt	605	605	605
Long term debt due within one year	420	902	1,008
Long term debt	11,042	11,262	6,672
Trust Unit Liability	722	703	688
Capital securities	225	224	224
Certain other liabilities	28	39	39
Total debt	\$ 13,204	\$ 14,030	\$ 9,236
Less:			
Independent Securitization Trusts	1,355	1,355	1,355
Independent Funding Trusts	498	469	475
Trust Unit Liability	722	703	688
Guaranteed Investment Certificates	634	443	430
Adjusted debt	\$ 9,995	\$ 11,060	\$ 6,288

Adjusted debt to adjusted EBITDA is calculated as adjusted debt divided by adjusted EBITDA.



**Choice Properties' Adjusted Funds from Operations** The following table reconciles Choice Properties' adjusted funds from operations to GAAP measures for the periods ended January 3, 2015 and December 28, 2013. The Company believes adjusted funds from operations is useful in measuring economic performance and is indicative of Choice Properties ability to pay distributions.

(millions of Canadian dollars)	2014 <sup>(5)</sup> (13 weeks)	2013 <sup>(5)</sup> (12 weeks)	2014 <sup>(5)</sup> (53 weeks)	2013 <sup>(5),(6)</sup> (52 weeks)
<b>Net income</b>	\$ 87	\$ (6)	\$ 200	\$ 67
Fair value adjustments on Class B Limited Partnership units	51	112	(12)	147
Fair value adjustments on investment properties	(98)	(69)	(82)	(144)
Fair value adjustments on unit-based compensation	—	—	(1)	—
Distributions on Class B Limited Partnership units	50	46	191	89
Amortization of tenant improvement allowances	—	—	1	—
<b>Funds from Operations</b>	<b>\$ 90</b>	<b>\$ 83</b>	<b>\$ 297</b>	<b>\$ 159</b>
Restructuring	—	—	2	—
Business start-up costs	—	—	—	3
Straight-line rental revenue	(9)	(8)	(35)	(16)
Amortization of finance charges	—	1	50	1
Unit-based compensation expense	—	—	2	—
Sustaining property and leasing capital expenditures, normalized <sup>(6)</sup>	(7)	(11)	(31)	(16)
<b>Adjusted Funds from Operations</b>	<b>\$ 74</b>	<b>\$ 65</b>	<b>\$ 285</b>	<b>\$ 131</b>

(i) Based on operations beginning July 5, 2013.

(ii) Seasonality impacts the timing of capital expenditures. The adjusted funds from operations calculation has been adjusted for this factor to make the quarters more comparable.

## 21. Additional Information

Additional information about the Company 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 [sedar.com](http://sedar.com) and with the Office of the Superintendent of Financial Institutions (OSFI) as the primary regulator for the Company's subsidiary, PC Bank.

February 25, 2015  
Toronto, Canada

## Financial Results

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## Management's Statement of Responsibility for Financial Reporting

The management of Loblaw Companies Limited is responsible for the preparation, presentation and integrity of the accompanying consolidated financial statements, Management's Discussion and Analysis and all other information in the Annual Report – Financial Review ("Annual Report"). This responsibility includes the selection and consistent application of appropriate accounting principles and methods in addition to making the judgments and estimates necessary to prepare the consolidated financial statements in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board. It also includes ensuring that the financial information presented elsewhere in the Annual Report is consistent with that in the consolidated financial statements.

Management is also responsible to provide reasonable assurance that assets are safeguarded and that relevant and reliable financial information is produced. Management is required to design a system of internal controls and certify as to the design and operating effectiveness of internal controls over financial reporting. A dedicated control compliance team reviews and evaluates internal controls, the results of which are shared with management on a quarterly basis. KPMG LLP, whose report follows, were appointed as independent auditors by a vote of the Company's shareholders to audit the consolidated financial statements.

The Board of Directors, acting through an Audit Committee comprised solely of directors who are independent, is responsible for determining that management fulfills its responsibilities in the preparation of the consolidated financial statements and the financial control of operations. The Audit Committee recommends the independent auditors for appointment by the shareholders. The Audit Committee meets regularly with senior and financial management, internal auditors and the independent auditors to discuss internal controls, auditing activities and financial reporting matters. The independent auditors and internal auditors have unrestricted access to the Audit Committee. These consolidated financial statements and Management's Discussion and Analysis have been approved by the Board of Directors for inclusion in the Annual Report based on the review and recommendation of the Audit Committee.

Toronto, Canada  
February 25, 2015

*[signed]*

**Galen G. Weston**

President and Executive Chairman

*[signed]*

**Richard Dufresne**

Chief Financial Officer

## Independent Auditors' Report

To the Shareholders of Loblaw Companies Limited:

We have audited the accompanying consolidated financial statements of Loblaw Companies Limited, which comprise the consolidated balance sheets as at January 3, 2015 and December 28, 2013, the consolidated statements of earnings, comprehensive income, changes in equity and cash flows for the 53 and 52 week years then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

### Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

### Auditors' Responsibility

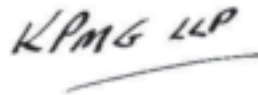
Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

### Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of Loblaw Companies Limited as at January 3, 2015 and December 28, 2013, and its consolidated financial performance and its consolidated cash flows for the 53 and 52 week years then ended in accordance with International Financial Reporting Standards.

Handwritten signature of KPMG LLP in blue ink, with a horizontal line underneath.

Toronto, Canada  
February 25, 2015

Chartered Professional Accountants, Licensed Public Accountants

## Consolidated Statements of Earnings

For the years ended January 3, 2015 and December 28, 2013  
(millions of Canadian dollars except where otherwise indicated)

	2014	2013 <sup>(i)</sup>
<b>Revenue</b>	<b>\$ 42,611</b>	<b>\$ 32,371</b>
<b>Cost of Merchandise Inventories Sold (note 12)</b>	<b>32,063</b>	<b>24,701</b>
<b>Selling, General and Administrative Expenses</b>	<b>9,886</b>	<b>6,349</b>
<b>Operating Income</b>	<b>\$ 662</b>	<b>\$ 1,321</b>
Net interest expense and other financing charges (note 6)	584	468
<b>Earnings Before Income Taxes</b>	<b>\$ 78</b>	<b>\$ 853</b>
Income taxes (note 7)	25	226
<b>Net Earnings</b>	<b>\$ 53</b>	<b>\$ 627</b>
<b>Net Earnings per Common Share (\$) (note 8)</b>		
Basic	\$ 0.14	\$ 2.23
Diluted	\$ 0.14	\$ 2.21
<b>Weighted Average Common Shares Outstanding (note 8) (millions)</b>		
Basic	380.5	281.1
Diluted	384.4	284.1

(i) Certain comparative figures have been amended. See note 2.  
See accompanying notes to the consolidated financial statements.



## Consolidated Statements of Comprehensive Income

For the years ended January 3, 2015 and December 28, 2013

(millions of Canadian dollars)

	2014	2013 <sup>(i)</sup>
Net Earnings	\$ 53	\$ 627
Other comprehensive income (loss), net of taxes		
Items that are or may be subsequently reclassified to profit or loss:		
Foreign currency translation adjustment	\$ 8	\$ —
Gain on derecognized derivative instrument (note 30)	—	(5)
Items that will not be reclassified to profit or loss:		
Net defined benefit plan actuarial (loss) gain (note 27)	(46)	234
Other comprehensive (loss) income	\$ (38)	\$ 229
<b>Total Comprehensive Income</b>	<b>\$ 15</b>	<b>\$ 856</b>

(i) Certain comparative figures have been amended. See note 2.  
See accompanying notes to the consolidated financial statements.

## Consolidated Statements of Changes in Equity

(millions of Canadian dollars except where otherwise indicated)	Common Share Capital	Retained Earnings <sup>(i)</sup>	Contributed Surplus	Accumulated Other Comprehensive Income	Non-Controlling Interests	Total Equity <sup>(i)</sup>
<b>Balance at December 28, 2013</b>	\$ 1,642	\$ 5,271	\$ 87	\$ —	\$ —	\$ 7,000
Net Earnings	\$ —	\$ 53	\$ —	\$ —	\$ —	\$ 53
Other comprehensive (loss) income	—	(46)	—	8	—	(38)
<b>Total Comprehensive Income</b>	\$ —	\$ 7	\$ —	\$ 8	\$ —	\$ 15
Acquisition of Shoppers Drug Mart Corporation (note 5 and 24)	6,119	—	—	—	—	6,119
Contribution from non-controlling interests (note 18)	—	—	—	—	8	8
Net effect of equity-based compensation (note 24 and 26)	156	(1)	17	—	—	172
Net effect of shares held in trust (note 24 and 26)	3	19	—	—	—	22
Common shares purchased for cancellation (note 24)	(63)	(115)	—	—	—	(178)
Dividends declared per common share – \$0.975 (note 24)	—	(371)	—	—	—	(371)
	\$ 6,215	\$ (461)	\$ 17	\$ 8	\$ 8	\$ 5,787
<b>Balance at January 3, 2015</b>	\$ 7,857	\$ 4,810	\$ 104	\$ 8	\$ 8	\$ 12,787

(millions of Canadian dollars except where otherwise indicated)	Common Share Capital	Retained Earnings <sup>(i)</sup>	Contributed Surplus	Accumulated Other Comprehensive Income	Non-Controlling Interests	Total Equity <sup>(i)</sup>
<b>Balance at December 29, 2012</b>	\$ 1,567	\$ 4,777	\$ 55	\$ 5	\$ —	\$ 6,404
Net earnings	\$ —	\$ 627	\$ —	\$ —	\$ —	\$ 627
Other comprehensive income (loss)	—	234	—	(5)	—	229
<b>Total Comprehensive Income (Loss)</b>	\$ —	\$ 861	\$ —	\$ (5)	\$ —	\$ 856
Net effect of equity-based compensation (note 24 and 26)	90	—	32	—	—	122
Net effect of shares held in trust (note 24 and 26)	(6)	(39)	—	—	—	(45)
Common shares purchased for cancellation (note 24)	(9)	(64)	—	—	—	(73)
Dividends declared per common share – \$0.940 (note 24)	—	(264)	—	—	—	(264)
	\$ 75	\$ 494	\$ 32	\$ (5)	\$ —	\$ 596
<b>Balance at December 28, 2013</b>	\$ 1,642	\$ 5,271	\$ 87	\$ —	\$ —	\$ 7,000

(i) Certain comparative figures have been amended. See note 2. See accompanying notes to the consolidated financial statements.

## Consolidated Balance Sheets

(millions of Canadian dollars)	As at January 3, 2015	As at December 28, 2013 <sup>(i)</sup>
<b>Assets</b>		
Current Assets		
Cash and cash equivalents (note 9)	\$ 999	\$ 2,260
Short term investments (note 9)	21	290
Accounts receivable (note 10)	1,209	579
Credit card receivables (note 11)	2,630	2,538
Inventories (note 12)	4,309	2,097
Prepaid expenses and other assets	214	75
Assets held for sale (note 13)	23	22
<b>Total Current Assets</b>	<b>\$ 9,405</b>	<b>\$ 7,861</b>
Fixed Assets (note 14)	10,794	9,105
Investment Properties (note 15)	185	99
Intangible Assets (note 16)	9,177	111
Goodwill (note 17)	3,243	943
Deferred Income Tax Assets (note 7)	193	261
Security Deposits (note 9)	7	1,701
Franchise Loans Receivable (note 30)	399	375
Other Assets (note 19)	281	285
<b>Total Assets</b>	<b>\$ 33,684</b>	<b>\$ 20,741</b>
<b>Liabilities</b>		
Current Liabilities		
Bank indebtedness (note 33)	\$ 162	\$ —
Trade payables and other liabilities	4,672	3,797
Provisions (note 21)	84	66
Income taxes payable	34	37
Short term debt (note 20)	605	605
Long term debt due within one year (note 22)	420	1,008
Associate interest	193	—
Capital securities (note 24)	225	—
<b>Total Current Liabilities</b>	<b>\$ 6,395</b>	<b>\$ 5,513</b>
Provisions (note 21)	76	56
Long Term Debt (note 22)	11,042	6,672
Trust Unit Liability (note 30)	722	688
Deferred Income Tax Liabilities (note 7)	1,880	34
Capital Securities (note 24)	—	224
Other Liabilities (note 23)	782	554
<b>Total Liabilities</b>	<b>\$ 20,897</b>	<b>\$ 13,741</b>
<b>Equity</b>		
Share Capital (note 24)	\$ 7,857	\$ 1,642
Retained Earnings	4,810	5,271
Contributed Surplus (note 26)	104	87
Accumulated Other Comprehensive Income	8	—
<b>Total Equity Attributable to Shareholders of the Company</b>	<b>12,779</b>	<b>7,000</b>
Non-Controlling Interests (note 18)	8	—
<b>Total Equity</b>	<b>\$ 12,787</b>	<b>\$ 7,000</b>
<b>Total Liabilities and Equity</b>	<b>\$ 33,684</b>	<b>\$ 20,741</b>

(i) Certain comparative figures have been amended. See note 2.

Leases (note 29). Contingent Liabilities (note 32). Financial Guarantees (note 33). Subsequent Events (note 36).

See accompanying notes to the consolidated financial statements.

## Consolidated Statements of Cash Flows

For the years ended January 3, 2015 and December 28, 2013

(millions of Canadian dollars)

	2014	2013 <sup>(i)</sup>
<b>Operating Activities</b>		
Net earnings	\$ 53	\$ 627
Income taxes (note 7)	25	226
Net interest expense and other financing charges (note 6)	584	468
Depreciation and amortization	1,472	824
Income taxes paid	(293)	(272)
Interest received	29	49
Settlement of equity forward contracts (note 30)	—	(16)
Settlement of cross currency swaps (note 30)	—	94
Change in credit card receivables (note 11)	(92)	(233)
Change in non-cash working capital	(321)	(224)
Fixed asset and other related impairments (recoveries)	16	(32)
Loss (gain) on disposal of assets	3	(1)
Recognition of fair value increment on inventory sold (note 12)	798	—
Charge related to inventory measurement and other conversion differences (note 12)	190	—
Gain on defined benefit plan amendments (note 27)	—	(51)
Other	105	32
<b>Cash Flows from Operating Activities</b>	<b>\$ 2,569</b>	<b>\$ 1,491</b>
<b>Investing Activities</b>		
Acquisition of Shoppers Drug Mart Corporation, net of cash acquired (note 5)	\$ (6,619)	\$ —
Fixed asset purchases	(996)	(865)
Change in short term investments (note 9)	269	451
Proceeds from disposal of assets	129	26
Change in franchise investments and other receivables	(25)	5
Change in security deposits (note 9)	1,694	(1,444)
Intangible asset additions	(90)	(12)
Investment in joint venture	(6)	—
Other	(40)	—
<b>Cash Flows used in Investing Activities</b>	<b>\$ (5,684)</b>	<b>\$ (1,839)</b>
<b>Financing Activities</b>		
Change in bank indebtedness	\$ (133)	\$ —
Change in Associate interest	19	—
Change in short term debt	—	(300)
Long Term Debt (note 22)		
Issued	5,865	2,770
Retired	(3,336)	(871)
Deferred debt financing costs	(28)	(21)
Issuance of Trust Units (note 30)	1	660
Trust Unit issuance costs	—	(44)
Interest paid	(506)	(370)
Dividends paid (note 24)	(496)	(259)
Share capital (note 24)		
Issued	629	75
Purchased and held in trust	—	(46)
Purchased for cancellation	(178)	(73)
Contribution from non-controlling interests (note 18)	8	—
<b>Cash Flows from Financing Activities</b>	<b>\$ 1,845</b>	<b>\$ 1,521</b>
Effect of foreign currency exchange rate changes on cash and cash equivalents	\$ 9	\$ 8
Change in cash and cash equivalents	\$ (1,261)	\$ 1,181
Cash and cash equivalents, beginning of year	2,260	1,079
<b>Cash and Cash Equivalents, end of year</b>	<b>\$ 999</b>	<b>\$ 2,260</b>

(i) Certain comparative figures have been amended. See note 2.  
See accompanying notes to the consolidated financial statements.

## Notes to the Consolidated Financial Statements

For the years ended January 3, 2015 and December 28, 2013 (millions of Canadian dollars except where otherwise indicated)

### Note 1. Nature and Description of the Reporting Entity

Loblaw Companies Limited is a Canadian public company incorporated in 1956 and is Canada's food and pharmacy leader, the nation's largest retailer and the majority unitholder of Choice Properties Real Estate Investment Trust ("Choice Properties"). Loblaw Companies Limited provides Canadians with grocery, pharmacy, health and beauty, apparel, general merchandise, and financial products and services. Its registered office is located at 22 St. Clair Avenue East, Toronto, Canada M4T 2S7. Loblaw Companies Limited and its subsidiaries are together referred to, in these consolidated financial statements, as the "Company" or "Loblaw".

The Company's controlling shareholder is George Weston Limited ("Weston") which owns approximately 46% of the Company's outstanding common shares. The Company's ultimate parent is Wittington Investments, Limited ("Wittington"). The remaining common shares are widely held.

In 2014, the Company acquired all of the outstanding shares of Shoppers Drug Mart Corporation ("Shoppers Drug Mart") (see note 5).

The Company has three reportable operating segments: Retail, Financial Services and Choice Properties (see note 35).

### Note 2. Significant Accounting Policies

**Statement of Compliance** The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS" or "GAAP") as issued by the International Accounting Standards Board ("IASB") and using the accounting policies described herein.

The consolidated financial statements were authorized for issuance by the Company's Board of Directors ("Board") on February 25, 2015.

**Basis of Preparation** The consolidated financial statements were prepared on a historical cost basis except for the following items that were measured at fair value:

- liabilities for cash-settled equity-based compensation arrangements as described in note 26;
- defined benefit plan assets with the obligations related to these pension plans measured at their discounted present value as described in note 27; and
- certain financial instruments as described in note 30.

The significant accounting policies set out below have been applied consistently in the preparation of the consolidated financial statements for all periods presented.

The consolidated financial statements are presented in Canadian dollars.

**Basis of Consolidation** The consolidated financial statements include the accounts of the Company and other entities that the Company controls. Control exists when the Company has the existing rights that give it the current ability to direct the activities that significantly affect the entities' returns. The Company reassesses control on an ongoing basis.

Structured entities are entities controlled by the Company which were designed so that voting or similar rights are not the dominant factor in deciding who controls the entity. Structured entities are consolidated if, based on an evaluation of the substance of its relationship with the Company, the Company concludes that it controls the structured entity. Structured entities controlled by the Company were established under terms that impose strict limitations on the decision-making powers of the structured entities' management and that results in the Company receiving the majority of the benefits related to the structured entities' operations and net assets, being exposed to the majority of risks incident to the structured entities' activities, and retaining the majority of the residual or ownership risks related to the structured entities or their assets.

Transactions and balances between the Company and its consolidated entities have been eliminated on consolidation.

Non-controlling interests are separately presented in the consolidated financial statements and represent the non-controlling shareholders' equity in an entity consolidated by the Company for which its ownership is less than 100%. Transactions with non-controlling interests are treated as transactions with equity owners of the Company. Changes in the Company's ownership interest in its subsidiaries are accounted for as equity transactions.

Choice Properties' Trust Units ("Units") held by unitholders other than the Company are presented as a Trust Unit Liability in the consolidated financial statements, as the Units are redeemable for cash at the option of the holder, subject to certain restrictions. As at the end of the fourth quarter of 2014, the Company held an 82.9% ownership interest in Choice Properties.



The Company consolidates the Shoppers Drug Mart licensees ("Associates"). An Associate is a pharmacist-owner of a corporation that is licensed to operate a retail drug store at a specific location using Shoppers Drug Mart's trademarks. The consolidation of the Associates is based on the concept of control, for accounting purposes, which was determined to exist primarily through Shoppers Drug Mart's agreements that govern the relationship between Shoppers Drug Mart and the Associates ("Associate Agreements"). The Company does not have any direct or indirect shareholdings in the corporations that operate the Associates. Accordingly, included in the consolidated financial statements is associate interest to reflect the investment the Associates have in the net assets of their businesses. Under the terms of the Associate Agreements, Shoppers Drug Mart agrees to purchase the assets that the Associates use in store operations, primarily at the carrying value to the Associate, when Associate Agreements are terminated by either party.

**Fiscal Year** The fiscal year of the Company ends on the Saturday closest to December 31. Under an accounting convention common in the retail industry, the Company follows a 52-week reporting cycle, which periodically necessitates a fiscal year of 53 weeks. The years ended January 3, 2015 and December 28, 2013 contained 53 weeks and 52 weeks, respectively.

**Business Combinations** Business combinations are accounted for using the acquisition method as of the date when control is transferred to the Company. The Company measures goodwill as the excess of the sum of the fair value of the consideration transferred over the net identifiable assets acquired and liabilities assumed, all measured as at the acquisition date. Transaction costs that the Company incurs in connection with a business combination, other than those associated with the issue of debt or equity securities, are expensed as incurred.

**Net Earnings per Common Share** Basic net earnings per common share ("EPS") is calculated by dividing the net earnings available to common shareholders by the weighted average number of common shares outstanding during the period. Diluted EPS is calculated by adjusting the net earnings available to common shareholders and the weighted average number of common shares outstanding for the effects of all potential dilutive instruments.

**Revenue Recognition** The Company recognizes revenue when the amount can be reliably measured, when it is probable that future economic benefits will flow to the entity and when specific criteria have been met for each of the Company's activities as described below.

*Retail* segment revenue includes sale of goods and services to customers through corporate stores and Associates, sales to franchised stores, and independent account customers. Revenue is measured at the fair value of the consideration received or receivable, net of estimated returns and sales incentives. The Company recognizes revenue at the time the sale is made or service is delivered to its customers and at the time of delivery of inventory to its franchise stores. Revenue also includes services fees from franchised stores, and independent account customers, which are recognized when services are rendered.

Customer loyalty awards are accounted for as a separate component of the sales transaction in which they are granted. A portion of the consideration received in a transaction that includes the issuance of an award is deferred until the awards are ultimately redeemed. The allocation of the consideration to the award is based on an evaluation of the award's estimated fair value at the date of the transaction using the residual fair value method.

On the initial sale of franchising arrangements, the Company offers products and services as part of a multiple deliverable arrangement, which is recorded using a relative fair value approach.

*Financial Services* segment revenue includes interest income on credit card loans, service fees and other revenue related to financial services. Interest income is recognized using the effective interest method. Service fees are recognized when services are rendered. Other revenue is recognized periodically or according to contractual provisions.

*Choice Properties* segment revenue includes rental revenue on base rents earned from tenants under lease agreements, realty tax and operating cost recoveries and other incidental income, including intersegment revenue earned from the Retail segment. The rental revenue is recognized on a straight-line basis over the terms of the respective leases. Property tax and operating cost recoveries are recognized in the period that recoverable costs are chargeable to tenants. Percentage participation rents are recognized when tenants' specified sales targets have been met as set out in the lease agreements.

**Taxation** Current and deferred taxes are recognized in the consolidated statement of earnings, except when it relates to a business combination, or items recognized directly to equity or to other comprehensive income.

Current tax is the expected tax payable or receivable on the taxable income or loss for the period, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognized using the asset and liability method of accounting on temporary differences arising between the financial statement carrying values of existing assets and liabilities and their respective income tax bases. Deferred tax is measured using enacted or substantively enacted income tax rates expected to apply in the years in which those temporary differences are expected to be recovered or settled. A deferred tax asset is recognized for unused tax losses and credits to the extent that it is probable that future taxable profits will be available against which they can be utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets and they relate to income taxes levied by the same taxation authority on the same taxable entity, or on different taxable entities where the Company intends to settle its current tax assets and liabilities on a net basis.

Deferred tax is provided on temporary differences arising on investments in subsidiaries, except where the timing of the reversal of the temporary difference is controlled by the Company and it is probable that the temporary difference will not reverse in the foreseeable future.

Choice Properties qualifies as a "mutual fund trust" under the Income Tax Act (Canada). The Trustees intend to distribute all taxable income directly earned by Choice Properties to unitholders and to deduct such distributions for income tax purposes. Legislation relating to the federal income taxation of Specified Investment Flow Through trusts or partnerships ("SIFT") provide that certain distributions from a SIFT will not be deductible in computing the SIFT's taxable income and that the SIFT will be subject to tax on such distributions at a rate that is substantially equivalent to the general tax rate applicable to Canadian corporations. However, distributions paid by a SIFT as return of capital should generally not be subject to tax.

Under the SIFT rules, the taxation regime will not apply to a real estate investment trust ("REIT") that meets prescribed conditions relating to the nature of its assets and revenue (the "REIT Conditions"). Choice Properties has reviewed the SIFT rules and has assessed its interpretation and application to the REIT's assets and revenue. While there are uncertainties in the interpretation and application of the SIFT rules, Choice Properties has determined that it meets the REIT Conditions.

**Cash and Cash Equivalents** Cash and cash equivalents consist of highly liquid marketable investments with an original maturity date of 90 days or less from the date of acquisition.

**Short Term Investments** Short term investments consist of marketable investments with an original maturity date greater than 90 days and less than 365 days from the date of acquisition.

**Security Deposits** Security deposits consist of cash and cash equivalents and short term investments. Security deposits also include amounts which are required to be placed with counterparties as collateral to enter into and maintain outstanding letters of credit and financial derivative contracts.

**Accounts Receivable** Accounts receivable, net of allowances for doubtful accounts, include amounts due from independent franchisees, government, prescription sales and third-party drug plans, independent accounts and amounts owed from vendors.

**Credit Card Receivables** The Company, through President's Choice Bank ("PC Bank"), a wholly owned subsidiary of the Company, has credit card receivables that are stated net of an allowance. Interest income is recorded in revenue and interest expense is recorded in net interest expense and other financing charges using the effective interest method. The effective interest rate is the rate that discounts the estimated future cash receipts through the expected life of the credit card receivable (or, where appropriate, a shorter period) to the carrying amount. When calculating the effective interest rate, the Company estimates future cash flows considering all contractual terms of the financial instrument, but not future credit losses.

The Company periodically transfers credit card receivables by selling them to and repurchasing them from independent securitization trusts. PC Bank is required to absorb a portion of the related credit losses. As a result, the Company has not transferred all of the risks and rewards related to these assets and continues to recognize these assets in credit card receivables. The transferred receivables are accounted for as financing transactions. The Company consolidates *Eagle Credit Card Trust*<sup>®</sup> ("*Eagle*"), one of the independent securitization trusts, as a structured entity. The associated liabilities secured by these assets are included in either short term debt or long term debt based on their characteristics and are carried at amortized cost.

Credit card receivables are considered past due when a cardholder has not made a payment by the contractual due date, taking into account a grace period. The amount of credit card receivables that fall within the grace period is considered current. Credit card receivables past due but not impaired are those receivables that are either less than 90 days past due or whose past due status is reasonably expected to be remedied. Any credit card receivables with a payment that is contractually 180 days in arrears, or where the likelihood of collection is considered remote, is written off.

**Franchise Loans Receivable** Franchise loans receivable are comprised of amounts due from independent franchisees for loans issued through a consolidated independent funding trust. Each independent franchisee provides security to the independent funding trust for its obligations by way of a general security agreement. In the event that an independent franchisee defaults on its loan and the Company has not, within a specified time period, assumed the loan or the default is not otherwise remedied, the independent funding trust would assign the loan to the Company and draw upon a standby letter of credit. The Company has agreed to reimburse the issuing bank for any amount drawn on the standby letter of credit. The carrying amount of franchise loan receivables approximates fair value.

**Inventories** The Company values merchandise inventories at the lower of cost and net realizable value.

Cost includes the costs of purchases net of vendor allowances plus other costs, such as transportation, that are directly incurred to bring inventories to their present location and condition. The cost of inventories at retail stores and distribution centres are measured at weighted average cost, with the exception of inventories at Shoppers Drug Mart, which are measured on a first-in first-out basis.

The Company estimates net realizable value as the amount that inventories are expected to be sold taking into consideration fluctuations in retail prices due to seasonality less estimated costs necessary to make the sale. Inventories are written down to net realizable value when the cost of inventories is estimated to be unrecoverable due to obsolescence, damage or declining selling prices. When circumstances that previously caused inventories to be written down below cost no longer exist or when there is clear evidence of an increase in retail selling prices, the amount of the write-down previously recorded is reversed. Storage costs, indirect administrative overhead and certain selling costs related to inventories are expensed in the period that these costs are incurred.

**Vendor Allowances** The Company receives allowances from certain of its vendors whose products it purchases for resale. These allowances are received for a variety of buying and/or merchandising activities, including vendor programs such as volume purchase allowances, purchase discounts, listing fees and exclusivity allowances. Allowances received from a vendor is a reduction in the cost of the vendor's products and is recognized as a reduction in the cost of merchandise inventories sold and the related inventory when recognized in the consolidated statements of earnings and the consolidated balance sheets, respectively, when it is probable that they will be received and the amount of the allowance can be reliably estimated. Amounts received but not yet earned are presented in other liabilities as deferred vendor allowances.

Certain exceptions apply if the consideration is a payment for assets or services delivered to the vendor or for reimbursement of selling expenses incurred to promote the vendor's products. The consideration is then recognized as a reduction of the expense incurred in the consolidated statements of earnings.

**Fixed Assets** Fixed assets are recognized at cost and subsequently measured at cost less accumulated depreciation and any accumulated impairment losses. Cost includes expenditures that are directly attributable to the acquisition of the asset, including costs incurred to prepare the asset for its intended use and capitalized borrowing costs. The commencement date for capitalization of costs occurs when the Company first incurs expenditures for the qualifying assets and undertakes the required activities to prepare the assets for their intended use.

Borrowing costs directly attributable to the acquisition, construction or production of fixed assets that necessarily take a substantial period of time to prepare for their intended use and a proportionate share of general borrowings, are capitalized to the cost of those fixed assets, based on a quarterly weighted average cost of borrowing. All other borrowing costs are expensed as incurred and recognized in net interest expense and other financing charges.

The cost of replacing a fixed asset component is recognized in the carrying amount of the item if it is probable that the future economic benefits embodied within the component will flow to the Company and its cost can be measured reliably. The carrying amount of the replaced part is de-recognized. The cost of repairs and maintenance of fixed assets are expensed as incurred and recognized in operating income.

Gains and losses on disposal of fixed assets are determined by comparing the fair value of the proceeds from disposal with the net book value of the assets and are recognized net, in operating income.

Fixed assets are depreciated on a straight-line basis over their estimated useful lives to their estimated residual value when the assets are available for use. When significant parts of a fixed asset have different useful lives, they are accounted for as separate components and depreciated separately. Depreciation methods, useful lives and residual values are reviewed at each financial year end and are adjusted for prospectively, if appropriate. Estimated useful lives are as follows:

Buildings	10 to 40 years
Equipment and fixtures	2 to 10 years
Building improvements	up to 10 years
Leasehold improvements	Lesser of term of the lease and useful life up to 25 years
Assets held under financing leases	Lesser of term of the lease <sup>(i)</sup> and useful life <sup>(ii)</sup>

(i) If it is reasonably certain that the Company will obtain ownership by the end of the lease term, assets under finance leases would be depreciated over the life of the asset.

(ii) Same basis as owned assets.

Non-current assets are classified as assets held for sale if their carrying amount will be recovered principally through a sale transaction rather than through continuing use. To qualify as assets held for sale, the sale must be highly probable, assets must be available for immediate sale in their present condition and management must be committed to a plan to sell assets that should be expected to close within one year from the date of classification. Assets held for sale are recognized at the lower of their carrying amount and fair value less costs to sell and are not depreciated.

Fixed assets are reviewed at each balance sheet date to determine whether there is any indication of impairment. Refer to the Impairment of Non-Financial Assets policy.

**Investment Properties** Investment properties are properties owned by the Company that are held to either earn rental income, for capital appreciation, or both. The Company's investment properties include single tenant properties held to earn rental income and certain multiple tenant properties. Land and buildings leased to franchisees are not accounted for as investment properties as these properties are related to the Company's operating activities.

Investment property assets are recognized at cost less accumulated depreciation and any accumulated impairment losses. The depreciation policies for investment properties are consistent with those described in the accounting policy for fixed assets.

Investment properties are reviewed at each balance sheet date to determine whether there is any indication of impairment. Refer to the Impairment of Non-Financial Assets policy.

**Joint Ventures** A joint venture is a joint arrangement whereby the parties to the arrangement have rights to the net assets of the joint arrangement. Investments in joint ventures are accounted for using the equity method, where the investment is initially recognized in the consolidated balance sheet at cost and adjusted thereafter to recognize the Company's share of the profit or loss and other comprehensive income of the joint venture.

**Goodwill** Goodwill arising in a business combination is recognized as an asset at the date that control is acquired. Goodwill is subsequently measured at cost less any accumulated impairment losses. Goodwill is not amortized but is tested for impairment on an annual basis or more frequently if there are indicators that goodwill may be impaired as described in the Impairment of Non-Financial Assets policy.

**Intangible Assets** Intangible assets with finite lives are measured at cost less accumulated amortization and any accumulated impairment losses. These intangible assets are amortized on a straight-line basis over their estimated useful lives, ranging from three to 18 years, and are tested for impairment as described in the Impairment of Non-Financial Assets policy. Useful lives, residual values and amortization methods for intangible assets with finite useful lives are reviewed at least annually.

Indefinite life intangible assets are measured at cost less any accumulated impairment losses. These intangible assets are tested for impairment on an annual basis or more frequently if there are indicators that intangible assets may be impaired as described in the Impairment of Non-Financial Assets policy.

**Impairment of Non-Financial Assets** At each balance sheet date, the Company reviews the carrying amounts of its non-financial assets, other than inventories and deferred tax assets, to determine whether there is any indication of impairment. If any such indication exists, the asset is then tested for impairment by comparing its recoverable amount to its carrying value. Goodwill and indefinite life intangible assets are tested for impairment at least annually.

For the purpose of impairment testing, assets are grouped together into the smallest group of assets that generate cash inflows from continuing use that are largely independent of cash inflows of other assets or groups of assets. This grouping is referred to as a cash generating unit ("CGU"). The Company has determined that each location is a separate CGU for purposes of impairment testing.

Corporate assets, which include head office facilities and distribution centers, do not generate separate cash inflows. Corporate assets are tested for impairment at the minimum grouping of CGUs to which the corporate assets can be reasonably and consistently allocated. Goodwill arising from a business combination is tested for impairment at the minimum grouping of CGUs that are expected to benefit from the synergies of the combination.

The recoverable amount of a CGU or CGU grouping is the higher of its value in use and its fair value less costs to sell. Value in use is based on the estimated future cash flows from the CGU or CGU grouping, discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the CGU or CGU group. The fair value less costs to sell is based on the best information available to reflect the amount that could be obtained from the disposal of the CGU or CGU group in an arm's length transaction between knowledgeable and willing parties, net of estimates of the costs of disposal.

An impairment loss is recognized if the carrying amount of a CGU or CGU group exceeds its recoverable amount. For asset impairments other than goodwill, the impairment loss reduces the carrying amounts of the non-financial assets in the CGU on a pro-rata basis. Any loss identified from goodwill impairment testing is first applied to reduce the carrying amount of goodwill allocated to the CGU grouping, and then to reduce the carrying amounts of the other non-financial assets in the CGU or CGU group on a pro-rata basis. Impairment losses are recognized in operating income.

For other assets other than goodwill, an impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortization, if no impairment loss had been recognized. An impairment loss in respect of goodwill is not reversed.

**Bank Indebtedness** Bank indebtedness is comprised of Associate bank lines of credit.

**Provisions** Provisions are recognized when there is a present legal or constructive obligation as a result of a past event, it is probable that the Company will be required to settle the obligation and a reliable estimate of the amount of the obligation can be made. The amount recognized as a provision is the present value of the best estimate of the consideration required to settle the present obligation at the end of the reporting period, taking into account the risks and uncertainties specific to the obligation. The unwinding of the discount rate is recognized in net interest expense and other financing charges.

**Financial Instruments and Derivative Financial Instruments** Financial assets and liabilities are recognized when the Company becomes party to the contractual provisions of the financial instrument. Financial instruments, including derivatives and embedded derivatives in certain contracts, upon initial recognition are measured at fair value and classified as either financial assets or financial liabilities at fair value through profit or loss, held-to-maturity investments, loans and receivables or other financial liabilities. Loans and receivables, and other financial liabilities are subsequently measured at cost or amortized cost. Derivatives and non-financial derivatives must be recorded at fair value on the consolidated balance sheets. Fair values are based on quoted market prices where available from active markets, otherwise fair values are estimated using valuation methodologies, primarily discounted cash flows taking into account external market inputs where possible.

Financial derivative instruments in the form of cross currency swaps, interest rate swaps, foreign exchange forwards and equity forwards, as well as non-financial derivatives in the form of futures contracts, options contracts and forward contracts, are recorded at fair value on the consolidated balance sheets. The Company does not use derivative instruments for speculative purposes. Any embedded derivative instruments that may be identified are separated from their host contract and recorded on the consolidated balance sheets at fair value. Derivative instruments are recorded in current or non-current assets and liabilities based on their remaining terms to maturity. All changes in fair values of the derivative instruments are recorded in net earnings unless the derivative qualifies and is effective as a hedging instrument in a designated hedging relationship.

**Classification** The following table summarizes the classification and measurement of the Company's financial assets and liabilities:

Asset/Liability	Classification	Measurement
Cash and cash equivalents	Fair value through profit and loss <sup>(i)</sup>	Fair value
Short term investments	Fair value through profit and loss <sup>(i)</sup>	Fair value
Accounts receivable	Loans and receivables	Amortized cost
Credit card receivables	Loans and receivables	Amortized cost
Security deposits	Fair value through profit and loss <sup>(i)</sup>	Fair value
Franchise loans receivable	Loans and receivables	Amortized cost
Certain other assets	Loans and receivables	Amortized cost
Bank indebtedness	Other liabilities	Amortized cost
Trade payables and other liabilities	Other liabilities	Amortized cost
Short term debt	Other liabilities	Amortized cost
Long term debt	Other liabilities	Amortized cost
Trust Unit Liability	Fair value through profit and loss <sup>(ii)</sup>	Fair value
Certain other liabilities	Other liabilities	Amortized cost
Capital securities	Other liabilities	Amortized cost
Derivatives	Fair value through profit and loss <sup>(ii)</sup>	Fair value

(i) Financial instruments designated at fair value through profit and loss.

(ii) Financial instruments required to be classified at fair value through profit and loss.

The Company has not classified any financial assets as held-to-maturity.



**Fair Value** The Company measures financial assets and financial liabilities under the following fair value hierarchy. The different levels have been defined as follows:

- Fair Value Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Fair Value Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e., as prices) or indirectly (i.e., derived from prices); and
- Fair Value Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

Determination of fair value and the resulting hierarchy requires the use of observable market data whenever available. The classification of a financial instrument in the hierarchy is based upon the lowest level of input that is significant to the measurement of fair value.

Transaction costs other than those related to financial instruments classified as fair value through profit or loss, which are expensed as incurred, are capitalized to the carrying amount of the instrument and amortized using the effective interest method.

Gains and losses on fair value through profit or loss financial assets and financial liabilities are recognized in earnings before income taxes in the period in which they are incurred. Settlement date accounting is used to account for the purchase and sale of financial assets. Gains or losses between the trade date and settlement date on fair value through profit or loss financial assets are recorded in earnings before income taxes.

**Valuation process** The determination of the fair value of financial instruments is performed by the Company's treasury and financial reporting departments on a quarterly basis. There was no change in the valuation techniques applied to financial instruments in the current year. The following table describes the valuation techniques used in the determination of the fair values of financial instruments:

Type	Valuation Approach
Cash and cash equivalents, short term investments, security deposits, accounts receivable, credit card receivables, bank indebtedness, trade payables and other liabilities and short term debt	The carrying amount approximates fair value due to the short term maturity of these instruments.
Franchise loans receivable	The carrying amount approximates fair value as fluctuations in the forward interest rates would not have significant impacts on the valuation and the provisions recorded for all impaired receivables.
Derivatives	Specific valuation techniques used to value derivative financial instruments include: <ul style="list-style-type: none"> <li>▪ Quoted market prices or dealer quotes for similar instruments;</li> <li>▪ The fair value of interest rate swaps is calculated as the present value of the estimated future cash flows based on observable yield curves; and</li> <li>▪ The fair value of other derivative instruments are determined based on observable market information as well as valuations determined by external valuers with experience in financial markets.</li> </ul>
Long term debt, Trust Unit Liability, capital securities and certain other financial instruments	The fair value is based on the present value of contractual cash flows, discounted at the Company's current incremental borrowing rate for similar types of borrowing arrangements or, where applicable, quoted market prices.

Financial assets are derecognized when the contractual rights to receive cash flows and benefits from the financial asset expire, or if the Company transfers the control or substantially all the risks and rewards of ownership of the financial asset to another party. The difference between the carrying amount of the financial asset and the sum of the consideration received and receivable is recognized in earnings before income taxes.

Financial liabilities are derecognized when obligations under the contract expire, are discharged or cancelled. The difference between the carrying amount of the financial liability derecognized and the consideration paid and payable is recognized in earnings before income taxes.

**Impairment of Financial Assets** An assessment of whether there is objective evidence that a financial asset or a group of financial assets is impaired is performed at each balance sheet date. A financial asset or group of financial assets is considered to be impaired if one or more loss events that have an impact on the estimated future cash flows occur after their initial recognition and the loss can be reliably measured. If such objective evidence has occurred, the loss is based on the difference between the carrying amount of the financial asset, or portfolio of financial assets, and the respective estimated future cash flows discounted at the financial assets' original effective interest rate. Impairment losses are recorded in the consolidated statement of earnings with the carrying amount of the financial asset or group of financial assets reduced through the use of impairment allowance accounts.

In periods subsequent to the impairment where the impairment loss has decreased, and such decrease can be related objectively to an event occurring after the impairment was initially recognized, the previously recognized impairment loss is reversed through the consolidated statement of earnings. The impairment reversal is limited to the lesser of the decrease in impairment or the extent that the carrying amount of the financial asset at the date the impairment is reversed does not exceed what the amortized cost would have been had the impairment not been recognized, after the reversal.

**Foreign Currency Translation** The functional currency of the Company is the Canadian dollar.

The assets and liabilities of foreign operations that have a functional currency different from that of the Company, including goodwill and fair value adjustments arising on acquisition, are translated into Canadian dollars at the foreign currency exchange rate in effect at the balance sheet date. The resulting foreign currency exchange gains or losses are recognized in the foreign currency translation adjustment as part of other comprehensive income. When such foreign operation is disposed of, the related foreign currency translation reserve is recognized in net earnings as part of the gain or loss on disposal. On the partial disposal of such foreign operation, the relevant proportion is reclassified to net earnings.

Assets and liabilities of foreign operations that have the same functional currency as the Company are translated into Canadian dollars at the foreign currency exchange rate in effect at the balance sheet date. The resulting foreign currency exchange gains or losses are recognized in operating income.

Revenues and expenses of foreign operations are translated into Canadian dollars at the foreign currency exchange rates that approximate the rates in effect at the dates when such items are transacted.

**Short term Employee Benefits** Short term employee benefits include wages, salaries, compensated absences, profit-sharing and bonuses. Short term employee benefit obligations are measured on an undiscounted basis and are recognized in operating income as the related service is provided or capitalized if the service rendered is in connection with the creation of a tangible or intangible asset. A liability is recognized for the amount expected to be paid under short term cash bonus or profit sharing plans if the Company has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

**Defined Benefit Post-Employment Plans** The Company has a number of contributory and non-contributory defined benefit post-employment plans providing pension and other benefits to eligible employees. The defined benefit pension plans provide a pension based on length of service and eligible pay. The other defined benefits include health care, life insurance and dental benefits provided to eligible employees who retire at certain ages having met certain service requirements. The Company's net defined benefit plan obligations (assets) for each plan are actuarially calculated by a qualified actuary at the end of each annual reporting period using the projected unit credit method pro-rated based on service and management's best estimate of the discount rate, the rate of compensation increase, retirement rates, termination rates, mortality rates and expected growth rate of health care costs. The discount rate used to value the defined benefit plan obligation for accounting purposes is based on the yield on a portfolio of Corporate AA bonds denominated in the same currency with cash flows that match the terms of the defined benefit plan obligations. Past service costs (credits) arising from plan amendments are recognized in operating income in the year that they arise. The actuarially determined net interest costs on the net defined benefit plan obligation are recognized in net interest expense and other financing charges.

The fair values of plan assets are deducted from the defined benefit plan obligations to arrive at the net defined benefit plan obligations (assets). For plans that result in a net defined benefit asset, the recognized asset is limited to the present value of economic benefits available in the form of future refunds from the plan or reductions in future contributions to the plan (the "asset ceiling"). If it is anticipated that the Company will not be able to recover the value of the net defined benefit asset, after considering minimum funding requirements for future service, the net defined benefit asset is reduced to the amount of the asset ceiling. When the payment in the future of minimum funding requirements related to past service would result in a net defined benefit surplus or an increase in a surplus, the minimum funding requirements are recognized as a liability to the extent that the surplus would not be fully available as a refund or a reduction in future contributions.

Re-measurements including actuarial gains and losses, the effect of the asset ceiling (if applicable) and the impact of any minimum funding requirements are recognized through other comprehensive income and subsequently reclassified from accumulated other comprehensive income to retained earnings.

**Other Long Term Employee Benefit Plans** The Company offers other long term employee benefits including contributory long term disability benefits and non-contributory continuation of health care and dental benefits to employees who are on long term disability leave. As the amount of the long term disability benefit does not depend on length of service, the obligation is recognized when an event occurs that gives rise to an obligation to make payments. The accounting for other long term employee benefit plans is similar to the method used for defined benefit plans except that all actuarial gains and losses are recognized in operating income.

**Defined Contribution Plans** The Company maintains a number of defined contribution pension plans for employees in which the Company pays fixed contributions for eligible employees into a registered plan and has no further significant obligation to pay any further amounts. The costs of benefits for defined contribution plans are expensed as employees have rendered service.

**Multi-Employer Pension Plans** The Company participates in multi-employer pension plans which are accounted for as defined contribution plans. The Company's responsibility to make contributions to these plans is limited by amounts established pursuant to its collective agreements. Defined benefit multi-employer pension plans are accounted for as defined contribution plans as adequate information to account for the Company's participation in the plans is not available due to the size and number of contributing employers in the plans. The contributions made by the Company to multi-employer plans are expensed as contributions are due.

**Termination Benefits** Termination benefits are recognized as an expense at the earlier of when the Company can no longer withdraw the offer of those benefits and when the Company recognizes costs for a restructuring. Benefits payable are discounted to their present value when the effect of the time value of money is material.

**Equity-Settled Equity-Based Compensation Plans** Stock options, Restricted Share Units ("RSUs"), Performance Share Units ("PSUs"), Director Deferred Share Units ("DSUs") and Executive Deferred Share Units ("EDSUs") issued by the Company are settled in common shares and are accounted for as equity-settled awards.

Stock options may have a five to ten year term, vest 20% or 33% cumulatively on each anniversary date of the grant and are exercisable at the designated common share price, which is based on the greater of the volume weighted average trading price of the Company's common share for either the five trading days prior to the date of grant or the trading day immediately preceding the grant date. The fair value of each tranche of options granted is measured separately at the grant date using a Black-Scholes option pricing model, and includes the following assumptions:

- The expected dividend yield is estimated based on the expected annual dividend prior to the option grant date and the closing share price as at the option grant date;
- The expected share price volatility is estimated based on the Company's historical volatility over a period consistent with the expected life of the options;
- The risk-free interest rate is estimated based on the Government of Canada bond yield in effect at the grant date for a term to maturity equal to the expected life of the options; and
- The effect of expected exercise of options prior to expiry is incorporated into the weighted average expected life of the options, which is based on historical experience and general option holder behaviour.

RSUs and PSUs vest after the end of a performance period, ranging from three to five years. The number of PSUs that vest is based on the achievement of specified performance measures. The fair value of each RSU and PSU granted is measured separately at the grant date based on the market value of a Loblaw common share less the net present value of the expected dividend stream at the date on which RSUs and PSUs are awarded to each participant.

Members of the Board, who are not management of the Company, may elect to receive a portion of their annual retainers and fees in the form of DSUs. Eligible executives of the Company may elect to defer up to 100% of the Short Term Incentive Plan earned in any year into the EDSU plan. Dividends paid earn fractional DSUs and EDSUs, respectively and are treated as additional awards. DSUs and EDSUs vest upon grant.

The compensation expense for equity-settled plans is prorated over the vesting or performance period, with a corresponding increase to contributed surplus. Forfeitures are estimated at the grant date and are revised to reflect changes in expected or actual forfeitures.

Upon exercise of options, the amount recognized in contributed surplus for the award plus the cash received upon exercise is recognized as an increase in share capital. Upon settlement of RSUs and PSUs, the amount recognized in contributed surplus for the award is reclassified to share capital, with any premium or discount applied to retained earnings.

The Company established a trust for each of the RSU and PSU plans to facilitate the purchase of shares for future settlement upon vesting. The trusts are considered structured entities and are consolidated in the Company's financial statements with the cost of the acquired shares recorded at book value as a reduction to share capital. Any premium on the acquisition of the shares above book value is applied to retained earnings until the shares are issued to settle RSU and PSU plan obligations.

**Cash-Settled Equity-Based Compensation** Unit Options, Restricted Units (“RUs”) and Trustee Deferred Units (“DUs”) issued by Choice Properties, and certain DSUs are accounted for as cash-settled awards.

Choice Properties’ Unit Options may have a five to ten year term, vest 25% cumulatively on each anniversary date of the grant and are exercisable at the designated Unit price, which is based on the greater of the volume weighted average trading price of a Unit for the five trading days prior to the date of grant or the trading day immediately preceding the grant date. The fair value of each tranche is valued separately using a Black-Scholes option pricing model, and includes the following assumptions:

- The expected distribution yield is estimated based on the expected annual distribution prior to the balance sheet date and the closing share price as at the balance sheet date;
- The expected unit price volatility is estimated based on the average volatility of investment grade entities in the Standard & Poor’s/ Toronto Stock Exchange (“TSX”) REIT Index over a period consistent with the expected life of the options;
- The risk-free interest rate is estimated based on the Government of Canada bond yield in effect at the balance sheet date for a term to maturity equal to the expected life of the options; and
- The effect of expected exercise of options prior to expiry is incorporated into the weighted average expected life of the options, which is based on expectations of option holder behaviour.

RUs entitle certain employees to receive the value of the RU award in cash or Units at the end of the applicable vesting period, which is usually three years in length. The RU plan provides for the crediting of additional RUs in respect of distributions paid on Units for the period when an RU is outstanding. The fair value of each RU granted is measured based on the market value of a Unit at the balance sheet date.

Members of the Choice Properties’ Board of Trustees, who are not management of Choice Properties, are required to receive a portion of their annual retainer in the form of DUs and may also elect to receive up to 100% of their remaining fees in DUs. Distributions paid earn fractional DUs, which are treated as additional awards. DUs vest upon grant.

The fair value of the amount payable to employees in respect of these cash settled awards plan is re-measured at each balance sheet date, and a compensation expense is recognized in selling, general and administrative expenses (“SG&A”) over the vesting period for each tranche with a corresponding change in the liability.

On the acquisition of Shoppers Drug Mart, the Company converted Shoppers Drug Mart DSUs to Loblaw DSUs. Former directors of Shoppers Drug Mart who continue to serve the Company in the same capacity, hold DSU’s that they have previously elected to receive in lieu of director fees. These converted DSUs, which vested upon grant, will be settled in cash based on the market value of the Company’s shares on the date the recipient ceases to serve the Company as director. Dividends paid earn fractional DSUs and are treated as additional awards. The fair value of each converted DSU granted is measured based on the market value of a Loblaw common share at the balance sheet date.

**Employee Share Ownership Plan** The Company’s contributions to the Employee Share Ownership Plan (“ESOP”) are measured at cost and recorded as compensation expense in operating income when the contribution is made. The ESOP is administered through a trust which purchases the Company’s common shares on the open market on behalf of its employees.

## Accounting Standards Implemented in 2014 and Changes to Significant Accounting Policies

The Company implemented the amendments to International Accounting Standards ("IAS") 32, "Financial Instruments: Presentation" and International Financial Reporting Interpretations Committee ("IFRIC") 21, "Levies" retrospectively in 2014. There was no significant impact on the Company's annual audited consolidated financial statements as a result of the implementation of these standards.

**Vendor Allowances** The timing of recognition of vendor allowances requires judgment to determine the point at which the Company has earned the allowance. In conjunction with the acquisition of Shoppers Drug Mart, management reviewed the timing of recognition of certain vendor allowances and has determined that it would be appropriate to align the policies of both companies. The Company has implemented the change retrospectively in 2014, as follows:

### Consolidated Statement of Earnings and Comprehensive Income

Increase (Decrease)

(millions of Canadian dollars except where otherwise indicated)

		2013
Cost of Merchandise Inventories Sold	\$	5
Operating Income	\$	(5)
Earnings Before Income Taxes	\$	(5)
Income taxes		(2)
Net Earnings	\$	(3)
Total Comprehensive Income	\$	(3)
<hr/>		
Net Earnings per Common Share (\$)		
Basic	\$	(0.01)
Diluted	\$	(0.01)

### Consolidated Balance Sheets

Increase (Decrease)

(millions of Canadian dollars)

	As at	As at
	December 28, 2013	December 30, 2012
Accounts receivable	\$ (39)	\$ (32)
Inventories	13	11
Deferred Income Tax Assets	8	6
Total Equity Attributable to Shareholders of the Company	\$ (18)	\$ (15)

## Note 3. Critical Accounting Estimates and Judgments

The preparation of the consolidated financial statements requires management to make estimates and judgments in applying the Company's accounting policies that affect the reported amounts and disclosures made in the consolidated financial statements and accompanying notes.

Within the context of these consolidated financial statements, a judgment is a decision made by management in respect of the application of an accounting policy, a recognized or unrecognized financial statement amount and/or note disclosure, following an analysis of relevant information that may include estimates and assumptions. Estimates and assumptions are used mainly in determining the measurement of balances recognized or disclosed in the consolidated financial statements and are based on a set of underlying data that may include management's historical experience, knowledge of current events and conditions and other factors that are believed to be reasonable under the circumstances. Management continually evaluates the estimates and judgments it uses.

The following are the accounting policies subject to judgments and key sources of estimation uncertainty that the Company believes could have the most significant impact on the amounts recognized in the consolidated financial statements. The Company's significant accounting policies are disclosed in note 2.



## Consolidation

***Judgments Made in Relation to Accounting Policies Applied*** The Company uses judgment in determining the entities that it controls and therefore consolidates. The Company controls an entity when the Company has the existing rights that give it the current ability to direct the activities that significantly affect the entities' returns. The Company consolidates all of its wholly owned subsidiaries. Judgment is applied in determining whether the Company controls the entities in which it does not have ownership rights or does not have full ownership rights. Most often, judgment involves reviewing contractual rights to determine if rights are participating (giving power over the entity) or protective rights (protecting the Company's interest without giving it power).

## Inventories

***Key Sources of Estimation*** Inventories are carried at the lower of cost and net realizable value which requires the Company to utilize estimates related to fluctuations in shrink, future retail prices, the impact of vendor rebates on cost, seasonality and costs necessary to sell the inventory.

## Impairment of Non-Financial Assets (Goodwill, Intangible Assets, Fixed Assets and Investment Properties)

***Judgments Made in Relation to Accounting Policies Applied*** Management is required to use judgment in determining the grouping of assets to identify their CGUs for the purposes of testing fixed assets for impairment. Judgment is further required to determine appropriate groupings of CGUs, for the level at which goodwill and intangible assets are tested for impairment. The Company has determined that each location is a separate CGU for purposes of fixed asset impairment testing. For the purpose of goodwill and indefinite life intangible impairment testing, CGUs are grouped at the lowest level at which goodwill and intangibles are monitored for internal management purposes. In addition, judgment is used to determine whether a triggering event has occurred requiring an impairment test to be completed.

***Key Sources of Estimation*** In determining the recoverable amount of a CGU or a group of CGUs, various estimates are employed. The Company determines fair value less costs to sell using such estimates as market rental rates for comparable properties, recoverable operating costs for leases with tenants, non-recoverable operating costs, discount rates, capitalization rates and terminal capitalization rates. The Company determines value in use by using estimates including projected future sales, earnings and capital investment consistent with strategic plans presented to the Board. Discount rates are consistent with external industry information reflecting the risk associated with the specific cash flows.

## Franchise Loans Receivable and Certain Other Financial Assets

***Judgments Made in Relation to Accounting Policies Applied*** Management reviews franchise loans receivable, trade receivables and certain other assets relating to the Company's franchise business at each balance sheet date utilizing judgment to determine whether a triggering event has occurred requiring an impairment test to be completed.

***Key Sources of Estimation*** Management determines the initial fair value of its franchise loans and certain other financial assets using discounted cash flow models. The process of determining these fair values requires management to make estimates of a long term nature regarding discount rates, projected revenues, and margins, as applicable, derived from past experience, actual operating results, budgets and the Company's five year forecast.

## Loyalty Programs

***Key Sources of Estimation*** The Company defers revenue equal to the fair value of the award points earned by loyalty program members at the time of award. The Company determines fair value using such estimates as breakage (the amount of points that will never be redeemed) and the estimated retail value per point on redemption. The trends in breakage are reviewed on an ongoing basis and the estimated retail value per point is adjusted based on expected future activity.

## Income and Other Taxes

***Judgments Made in Relation to Accounting Policies Applied*** The calculation of current and deferred income taxes requires management to make certain judgments regarding the tax rules in jurisdictions where the Company performs activities. Application of judgments is required regarding the classification of transactions and in assessing probable outcomes of claimed deductions including expectations about future operating results, the timing and reversal of temporary differences and possible audits of income tax and other tax filings by the tax authorities.

#### Note 4. Future Accounting Standards

In May 2014, the IASB issued IFRS 15, "Revenue from Contracts with Customers" ("IFRS 15"). The new standard provides a comprehensive framework for the recognition, measurement and disclosure of revenue from contracts with customers, excluding contracts within the scope of the accounting standards on leases, insurance contracts and financial instruments. IFRS 15 becomes effective for annual periods beginning on or after January 1, 2017, and is to be applied retrospectively. Early adoption is permitted. The Company is currently assessing the impact of the new standard on its consolidated financial statements.

In July 2014, the IASB issued IFRS 9, "Financial Instruments", replacing IAS 39, "Financial Instruments: Recognition and Measurement." The standard had three main phases: classification and measurement, impairment, and general hedging. The standard becomes effective for annual periods beginning on or after January 1, 2018 and is to be applied retrospectively with the exception of the general hedging phase which is applied prospectively. Early adoption is permitted. The Company is currently assessing the impact of the new standard on its consolidated financial statements.

In December 2014, the IASB issued amendments to IAS 1, "Presentation of Financial Statements" ("IAS 1 amendments"). The IAS 1 amendments provide guidance on the application of judgment in the preparation of financial statements and disclosures. The IAS 1 amendments are effective for annual periods beginning on or after January 1, 2016. Early adoption is permitted. The Company is currently assessing the impact of the IAS 1 amendments on its consolidated financial statements.

#### Note 5. Acquisition of Shoppers Drug Mart Corporation

On March 28, 2014, the Company acquired all of the outstanding shares of Shoppers Drug Mart for total consideration of \$12,273 million, comprised of approximately \$6,600 million of cash and the issuance of approximately 119.5 million common shares of the Company.

The cash portion of the acquisition of Shoppers Drug Mart was financed as follows:

- \$3,500 million unsecured term loan facility (see note 22);
- \$1,600 million of proceeds from the issuance of unsecured notes in 2013 (see note 9);
- \$500 million was received in consideration of the issuance of 10.5 million common shares to Weston; and
- approximately \$1,000 million was used from cash on hand.

The preliminary purchase equation is based on management's current best estimates of fair value. The actual amount allocated to certain identifiable net assets could vary as the purchase equation is finalized. The preliminary purchase price allocation as at March 28, 2014 is as follows:

(millions of Canadian dollars)

<b>Net Assets Acquired:</b>	
Cash and cash equivalents	\$ 27
Accounts receivable	534
Inventories	3,003
Prepaid expenses and other assets	67
Fixed assets	1,792
Investment properties	16
Intangible assets	9,440
Goodwill	2,285
Deferred income tax assets	68
Other assets	7
Bank indebtedness	(295)
Trade payables and other liabilities	(924)
Income taxes payable	(11)
Associate interest	(174)
Provisions	(19)
Long term debt	(1,127)
Deferred income tax liabilities	(2,252)
Other liabilities	(164)
<b>Total Net Assets Acquired</b>	<b>\$ 12,273</b>

As at January 3, 2015, the Company has not yet finalized the above purchase price allocation. In the fourth quarter of 2014, the Company revised its fair value estimate of intangible assets and updated the purchase price equation. The result was to decrease intangible assets by \$35 million to \$9,440 million, decrease deferred income tax liabilities by \$9 million to \$2,252 million and increase goodwill by \$26 million to \$2,285 million. The Company has one year from the date of acquisition to finalize the fair value of net tangible assets, goodwill and intangible assets and any further changes to the amounts presented above will be reflected in the first half of 2015.

Goodwill is attributable to synergies expected following the integration of Shoppers Drug Mart, improved competitive positioning in the retail market, and future growth of the Company's customer base as a result of the acquisition. The goodwill arising from this acquisition is not deductible for tax purposes.

Intangible assets are comprised of the following:

(millions of Canadian dollars)

Intangible Assets:		Estimated Useful Life
Prescription files	\$ 5,005	11 years
Brands	3,390	indefinite
Optimum loyalty program	490	18 years
Other	555	5 to 10 years
<b>Total Intangible Assets</b>	<b>\$ 9,440</b>	

Pursuant to a Consent Agreement reached with the Competition Bureau in 2014, the Company was required to divest 16 Shoppers Drug Mart stores, two of the Company's franchise grocery stores, as well as nine of the Company's in-store pharmacy operations. As at January 3, 2015, the Competition Bureau has approved the sale of all properties. During 2014, the divestitures of all but three Shoppers Drug Mart stores were completed (see note 36) and the Company received total proceeds of \$60 million and recorded a loss of \$12 million in operating income related to divestitures that have been completed.

The Company has incurred costs of \$75 million (2013 – \$31 million) related to the acquisition of Shoppers Drug Mart, of which \$60 million (2013 – \$6 million) was recorded in SG&A and \$15 million (2013 – \$25 million) was recorded in net interest expense and other financing charges.

Upon closing of the acquisition, all amounts owing on Shoppers Drug Mart's revolving bank credit facility were repaid and the facility was cancelled. In addition, upon closing, the Company guaranteed the outstanding principal amount of Shoppers Drug Mart medium term notes ("MTNs") of \$500 million, along with accrued interest. The Company has also provided guarantees to various Canadian banks in support of the financing obtained by Shoppers Drug Mart's Associates (see note 33).

Included in the consolidated statement of earnings for the year ended January 3, 2015 are approximately \$9,100 million in revenue and approximately \$542 million in net earnings contributed by Shoppers Drug Mart, since the date of acquisition, excluding the impact of purchase price adjustments, acquisition costs and divestitures required by the Competition Bureau.

On a combined pro forma basis for 2014, the Company's total revenue would have amounted to approximately \$45,100 million and the Company's net earnings would have amounted to approximately \$83 million. This pro forma information incorporates the effect of the preliminary purchase equation as if the acquisition had been effective December 29, 2013.

## Note 6. Net Interest Expense and Other Financing Charges

(millions of Canadian dollars)	2014	2013
Interest expense and other financing charges:		
Long term debt	\$ 466	\$ 287
Choice Properties Initial Public Offering transaction costs	—	44
Early debt settlement costs (note 22)	—	18
Shoppers Drug Mart acquisition-related costs (note 5)	18	30
Borrowings related to credit card receivables	37	39
Trust Unit distributions	44	21
Post-employment and other long term employee benefits (note 27)	12	23
Independent funding trusts	15	15
Dividends on capital securities (note 24)	14	14
Fair value adjustment of Trust Unit Liability (note 30)	17	27
Bank indebtedness (note 33)	6	—
Capitalized interest (capitalization rate 6.2% (2013 – 6.4%)) (note 14 and 16)	(4)	(2)
	\$ 625	\$ 516
Interest income:		
Accretion income	\$ (25)	\$ (21)
Derivative financial instruments	—	(10)
Short term interest income	(12)	(11)
Security deposits <sup>(i)</sup>	(4)	(6)
	\$ (41)	\$ (48)
Net interest expense and other financing charges	\$ 584	\$ 468

(i) Includes interest income of \$3 million (2013 – \$5 million) related to \$1,599 million of proceeds from the issuance of senior unsecured notes previously held in escrow (see note 9), which were used to partially fund the acquisition of all of the outstanding common shares of Shoppers Drug Mart (see note 5).

## Note 7. Income Taxes

Income taxes recognized in the consolidated statements of earnings were as follows:

(millions of Canadian dollars)	2014	2013
Current income taxes:		
Current period	\$ 297	\$ 287
Adjustment in respect of prior periods	(18)	(1)
	\$ 279	\$ 286
Deferred income taxes:		
Origination and reversal of temporary differences	(273)	(50)
Adjustment in respect of prior periods	19	(10)
	(254)	(60)
Income taxes	\$ 25	\$ 226

Notes to the Consolidated Financial Statements

Income tax (recovery) expense recognized in other comprehensive income (loss) was as follows:

(millions of Canadian dollars)	2014	2013
Defined benefit plan actuarial (loss) income	\$ (16)	\$ 85
Derecognized derivative instrument	—	(2)
Other comprehensive (loss) income	\$ (16)	\$ 83

The effective income tax rate in the consolidated statements of earnings was reported at rates different than the weighted average basic Canadian federal and provincial statutory income tax rates for the following reasons:

	2014	2013
Weighted average basic Canadian federal and provincial statutory income tax rate	26.1%	26.0%
Net increase (decrease) resulting from:		
Effect of tax rate in foreign jurisdictions	(3.2)	(0.6)
Non-deductible items	2.2	1.7
Impact of fair value adjustments of the Trust Unit Liability	5.8	0.8
Impact of statutory income tax rate changes on deferred income tax balances	—	(0.1)
Adjustments in respect of prior periods	1.2	(1.3)
Effective income tax rate applicable to earnings before income taxes	32.1%	26.5%

**Unrecognized deferred tax assets** Deferred income tax assets were not recognized on the consolidated balance sheet in respect of the following items:

(millions of Canadian dollars)	2014	2013
Deductible temporary differences	\$ 19	\$ 12
Income tax losses	57	29
Unrecognized deferred tax assets	\$ 76	\$ 41

The income tax losses expire in the years 2027 to 2034. The deductible temporary differences do not expire under current income tax legislation. Deferred income tax assets were not recognized in respect of these items because it is not probable that future taxable income will be available to the Company to utilize the benefits.



**Recognized deferred tax assets and liabilities** Deferred tax assets and liabilities were attributable to the following:

(millions of Canadian dollars)	As at January 3, 2015	As at December 28, 2013
Trade payables and other liabilities	\$ 56	\$ 48
Other liabilities	347	243
Fixed assets	(517)	(356)
Goodwill and intangible assets	(1,816)	(4)
Other assets	10	38
Non-capital loss carryforwards (expiring 2030 to 2034)	161	201
Capital loss carryforwards	20	1
Other	52	56
Net deferred income tax (liabilities) assets	\$ (1,687)	\$ 227
Recorded on the consolidated balance sheets as follows:		
Deferred income tax assets	193	261
Deferred income tax liabilities	(1,880)	(34)
Net deferred income tax (liabilities) assets	\$ (1,687)	\$ 227

**Note 8. Basic and Diluted Net Earnings per Common Share**

(millions of Canadian dollars except where otherwise indicated)	2014	2013
Net earnings	\$ 53	\$ 627
Weighted average common shares outstanding (note 24) (in millions)	380.5	281.1
Dilutive effect of equity-based compensation (in millions)	3.4	2.1
Dilutive effect of certain other liabilities (in millions)	0.5	0.9
Diluted weighted average common shares outstanding (in millions)	384.4	284.1
Basic net earnings per common share (\$)	\$ 0.14	\$ 2.23
Diluted net earnings per common share (\$)	\$ 0.14	\$ 2.21

Excluded from the computation of diluted net earnings per common share were 10,620,095 (2013 – 11,503,993) potentially dilutive instruments, as they were anti-dilutive.

**Note 9. Cash and Cash Equivalents, Short Term Investments and Security Deposits**

The components of cash and cash equivalents, short term investments and security deposits were as follows:

**Cash and Cash Equivalents**

(millions of Canadian dollars)	As at January 3, 2015	As at December 28, 2013
Cash	\$ 464	\$ 515
Cash equivalents:		
Bankers' acceptances	57	270
Government treasury bills	463	1,420
Bank term deposits	—	42
Corporate commercial paper	15	13
<b>Total cash and cash equivalents</b>	<b>\$ 999</b>	<b>\$ 2,260</b>

**Short Term Investments**

(millions of Canadian dollars)	As at January 3, 2015	As at December 28, 2013
Bankers' acceptances	\$ 2	\$ 162
Government treasury bills	17	98
Corporate commercial paper	1	—
Government agencies securities	—	30
Other	1	—
<b>Total short term investments</b>	<b>\$ 21</b>	<b>\$ 290</b>

**Security Deposits**

(millions of Canadian dollars)	As at January 3, 2015	As at December 28, 2013
Cash	\$ 7	\$ 102
Government treasury bills <sup>(i)</sup>	—	1,599
<b>Total security deposits</b>	<b>\$ 7</b>	<b>\$ 1,701</b>

- (i) As at December 28, 2013, Government treasury bills included \$1,599 million of proceeds from the issuance of senior unsecured notes that were held in escrow as part of the financing for the acquisition of Shoppers Drug Mart. In 2014, the Company completed the acquisition of Shoppers Drug Mart and the proceeds were released from escrow (see note 5).

As at January 3, 2015, the Company had agreements to cash collateralize certain of its uncommitted credit facilities up to an amount of \$141 million (December 28, 2013 – \$136 million), of which \$7 million (December 28, 2013 – \$102 million) was deposited with major financial institutions and classified as security deposits.

## Note 10. Accounts Receivable

The following is an aging of the Company's accounts receivable:

(millions of Canadian dollars)	As at January 3, 2015				As at December 28, 2013			
	0-90 days	91-180 days	> 180 days	Total	0-90 days	91-180 days	> 180 days	Total
Accounts receivable	\$ 1,104	\$ 38	\$ 67	\$ 1,209	\$ 546	\$ 17	\$ 16	\$ 579

The following are continuities of the Company's allowances for uncollectable accounts receivable:

(millions of Canadian dollars)	2014	2013
Allowance, beginning of year	\$ (118)	\$ (110)
Net reversals (additions)	22	(8)
Allowance, end of year	\$ (96)	\$ (118)

Credit risk associated with accounts receivable are discussed in note 31.

## Note 11. Credit Card Receivables

The components of credit card receivables were as follows:

(millions of Canadian dollars)	As at January 3, 2015	As at December 28, 2013
Gross credit card receivables	\$ 2,684	\$ 2,585
Allowance for credit card receivables	(54)	(47)
Credit card receivables	\$ 2,630	\$ 2,538
Securitized to independent securitization trusts:		
Securitized to <i>Eagle Credit Card Trust</i> <sup>®</sup>	\$ 750	\$ 750
Securitized to Other Independent Securitization Trusts	605	605

The Company, through PC Bank, participates in various securitization programs that provide the primary source of funds for the operation of its credit card business. PC Bank sells and repurchases credit card receivables with independent securitization trusts, including *Eagle* and Other Independent Securitization Trusts, from time to time, depending on PC Bank's financing requirements.

The associated liability of *Eagle* is recorded in long term debt (see note 22). The associated liabilities of credit card receivables securitized to the Other Independent Securitization Trusts are recorded in short term debt (see note 20).

The Company has arranged letters of credit on behalf of PC Bank, for the benefit of the independent securitization trusts (see note 33).

Under its securitization programs, PC Bank is required to maintain at all times a credit card receivable pool balance equal to a minimum of 107% of the outstanding securitized liability and was in compliance with this requirement as at January 3, 2015 and throughout the year.

The following is an aging of the Company's gross credit card receivables:

(millions of Canadian dollars)	As at January 3, 2015				As at December 28, 2013			
	Current	1-90 days past due	> 90 days past due	Total	Current	1-90 days past due	> 90 days past due	Total
Gross credit card receivables	\$ 2,505	\$ 150	\$ 29	\$ 2,684	\$ 2,416	\$ 142	\$ 27	\$ 2,585

The following are continuities of the Company's allowances for credit card receivables:

(millions of Canadian dollars)	2014	2013
Allowances, beginning of year	\$ (47)	\$ (43)
Provision for losses	(121)	(105)
Recoveries	(19)	(14)
Write-offs	133	115
Allowances, end of year	\$ (54)	\$ (47)

The allowance for credit card receivables recorded in credit card receivables on the consolidated balance sheets is maintained at a level which is considered adequate to absorb credit related losses on credit card receivables.

#### Note 12. Inventories

For inventories recorded as at January 3, 2015, the Company recorded \$23 million (December 28, 2013 – \$16 million) as an expense for the write-down of inventories below cost to net realizable value. The write-down was included in cost of merchandise inventories sold. There were no reversals of previously recorded write-downs of inventories during 2014 and 2013.

In connection with the acquisition of Shoppers Drug Mart, acquired assets and liabilities were recorded on the Company's consolidated balance sheet at their fair value. This resulted in a fair value adjustment to Shoppers Drug Mart inventory on the date of acquisition of \$798 million representing the difference between inventory cost and its fair value. This difference was recognized in cost of merchandise inventories sold during 2014, with a resulting negative impact to operating income.

As at the end of 2014, with the upgrade of its information technology ("IT") infrastructure, the Company had completed the conversion of substantially all of its corporate grocery stores to the new systems. The implementation of a perpetual inventory system, combined with visibility to integrated costing information provided by the new IT systems, enabled the Company to estimate the cost of inventory using a more precise system-generated average cost. As a result of the conversion, the Company recognized a \$190 million charge to cost of merchandise inventories sold and a corresponding reduction in inventory, representing the estimate of the difference between the measurement of the cost of corporate grocery store inventory using a system generated weighted average cost compared to the retail inventory method and other conversion differences associated with the implementation of a perpetual inventory system.

#### Note 13. Assets Held for Sale

The Company holds land and buildings as assets held for sale that it intends to dispose of in the next 12 months. These assets were previously used in the Company's retail business segment. There were no impairment or other charges recognized on these properties during 2014 (2013 – nil). In 2014, the Company recorded a \$4 million gain (2013 – \$7 million) from the sale of these assets, excluding the impact of completed divestitures related to the acquisition of Shoppers Drug Mart (see note 5).

As a condition to receiving the approval of the Competition Bureau in relation to the acquisition of Shoppers Drug Mart, the Company was required to divest 16 Shoppers Drug Mart stores, two of the Company's franchise grocery stores, as well as nine of the Company's in-store pharmacy operations. During 2014, a \$12 million net loss was recorded in operating income from the divestiture of properties required by the Competition Bureau related to the acquisition of Shoppers Drug Mart.

As at January 3, 2015, assets totalling \$8 million, including intangible assets of \$3 million, inventories of \$3 million and fixed assets of \$2 million, relating to the three remaining Shoppers Drug Mart stores expected to be sold in the first quarter of 2015, have been included in assets held for sale.

## Note 14. Fixed Assets

The following are continuities of the cost and accumulated depreciation of fixed assets for the years ended January 3, 2015 and December 28, 2013:

	2014							
(millions of Canadian dollars)	Land	Buildings	Equipment and Fixtures	Leasehold Improvements	Finance Leases - Land, Buildings, Equipment and Fixtures	Assets Under Construction	Total	
<b>Cost</b>								
Balance, beginning of year	\$ 1,678	\$ 6,849	\$ 6,424	\$ 846	\$ 567	\$ 596	\$ 16,960	
Additions	7	13	101	82	102	776	1,081	
Business acquisitions <sup>(i)</sup>	88	268	374	830	162	72	1,794	
Disposals	(11)	(13)	(108)	(11)	(14)	(13)	(170)	
Net transfer to assets held for sale	(5)	(16)	(11)	(14)	—	—	(46)	
Net transfer (to) from investment properties	5	12	—	—	—	(73)	(56)	
Transfer from assets under construction	38	255	472	32	—	(797)	—	
Balance, end of year	\$ 1,800	\$ 7,368	\$ 7,252	\$ 1,765	\$ 817	\$ 561	\$ 19,563	
<b>Accumulated depreciation and impairment losses</b>								
Balance, beginning of year	\$ 2	\$ 2,429	\$ 4,663	\$ 493	\$ 261	\$ 7	\$ 7,855	
Depreciation	—	201	658	132	47	1	1,039	
Impairment losses	1	11	12	13	1	2	40	
Reversal of impairment losses	(1)	(31)	(1)	(2)	—	—	(35)	
Disposals	—	(9)	(86)	(9)	(14)	—	(118)	
Transfer to assets held for sale	—	(4)	(10)	(7)	—	—	(21)	
Net transfer from investment properties	1	8	—	—	—	—	9	
Balance, end of year	\$ 3	\$ 2,605	\$ 5,236	\$ 620	\$ 295	\$ 10	\$ 8,769	
<b>Carrying amount as at:</b>								
January 3, 2015	\$ 1,797	\$ 4,763	\$ 2,016	\$ 1,145	\$ 522	\$ 551	\$ 10,794	

(i) Includes \$1,792 million related to the acquisition of Shoppers Drug Mart (see note 5).



2013

(millions of Canadian dollars)	Land	Buildings	Equipment and Fixtures	Leasehold Improvements	Finance Leases - Land, Buildings, Equipment and Fixtures	Assets Under Construction	Total
<b>Cost</b>							
Balance, beginning of year	\$ 1,650	\$ 6,555	\$ 5,950	\$ 790	\$ 554	\$ 664	\$ 16,163
Additions	1	—	14	9	62	837	923
Disposals	(2)	(4)	(57)	(7)	(53)	—	(123)
Net transfer from assets held for sale	1	—	—	—	—	—	1
Net transfer (to) from investment properties	(2)	(1)	—	—	4	(5)	(4)
Transfer from assets under construction	30	299	517	54	—	(900)	—
Balance, end of year	\$ 1,678	\$ 6,849	\$ 6,424	\$ 846	\$ 567	\$ 596	\$ 16,960
<b>Accumulated depreciation and impairment losses</b>							
Balance, beginning of year	\$ 7	\$ 2,298	\$ 4,176	\$ 433	\$ 269	\$ 7	\$ 7,190
Depreciation	—	184	532	44	44	—	804
Impairment losses	—	20	5	24	3	—	52
Reversal of impairment losses	(4)	(71)	(2)	(3)	(3)	—	(83)
Disposals	(1)	(1)	(48)	(5)	(53)	—	(108)
Net transfer (to) from investment properties	—	(1)	—	—	1	—	—
Balance, end of year	\$ 2	\$ 2,429	\$ 4,663	\$ 493	\$ 261	\$ 7	\$ 7,855
<b>Carrying amount as at:</b>							
December 28, 2013	\$ 1,676	\$ 4,420	\$ 1,761	\$ 353	\$ 306	\$ 589	\$ 9,105

**Assets Held under Finance Leases** The Company leases various land and buildings, and equipment and fixtures under a number of finance lease arrangements. As at January 3, 2015, the net carrying amount of leased land and buildings was \$466 million (December 28, 2013 – \$274 million), and the net carrying amount of leased equipment and fixtures was \$56 million (December 28, 2013 – \$32 million).

**Assets under Construction** The cost of additions to properties under construction for the year ended January 3, 2015 was \$776 million (December 28, 2013 – \$837 million). Included in this amount are capitalized borrowing costs of \$3 million (2013 – \$2 million), with a weighted average capitalization rate of 6.2% (2013 – 6.4%).

**Security and Assets Pledged** As at January 3, 2015, fixed assets with a carrying amount of \$191 million (December 28, 2013 – \$187 million) were encumbered by mortgages of \$86 million (December 28, 2013 – \$87 million).

**Fixed Asset Commitments** As at January 3, 2015, the Company had entered into commitments of \$192 million (December 28, 2013 – \$55 million) for the construction, expansion and renovation of buildings and the purchase of real property.

**Impairment Losses** For the year ended January 3, 2015, the Company recorded \$26 million (2013 – \$48 million) of impairment losses on fixed assets in respect of 13 CGUs (2013 – 21 CGUs) in the retail operating segment. Additional impairment losses of \$14 million (2013 – \$4 million) were incurred related to store closures, renovations and conversions. Impairment losses are recorded where the carrying amount of the retail location exceeds its recoverable amount. The recoverable amount was based on the greater of the CGU's fair value less costs to sell and its value in use. Approximately 23% (2013 – 10%) of impaired CGUs had carrying values which were \$7 million (2013 – \$6 million) greater than their fair value less costs to sell. The remaining 77% (2013 – 90%) of impaired CGUs had carrying values which were \$19 million (2013 – \$46 million) greater than their value in use.

For the year ended January 3, 2015, the Company recorded \$35 million (2013 – \$83 million) of impairment reversals on fixed assets in respect of 14 CGUs (2013 – 26 CGUs) in the retail operating segment. Impairment reversals are recorded where the recoverable amount of the retail location exceeds its carrying amount. Approximately 93% (2013 – 92%) of CGUs with impairment reversals had fair value less costs to sell which were \$33 million (2013 – \$75 million) greater than their carrying values. The remaining 7% (2013 – 8%) of CGUs with impairment reversals had value in use which were \$2 million (2013 – \$8 million) greater than carrying values.

When determining the value in use of a retail location, the Company develops a discounted cash flow model for each CGU. The duration of the cash flow projections for individual CGUs varies based on the remaining useful life of the significant assets within the CGU. Sales forecasts for cash flows are based on actual operating results, operating budgets, and long term growth rates that were consistent with industry averages, all of which is consistent with strategic plans presented to the Company's Board. The estimate of the value in use of the relevant CGUs was determined using a pre-tax discount rate of 8.0% to 8.5% at January 3, 2015 (December 28, 2013 – 8.0% to 8.5%).

#### Note 15. Investment Properties

The following are continuities of investment properties:

(millions of Canadian dollars)	2014	2013
<b>Cost</b>		
Balance, beginning of year	\$ 172	\$ 169
Business acquisitions <sup>(i)</sup>	16	—
Additions	16	1
Disposals	(4)	(2)
Net transfer from fixed assets	56	4
Net transfer to assets held for sale	(1)	—
Balance, end of year	\$ 255	\$ 172
<b>Accumulated depreciation and impairment losses</b>		
Balance, beginning of year	\$ 73	\$ 69
Depreciation	2	2
Impairment losses	11	—
Reversal of impairment losses	—	(1)
Disposals	(2)	(1)
Net transfer to fixed assets	(9)	—
Net transfer (to) from assets held for sale	(5)	4
Balance, end of year	\$ 70	\$ 73
Carrying amount	\$ 185	\$ 99
Fair value	225	144

(i) Relates to the acquisition of Shoppers Drug Mart (see note 5).

During 2014, the Company recognized in operating income \$7 million of rental income (2013 – \$4 million) and incurred direct operating costs of \$3 million (2013 – \$3 million) related to its investment properties. In addition, the Company recognized direct operating costs of \$2 million (2013 – \$1 million) related to its investment properties for which no rental income was earned.

An external, independent valuation company, having appropriate recognized professional qualifications and recent experience in the location and category of property being valued, provided appraisals for certain of the Company's investment properties. For the other investment properties, the Company determined the fair value by relying on comparable market information. Where available, the fair values are based on market values, being the estimated amount for which a property could be exchanged on the date of the valuation between a willing buyer and a willing seller in an arm's length transaction after proper marketing wherein the parties had each acted knowledgeably and willingly. Where market values are not available, valuations are prepared using the income approach by considering the estimated cash flows expected from renting out the property based on existing lease terms and where appropriate, the ability to renegotiate the lease terms once the initial term or option term(s) expire plus the net proceeds from a sale of the property at the end of the investment horizon.

The valuations of investment properties using the income approach include assumptions as to market rental rates for properties of similar size and condition located within the same geographical areas, recoverable operating costs for leases with tenants, non-recoverable operating costs, vacancy periods, tenant inducements and capitalization rates for the purposes of determining the estimated net proceeds from the sale of the property. At January 3, 2015, the pre-tax discount rates used in the valuations for investment properties ranged from 6.00% to 9.75% (December 28, 2013 – 6.50% to 9.75%) and the terminal capitalization rates ranged from 5.50% to 8.50% (December 28, 2013 – 5.75% to 8.75%).

For the year ended January 3, 2015, the Company recorded \$11 million (2013 – nil) of impairment losses in operating income on investment properties as the carrying amounts of all impaired properties were lower than their recoverable amounts. The Company recorded no reversals of impairment losses on investment properties (2013 – \$1 million) in operating income where their fair values less costs to sell were greater than their carrying values.

#### Note 16. Intangible Assets

The following are continuities of the cost and accumulated amortization of intangible assets for the years ended January 3, 2015 and December 28, 2013:

(millions of Canadian dollars)	2014				Total
	Indefinite Life Intangible Assets	Definite Life Internally Generated Intangible Assets	Definite Life Other Intangible Assets		
<b>Cost</b>					
Balance, beginning of year	\$ 71	\$ 20	\$ 71	\$	162
Business acquisitions <sup>(i)</sup>	3,390	230	5,824		9,444
Additions	—	85	5		90
Disposal	—	(3)	(2)		(5)
Transfer to assets held for sale	—	—	(29)		(29)
Write off of cost for fully amortized assets	—	—	(1)		(1)
Balance, end of year	\$ 3,461	\$ 332	\$ 5,868	\$	9,661
<b>Accumulated amortization and impairment losses</b>					
Balance, beginning of year	\$ —	\$ 19	\$ 32	\$	51
Amortization	—	23	414		437
Transfer to assets held for sale	—	—	(3)		(3)
Write off of amortization for fully amortized assets	—	—	(1)		(1)
Balance, end of year	\$ —	\$ 42	\$ 442	\$	484
<b>Carrying amount as at:</b>					
January 3, 2015	\$ 3,461	\$ 290	\$ 5,426	\$	9,177

(i) Includes \$9,440 million related to the acquisition of Shoppers Drug Mart (see note 5).

(millions of Canadian dollars)	2013				Total
	Indefinite Life Intangible Assets	Definite Life Internally Generated Intangible Assets	Definite Life Other Intangible Assets		
<b>Cost</b>					
Balance, beginning of year	\$ 62	\$ 20	\$ 76	\$	158
Additions	9	—	3		12
Write off of cost for fully amortized assets	—	—	(8)		(8)
Balance, end of year	\$ 71	\$ 20	\$ 71	\$	162
<b>Accumulated amortization and impairment losses</b>					
Balance, beginning of year	\$ —	\$ 14	\$ 30	\$	44
Amortization	—	5	10		15
Write off of amortization for fully amortized assets	—	—	(8)		(8)
Balance, end of year	\$ —	\$ 19	\$ 32	\$	51
<b>Carrying amount as at:</b>					
December 28, 2013	\$ 71	\$ 1	\$ 39	\$	111

Indefinite life intangible assets are comprised of brand names, trademarks, and import purchase quota. The brand names and trademarks are a result of the Company's acquisition of Shoppers Drug Mart and T&T Supermarket Inc. The Company expects to renew the registration of the brand names, trademarks, and import purchase quota at each expiry date indefinitely, and expects these assets to generate economic benefit in perpetuity. As such, the Company assessed these intangibles to have indefinite useful lives.

The Company completed its annual impairment tests for indefinite life intangible assets and concluded that there was no impairment.

**Key Assumptions** The key assumptions used to calculate the fair value less costs to sell are those regarding discount rates, growth rates and expected changes in margins. These assumptions are consistent with the assumptions used to calculate fair value less costs to sell for goodwill (see note 17).

**Definite Life Intangible Assets** Definite life intangible assets are primarily comprised of Shoppers Drug Mart prescription files and the carrying value of the Optimum loyalty program (see note 5), and software purchases and development. Included in these amounts are capitalized borrowing costs of \$1 million (2013 – nil).

#### Note 17. Goodwill

The following is a continuity of the cost and accumulated amortization of goodwill for the years ended January 3, 2015 and December 28, 2013:

(millions of Canadian dollars)	2014	2013
<b>Cost</b>		
Balance, beginning of year	\$ 1,932	\$ 1,932
Business acquisitions <sup>(i)</sup>	2,300	—
Balance, end of year	\$ 4,232	\$ 1,932
<b>Accumulated amortization and impairment losses</b>		
Balance, beginning of year	\$ 989	\$ 989
Balance, end of year	\$ 989	\$ 989
Carrying amount as at the end of the year:	\$ 3,243	\$ 943

(i) Includes \$2,285 million related to the acquisition of Shoppers Drug Mart (see note 5).

The carrying amount of goodwill attributed to each CGU grouping was as follows:

(millions of Canadian dollars)	As at January 3, 2015	As at December 28, 2013
Shoppers Drug Mart	\$ 2,294	\$ —
Market	337	—
Discount	459	—
Quebec region	—	700
T&T Supermarket Inc.	129	129
All other	24	114
Carrying amount of goodwill	\$ 3,243	\$ 943

The Company completed its annual impairment tests for goodwill and concluded that there was no impairment. Subsequent to the acquisition of Shoppers Drug Mart, the Company reorganized its senior management, including the heads of the Company's banner groups, and as a result, the Company reallocated goodwill to this reorganized structure subsequent to the completion of the annual impairment test in 2014. CGU groupings for goodwill allocation are done by banner or groups of banners, whereas they were previously grouped by region.

**Key Assumptions** The key assumptions used to calculate the fair value less costs to sell are those regarding discount rates, growth rates and expected changes in margins. These assumptions are considered to be Level 3 in the fair value hierarchy.

The weighted average cost of capital was determined to be in the range of 6.0% to 6.5% (December 28, 2013 – 6.5% to 7.0%) and is based on a risk-free rate, an equity risk premium adjusted for betas of comparable publicly traded companies, an unsystematic risk premium, an after-tax cost of debt based on corporate bond yields and the capital structure of the Company.

Cash flow projections have been discounted using a range of rates derived from the Company's after-tax weighted average cost of capital adjusted for specific risks relating to each CGU. At January 3, 2015, the after-tax discount rates used in the recoverable amount calculations ranged from 8.5% to 9.5% (December 28, 2013 – 9.5%). The pre-tax discount rates ranged from 11.4% to 13.0% (December 28, 2013 – 12.8% to 13.0%).

The Company included a minimum of five years of cash flows in its discounted cash flow model. The cash flow forecasts were extrapolated beyond the five year period using estimated long term growth rate of 2.0% (December 28, 2013 – 2.0%). The budgeted EBITDA<sup>(1)</sup> growth is based on the Company's five year strategic plan approved by the Board.

(1) See Section 20 "Non-GAAP Financial Measures" of the Company's Management's Discussion and Analysis.



## Note 18. Interest in Other Entities

### Subsidiaries

Loblaw Companies Limited is a holding company which carries on its business through its subsidiaries. The subsidiaries of the Company that carry on its principal business are: Loblaws Inc., a retail operations company incorporated in Ontario, Shoppers Drug Mart Corporation, a pharmacy operations company incorporated in Canada, President's Choice Bank, a financial services company incorporated in Canada; Choice Properties Real Estate Investment Trust, a trust formed in Ontario; and Choice Properties Limited Partnership, a limited partnership formed in Ontario. During 2014 and 2013, the Company owned, either directly or indirectly, 100% of the voting securities of its subsidiaries, other than Choice Properties Real Estate Investment Trust and its subsidiaries, including Choice Properties Limited Partnership, of which Loblaw held an 82.9% (2013 – 82.2%) effective interest.

As at year end 2014, there were no significant restrictions on the ability to access or use assets and settle liabilities of the subsidiaries. In addition, there was no change in control of any subsidiary during 2014 and 2013.

The Company acquired and began consolidating Shoppers Drug Mart Corporation in 2014 (see note 5).

In 2014, Choice Properties Real Estate Investment Trust entered into an agreement with a third party for a controlling 70% ownership interest in Choice Properties PRC Brampton Limited Partnership, a subsidiary which holds land for future retail development. Choice Properties Real Estate Investment Trust fully consolidates this subsidiary and recognized non-controlling interests of \$8 million, which was included as a component of total equity.

### Consolidated Associates

**Associates** The Company consolidates the Associates based on the concept of control, which is determined, for accounting purposes, to exist through Associate Agreements. The Company does not have any direct or indirect shareholdings in the corporations (the "Associates' corporations") that operate the Associates. The Associates' corporations remain separate legal entities.

### Consolidated Structured Entities

**Independent Funding Trusts** Certain independent franchisees of the Company obtain financing through a structure involving independent funding trusts, which were created to provide loans to franchisees to facilitate their purchase of inventory and fixed assets, consisting mainly of fixtures and equipment. The Company provides a standby letter of credit for the benefit of the independent funding trust (see note 33).

**Eagle Credit Card Trust<sup>®</sup>** The Company, through PC Bank, participates in various securitization programs that provide the primary source of funds for the operation of its credit card business. Under these securitization programs, a portion of the total interest in credit card receivables is sold to third parties pursuant to co-ownership agreements that issue interest bearing securities. PC Bank participates in a single seller revolving co-ownership securitization program with *Eagle* and continues to service the credit card receivables on behalf of *Eagle*, but does 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. The Company provides a standby letter of credit for the benefit of the independent securitization trust (see note 33).

**Equity-Based Compensation Trusts** In 2013, the Company established trusts to facilitate the purchase of shares for future settlement of each of the RSU and PSU plans upon vesting. The Company is the sponsor of the trusts and has assigned Computershare Trust Company of Canada as the trustee. The Company funds the purchase of shares for settlement and earns management fees from the trusts.

### Unconsolidated Structured Entities

**Other Independent Securitization Trusts** The Other Independent Securitization Trusts administer multi-seller, multi-asset securitization programs that acquire assets from various participants, including credit card receivables from PC Bank. These trusts are managed by major Canadian chartered banks. PC Bank does not control the trusts through voting interests and does not exercise any control over the trusts' management, administration or assets. The activities of these trusts are conducted on behalf of the participants and each trust is a conduit through which funds are raised to purchase assets through the issue of senior and subordinated short term and medium term asset backed notes. The Company provides standby letters of credit for the benefit of these trusts (see note 33).

**Note 19. Other Assets**

(millions of Canadian dollars)	As at January 3, 2015	As at December 28, 2013
Sundry investments and other receivables	\$ 141	\$ 136
Accrued benefit plan asset (note 27)	90	106
Interest in joint venture (note 34)	6	—
Other	44	43
Other assets	\$ 281	\$ 285

**Note 20. Short Term Debt**

The outstanding short term debt balance of \$605 million (2013 – \$605 million) includes credit card receivables securitized to the Other Independent Securitization Trusts (see note 11).

In 2014, PC Bank extended the maturity date for one of its Other Independent Securitization Trust agreements from the third quarter of 2015 to the third quarter of 2016, with all other terms and conditions remaining substantially the same. In addition, PC Bank extended the maturity date for two of its Other Independent Securitization Trust agreements from the second quarter of 2015 to the second quarter of 2016, with all other terms and conditions remaining substantially the same.

During 2013, PC Bank repurchased \$300 million of co-ownership interests in the securitized receivables from the Other Independent Securitization Trusts, and recorded a corresponding decrease to short term debt.

The undrawn commitments on facilities available from the Other Independent Securitization Trusts as at January 3, 2015 were \$120 million (December 28, 2013 – \$120 million). The Company has arranged letters of credit on behalf of PC Bank, for the benefit of the Other Independent Securitization Trusts (see note 33).

**Note 21. Provisions**

Provisions consist primarily of amounts recorded in respect of restructuring, self-insurance, commodity taxes, environmental and decommissioning liabilities and onerous lease arrangements. The following are continuities relating to the Company's provisions:

(millions of Canadian dollars)	2014	2013
Provisions, beginning of year	\$ 122	\$ 137
Acquisition of Shoppers Drug Mart	19	—
Additions	81	38
Payments	(60)	(43)
Reversals	(2)	(10)
Provisions, end of year	\$ 160	\$ 122

(millions of Canadian dollars)	2014	2013
Recorded on the consolidated balance sheets as follows:		
Current portion of provisions	\$ 84	\$ 66
Non-current portion of provisions	76	56
Total provisions	\$ 160	\$ 122

During 2014, the Company recorded \$46 million (2013 – \$32 million) of restructuring and reorganization costs in operating income, primarily associated with the reduction of corporate and store-support positions, the departure of certain executives and the realignment of certain of the Company's central office functions. As at January 3, 2015, \$37 million was included in provisions relating to these restructuring initiatives (2013 – \$39 million).

## Note 22. Long Term Debt

(millions of Canadian dollars)	As at January 3, 2015	As at December 28, 2013
<b>Loblaw Companies Limited Notes (a)</b>		
6.00%, due 2014	\$ —	\$ 100
4.85%, due 2014	—	350
7.10%, due 2016	300	300
3.75%, due 2019	800	800
5.22%, due 2020	350	350
4.86%, due 2023	800	800
6.65%, due 2027	100	100
6.45%, due 2028	200	200
6.50%, due 2029	175	175
11.40%, due 2031		
Principal	151	151
Effect of coupon repurchase	(57)	(67)
6.85%, due 2032	200	200
6.54%, due 2033	200	200
8.75%, due 2033	200	200
6.05%, due 2034	200	200
6.15%, due 2035	200	200
5.90%, due 2036	300	300
6.45%, due 2039	200	200
7.00%, due 2040	150	150
5.86%, due 2043	55	55
<b>Shoppers Drug Mart Notes (b)</b>		
2.01%, due 2016	225	—
2.36%, due 2018	275	—
<b>Unsecured Term Loan Facility (c)</b>		
1.45% + Bankers' Acceptance, due 2019	1,229	—
<b>Long Term Debt Secured by Mortgage</b>		
5.49%, due 2018 (note 14)	86	87
<b>Guaranteed Investment Certificates (d)</b>		
Due 2015 - 2019 (1.20% - 3.78%)	634	430
<b>Independent Securitization Trusts (e)</b>		
<i>Eagle Credit Card Trust</i> <sup>®</sup> , 3.58%, due 2015	350	350
<i>Eagle Credit Card Trust</i> <sup>®</sup> , 2.91%, due 2018	400	400
<b>Independent Funding Trusts (f)</b>	498	475
<b>Finance Lease Obligations</b>	600	388
<b>Choice Properties (g)</b>		
Series A 3.55%, due 2018	400	400
Series B 4.90%, due 2023	200	200
Series C 3.50%, due 2021	250	—
Series D 4.29%, due 2024	200	—
Series 5 3.00%, due 2016	300	—
Series 6 3.00%, due 2017	200	—
Series 7 3.00%, due 2019	200	—
Series 8 3.60%, due 2020	300	—
Series 9 3.60%, due 2021	200	—
Series 10 3.60%, due 2022	300	—
Choice Properties Credit Facility	122	—
Transaction costs and other	(31)	(14)
<b>Total long term debt</b>	<b>\$ 11,462</b>	<b>\$ 7,680</b>
Less amount due within one year	420	1,008
<b>Long Term Debt</b>	<b>\$ 11,042</b>	<b>\$ 6,672</b>

**a) Loblaw Companies Limited Notes** During 2014, the Company's \$100 million 6.00% and \$350 million 4.85% MTNs matured and were repaid. In 2013, the Company's \$200 million 5.40% MTN matured and was repaid.

During 2013, the Company issued \$1,600 million aggregate principal amount of senior unsecured notes, consisting of \$800 million of Senior Unsecured Notes, 3.75% Series 2019 due March 12, 2019 and \$800 million of Senior Unsecured Notes, 4.86% Series 2023, due September 12, 2023. The net proceeds from the offering were initially placed in escrow until used in connection with acquisition of Shoppers Drug Mart (see note 5).

**b) Shoppers Drug Mart Notes** In connection with the acquisition of Shoppers Drug Mart, the Company assumed MTNs of \$225 million at 2.01% and \$275 million at 2.36%, maturing in 2016 and 2018, respectively.

**c) Unsecured Term Loan Facility** In connection with the financing of the acquisition of Shoppers Drug Mart, \$3,500 million was obtained through an unsecured term loan facility bearing interest at a rate equal to the Bankers' Acceptance rate plus 1.75% maturing March 28, 2019. The Company incurred \$41 million in financing costs related to the unsecured term loan facility, which were capitalized. On July 23, 2014, the Company reached an agreement to re-price the interest rate on its unsecured term loan facility to reduce the rate from Bankers' Acceptance rate plus 1.75% to Bankers' Acceptance rate plus 1.45%.

During 2014, the Company repaid \$2,271 million of the unsecured term loan facility using net proceeds of \$1,500 million from the sale of Choice Properties Transferor Notes to unrelated parties, \$714 million of existing cash and \$57 million from the proceeds of divested assets required by the Competition Bureau. As at January 3, 2015, the outstanding balance on the unsecured term loan facility was \$1,229 million. The amortization of the financing costs related to the unsecured term loan facility was \$25 million, of which \$23 million was accelerated due to early repayments on the facility.

As required by the unsecured term loan facility agreement, \$478 million, which was the outstanding balance owing on Shoppers Drug Mart's revolving bank credit facility, was repaid and the facility was cancelled upon closing of the acquisition of Shoppers Drug Mart.

**d) Guaranteed Investment Certificates** The following table summarizes PC Bank's Guaranteed Investment Certificates ("GICs") activity, before commissions, for the years ended 2014 and 2013:

(millions of Canadian dollars)	2014	2013
Balance, beginning of year	\$ 430	\$ 303
GICs issued	261	167
GICs matured	(57)	(40)
Balance, end of year	\$ 634	\$ 430

**e) Independent Securitization Trust** The notes issued by *Eagle* are MTNs, which are collateralized by PC Bank's credit card receivables (see note 11). In 2014, the Company has arranged letters of credit on behalf of PC Bank, for the benefit of *Eagle* (see note 33).

In 2013, *Eagle* issued \$400 million of senior and subordinated term notes with a maturity date of October 17, 2018 at a weighted average interest rate of 2.91%, and repaid \$250 million of senior and subordinated term notes which matured on December 17, 2013.

**f) Independent Funding Trusts** As at January 3, 2015, the independent funding trusts had drawn \$498 million (December 28, 2013 – \$475 million) from the revolving committed credit facility that is the source of funding to the independent funding trusts. In 2014, the Company renewed the revolving committed credit facility and extended the maturity date to May 6, 2017, with all other terms and conditions remaining substantially the same. The Company provides credit enhancement in the form of a standby letter of credit for the benefit of the independent funding trusts (see note 33).

**g) Choice Properties** In 2014, Choice Properties Limited Partnership entered into a Master Trust Indenture agreement with Computershare Trust Company of Canada to create supplemental indentures in order to facilitate the replacement of all tranches of Transferor Notes held by Loblaw, with Series 5 to Series 10 notes containing the same principal amounts, interest rates and maturity dates. These replacement notes bear fixed interest rates between 3.00% and 3.60% and mature during 2016 through 2022. The remaining terms and conditions were substantially similar to the original notes. Loblaw subsequently sold the replacement notes to unrelated parties and received net proceeds of \$1,500 million. Loblaw used these proceeds to partially repay the \$3,500 million unsecured term loan facility drawn to fund a portion of the cost to acquire Shoppers Drug Mart (see note 5).

In 2014, Choice Properties issued \$250 million principal amount of Series C senior unsecured debentures with a 7-year term and a coupon rate of 3.50% per annum and \$200 million principal amount of Series D senior unsecured debentures with a 10-year term and a coupon rate of 4.29% per annum, under its Short Form Base Shelf Prospectus. The majority of the proceeds were used to repay \$440 million of Transferor Notes held by Loblaw.

As part of the Choice Properties initial public offering on July 5, 2013, Choice Properties issued \$400 million Series A Debentures with a 5-year term and a coupon of 3.55% per annum due July 5, 2018 and \$200 million Series B Debentures with a 10-year term and a coupon of 4.90% per annum due July 5, 2023.

In 2013, Choice Properties entered into an agreement for a \$500 million, 5 year senior unsecured committed credit facility ("Choice Properties Credit Facility") provided by a syndicate of lenders. In 2014, Choice Properties extended the maturity date of the Choice Properties Credit Facility to July 5, 2019. This facility bears interest at variable rates: Prime plus 0.45% or Banker's Acceptance rate plus 1.45%. The facility contains certain financial covenants (see note 25). As at January 3, 2015, Choice Properties had drawn \$122 million (2013 – nil) under the Choice Properties Credit Facility.

**Committed Credit Facility** In 2014, effective on the closing of the acquisition of Shoppers Drug Mart, the Company's \$800 million committed credit facility ("Credit Facility") was increased to \$1,000 million and the term was extended to December 31, 2018, with all other terms and conditions remaining substantially the same. The Credit Facility contains certain financial covenants (see note 25). As at January 3, 2015 and December 28, 2013, there were no amounts drawn under the Credit Facility.

**Private Placement Notes** During 2013, the Company settled its USD \$300 million U.S. Private Placement ("USPP") notes and related cross currency swaps (see note 30). The Company incurred approximately \$18 million of early-settlement costs related to the settlement of the USPP note due on May 29, 2015, which was recorded in net interest expense and other financing charges.

**Long Term Debt due Within One Year** The following table summarizes long term debt due within one year:

(millions of Canadian dollars)	As at January 3, 2015	As at December 28, 2013
Loblaw Companies Limited Notes	\$ —	\$ 450
Independent Funding Trust	—	475
Independent Securitization Trusts	350	—
Finance Lease Obligations	38	28
Guaranteed Investment Certificates	29	52
Long term debt secured by mortgage	3	3
<b>Total long term debt due within one year</b>	<b>\$ 420</b>	<b>\$ 1,008</b>

**Schedule of Repayments** The schedule of repayment of long term debt, based on maturity is as follows:

(millions of Canadian dollars)	As at January 3, 2015
2015	\$ 420
2016	983
2017	847
2018	1,353
2019	2,588
Thereafter	5,359
<b>Total Long Term Debt (excludes transaction costs)</b>	<b>\$ 11,550</b>

See note 30 for the fair value of long term debt.



**Note 23. Other Liabilities**

(millions of Canadian dollars)	As at January 3, 2015	As at December 28, 2013
Net defined benefit plan obligation (note 27)	\$ 311	\$ 238
Other long term employee benefit obligation	116	107
Equity-based compensation liability (note 26)	7	1
Fair value adjustment to acquired leases	104	—
Deferred lease obligation	77	25
Other	167	183
Other liabilities	\$ 782	\$ 554

**Note 24. Share Capital**

**First Preferred Shares (authorized – 1.0 million shares)** There were no non-voting First Preferred Shares outstanding at year end.

**Second Preferred Shares, Series A (authorized – 12.0 million shares)** The Company has outstanding 9.0 million 5.95% non-voting Second Preferred Shares, Series A, with a face value of \$225 million, which were issued for net proceeds of \$218 million, and entitle the holder to a fixed cumulative preferred cash dividend of \$1.4875 per share per annum which, if declared, will be payable quarterly. These preferred shares which are presented as capital securities on the consolidated balance sheets are classified as other financial liabilities, and measured using the effective interest method.

On and after July 31, 2014 and July 31, 2015 the Company may, at its option, redeem for cash, in whole or in part, these outstanding preferred shares for \$25.50 and \$25.00 respectively. The Company may, at its option, convert these preferred shares into that number of common shares of the Company determined by dividing the then applicable redemption price, together with all accrued and unpaid dividends to but excluding the date of conversion, by the greater of \$2.00 and 95% of the then current market price of the common shares. On and after July 31, 2015, these outstanding preferred shares are convertible, at the option of the holder, into that number of common shares of the Company determined by dividing \$25.00, together with accrued and unpaid dividends to but excluding the date of conversion, by the greater of \$2.00 and 95% of the then current market price of the common shares. This option is subject to the Company's right to redeem the preferred shares for cash or arrange for their sale to substitute purchasers. As at January 3, 2015, the capital securities have been recorded as a current liability.

**Common Shares (authorized – unlimited)** Common shares issued are fully paid and have no par value. The activity in the common shares issued and outstanding during 2014 and 2013 were as follows:

(millions of Canadian dollars except where otherwise indicated)	2014		2013	
	Number of Common Shares	Common Share Capital	Number of Common Shares	Common Share Capital
Issued and outstanding, beginning of year	282,311,573	\$ 1,648	281,680,157	\$ 1,567
Issued for settlement of stock options	3,536,489	156	2,131,416	90
Issued for acquisition of Shoppers Drug Mart (note 5)	119,471,382	5,619	—	—
Issued to controlling shareholder (note 5)	10,515,247	500	—	—
Purchased for cancellation	(3,353,800)	(63)	(1,500,000)	(9)
Issued and outstanding, end of year	412,480,891	\$ 7,860	282,311,573	\$ 1,648
Shares held in trust, beginning of year	(1,067,323)	\$ (6)	—	\$ —
Purchased for future settlement of RSUs and PSUs	—	—	(1,103,500)	(6)
Release for settlement of RSUs and PSUs (note 26)	512,277	3	36,177	—
Shares held in trust, end of year	(555,046)	\$ (3)	(1,067,323)	\$ (6)
Issued and outstanding, net of shares held in trust, end of year	411,925,845	\$ 7,857	281,244,250	\$ 1,642
Weighted average outstanding, net of shares held in trust	380,540,877		281,123,452	

**Dividends** The following table summarizes the Company's cash dividends declared for 2014 and 2013:

	2014 <sup>(i)</sup>	2013
Dividends declared per share (\$):		
Common share	\$ 0.975	\$ 0.940
Second Preferred Share, Series A	1.49	1.49

(i) The fourth quarter dividends of \$0.245 per share declared on common shares were paid on December 30, 2014. The fourth quarter dividends of \$0.37 per share declared on Second Preferred Shares, Series A have a payment date of January 31, 2015.

For financial statement presentation purposes, Second Preferred Shares, Series A dividends of \$14 million for the year ended January 3, 2015 was included as a component of net interest expense and other financing charges in the consolidated statements of earnings (2013 – \$14 million) (see note 6).

Subsequent to the end of the year, the Board declared a quarterly dividend of \$0.245 per common share, payable April 1, 2015, and declared a quarterly dividend of \$0.37 per Second Preferred Share, Series A, payable April 30, 2015.

**Normal Course Issuer Bid** The activity under the Company's Normal Course Issuer Bid ("NCIB") is summarized as follows:

(millions of Canadian dollars except where otherwise indicated)	2014	2013
Shares repurchased under the NCIB for cancellation (number of shares)	3,353,800	1,500,000
Cash consideration paid	\$ 178	\$ 73
Premium charged to Retained Earnings	115	64
Reduction in common shares	63	9
Shares repurchased under the NCIB and held in trusts (number of shares)	—	1,103,500
Cash consideration paid	\$ —	\$ 46
Premium charged to Retained Earnings	—	40
Reduction in common shares	—	6

In 2014, the Company renewed its NCIB to purchase on the TSX or to enter into equity derivatives to purchase up to 20,636,596 of the Company's common shares, representing approximately 5% of the common shares outstanding after taking into account shares issued in connection with the acquisition of Shoppers Drug Mart. In accordance with the rules and by-laws of the TSX, the Company may purchase its common shares from time to time at the then market price of such shares.

## Note 25. Capital Management

In order to manage its capital structure, the Company, among other activities, may adjust the amount of dividends paid to shareholders, purchase shares for cancellation pursuant to its NCIB, issue new shares or issue or repay long term debt with the objective of:

- ensuring sufficient liquidity is available to support its financial obligations and to execute its operating and strategic plans;
- targeting a reduction in debt following the Shoppers Drug Mart transaction to return to credit rating metrics consistent with those of investment grade companies;
- maintaining financial capacity and flexibility through access to capital to support future development of the business;
- minimizing the after-tax cost of its capital while taking into consideration current and future industry, market and economic risks and conditions; and
- utilizing short term funding sources to manage its working capital requirements and long term funding sources to manage the long term capital investments of the business.

The Company has policies in place which govern debt financing plans and risk management strategies for liquidity, interest rates and foreign exchange. These policies outline measures and targets for managing capital, including a range for leverage consistent with the desired credit rating. Management and the Audit Committee regularly review the Company's compliance with, and performance against, these policies. In addition, management regularly reviews these policies to ensure they remain consistent with the risk tolerance acceptable to the Company.

The following table summarizes the Company's total capital under management:

(millions of Canadian dollars)	As at January 3, 2015	As at December 28, 2013
Bank indebtedness	\$ 162	\$ —
Short term debt	605	605
Long term debt due within one year	420	1,008
Long term debt	11,042	6,672
Certain other liabilities	28	39
Total debt	\$ 12,257	\$ 8,324
Capital securities	225	224
Equity attributable to shareholders of the Company	12,779	7,000
Total capital under management	\$ 25,261	\$ 15,548

**Covenants and Regulatory Requirements** The Company is subject to certain key financial and non-financial covenants under its existing Credit Facility, unsecured term loan facility, certain MTNs, and letters of credit. These covenants, which include interest coverage and leverage ratios, as defined in the respective agreements, are measured by the Company on a quarterly basis to ensure compliance with these agreements. As at January 3, 2015 and throughout the year, the Company was in compliance with each of the covenants under these agreements.

Choice Properties has certain key financial and non-financial covenants in its Debentures and the Choice Properties Credit Facility, which include debt service ratios and leverage ratios. These ratios are measured by Choice Properties on a quarterly basis to ensure compliance. As at January 3, 2015 and throughout the year, Choice Properties was in compliance with the covenants under these agreements.

The Company is subject to externally imposed capital requirements from the Office of the Superintendent of Financial Institutions ("OSFI"), the primary regulator of PC Bank. PC Bank's capital management objectives are to maintain a consistently strong capital position while considering the economic risks generated by its credit card receivables portfolio and to meet all regulatory capital requirements as defined by OSFI. PC Bank uses Basel III as its regulatory capital management framework which includes a common equity Tier 1 capital ratio of 4.0%, a Tier 1 capital ratio of 5.5% and a total capital ratio of 8%. In addition to the regulatory capital ratios requirement, prior to January 1, 2015, financial institutions were expected to meet an assets-to-capital multiple test. As at the end of 2014 and 2013, and throughout these years, PC Bank has met all applicable regulatory requirements related to capital ratios and the assets-to-capital multiple test. Effective January 1, 2015, the Basel III Leverage ratio replaced the assets-to-capital multiple test.

In 2014, OFSI released the final Guideline on Liquidity Adequacy Requirements ("LARs"). The LARs guideline establishes standards based on the Basel III framework, including a Liquidity Coverage Ratio ("LCR") standard effective January 1, 2015 and a Net Stable Funding Ratio standard effective January 1, 2018. The LCR standard specifies the level of liquid securities that PC Bank is required to maintain to meet its financial liabilities.

## Note 26. Equity-Based Compensation

The Company's equity-based compensation expense, which includes Loblaw Stock Option, RSU, PSU, DSU, EDSU plans, and the unit-based compensation plans of Choice Properties, was \$73 million for year (2013 – \$35 million). The expense was recognized in operating income.

As a result of the acquisition of Shoppers Drug Mart, all awards that were based on Shoppers Drug Mart shares were converted to awards based on shares of the Company. Accordingly, included in the Company's equity-based compensation expense during 2014 above was \$28 million related to these converted awards, of which \$7 million related to the fair value adjustment of converted awards that initially required settlement in cash.

The carrying amount of the Company's equity-based compensation arrangements including Loblaw Stock Option, RSU, PSU, DSU, EDSU plans, and the unit-based compensation plans of Choice Properties, are recorded on the consolidated balance sheet as follows:

(millions of Canadian dollars)	As at January 3, 2015	As at December 28, 2013
Trade payables and other liabilities	\$ 3	\$ —
Other liabilities	7	1
Contributed surplus	104	87

The following are details related to the equity-based compensation plans of the Company:

**Stock Option Plan** The Company maintains a stock option plan for certain employees. Under this plan, the Company may grant options for up to 28,137,162 common shares which is the Company's guideline for the number of stock option grants.

The following is a summary of the Company's stock option plan activity:

	2014		2013	
	Options (number of shares)	Weighted Average Exercise Price / Share	Options (number of shares)	Weighted Average Exercise Price / Share
Outstanding options, beginning of year	10,995,995	\$ 37.37	12,538,928	\$ 36.74
Granted	1,688,368	47.67	1,484,264	40.62
Converted options	1,026,118	35.26	—	—
Exercised	(3,536,489)	36.47	(2,131,416)	35.25
Forfeited/cancelled	(1,074,427)	40.75	(847,039)	38.03
Expired	(734,681)	45.49	(48,742)	54.71
Outstanding options, end of year	8,364,884	\$ 38.42	10,995,995	\$ 37.37
Options exercisable, end of year	3,195,241	\$ 35.95	4,200,472	\$ 38.04

	2014 Outstanding Options			2014 Exercisable Options	
	Number of Options Outstanding	Weighted Average Remaining Contractual Life (years)	Weighted Average Exercise Price/Share	Number of Exercisable Options	Weighted Average Exercise Price/Share
Range of Exercise Prices					
\$28.95 - \$35.55	3,424,670	4	\$ 34.08	1,553,396	\$ 33.09
\$35.56 - \$39.92	2,414,922	3	\$ 38.14	1,354,570	\$ 37.88
\$39.93 - \$60.29	2,525,292	6	\$ 44.57	287,275	\$ 42.33
	8,364,884		38.42	3,195,241	35.95

During 2014, the Company issued common shares on the exercise of stock options with a weighted average market share price of \$51.20 (2013 – \$46.54). The Company received cash consideration of \$129 million (2013 – \$75 million) related to the exercise of these option.

In connection with the acquisition of Shoppers Drug Mart, the Company converted Shoppers Drug Mart stock options to Loblaw stock options. The fair value of converted Shoppers Drug Mart stock options to Loblaw stock options was \$13 million. The fair value of stock options granted during 2014 was \$13 million (2013 – \$11 million). The assumptions used to measure the fair value of options granted and converted during 2014 and 2013 under the Black-Scholes valuation model at date of grant or conversion were as follows:

	2014	2013
Expected dividend yield	1.8%	2.1%
Expected share price volatility	18.5% – 23.2%	19.2% – 23.8%
Risk-free interest rate	1.1% – 1.9%	1.2% – 2.0%
Expected life of options	1.0 – 6.5 years	4.2 – 6.5 years

Estimated forfeiture rates are incorporated into the measurement of stock option plan expense. The forfeiture rate applied as at January 3, 2015 was 11.0% (December 28, 2013 – 12.0%).

**Restricted Share Unit Plan** The following is a summary of the Company's RSU plan activity:

(Number of Awards)	2014	2013
RSUs, beginning of year	1,084,514	1,038,271
Granted	435,976	379,899
Converted RSUs	542,175	—
Settled	(494,912)	(273,937)
Forfeited	(104,963)	(59,719)
RSUs, end of year	1,462,790	1,084,514

The fair value of RSUs granted during 2014 was \$20 million (2013 – \$15 million).

In connection with the acquisition of Shoppers Drug Mart, the Company converted Shoppers Drug Mart RSUs to Loblaw RSUs, which initially required settlement in cash. On November 10, 2014, the Company amended the plan for the remaining 542,175 converted RSUs to require settlement in shares. The fair value of these converted awards on the amendment date was \$32 million. These converted RSUs will vest on December 1, 2015 and earn Loblaw dividends during the vesting period, which are reinvested as additional RSUs.

During 2014, the Company settled \$2 million of Shoppers Drug Mart converted RSUs in cash prior to amending the RSU plan for converted awards to require settlement in shares on November 10, 2014. During 2013, the Company settled \$10 million of RSUs in cash prior to amending its RSU plan to require settlement in shares.

**Performance Share Unit Plan** The following is a summary of the Company's PSU plan activity:

(Number of Awards)	2014	2013
PSUs, beginning of year	309,110	50,818
Granted	871,355	283,569
Settled	(17,365)	(2,794)
Forfeited	(143,796)	(22,483)
PSUs, end of year	1,019,304	309,110

The fair value of PSUs granted during 2014 was \$39 million (2013 – \$11 million).

**Settlement of Awards from Shares Held in Trust** In 2013, the Company established a trust for each of the RSU and PSU plans to facilitate the purchase of shares for future settlement upon vesting. During 2014, the Company settled RSUs and PSUs totaling 512,277 (2013 – 36,177) through the trusts established for settlement of each of the RSU and PSU plans (see note 24). The settlements resulted in a \$3 million (2013 – nominal) increase to share capital and a \$18 million (2013 – \$1 million) increase to retained earnings.

**Director Deferred Share Unit Plan** The following is a summary of the Company's DSU plan activity:

(Number of Awards)	2014	2013
DSUs outstanding, beginning of year	226,601	198,780
Granted	31,322	24,582
Reinvested	5,901	3,239
DSUs outstanding, end of year	263,824	226,601

The fair value of DSUs granted during 2014 was \$2 million (2013 – \$1 million).

In 2014, in addition to the awards granted under the Company's equity settled DSU plan, the Company converted Shoppers Drug Mart DSUs to Loblaw DSUs. These converted DSUs, which have all vested, will be settled in cash. As at January 3, 2015, the number of converted DSUs outstanding was 101,788.

**Executive Deferred Share Unit Plan** The following is a summary of the Company's EDSU plan activity:

(Number of Awards)	2014	2013
EDSUs outstanding, beginning of year	22,126	26,707
Granted	4,929	2,606
Reinvested	599	421
Settled	(4,739)	(7,608)
EDSUs outstanding, end of year	22,915	22,126

The fair value of EDSUs granted during 2014 was nominal (2013 – nominal).

**Choice Properties** The following are details related to the unit-based compensation plans of Choice Properties:

**Unit Option Plan** Choice Properties maintains a Unit Option plan for certain employees. Under this plan, Choice Properties may grant Options totaling up to 4,075,000 Units. The Unit Options vest in tranches over a period of four years. The following is a summary of Choice Properties' Unit Option plan activity:

	2014		2013	
	Number of awards	Weighted average exercise price/unit	Number of awards	Weighted average exercise price/unit
Outstanding Unit Options, beginning of year	1,196,866	\$ 10.04	—	\$ —
Granted	1,247,247	\$ 10.80	1,196,866	\$ 10.04
Forfeited	(643,294)	\$ 10.35	—	\$ —
Exercised	(118,309)	\$ 10.05	—	\$ —
<b>Outstanding Unit Options, end of year</b>	<b>1,682,510</b>	<b>\$ 10.48</b>	<b>1,196,866</b>	<b>\$ 10.04</b>
Unit Options exercisable, end of year	—	\$ —	—	\$ —



The assumptions used to measure the fair value of the Unit Options under the Black-Scholes model were as follows:

	2014	2013
Expected average distribution yield	6.2%	6.2%
Expected average Unit price volatility	14.2% – 18.9%	19.1% – 30.2%
Average risk-free interest rate	1.0% – 1.4%	1.6% – 2.0%
Expected average life of options	2.5 – 5.4 years	4.0 – 5.5 years

Estimated forfeiture rates are incorporated into the measurement of the Unit Option expense. The forfeiture rate applied as at January 3, 2015 was nil (December 28, 2013 – nil).

**Restricted Unit Plan** The following is a summary of Choice Properties' RU plan activity:

(Number of awards)	2014	2013
Outstanding Restricted Units, beginning of year	108,746	—
Granted	100,523	105,948
Reinvested	10,804	2,798
Forfeited	(35,919)	—
Outstanding Restricted Units, end of year	184,154	108,746

RUs vest over a period of three years. There were no RUs vested as at January 3, 2015 (December 28, 2013 – nil).

**Trustee Deferred Unit Plan** A summary of the DU plan activity is as follows:

(Number of awards)	2014	2013
Outstanding Trustee Deferred Units, beginning of year	31,936	—
Granted	64,150	31,758
Reinvested	3,144	178
Outstanding Trustee Deferred Units, end of year	99,230	31,936

All the DUs vest when issued, however, they cannot be exercised while Trustees are members of the Board.

## Note 27. Post-Employment and Other Long Term Employee Benefits

The Company sponsors a number of pension plans, including registered defined benefit pension plans, registered defined contribution pension plans and supplemental unfunded arrangements providing pension benefits in excess of statutory limits. Certain obligations of the Company under these supplemental pension arrangements are secured by a standby letter of credit issued by a major Canadian chartered bank.

The Company's Pension Committee ("The Committee") oversees the Company's pension plans. The Committee is responsible for assisting the Board in fulfilling its general oversight responsibilities for the plans. The Committee assists the Board with administration of the plans, pension investment and monitoring responsibilities, and compliance with legal and regulatory requirements.

The Company's defined benefit pension plans are primarily funded by the Company, predominantly non-contributory and the benefits are, in general, based on career average earnings subject to limits. The funding is based on a solvency valuation for which the assumptions may differ from the assumptions used for accounting purposes as detailed in this note.

The Company also offers certain other defined benefit plans other than pension plans. These other defined benefit plans are generally not funded, are mainly non-contributory and include health care, life insurance and dental benefits. Employees eligible for these other defined benefits are those who retire at certain ages having met certain service requirements. The majority of other defined benefit plans for current and future retirees include a limit on the total benefits payable by the Company.

The Company's defined benefit pension plans and other defined benefit plans expose it to a number of actuarial risks, such as longevity risk, interest rate risk and market risk.

In Canada, the Company also has a national defined contribution plan for salaried employees. All newly hired salaried employees are only eligible to participate in this defined contribution plan.

The Company also contributes to various multi-employer pension plans, which are administered by independent boards of trustees generally consisting of an equal number of union and employer representatives. The Company's responsibility to make contributions to these plans is limited by amounts established pursuant to its collective agreements.

The Company expects to make contributions in 2015 to its defined benefit and defined contribution plans and the multi-employer pension plans in which it participates as well as benefit payments to the beneficiaries of the supplemental unfunded defined benefit pension plans, other defined benefit plans and other long term employee benefit plans.

### Other Long Term Employee Benefits

The Company offers other long term employee benefit plans that include long term disability benefits and continuation of health care and dental benefits while on disability.

### Defined Benefit Pension Plans and Other Defined Benefit Plans

Information on the Company's defined benefit pension plans and other defined benefit plans, in aggregate, is summarized as follows:

	2014		2013	
	Defined Benefit Pension Plans	Other Defined Benefit Plans	Defined Benefit Pension Plans	Other Defined Benefit Plans
(millions of Canadian dollars)				
Present value of funded obligations	\$ (2,077)	\$ —	\$ (1,597)	\$ —
Present value of unfunded obligations	(81)	(197)	(71)	(167)
Total present value of defined benefit obligation	(2,158)	(197)	(1,668)	(167)
Fair value of plan assets	2,136	—	1,709	—
Total funded status of (obligations) surplus	(22)	(197)	41	(167)
Liability arising from minimum funding requirement for past service	(2)	—	(6)	—
<b>Total net defined benefit plan (obligation) surplus</b>	<b>\$ (24)</b>	<b>\$ (197)</b>	<b>\$ 35</b>	<b>\$ (167)</b>
Recorded on the consolidated balance sheets as follows:				
Other Assets (note 19)	\$ 90	\$ —	\$ 106	\$ —
Other Liabilities (note 23)	\$ (114)	\$ (197)	\$ (71)	\$ (167)

The following are the continuities of the fair value of plan assets and the present value of the defined benefit plan obligations:

	2014			2013		
	Defined Benefit Pension Plans	Other Defined Benefit Plans	Total	Defined Benefit Pension Plans	Other Defined Benefit Plans	Total
(millions of Canadian dollars)						
<b>Changes in the fair value of plan assets</b>						
Fair value, beginning of year	\$ 1,709	\$ —	\$ 1,709	\$ 1,532	\$ —	\$ 1,532
Additions from the acquisition of Shoppers Drug Mart	161	—	161	—	—	—
Employer contributions	55	—	55	99	—	99
Employee contributions	3	—	3	2	—	2
Benefits paid	(83)	—	(83)	(82)	—	(82)
Interest Income	86	—	86	62	—	62
Actuarial gains in other comprehensive (loss) income	210	—	210	101	—	101
Other	(5)	—	(5)	(5)	—	(5)
Fair value, end of year	\$ 2,136	\$ —	\$ 2,136	\$ 1,709	\$ —	\$ 1,709
<b>Changes in the present value of the defined benefit plan obligations</b>						
Balance, beginning of year	\$ 1,668	\$ 167	\$ 1,835	\$ 1,811	\$ 247	\$ 2,058
Additions from the acquisition of Shoppers Drug Mart	173	6	179	—	—	—
Current service cost	51	7	58	52	9	61
Interest cost	86	8	94	72	9	81
Benefits paid	(87)	(6)	(93)	(86)	(6)	(92)
Employee contributions	3	—	3	2	—	2
Actuarial losses (gains) in other comprehensive (loss) income	261	15	276	(159)	(62)	(221)
Plan amendments	—	—	—	(28)	(23)	(51)
Contractual termination benefits <sup>(i)</sup>	1	—	1	2	—	2
Special termination benefits <sup>(i)</sup>	2	—	2	—	—	—
Other	—	—	—	2	(7)	(5)
Balance, end of year	\$ 2,158	\$ 197	\$ 2,355	\$ 1,668	\$ 167	\$ 1,835

(i) Contractual and special termination benefits include \$3 million (2013 – \$2 million) related to the reduction of head office and administrative positions.

For the fiscal year ended 2014, the actual return on plan assets was \$296 million (2013 – \$163 million).

The net defined benefit obligation can be allocated to the plans' participants as follows:

- Active plan participants 46% (2013 – 46%)
- Deferred plan participants 11% (2013 – 12%)
- Retirees 43% (2013 – 42%)

During 2015, the Company expects to contribute approximately \$34 million (2014 – contributed \$55 million) to its registered defined benefit pension plans. The actual amount paid may vary from the estimate based on actuarial valuations being completed, investment performance, volatility in discount rates, regulatory requirements and other factors.

The net cost recognized in net earnings before income taxes for the Company's defined benefit pension plans and other defined benefit plans was as follows:

	2014			2013		
	Defined Benefit Pension Plans	Other Defined Benefit Plans	Total	Defined Benefit Pension Plans	Other Defined Benefit Plans	Total
(millions of Canadian dollars)						
Current service cost	\$ 51	\$ 7	\$ 58	\$ 52	\$ 9	\$ 61
Interest cost on net defined benefit plan obligations	—	8	8	10	9	19
Contractual and special termination benefits <sup>(i)</sup>	3	—	3	2	—	2
Past service cost <sup>(ii)</sup>	—	—	—	(28)	(23)	(51)
Other	5	—	5	7	(3)	4
<b>Net post-employment defined benefit cost</b>	<b>\$ 59</b>	<b>\$ 15</b>	<b>\$ 74</b>	<b>\$ 43</b>	<b>\$ (8)</b>	<b>\$ 35</b>

(i) Includes \$3 million (2013 – \$2 million) of contractual and special termination benefits related to the reduction in head office and administrative positions (see note 21).

(ii) Relates to the announced amendments to certain of the Company's defined benefit plans impacting certain employees retiring after January 1, 2015.

The actuarial losses (gains) recognized in other comprehensive (loss) income net of taxes for defined benefit plans was as follows:

	2014			2013		
	Defined Benefit Pension Plans	Other Defined Benefit Plans	Total	Defined Benefit Pension Plans	Other Defined Benefit Plans	Total
(millions of Canadian dollars)						
Return on plan assets, excluding amounts included in net interest expense and other financing charges	\$ (210)	\$ —	\$ (210)	\$ (101)	\$ —	\$ (101)
Experience adjustments	11	(1)	10	(10)	(51)	(61)
Actuarial losses from change in demographic assumptions	23	3	26	70	4	74
Actuarial losses (gains) from change in financial assumptions	227	13	240	(219)	(15)	(234)
Change in liability arising from minimum funding requirements for past service	(4)	—	(4)	3	—	3
Total net actuarial losses (gains) recognized in other comprehensive (loss) income before income taxes	\$ 47	\$ 15	\$ 62	\$ (257)	\$ (62)	\$ (319)
Income tax (recoveries) expenses on actuarial losses (gains) (note 7)	(12)	(4)	(16)	68	17	85
Actuarial losses (gains) net of income tax recoveries	\$ 35	\$ 11	\$ 46	\$ (189)	\$ (45)	\$ (234)

The cumulative actuarial losses (gains) before income taxes recognized in equity for the Company's defined benefit plans were as follows:

	2014			2013		
	Defined Benefit Pension Plans	Other Defined Benefit Plans	Total	Defined Benefit Pension Plans	Other Defined Benefit Plans	Total
(millions of Canadian dollars)						
Cumulative amount, beginning of year	\$ 123	\$ (31)	\$ 92	\$ 380	\$ 31	\$ 411
Net actuarial losses (gains) recognized in the year before income taxes	47	15	62	(257)	(62)	(319)
Cumulative amount, end of year	\$ 170	\$ (16)	\$ 154	\$ 123	\$ (31)	\$ 92

**Composition of Plan Assets** The defined benefit pension plan assets are held in trust and consisted of the following asset categories:

(millions of Canadian dollars, except where otherwise indicated)	2014		2013	
<b>Equity securities</b>				
Canadian:				
- common	\$ —	—%	\$ 131	8%
- pooled funds	303	14%	178	10%
Foreign:				
- pooled funds	\$ 511	24%	\$ 518	30%
<b>Total Equity Securities</b>	\$ 814	38%	\$ 827	48%
<b>Debt securities</b>				
Fixed income securities:				
- government	\$ 665	31%	\$ 452	27%
- corporate	239	11%	151	9%
Fixed income pooled funds <sup>(i)</sup> :				
- government	314	15%	203	12%
- corporate	19	1%	20	1%
<b>Total Debt Securities</b>	\$ 1,237	58%	\$ 826	49%
<b>Other investments</b>	54	3%	—	—%
<b>Cash and cash equivalents</b>	16	1%	56	3%
<b>Refundable tax on account with CRA</b>	15	—%	—	—%
<b>Total</b>	\$ 2,136	100%	\$ 1,709	100%

(i) Both government and corporate securities may be included within the same fixed income pooled fund.

As at January 3, 2015 and December 28, 2013, the defined benefit pension plans did not directly include any of the Company's securities.

All equity and debt securities and other investments are valued based on quoted prices (unadjusted) in active markets for identical assets or liabilities or based on inputs other than quoted prices in active markets that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).

The Company's asset allocation reflects a balance of interest-rate sensitive investments, such as fixed income investments and equities, which are expected to provide higher returns over the long term. The Company's targeted asset allocations are actively monitored and adjusted on a plan by plan basis to align the asset mix with the liability profiles of the plans.

**Principal Actuarial Assumptions** The principal actuarial assumptions used in calculating the Company's defined benefit plan obligations and net defined benefit plan cost for the year were as follows (expressed as weighted averages):

	2014		2013	
	Defined Benefit Pension Plans	Other Defined Benefit Plans	Defined Benefit Pension Plans	Other Defined Benefit Plans
<b>Defined Benefit Plan Obligations</b>				
Discount rate	4.00%	4.00%	4.75%	4.50%
Rate of compensation increase	3.50%	n/a	3.50%	n/a
Mortality table	CPM-RPP2014 Pub/Priv Generational	CPM-RPP2014 Pub/Priv Generational	CPM-RPP2014 Priv Generational	CPM-RPP2014 Priv Generational
<b>Net Defined Benefit Plan Cost</b>				
Discount rate	4.75%	4.50%	4.00%	4.00%
Rate of compensation increase	3.50%	n/a	3.50%	n/a
Mortality table	CPM-RPP2014 Priv Generational	CPM-RPP2014 Priv Generational	UP94@Fully Generational	UP94@Fully Generational

n/a – not applicable

The weighted average duration of the defined benefit obligation at the end of the reporting period is 15.8 years (2013 – 16.2 years).

The growth rate of health care costs, primarily drug and other medical costs, for the other defined benefit plan obligations as at the end of the year was estimated at 4.50% and is expected to remain at 4.50% at the end of 2015 and thereafter.

**Sensitivity of Key Actuarial Assumptions** The following table outlines the key assumptions for 2014 (expressed as weighted averages) and the sensitivity of a 1% change in each of these assumptions on the defined benefit plan obligations and the net defined benefit plan cost.

The sensitivity analysis provided in the table is hypothetical and should be used with caution. The sensitivities of each key assumption have been calculated independently of any changes in other key assumptions. Actual experience may result in changes in a number of key assumptions simultaneously. Changes in one factor may result in changes in another, which could amplify or reduce the impact of such assumptions.

Increase (Decrease) (millions of Canadian dollars except where otherwise indicated)	2014			
	Defined Benefit Pension Plans		Other Defined Benefit Plans	
	Defined Benefit Plan Obligations	Net Defined Benefit Plan Cost <sup>(i)</sup>	Defined Benefit Plan Obligations	Net Defined Benefit Plan Cost <sup>(i)</sup>
Discount rate	4.00%	4.75%	4.00%	4.50%
Impact of:				
1% increase	\$ (316)	\$ (29)	\$ (24)	\$ —
1% decrease	\$ 371	\$ 29	\$ 31	\$ 1
Expected growth rate of health care costs			4.50%	4.00%
Impact of:				
1% increase	n/a	n/a	\$ 25	\$ 2
1% decrease	n/a	n/a	\$ (20)	\$ (2)

n/a – not applicable

(i) Discount rate and expected growth rate of health care costs sensitivity is for current service and interest costs only.



**Multi-Employer Pension Plans**

During 2014, the Company recognized an expense of \$55 million (2013 – \$55 million) in operating income, which represents the contributions made in connection with multi-employer pension plans. During 2015, the Company expects to continue to make contributions into these multi-employer pension plans.

The Company, together with its independent franchises, is the largest participating employer in the Canadian Commercial Workers Industry Pension Plan ("CCWIPP"), with approximately 52,000 (2013 – 53,000) employees as members. Included in the 2014 expense described above are contributions of \$54 million (2013 – \$54 million) to CCWIPP.

**Post-Employment and Other Long Term Employee Benefit Costs**

The net cost recognized in net earnings before income taxes for the Company's post-employment and other long term employee benefit plans was as follows:

(millions of Canadian dollars)	2014	2013
Net post-employment defined benefit cost	\$ 74	\$ 35
Defined contribution costs <sup>(i)</sup>	20	20
Multi-employer pension plan costs <sup>(ii)</sup>	55	55
Total net post-employment benefit costs	\$ 149	\$ 110
Other long term employee benefit costs <sup>(iii)</sup>	28	21
Net post-employment and other long term employee benefit costs	\$ 177	\$ 131
Recorded on the consolidated statements of earnings as follows:		
Selling, general and administrative expenses	\$ 165	\$ 108
Net interest expense and other financing charges	12	23
Net post-employment and other long term employee benefit costs	\$ 177	\$ 131

(i) Amounts represent the Company's contributions made in connection with defined contribution plans.

(ii) Amounts represent the Company's contributions made in connection with multi-employer pension plans.

(iii) Other long term employee benefit costs include \$4 million (2013 – \$4 million) of net interest expense and other financing charges.

**Note 28. Employee Costs**

Included in operating income are the following employee costs:

(millions of Canadian dollars)	2014	2013
Wages, salaries and other short term employment benefits	\$ 4,494	\$ 3,042
Post-employment benefits	141	91
Other long term employee benefits	24	17
Equity-based compensation	71	32
Capitalized to fixed assets	(30)	(10)
Total employee costs	\$ 4,700	\$ 3,172

## Note 29. Leases

The Company leases certain of its retail stores, distribution centres, corporate offices, and other assets under operating or finance lease arrangements. Substantially all of the retail store leases have renewal options for additional terms. The contingent rents under certain of the retail store leases are based on a percentage of Retail segment sales. The Company also has properties which are sub-leased to third parties.

Determining whether a lease arrangement is classified as finance or operating requires judgment with respect to the fair value of the leased asset, the economic life of the lease, the discount rate and the allocation of leasehold interests between the land and building elements of property leases.

**Operating Leases – As Lessee** Future minimum lease payments relating to the Company's operating leases are as follows:

(millions of Canadian dollars)	Payments due by year						As at	As at
	2015	2016	2017	2018	2019	Thereafter	January 3, 2015 Total	December 28, 2013 Total
Operating lease payments	\$ 674	\$ 654	\$ 620	\$ 573	\$ 529	\$ 2,818	\$ 5,868	\$ 1,224
Sub-lease income	(60)	(51)	(40)	(33)	(23)	(88)	(295)	(166)
Net operating lease payments	\$ 614	\$ 603	\$ 580	\$ 540	\$ 506	\$ 2,730	\$ 5,573	\$ 1,058

During 2014, the Company recorded \$572 million (2013 – \$206 million) as an expense included in operating income in respect of operating leases. During that period, contingent rent recognized as an expense in respect of operating leases totaled \$1 million (2013 – \$1 million), while sub-lease income earned totaled \$58 million (2013 – \$50 million) which is recognized in operating income. During 2014, contingent rent recognized as income in respect of sub-leased operating leases was \$3 million (2013 – \$1 million).

**Operating Leases – As Lessor** As at January 3, 2015, the Company leased certain owned land and buildings with a cost of \$2,578 million (December 28, 2013 – \$2,076 million) and related accumulated depreciation of \$718 million (December 28, 2013 – \$562 million). For the year ended January 3, 2015, rental income was \$148 million (2013 – \$136 million) and contingent rent was \$3 million (2013 – \$2 million), both of which were recognized in operating income.

(millions of Canadian dollars)	Payments to be received by year						As at	As at
	2015	2016	2017	2018	2019	Thereafter	January 3, 2015 Total	December 28, 2013 Total
Net operating lease income	\$ 137	\$ 116	\$ 93	\$ 76	\$ 55	\$ 170	\$ 647	\$ 559

**Finance Leases – As Lessee** Future minimum lease payments relating to the Company's finance leases are as follows:

(millions of Canadian dollars)	Payments due by year						As at	As at
	2015	2016	2017	2018	2019	Thereafter	January 3, 2015 Total	December 28, 2013 Total
Finance lease payments	\$ 85	\$ 88	\$ 78	\$ 65	\$ 60	\$ 715	\$ 1,091	\$ 771
Less future finance charges	(47)	(43)	(46)	(36)	(32)	(287)	(491)	(383)
Present value of minimum lease payments	\$ 38	\$ 45	\$ 32	\$ 29	\$ 28	\$ 428	\$ 600	\$ 388

During 2014, contingent rent recognized by the Company as an expense in respect of finance leases was \$1 million (2013 – \$1 million).

Future sub-lease income relating to the Company's sub-lease agreements are as follows:

(millions of Canadian dollars)	Payments to be received by year						As at	As at
	2015	2016	2017	2018	2019	Thereafter	January 3, 2015 Total	December 28, 2013 Total
Sub-lease income	\$ 16	\$ 12	\$ 11	\$ 9	\$ 8	\$ 33	\$ 89	\$ 45

At January 3, 2015, the sub-lease payments receivable under finance leases was \$16 million (December 28, 2013 – \$14 million).

### Note 30. Financial Instruments

The following table presents the fair value hierarchy of financial assets and financial liabilities, excluding those classified as amortized cost that are short term in nature:

(millions of Canadian dollars)	As at January 3, 2015				As at December 28, 2013			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
<b>Financial assets:</b>								
Cash and cash equivalents	\$ 984	\$ 15	\$ —	\$ 999	\$ 2,247	\$ 13	\$ —	\$ 2,260
Short term investments	19	2	—	21	290	—	—	290
Security deposits	7	—	—	7	1,701	—	—	1,701
Franchise loans receivable	—	—	399	399	—	—	375	375
Certain other assets	—	8	64	72	—	8	59	67
Derivatives included in prepaid expenses and other assets	—	10	—	10	—	2	—	2
<b>Financial liabilities:</b>								
Derivatives included in trade payables and other liabilities	—	11	4	15	—	—	4	4
Trust unit liability	722	—	—	722	688	—	—	688
Long term debt	—	12,508	—	12,508	—	8,188	—	8,188
Capital securities <sup>(i)</sup>	234	—	—	234	236	—	—	236
Certain other liabilities	—	—	28	28	—	—	40	40

(i) As at January 3, 2015, capital securities were classified as current liabilities.

The carrying value of the Company's financial instruments approximates its fair value except for long term debt and capital securities.

There were no transfers between levels of the fair value hierarchy.

The level 3 financial instruments classified as fair value through profit or loss as at January 3, 2015, and December 28, 2013 consist of embedded derivatives on purchase orders placed in neither Canadian dollars, nor the functional currency of the vendor. These derivatives are valued using a market approach based on the differential in exchange rates and timing of settlement. The significant unobservable input used in the fair value measurement is the cost of purchase orders. Significant increases (decreases) in any of the inputs would result in a significantly higher (lower) fair value measurement.

The fair value of the embedded foreign currency derivatives classified as Level 3 included in trade payables and other liabilities as at January 3, 2015 was \$4 million (December 28, 2013 – \$4 million). During 2014, a nominal loss (2013 – \$3 million) was recorded in operating income. As at January 3, 2015, a 1% increase (decrease) in foreign currency exchange rates would result in a \$1 million gain (loss) in fair value.

During 2014, the Company recognized a gain of \$11 million (2013 – \$33 million) in earnings before incomes taxes on financial instruments designated as fair value through profit or loss. In addition, during 2014 a loss of \$18 million (2013 – \$27 million) was recorded in earnings before income taxes related to financial instruments required to be classified as fair value through profit or loss.

During 2014, net interest expense of \$571 million (2013 – \$446 million) was recorded related to financial instruments not classified or designated as fair value through profit or loss.

The following is a discussion of the Company's derivative instruments:

**Cross Currency Swaps** In 2013, Glenhuron Bank Limited ("Glenhuron") unwound its cross currency swaps and received a net cash settlement of \$76 million, representing the cumulative fair value gain on the swaps. The swaps were offset by the effect of translation gains and losses relating to USD cash and cash equivalents, short term investments and security deposits.

In 2013, the Company settled its USD \$300 million USPP cross currency swaps in conjunction with the settlement of the underlying USD \$300 million USPP notes, and received a net cash settlement of \$18 million (see note 22). The USPP cross currency swaps were used to manage the effect of translation (gains) losses on the underlying USD USPP notes in long term debt. As part of the full settlement, the Company settled its USD \$150 million USPP cross currency swap, which matured on May 29, 2013. On settlement of the swap, an unrealized fair value gain of \$5 million, net of tax of \$2 million, which had been deferred in accumulated other comprehensive income was realized in operating income.

The following table summarizes the 2013 impact to operating income resulting from changes in the fair value of the cross currency swaps and the underlying exposures:

(millions of Canadian dollars)	<u>Glenhuron</u> <u>Cross Currency</u> <u>Swaps</u> 2013	<u>USPP</u> <u>Cross Currency</u> <u>Swaps</u> 2013
Fair value loss (gain) related to swaps <sup>(i)</sup>	\$ 37	\$ (11)
Translation (gain) loss related to the underlying exposures	(33)	14

(i) The impact to USPP cross currency swaps excludes the \$7 million gain on derecognized derivative instruments, before income taxes, reclassified from accumulated other comprehensive income.

**Interest Rate Swaps** During 2013, the Company settled its notional \$150 million in interest rate swaps and recognized a \$5 million fair value gain in operating income related to these swaps.

**Other Derivatives** The Company also maintains other financial derivatives including foreign exchange forwards, electricity forwards and fuel exchange traded futures and options. During 2014, the Company recognized a \$1 million loss (2013 – \$7 million gain) in operating income related to these derivatives. The following table summarizes the cumulative unrealized impact of these derivatives included in the consolidated balance sheet:

(millions of Canadian dollars)	2014	2013
Cumulative unrealized gains recorded in prepaid expenses and other assets	\$ 10	\$ 2
Cumulative unrealized losses recorded in trade payables and other liabilities	11	—

In connection with the issuance of \$1,600 million of senior unsecured notes in 2013 (see note 22), the Company hedged its exposure to interest rates in advance of the issuance. As this relationship did not qualify for hedge accounting, the resulting \$10 million gain on settlement was recorded in operating income.

**Trust Unit Liability** As at January 3, 2015, the fair value of the Trust Unit Liability of \$722 million (December 28, 2013 – \$688 million) was recorded on the consolidated balance sheet. In 2014, the Company recorded a fair value loss of \$17 million (2013 – \$27 million), in net interest expense and other financing charges related to Choice Properties' Units.

As at January 3, 2015, 67,755,010 Choice Properties Units were held by unitholders other than the Company (December 28, 2013 – 66,114,229). During 2014, Choice Properties issued 1,640,781 Units (2013 – 114,229), to eligible unitholders under its distribution reinvestment plan. Units held by unitholders other than the Company are presented as a liability on the Company's consolidated balance sheet as the Units are redeemable for cash at the option of the holder, subject to certain restrictions. As at January 3, 2015, the Company held an 82.9% (December 28, 2013 – 82.2%) ownership interest in Choice Properties.

**Franchise Loans Receivable and Franchise Investments in Other Assets** The value of Loblaw franchise loans receivable of \$399 million (December 28, 2013 – \$375 million) was recorded on the consolidated balance sheets. In 2014, the Company recorded an impairment loss of \$12 million (2013 – \$14 million) in operating income related to these loans receivable.

The value of Loblaw franchise investments of \$62 million (December 28, 2013 – \$58 million) was recorded in other assets. In 2014, the Company recorded a \$3 million loss (2013 – \$6 million) in operating income related to these investments.

**Note 31. Financial Risk Management**

As a result of holding and issuing financial instruments, the Company is exposed to liquidity and capital availability risk, credit risk and market risk. The following is a description of those risks and how the exposures are managed:

**Level of Indebtedness** To fund the cash portion of the Shoppers Drug Mart acquisition, the Company utilized excess cash and significantly increased its indebtedness. Although the Company has made progress in reducing its indebtedness subsequent to the acquisition of Shoppers Drug Mart, there can be no assurance that the Company will generate sufficient free cash flow to significantly further reduce indebtedness and maintain adequate cash reserves. A failure to achieve these objectives could adversely affect the Company's credit ratings and its cost of funding.

If the Company, PC Bank or Choice Properties' financial performance and condition deteriorate or downgrades in the Company's or Choice Properties' current credit ratings occur, their ability to obtain funding from external sources could be restricted, which could adversely affect the financial performance of the Company.

**Liquidity** Liquidity risk is the risk that the Company is unable to generate or obtain sufficient cash or its equivalents in a cost effective manner to fund its obligations as they come due. The Company is exposed to liquidity risk through, among other areas, PC Bank and its credit card business, which requires a reliable source of funding for its credit card business. PC Bank relies on its securitization programs and the acceptance of GIC deposits to fund the receivables of its credit cards. The Company would experience liquidity risks if it fails to maintain appropriate levels of cash and short term investments, it is unable to access sources of funding or it fails to appropriately diversify sources of funding. If any of these events were to occur, they would adversely affect the financial performance of the Company.

Liquidity risk is mitigated by maintaining appropriate levels of cash and cash equivalents and short term investments, actively monitoring market conditions, and by diversifying sources of funding, including the Company's committed credit facility, and maintaining a well-diversified maturity profile of debt and capital obligations.

The following are the undiscounted contractual maturities of significant financial liabilities as at January 3, 2015:

	2015	2016	2017	2018	2019	Thereafter	Total <sup>(i)</sup>
<b>Derivative Financial Liabilities</b>							
Foreign exchange forward contracts	\$ 232	\$ —	\$ —	\$ —	\$ —	\$ —	\$ 232
<b>Non-Derivative Financial Liabilities</b>							
Short term debt <sup>(ii)</sup>	605	—	—	—	—	—	605
Bank Indebtedness	162	—	—	—	—	—	162
Long term debt including interest payments <sup>(iii)</sup>	911	1,445	1,278	1,767	2,920	8,263	16,584
Other liabilities <sup>(iv)</sup>	4	8	5	3	2	6	28
	\$ 1,914	\$ 1,453	\$ 1,283	\$ 1,770	\$ 2,922	\$ 8,269	\$ 17,611

(i) Capital securities and their related dividends, and the Trust Unit Liability have been excluded as these liabilities do not have a contractual maturity date. The Company also excluded trade payables and other liabilities, which are due within the next 12 months.

(ii) These are obligations owed to independent securitization trusts which are collateralized by the Company's credit card receivables (see note 11).

(iii) Fixed interest payments are based on the maturing face values and annual interest for each instrument, including GICs, long term independent securitization trusts and an independent funding trust, as well as annual payment obligations for structured entities, mortgages and finance lease obligations. Variable interest payments are based on the forward rates as of January 3, 2015.

(iv) Contractual obligation related to certain other liabilities.

**Choice Properties' Capital Availability** The real estate industry is highly capital intensive. Choice Properties requires access to capital to maintain its properties, refinance its indebtedness as well as to fund its growth strategy and certain capital investments from time to time. Although Choice Properties expects to have access to its credit facility, there can be no assurance that it will otherwise have sufficient capital or access to capital on acceptable terms for future property acquisitions, refinancing indebtedness, financing or refinancing properties, funding operating expenses or for other purposes. Further, in certain circumstances, Choice Properties may not be able to borrow funds due to certain limitations. Failure by Choice Properties to access required capital could have a material adverse effect on the Company's ability to pay its financial or other obligations. An inability to access capital could also impact Choice Properties' ability to make distributions which could have a material adverse effect on the trading price of Units which would adversely affect the financial performance of the Company.

**Credit** The Company is exposed to credit risk resulting from the possibility that counterparties could default on their financial obligations to the Company. Exposure to credit risk relates to derivative instruments, cash and cash equivalents, short term investments, security deposits, PC Bank's credit card receivables, franchise loans receivable, pension assets held in the Company's defined benefit plans and accounts receivable, including amounts due from independent franchisees, government, prescription sales and third-party drug plans, independent accounts and amounts owed from vendors. Failure to manage credit risk could adversely affect the financial performance of the Company.

The risk related to derivative instruments, cash and cash equivalents, short term investments and security deposits is reduced by policies and guidelines that require that the Company enters into transactions only with counterparties or issuers that have a minimum long term "A-" credit rating from a recognized credit rating agency and place minimum and maximum limits for exposures to specific counterparties and instruments.

Choice Properties mitigates the risk of credit loss relating to rent receivables by evaluating the creditworthiness of new tenants, obtaining security deposits wherever permitted by legislation, ensuring its tenant mix is diversified and by limiting its exposure to any one tenant except Loblaw. Choice Properties establishes an allowance for doubtful accounts that represents the estimated losses with respect to rents receivable. The allowance is determined on a tenant-by-tenant basis based on the specific factors related to the tenant.

PC Bank manages its credit card receivable risk by employing stringent credit scoring techniques, actively monitoring the credit card portfolio and reviewing techniques and technology that can improve the effectiveness of the collection process. In addition, these receivables are dispersed among a large, diversified group of credit card customers.

Franchise loans receivable and accounts receivable, including amounts due from independent franchisees, governments, prescription sales covered by third-party drug plans, independent accounts and amounts owed from vendors, are actively monitored on an ongoing basis and settled on a frequent basis in accordance with the terms specified in the applicable agreements.

**Market Risk** Market risk is the loss that may arise from changes in factors such as interest rates, foreign currency exchange rates, commodity prices, common share and Unit price and the impact these factors may have on other counterparties.

**Interest Rates** The Company is exposed to interest rate risk from fluctuations in interest rates on its floating rate debt and financial instruments, net of cash and cash equivalents, short term investments and security deposits. The Company manages interest rate risk by monitoring the respective mix of fixed and floating rate debt, net of cash and cash equivalents, short term investments and security deposits, and by taking action as necessary to maintain an appropriate balance considering current market conditions. The Company estimates that a 1% increase (decrease) in short term interest rates, with all other variables held constant, would result in a increase (decrease) of \$16 million to net interest expense and other financing charges.

**Foreign Currency Exchange Rates** The Company is exposed to foreign currency exchange rate variability, primarily on its USD denominated based purchases in trade payables and other liabilities. A depreciating Canadian dollar relative to the USD will have a negative impact on year-over-year changes in reported operating income and net earnings, while an appreciating Canadian dollar relative to the USD will have the opposite impact.

**Commodity Prices** The Company is exposed to increases in the prices of commodities in operating its stores and distribution networks, as well as to the indirect effect of changing commodity prices on the price of consumer products. To manage a portion of this exposure, the Company uses purchase commitments for a portion of its need for certain consumer products that are commodities based. The Company enters into exchange traded futures contracts and forward contracts to minimize cost volatility related to energy. Rising commodity prices could adversely affect the financial performance of the Company. The Company estimates that based on the outstanding derivative contracts held by the Company as at January 3, 2015, a 10% decrease in relevant energy prices, with all other variables held constant, would result in a net loss of \$3 million on earnings before income taxes.

**Choice Properties Unit Price** The Company is exposed to market price risk as a result of Choice Properties' Units that are held by unitholders other than the Company. These Units are presented as a liability on the Company's consolidated balance sheets as they are redeemable for cash at the option of the holder. The liability is recorded at fair value at each reporting period based on the market price of Units. The change in the fair value of the liability negatively impacts net earnings when the Unit price increases and positively impacts net earnings when the Unit price declines. A one dollar increase in the market value of Units, with all other variables held constant, would result in \$68 million increase to net interest expense and other financing charges.



### Note 32. Contingent Liabilities

The Company is involved in and potentially subject to various claims by third parties arising out of the normal course and conduct of its business including product liability, labour and employment, regulatory and environmental claims. In addition, the Company is involved in and potentially subject to regular audits from federal and provincial tax authorities relating to income, capital, commodity, property and other taxes and as a result of these audits may receive assessments and reassessments. Although such matters cannot be predicted with certainty, management currently considers the Company's exposure to such claims and litigation, tax assessments and reassessments, to the extent not covered by the Company's insurance policies or otherwise provided for, not to be material to the consolidated financial statements, but may have a material impact in future periods.

**Legal Proceedings** The Company is the subject of various legal proceedings and claims that arise in the ordinary course of business. The outcome of all of these proceedings and claims is uncertain. However, based on information currently available, these proceedings and claims, individually and in the aggregate, are not expected to have a material impact on the Company.

Shoppers Drug Mart has been served with an Amended Statement of Claim in a proposed class action proceeding that has been filed under the Ontario Superior Court of Justice by two licensed Associates, claiming various declarations and damages resulting from Shoppers Drug Mart's alleged breaches of the Associate Agreement, in the amount of \$500 million. The proposed class action comprises all of Shoppers Drug Mart's current and former licensed Associates residing in Canada, other than in Québec, who are parties to Shoppers Drug Mart's 2002 and 2010 forms of the Associate Agreement. On July 9, 2013, the Ontario Superior Court of Justice certified as a class proceeding portions of the action. While Shoppers Drug Mart continues to believe that the claim is without merit and will vigorously defend the claim, the outcome of this matter cannot be predicted with certainty.

**Tax** The Company is subject to tax audits from various government and regulatory agencies on an ongoing basis. As a result, from time to time, taxing authorities may disagree with the positions and conclusions taken by the Company in its tax filings or legislation could be amended or interpretations of current legislation could change, any of which events could lead to reassessments. These reassessments could have a material impact on the Company in future periods.

In 2012, the Company received indication from the Canada Revenue Agency (the "CRA") that the CRA intends to proceed with reassessments of the tax treatment of the Company's wholly owned subsidiary, Glenhuron. The CRA's position is that certain income earned by Glenhuron in Barbados in respect of the 2000 to 2010 taxation years should be treated, and taxed, as income in Canada.

Based on the proposal letter from the CRA, if the CRA and the relevant provincial tax authorities were to prevail in all of these reassessments, which the Company believes would be unlikely, the estimated total tax and interest for the 2000 to 2010 taxation years would be approximately \$440 million, which would increase as interest accrues. However, the Company is in discussions with the CRA about the amount of taxes in dispute. The Company believes it is likely that the CRA and the relevant provincial tax authorities will issue reassessments for 2011 to 2013 on the same or similar basis. No amount for any reassessments has been provided for in the Company's consolidated financial statements.

Subsequent to the end of 2014, the Company received a letter from the CRA stating that the CRA will be proceeding with the reassessments. The Company expects to receive reassessments from the CRA and the relevant provincial tax authorities sometime in the coming months. The Company strongly disagrees with the CRA's position and intends to vigorously defend its position including appealing the reassessments as and when they are received. The Company will make cash payments or provide other forms of security on a portion of the taxes in dispute. If the Company is successful in defending its position, in whole or in part, some or all of the cash payments or security would be returned to the Company.

**Indemnification Provisions** The Company from time to time enters into agreements in the normal course of its business, such as service and outsourcing arrangements and leases, in connection with business or asset acquisitions or dispositions. These agreements by their nature may provide for indemnification of counterparties. These indemnification provisions may be in connection with breaches of representation and warranty or with future claims for certain liabilities, including liabilities related to tax and environmental matters. The terms of these indemnification provisions vary in duration and may extend for an unlimited period of time. Given the nature of such indemnification provisions, the Company is unable to reasonably estimate its total maximum potential liability as certain indemnification provisions do not provide for a maximum potential amount and the amounts are dependent on the outcome of future contingent events, the nature and likelihood of which cannot be determined at this time. Historically, the Company has not made any significant payments in connection with these indemnification provisions.

### Note 33. Financial Guarantees

The Company established letters of credit used in connection with certain obligations mainly related to real estate transactions, benefit programs, purchase orders and performance guarantees with a gross potential liability of approximately \$293 million (December 28, 2013 – \$348 million). In addition, the Company has provided to third parties the following significant guarantees:

**Associate Guarantees** The Company has arranged for its Shoppers Drug Mart Associates to obtain financing to facilitate their inventory purchases and fund their working capital requirements by providing guarantees to various Canadian chartered banks that support Associate loans. As at January 3, 2015, the Company's maximum obligation in respect of such guarantees was \$570 million with an aggregate amount of \$476 million in available lines of credit allocated to the Associates by the various banks. As at January 3, 2015, Associates had drawn an aggregate amount of \$162 million against these available lines of credit. Any amounts drawn by the Associates are included in bank indebtedness on the Company's consolidated balance sheet. As recourse in the event that any payments are made under the guarantees, the Company holds a first-ranking security interest on all assets of Associates, subject to certain prior-ranking statutory claims.

**Independent Funding Trusts** The full balance relating to the debt of the independent funding trusts has been consolidated on the balance sheet of the Company (see note 22). As at January 3, 2015 the Company has agreed to provide a credit enhancement of \$50 million (December 28, 2013 – \$48 million) in the form of a standby letter of credit for the benefit of the independent funding trusts representing not less than 10% (2013 – 10%) of the principal amount of loans outstanding. This credit enhancement allows the independent funding trusts to provide financing to the Company's independent franchisees. As well, each independent franchisee provides security to the independent funding trusts for its obligations by way of a general security agreement. In the event that an independent franchisee defaults on its loan and the Company has not, within a specified time period, assumed the loan, or the default is not otherwise remedied, the independent funding trusts would assign the loan to the Company and draw upon this standby letter of credit. This standby letter of credit has never been drawn upon. The Company has agreed to reimburse the issuing bank for any amount drawn on the standby letter of credit.

**Lease Obligations** In connection with historical dispositions of certain of its assets, the Company has assigned leases to third parties. The Company remains contingently liable for these lease obligations in the event any of the assignees are in default of their lease obligations. The minimum rent, which does not include other lease related expenses such as property tax and common area maintenance charges, is in aggregate, approximately \$17 million (December 28, 2013 – \$14 million). Additionally, the Company has guaranteed lease obligations of a third party distributor in the amount of \$13 million (December 28, 2013 – \$17 million).

**Financial Services** The Company has provided a guarantee on behalf of PC Bank to MasterCard® International Incorporated ("MasterCard®") for accepting PC Bank as a card member and licensee of MasterCard®. As at January 3, 2015, the guarantee on behalf of PC Bank to MasterCard® was USD \$170 million (December 28, 2013 – USD \$170 million).

In 2014, the Company arranged for an irrevocable standby letter of credit from a major Canadian chartered bank on behalf of one of its wholly-owned subsidiaries in the amount of \$91 million.

Letters of credit for the benefit of independent securitization trusts with respect to the securitization programs of PC Bank have been issued by major financial institutions. These standby letters of credit can 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. The Company has agreed to reimburse the issuing banks for any amount drawn on the standby letters of credit. As at January 3, 2015, the aggregate gross potential liability under these arrangements for the Other Independent Securitization Trusts was \$61 million (December 28, 2013 – \$54 million), which represented 10% (2013 – 9%) of the securitized credit card receivables amount (see note 20). As at January 3, 2015, the aggregate gross potential liability under these arrangements for *Eagle* was \$68 million (December 28, 2013 – nil), which represented 9% (2013 – nil) of the *Eagle* notes outstanding (see note 22).

**Choice Properties** issues letters of credit to support performance guarantees related to its investment properties including maintenance and development obligations to municipal authorities. As at January 3, 2015, the aggregate gross potential liability related to these letters of credit totaled \$23 million (December 28, 2013 – \$20 million).

The Choice Properties Credit Facility and Choice Properties debentures are guaranteed by each of the General Partner, the Partnership and any other person that becomes a subsidiary of Choice Properties (with some exceptions). In the case of default by Choice Properties, the Indenture Trustee will be entitled to seek redress from the Guarantors for the guaranteed obligations in the same manner and upon the same terms that it may seek to enforce the obligations of Choice Properties. These guarantees are intended to eliminate structural subordination, which would otherwise arise as a consequence of Choice Properties' assets being primarily held in its various subsidiaries.

**Note 34. Related Party Transactions**

The Company's controlling shareholder is Weston, which owns, directly and indirectly, 187,815,136 of the Company's common shares, representing approximately 46% of the Company's outstanding common shares. Mr. W. Galen Weston controls Weston, directly and indirectly through private companies which he controls, including Wittington who owns a total of 80,746,099 of Weston's common shares, representing approximately 63% of Weston's outstanding common shares. Mr. Weston also beneficially owns 5,096,189 of the Company's common shares, representing approximately 1% of the Company's outstanding common shares. The Company's policy is to conduct all transactions and settle all balances with related parties on market terms and conditions.

## Transactions with Related Parties

(millions of Canadian dollars)	Transaction Value	
	2014	2013
<b>Included in Cost of Merchandise Inventories Sold</b>		
Inventory purchases from a subsidiary of Weston	\$ 615	\$ 601
Inventory purchases from a related party <sup>(i)</sup>	24	22
<b>Operating Income</b>		
Cost sharing agreements with Parent <sup>(ii)</sup>	\$ 20	\$ 9
Net administrative services provided by Parent <sup>(iii)</sup>	18	13
Choice Properties distributions to Parent <sup>(iv)</sup>	14	6
Lease of office space from a subsidiary of Wittington	3	3

- (i) Associated British Foods plc is a related party by virtue of Mr. W. Galen Weston being a director of such entity's parent company. Total balance outstanding owing to Associated British Foods plc as at January 3, 2015 was \$3 million (December 28, 2013 – \$4 million).
- (ii) Weston and the Company have each entered into certain contracts with third parties for administrative and corporate services, including telecommunication services and IT related matters on behalf of itself and the related party. Through cost sharing agreements that have been established between the Company and Weston concerning these costs, the Company has agreed to be responsible to Weston for the Company's proportionate share of the total costs incurred.
- (iii) The Company and Weston have entered into an agreement whereby certain administrative services are provided by one party to the other. The services to be provided under this agreement include those related to commodity management, pension and benefits, tax, medical, travel, information system, risk management, treasury and legal. Payments are made quarterly based on the actual costs of providing these services. Where services are provided on a joint basis for the benefit of the Company and Weston together, each party pays the appropriate proportion of the costs. Fees paid under this agreement are reviewed each year by the Audit Committee.
- (iv) Weston is a unitholder of Choice Properties and is entitled to receive distributions declared by the trust. Unitholders who elect to participate in the Choice Properties Distribution Reinvestment Plan ("DRIP") receive a further distribution, payable in Units, equal in value to 3% of each cash distribution. In 2014, Choice Properties issued 1,306,847 Units (2013 – 107,810 Units) to Weston under its DRIP at a weighted average price of \$10.30 (2013 – \$10.05) per Unit.

The net balances due to Weston are comprised as follows:

(millions of Canadian dollars)	As at January 3, 2015	As at December 28, 2013
Trade payables and other liabilities	\$ 7	\$ 27

**Joint Venture** In 2014, a joint venture, formed between Choice Properties and Wittington, completed the acquisition of property from Loblaw. The joint venture intends to develop the acquired site into a mixed-used property, anchored by a Loblaw food store. As at January 3, 2015, the joint venture did not have any operating activity. Choice Properties uses the equity method of accounting to record its 40% interest in the joint venture, which is included in other assets (see note 19).

**Post-Employment Benefit Plans** The Company sponsors a number of post-employment plans, which are related parties. Contributions made by the Company to these plans are disclosed in note 27.

**Income Tax Matters** From time to time, the Company, Weston and its affiliates may enter into agreements to make elections that are permitted or required under applicable income tax legislation with respect to affiliated corporations. In 2014, these elections and accompanying agreements did not have a material impact on the Company.

**Key Management Personnel** The Company's key management personnel are comprised of the Board and certain members of the executive team of the Company, as well as both the Board and certain members of the executive team of Weston and Wittington to the extent that they have the authority and responsibility for planning, directing and controlling the day-to-day activities of the Company.

**Compensation of Key Management Personnel** Annual compensation of key management personnel that is directly attributable to the Company was as follows:

(millions of Canadian dollars)	2014	2013
Salaries, director fees and other short term employee benefits	\$ 9	\$ 8
Equity-based compensation	3	6
Total compensation	\$ 12	\$ 14

**Note 35. Segment Information**

The Company has three reportable operating segments with all material operations carried out in Canada:

- The Retail segment consists primarily of retail food and Associate-owned drug stores, and also includes in-store pharmacies and other health and beauty products, gas bars and apparel and other general merchandise. This segment is comprised of several operating segments, which have been aggregated primarily due to similarities in the nature of products and services offered for sale in the retail operations and the customer base;
- The Financial Services segment provides credit card services, loyalty programs, insurance brokerage services, personal banking services provided by a major Canadian chartered bank, deposit taking services and telecommunication services; and
- The Choice Properties segment owns and leases income-producing commercial properties. The Choice Properties segment information presented below reflects the accounting policies of Choice Properties, which may differ from those of the consolidated Company. Differences in policies are eliminated in Consolidation and Eliminations.

The Company's chief operating decision maker evaluates segment performance on the basis of adjusted EBITDA<sup>(1)</sup> and adjusted operating income<sup>(1)</sup>, as reported to internal management, on a periodic basis.

Information for each reportable operating segment is included below:

(millions of Canadian dollars)	2014					2013 <sup>(i)</sup>				
	Retail	Financial Services <sup>(ii)</sup>	Choice Properties <sup>(ii)</sup>	Consolidation and Eliminations <sup>(iii)</sup>	Total	Retail	Financial Services	Choice Properties	Consolidation and Eliminations <sup>(iii)</sup>	Total
<b>Revenue<sup>(iv)</sup></b>	\$ 41,731	\$ 810	\$ 683	\$ (613)	\$ 42,611	\$ 31,600	\$ 739	\$ 319	\$ (287)	\$ 32,371
<b>EBITDA<sup>(v)</sup></b>	\$ 1,950	\$ 171	\$ 568	\$ (555)	\$ 2,134	\$ 1,989	\$ 151	\$ 370	\$ (365)	\$ 2,145
Adjustments <sup>(vi)</sup>	1,088	—	14	—	1,102	(42)	—	3	—	(39)
<b>Adjusted EBITDA<sup>(vi)</sup></b>	\$ 3,038	\$ 171	\$ 582	\$ (555)	\$ 3,236	\$ 1,947	\$ 151	\$ 373	\$ (365)	\$ 2,106
Depreciation and Amortization <sup>(vii)</sup>	1,036	7	—	12	1,055	809	9	—	6	824
<b>Adjusted Operating Income<sup>(vi)</sup></b>	\$ 2,002	\$ 164	\$ 582	\$ (567)	\$ 2,181	\$ 1,138	\$ 142	\$ 373	\$ (371)	\$ 1,282
Net interest expense and other financing charges	\$ 386	\$ 53	\$ 369	\$ (224)	\$ 584	\$ 315	\$ 49	\$ 303	\$ (199)	\$ 468

- (i) Certain 2013 figures have been amended to conform with the current year's presentation. See Accounting Standards Implemented in 2014 and Changes to Significant Accounting policies beginning on page 73.
- (ii) For segment presentation purposes, the results are for the year ended December 31, 2014, consistent with the fiscal calendars of both Financial Services and Choice Properties. Adjustments to January 3, 2015, are included in Consolidation and Eliminations.
- (iii) Consolidation and Eliminations includes the following items:
- Revenue includes the elimination of \$471 million (2013 – \$221 million) of rental revenue and \$142 million (2013 – \$66 million) of cost recovery recognized by Choice Properties, received from the Retail segment.
  - Operating income includes the elimination of the \$471 million (2013 – \$221 million) impact of rental revenue described above; the elimination of a \$82 million gain (2013 – \$144 million) recognized by Choice Properties related to the fair value adjustments on investment properties, which are classified as Fixed Assets or Investment Properties by the Company and measured at cost; the recognition of \$12 million (2013 – \$6 million) of depreciation expense for certain investment properties recorded by Choice Properties and measured at fair value; and the elimination of \$2 million (2013 – nil) intercompany charges.
  - Net interest expense and other financing charges includes the elimination of \$297 million (2013 – \$144 million) of interest expense included in Choice Properties related to debt owing to the Company; Unit distributions to external unitholders of \$44 million (2013 – \$21 million), which excludes distributions paid to the Company, and Choice Properties Unit issuance costs of nil (2013 – \$44 million), which are reflected as a reduction of equity in Choice Properties, and presented as interest expense for the consolidated Company; the elimination of a \$12 million fair value gain (2013 – \$147 million loss) recognized by Choice Properties on Class B Limited Partnership units held by the Company; and a \$17 million fair value loss (2013 – \$27 million) on the Company's Trust Unit Liability.
- (iv) Included in Financial Services revenue is \$356 million (2013 – \$325 million) of interest income.
- (v) EBITDA<sup>(1)</sup> is equal to Operating Income of \$662 million (2013 – \$1,321 million) plus Depreciation and Amortization of \$1,472 million (2013 – \$824 million).
- (vi) Certain items are excluded from operating income and EBITDA<sup>(1)</sup> to derive adjusted operating income<sup>(1)</sup> and adjusted EBITDA<sup>(1)</sup>, respectively. Adjusted operating income<sup>(1)</sup> and adjusted EBITDA<sup>(1)</sup> are used internally by management when analyzing segment underlying performance. Adjustments include: Recognition of fair value increment on inventory sold; Amortization of intangible assets acquired with Shoppers Drug Mart; Charge related to inventory measurement and other conversion differences; Shoppers Drug Mart acquisition-related costs and net divestitures loss; Restructuring costs; Restructuring of franchise fees; Fixed asset and other related impairments, net of recoveries; Choice Properties general and administrative costs; Fair value adjustment on Shoppers Drug Mart's equity-based compensation liability; Fair value adjustments on fuel and foreign currency contracts; Defined benefit plan amendments; Choice Properties start-up costs.
- (vii) Depreciation and amortization for the calculation of adjusted EBITDA<sup>(1)</sup> excludes \$417 million (2013 – nil) of amortization of intangible assets acquired with Shoppers Drug Mart.
- (1) See Section 20 "Non-GAAP Financial Measures" of the Company's Management's Discussion and Analysis.

(millions of Canadian dollars)	As at January 3, 2015	As at December 28, 2013
<b>Total Assets</b>		
Retail	\$ 29,973	\$ 17,290
Financial Services <sup>(i)</sup>	3,094	2,801
Choice Properties <sup>(i)</sup>	8,192	7,448
Consolidation and Eliminations <sup>(ii)</sup>	(7,575)	(6,798)
<b>Total</b>	<b>\$ 33,684</b>	<b>\$ 20,741</b>

- (i) For segment presentation purposes, the amounts are for the year ended December 31, 2014, consistent with the fiscal calendars of both Financial Services and Choice Properties. Adjustments to January 3, 2015, are included in Consolidation and Eliminations.
- (ii) Consolidation and Eliminations includes the elimination of certain investment properties held by Choice Properties measured at fair value, which are presented in the consolidated results as fixed assets and investment properties measured at cost.

(millions of Canadian dollars)	As at January 3, 2015	As at December 28, 2013
<b>Additions to Fixed Assets and Intangible Assets</b>		
Retail <sup>(i)</sup>	\$ 941	\$ 835
Financial Services <sup>(ii)</sup>	18	6
Choice Properties <sup>(ii)</sup>	280	7,129
Consolidation and Eliminations <sup>(iii)</sup>	(153)	(7,093)
<b>Total</b>	<b>\$ 1,086</b>	<b>\$ 877</b>

- (i) Excludes approximately \$11,300 million of fixed assets, investment properties and intangible assets, resulting from the acquisition of Shoppers Drug Mart (see note 5).
- (ii) For segment presentation purposes, the results are for the year ended December 31, 2014, consistent with the fiscal calendars of both Financial Services and Choice Properties. Adjustments to January 3, 2015, are included in Consolidation and Eliminations.
- (iii) Consolidations and Eliminations includes the elimination of \$179 million (2013 – \$7,093 million) of investment properties acquired by Choice Properties from the Retail Segment.

### Note 36. Subsequent Events

The following events have occurred subsequent to the end of the year:

The Company sold a warehouse to Choice Properties for approximately \$81 million. The warehouse is fully occupied by the Company as the single tenant with a 20-year initial lease term with six five-year renewal options.

The Company sold a parcel of land to Choice Properties for approximately \$12 million. Consideration for the acquisition included 265,665 Class B Limited Partnership units, \$7 million in cash and the assumption of a \$2 million obligation. The Class B Limited Partnership units issued to the Company as partial consideration for this transaction did not impact the Company's effective ownership percentage.

Choice Properties issued \$250 million aggregate principal amount of Series E senior unsecured debentures bearing interest at a rate of 2.30% per annum and maturing in 2020. The net proceeds from the issuance were used by Choice Properties to repay existing indebtedness and for general business purposes.

The Company, through PC Bank, extended the maturity date for certain Other Independent Securitization Trust agreements from the second quarter of 2016 to the second quarter of 2017, with all other terms and conditions remaining substantially the same.

PC Bank entered into USD foreign exchange forward agreements, which mature by December 2015. The notional amounts of the contracts total USD \$27 million.

Pursuant to the Consent Agreement reached with the Competition Bureau in 2014 (see note 5), the Company sold the remaining three Shoppers Drug Mart stores for estimated proceeds of \$9 million.



## Three Year Summary<sup>(1)</sup>

As at or for the years ended January 3, 2015, December 28, 2013 and December 29, 2012.

(millions of Canadian dollars except where otherwise indicated)

	2014	2013 <sup>(4)</sup>	2012 <sup>(3)</sup>
<b>Consolidated Results of Operations</b>			
Revenue	\$ 42,611	\$ 32,371	\$ 31,604
Operating income	662	1,321	1,195
Adjusted operating income <sup>(2)</sup>	2,181	1,282	1,264
EBITDA <sup>(2)</sup>	2,134	2,145	1,972
Adjusted EBITDA <sup>(2)</sup>	3,236	2,106	2,041
Net interest expense and other financing charges	584	468	351
Adjusted net interest expense and other financing charges <sup>(2)</sup>	529	354	351
Net earnings	53	627	634
Adjusted net earnings <sup>(2)</sup>	1,224	696	685
<b>Consolidated Financial Position and Cash Flows</b>			
Adjusted debt <sup>(2)</sup>	9,995	6,288	4,583
Cash and cash equivalents, short term investments and security deposits	1,027	4,251	2,047
Cash flows from operating activities	2,569	1,491	1,637
Capital investments	1,086	877	1,060
Free cash flow <sup>(2)</sup>	977	244	221
<b>Consolidated Per Common Share (\$)</b>			
Basic net earnings	\$ 0.14	\$ 2.23	\$ 2.25
Adjusted basic net earnings <sup>(2)</sup>	3.22	2.48	2.43
<b>Consolidated Financial Measures and Ratios</b>			
Revenue growth	31.6%	2.4 %	1.1 %
Adjusted operating margin <sup>(2)</sup>	5.1%	4.0 %	4.0 %
Adjusted EBITDA margin <sup>(2)</sup>	7.6%	6.5 %	6.5 %
Adjusted debt <sup>(2)</sup> to adjusted EBITDA <sup>(2)</sup>	3.1x	3.0x	2.2x
<b>Retail Results of Operations</b>			
Sales	\$ 41,731	\$ 31,600	\$ 30,960
Gross profit	9,734	6,961	6,819
Adjusted gross profit <sup>(2)</sup>	10,722	6,961	6,819
Operating income	497	1,180	1,100
Adjusted operating income <sup>(2)</sup>	2,002	1,138	1,169
Adjusted EBITDA <sup>(2)</sup>	3,038	1,947	1,936
<b>Retail Operating Statistics</b>			
Same-store sales <sup>(1), (6)</sup> growth (decline)	2.0%	1.1 %	(0.2)%
Adjusted gross profit percentage <sup>(2)</sup>	25.7%	22.0 %	22.0 %
Adjusted operating margin <sup>(2)</sup>	4.8%	3.6 %	3.8 %
Adjusted EBITDA margin <sup>(2)</sup>	7.3%	6.2 %	6.3 %
Total retail square footage (in millions)	70.0	51.9	51.5
Number of corporate stores	615	570	580
Number of franchise stores	527	496	473
Number of Associate-owned drug stores	1,302	—	—
<b>Financial Services Results of Operations<sup>(7)</sup></b>			
Revenue	\$ 810	\$ 739	\$ 644
Operating income	164	142	95
Earnings before income taxes	111	93	50
<b>Financial Services Operating Measures and Statistics<sup>(7)</sup></b>			
Average quarterly net credit card receivables	\$ 2,535	\$ 2,345	\$ 2,105
Credit card receivables	2,630	2,538	2,305
Allowance for credit card receivables	54	47	43
Annualized yield on average quarterly gross credit card receivables	13.7%	13.6 %	12.8 %
Annualized credit loss rate on average quarterly gross credit card receivables	4.4%	4.2 %	4.3 %
<b>Choice Properties Results of Operations<sup>(5)</sup></b>			
Revenue	\$ 683	\$ 319	\$ —
Operating income	568	370	—
Net interest expense and other financing charges	369	303	—
<b>Choice Properties Operating Measures<sup>(5)</sup></b>			
Adjusted funds from operations <sup>(2)</sup>	\$ 285	\$ 131	\$ —

Please refer to the inside cover of the 2014 Annual Report for the Footnote Legend.

## Glossary of Terms

Term	Definition	Term	Definition
<b>Adjusted basic net earnings per common share</b>	Adjusted net earnings available to common shareholders divided by the weighted average number of common shares outstanding during the year (see Section 20 "Non-GAAP Financial Measures" of the Company's Management's Discussion and Analysis).	<b>Choice Properties adjusted funds from operations</b>	Choice Properties' funds from operations adjusted for items that are not necessarily reflective of the REIT's underlying operating performance (see Section 20 "Non-GAAP Financial Measures" of the Company's Management's Discussion and Analysis).
<b>Adjusted debt</b>	Bank indebtedness, short term debt, long term debt, Trust Unit Liability, capital securities, certain other liabilities and the fair value of certain financial derivative liabilities less independent securitization trusts in short term and long term debt, independent funding trusts, Trust Unit Liability and President's Choice Bank's guaranteed investment certificates (see Section 20 "Non-GAAP Financial Measures" of the Company's Management's Discussion and Analysis).	<b>Control brand</b>	A brand and associated trademark that is owned by the Company for use in connection with its own products and services.
<b>Adjusted debt to adjusted EBITDA</b>	Adjusted debt divided by adjusted EBITDA (see Section 20 "Non-GAAP Financial Measures" of the Company's Management's Discussion and Analysis).	<b>Conversion</b>	A store that changes from one Company banner to another Company banner.
<b>Adjusted EBITDA</b>	Adjusted operating income before depreciation and amortization (see Section 20 "Non-GAAP Financial Measures" of the Company's Management's Discussion and Analysis).	<b>Diluted net earnings per common share</b>	Net earnings available to common shareholders of the Company adjusted for the impact of dilutive items divided by the weighted average number of common shares outstanding during the period adjusted for the impact of dilutive items.
<b>Adjusted EBITDA margin</b>	Adjusted EBITDA divided by sales (see Section 20 "Non-GAAP Financial Measures" of the Company's Management's Discussion and Analysis).	<b>EBITDA</b>	Operating income before depreciation and amortization (see Section 20 "Non-GAAP Financial Measures" of the Company's Management's Discussion & Analysis).
<b>Adjusted income tax expense</b>	Income taxes adjusted for the tax impact of items included in adjusted operating income less adjusted net interest and other financing charges (see Section 20 "Non-GAAP Financial Measures" of the Company's Management's Discussion and Analysis).	<b>Free Cash Flow</b>	Cash flows from operating activities less intangible asset additions, fixed asset purchases and interest paid (see Section 20 "Non-GAAP Financial Measures" of the Company's Management's Discussion and Analysis).
<b>Adjusted income tax rate</b>	Adjusted income taxes divided by adjusted operating income less adjusted net interest and other financing charges (see Section 20 "Non-GAAP Financial Measures" of the Company's Management's Discussion and Analysis).	<b>Major expansion/contraction</b>	Expansion/contraction of a store that results in an increase/decrease in square footage that is greater than 25% of the square footage of the store prior to the expansion/contraction.
<b>Adjusted net earnings</b>	Net earnings available to common shareholders of the Company adjusted for items that are not necessarily reflective of the Company's underlying operating performance (see Section 20 "Non-GAAP Financial Measures" of the Company's Management's Discussion and Analysis).	<b>Minor expansion</b>	Expansion of a store that results in an increase in square footage that is less than or equal to 25% of the square footage of the store prior to the expansion.
<b>Adjusted net interest and other financing charges</b>	Net interest expense and other financing charges adjusted for items that are not necessarily reflective of the Company's financial performance (see Section 20 "Non-GAAP Financial Measures" of the Company's Management's Discussion and Analysis).	<b>New store</b>	A newly constructed store, acquisition, conversion or major expansion.
<b>Adjusted operating income</b>	Operating income adjusted for items that are not necessarily reflective of the Company's underlying operating performance (see Section 20 "Non-GAAP Financial Measures" of the Company's Management's Discussion and Analysis).	<b>Operating income</b>	Earnings before net interest expense and other financing charges and income taxes.
<b>Adjusted operating margin</b>	Adjusted operating income divided by sales (see Section 20 "Non-GAAP Financial Measures" of the Company's Management's Discussion and Analysis).	<b>Renovation</b>	A capital investment in a store resulting in no significant change to the store square footage.
<b>Annualized credit loss rate on average quarterly gross credit card receivables</b>	Total credit card losses year-to-date divided by the number of days year-to-date times 365 divided by average quarterly gross credit card receivables.	<b>Retail segment adjusted gross profit</b>	Retail segment sales less cost of merchandise inventories sold, adjusted for items that are not necessarily reflective of the Company's underlying operating performance (see Section 20 "Non-GAAP Financial Measures" of the Company's Management's Discussion and Analysis).
<b>Annualized yield on average quarterly gross credit card receivables</b>	Interest earned on credit card receivables year-to-date divided by the number of days year-to-date times 365 divided by average quarterly gross credit card receivables.	<b>Retail segment adjusted gross profit percentage</b>	Retail segment adjusted gross profit divided by Retail segment sales.
<b>Basic net earnings per common share</b>	Net earnings available to common shareholders divided by the weighted average number of common shares outstanding during the period.	<b>Retail square footage</b>	Retail square footage includes corporate, independent franchised stores and associate-owned drug stores.
<b>Capital Investments</b>	Fixed asset purchases and intangible asset additions.	<b>Same-store sales</b>	Retail segment sales from the same location for stores in operation in that location in both periods excluding sales from a store that has undergone a major expansion/contraction in the period.
		<b>Weighted average common shares outstanding</b>	The number of common shares outstanding determined by relating the portion of time within the year the common shares were outstanding to the total time in that period.
		<b>Year</b>	The Company's fiscal year ends on the Saturday closest to December 31 and is usually 52 weeks in duration, but includes 53 weeks every 5 to 6 years. The years ended January 3, 2015 and December 28, 2013 contained 53 weeks and 52 weeks, respectively.

## National Head Office and Store Support Centre

Loblaw Companies Limited  
1 President's Choice Circle  
Brampton, Canada L6Y 5S5  
Tel: (905) 459-2500  
Fax: (905) 861-2206  
Internet: <http://loblaw.ca>

## Stock Exchange Listing and Symbol

The Company's common shares and second preferred shares are listed on the Toronto Stock Exchange and trade under the symbols "L" and "L.PR.A.", respectively.

## Common Shares

W. Galen Weston, directly and indirectly, including through his controlling interest in Weston, owns approximately 46% of the Company's common shares.

At year-end 2014, there were 412,480,891 common shares issued and outstanding.

The average daily trading volume of the Company's common shares for 2014 was 751,814.

## Preferred Shares

At year-end 2014, there were 9,000,000 second preferred shares issued and outstanding.

The average daily trading volume of the Company's second preferred shares for 2014 was 4,172.

## Trademarks

Loblaw Companies Limited and its subsidiaries own a number of trademarks. Several subsidiaries are licensees of additional trademarks. These trademarks are the exclusive property of Loblaw Companies Limited or the licensor and where used in this report, are in italics.

## Common Dividend Policy

The Company's dividend policy states: the declaration and payment of dividends and the amount thereof on the Company's common shares are at the discretion of the Board of Directors which takes into account the Company's financial results, capital requirements, available cash flow, future prospects of the Company's business and other factors considered relevant from time to time.

## Common Dividend Dates

The declaration and payment of quarterly dividends are made subject to approval by the Board of Directors. The anticipated record and payments dates for 2015 are:

Record Date	Payment Date
March 15	April 1
June 15	July 1
September 15	October 1
December 15	December 30

## Normal Course Issuer Bid

The Company has a Normal Course Issuer Bid on the Toronto Stock Exchange.

## Value of Common Shares

For capital gains purposes, the valuation day (December 22, 1971) cost base for the Company is \$0.958 per common share. The value on February 22, 1994 was \$7.67 per common share.

## Investor Relations

Shareholders, security analysts and investment professionals should direct their requests to Investor Relations at the Company's National Head Office or by e-mail at [investor@loblaw.ca](mailto:investor@loblaw.ca).

## Registrar and Transfer Agent

Computershare Investor Services Inc.  
100 University Avenue  
Toronto, Canada M5J 2Y1

Toll free: 1-800-564-6253 (Canada and U.S.)

Fax (416)263-9394

Toll free fax: 1-888-453-0330

International direct dial: (514) 982-7555

To change your address, eliminate multiple mailings or for other shareholder account inquiries, please contact Computershare Investor Services Inc.

Additional financial information has been filed electronically with various securities regulators in Canada through the System for Electronic Document Analysis and Retrieval (SEDAR) and with the Office of the Superintendent of Financial Institutions (OSFI) as the primary regulator for the Company's subsidiary, President's Choice Bank.

## Independent Auditors

KPMG LLP  
Chartered Professional Accountants  
Toronto, Canada

## Annual General Meeting

The 2015 Annual Meeting of Shareholders of Loblaw Companies Limited will be held on Thursday, May 7, 2015 at 11:00 a.m. (EST), at the Mattamy Athletic Centre, 50 Carlton Street, Toronto, Canada M5B 1J2.

The Company holds an analyst call shortly following the release of its quarterly results. These calls are archived in the Investor Centre section of the Company's website ([loblaw.ca](http://loblaw.ca)).

## Preferred Shares, Series A Dividend Dates

The declaration and payment of quarterly dividends are made subject to approval by the Board. The anticipated payment dates for 2015 are:

Record Date	Payment Date
January 15	January 31
April 15	April 30
July 15	July 31
October 15	October 31





### Environmental Savings Summary

By using 3,190 kg of paper manufactured with 30% post-consumer recycled waste fibre for the Annual Report and 2,789 kg of paper manufactured with 100% post-consumer recycled waste fibre for the Financial Review, Loblaw companies Limited reduced its environmental footprint by:

Wood Use:	19278 kg
Total Energy:	50 million BTU's
Greenhouse Gases:	3709 kg of CO <sub>2</sub> equivalent
Wastewater Flow:	167875 L
Solid Waste:	1347 kg

Environmental impact savings estimates were made using the Environmental Defense Paper Calculator, [www.papercalculator.org](http://www.papercalculator.org). Amounts calculated are approximate based on industry averages.

**Loblaw**

COMPANIES LIMITED

